

**BUSINESS REPORT OF THE MERCATOR GROUP AND  
THE COMPANY POSLOVNI SISTEM MERCATOR, D.D.,  
FOR THE PERIOD 1–9, 2017**



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# EXECUTIVE SUMMARY

In the first three quarters of 2017, Mercator Group successfully pursued its revised business strategy. Mercator Group's profit in the period 1–9, 2017 exceeded the figure from the same period of the year before by EUR 11.6 million, amounting to EUR 9.9 million. Mercator Group EBITDA in the 1–9, 2017 was at EUR 89.2 million. Improved performance is also evident in higher EBITDA margin which rose by 17.8% adjusted for divested activities.

## Improved performance

In 2017, Mercator Group improved its business performance and efficiency, which is reflected by higher profit and EBITDA. Mercator Group's profit in 1–9, 2017 exceeded the figure from the same period of the year before by EUR 11.6 million, amounting to EUR 9.9 million; in the same period of the year before, it was at EUR -1.7 million.

Mercator Group EBITDA in the 1–9, 2017 was at EUR 89.2 million. In the corresponding period of the preceding year, if the divested operations are not accounted for it amounted to EUR 77.8 million. Performance improvement is also evident in higher EBITDA margin which rose by 17.8% relative to the same period of the year before, adjusted for divested activities. Moreover, EBITDA was higher for the company Poslovni sistem Mercator, d.d., amounting to EUR 54.7 million, or EUR 11.2 million more than in the equivalent period prior year without divested activities. For this reason, EBITDA margin is higher by 29.1% relative to the same period of the year before without divested activities.

Revenue from sales of goods in the core activity of retail in Slovenia and Montenegro is higher relative to the comparable period of the preceding year. The drop of revenue in Serbia was primarily a result of closing down of some stores based on a decision of the country's regulator in Serbia.

In 2017, payment terms for our suppliers remain stable.

As at September 30, 2017, Mercator Group's net financial debt amounted to EUR 794,193 thousand, which is 1.4% less than as at the end of 2016, and 5.9% less than as at September 30, 2016.

## Entry into the market of Bosnia and Herzegovina

Mercator re-entered the market of Bosnia and Herzegovina. Transfer of possession and establishment of retail operations in 83 stores took place in September 2017. Mercator's goal is to offer the local consumers a new store concept as developed by Mercator, and especially a broad assortment tailored as closely as possible to the needs and desires of the customers.

## Changes in the Management Board composition at the parent company Poslovni sistem Mercator, d.d.

In April, Tomislav Čizmić was appointed new Management Board president; also in April, Draga Cukjati was appointed new Management Board member in charge of finance and IT. In April, Slovenian National Assembly adopted the Act on Conditions for Appointment of Extraordinary Management Board Member in Companies of Systemic Importance to the Republic of Slovenia. Based on the adopted Act, the government proposed Gregor Planteu for the position of the Management Board member, and the District Court of Ljubljana, consistently with its powers, appointed him extraordinary Management Board member as of May 2017. Thus, the Management Board of Poslovni sistem Mercator operates with the following composition: Tomislav Čizmić, President of the Management Board; and Management Board members Draga Cukjati, Igor Mamuza, and Gregor Planteu.

## Changes in subsidiary management and governance

In September, Entoni Sošić was appointed new managing director of the company Mercator - S, d.o.o., replacing his predecessor Aleksandar Seratlić.

## Changes in the composition of the Supervisory Board at the parent company Poslovni sistem Mercator, d.d.

As of April 25, 2017, two Supervisory Board members at the company Poslovni sistem Mercator, d.d., – Ante Todorčić as the Supervisory Board chairman and Ivan Crnjac as the Supervisory Board member – resigned from their respective positions. As of June 8, 2017, Darko Knez resigned from the position of a Supervisory Board member at the company Poslovni sistem Mercator, d.d. On June 15, 2017, the Shareholders Assembly appointed

Ante Ramljak, Vladimir Bošnjak, and Teo Vujčić as Supervisory Board members representing the interests of shareholders, for a four-year term of office. At the Supervisory Board session on June 15, 2017, Ante Ramljak was appointed new Supervisory Board chairman for the company Poslovni sistem Mercator, d.d. At the session held on June 28, 2017, members of the Works Council of Mercator, d.d., appointed Jože Lavrenčič as the new employee representative in the company Supervisory Board, as the term of the previous Supervisory Board member Veljko Tatić was to expire on November 4, 2017; in addition, they reappointed Vesna Stojanović for a new term of office.

#### **Operating risks related to the Agrokor Group**

In 2016, the companies Poslovni sistem Mercator, d.d., Mercator - H, d.o.o., and Mercator - BH, d.o.o., recognized impairments for receivables from the Agrokor Group companies that are not a part of the Mercator Group. At its extraordinary session held on April 14, 2017, the Supervisory Board instructed the Management Board to immediately examine all possibilities of settling or offsetting all mutual receivables and liabilities between the Mercator Group companies and Agrokor Group companies that are not a part of the Mercator Group as soon as possible.

In March and April of 2017, the Management Board of the company Poslovni sistem Mercator, d.d., maintained regular contact with the company creditors with regard to avoidance of a breach of long-term financing contracts which could result from the events pertaining at the time to the company's majority shareholder, and which eventually resulted in the invocation of the so-called Lex Agrokor. On April 9, 2017, the Management Board requested a waiver from the creditor banks in order to avoid a potential cross default. The waiver that the company requested pertained to the potential cross default with regard to the company Agrokor, d.d., and its restricted subsidiaries as a result of the events taking place at that time regarding the company's majority shareholder. The company Poslovni sistem Mercator, d.d., did not receive any rejections of such requests, meaning it only received positive response – waivers by the majority of the creditor banks, so that the required two-thirds majority for consent was reached.

In September 2017, a report by the extraordinary Management Board member for the period from May 8, 2017, to August 8, 2017, was released, which indicates that all transactions signed between the company Mercator, and Agrokor and the companies affiliated with it, complied with the principles of diligence, good management and credibility, and that the company did not sustain any loss or damage with regard to such transactions.



# INTRODUCTION

## PROFILE AND ORGANIZATION

### Mercator Group Profile

Mercator Group is one of the largest corporate groups in Slovenia and in the entire Southeastern European region. As at September 30, 2017, the company was present with ten companies in Slovenia and with seven subsidiaries in other markets of the Southeastern Europe. Poslovni sistem Mercator, d.d., headquartered in the Republic of Slovenia, is the parent company of the Mercator Group.

Poslovni sistem Mercator, d.d.	
Telephone	+386 1 560 10 00
E-address	info@mercator.si
Website	www.mercatorgroup.si
Company head office	Dunajska cesta 107, 1113 Ljubljana, Slovenia
Activity	Retail in non-specialized food retail outlets (G 47.110)
Registration number	5300231
VAT tax code	45884595
Legal Entity Identifier (LEI)	549300X47J0FW574JN34
Company share capital as at September 30, 2017	EUR 254,175,051.39
Number of shares issued and paid-up as at September 30, 2017	6,090,943
Share listing	Ljubljanska borza, d.d., official market, prime market, symbol MELR

### Corporate governance

In the period 1–9, 2017, the Supervisory Board of Poslovni sistem Mercator, d.d., held five regular sessions, five correspondence sessions, and one extraordinary session.

At the **12th correspondence session held on January 13, 2017**, the Supervisory Board reduced the number of Management Board members at the company Poslovni sistem Mercator, d.d., by one member, following the resignation of Management Board member Drago Kavšek. The Supervisory Board adopted the clean and consolidated copy of the Management Board Act of the company Poslovni sistem Mercator, d.d., which specifies the number of Management Board members and their respective fields of responsibility, powers and authorizations, and the conditions for appointment of the Management Board president and members.

At the **13th correspondence session held on March 30, 2017**, the Supervisory Board was presented the Annual Report on the work of the Internal Audit of Mercator Group in 2016.

At the **13th regular session held on April 5, 2017**, the Supervisory Board of Poslovni sistem Mercator, d.d., relieved Anton Balažič, based on a consensual agreement on early termination of the term of office and without any fault-based grounds or liability, from the position of the Management Board president of the company Poslovni sistem Mercator, d.d., and appointed Tomislav Čizmić as his replacement as of April 6, 2017 for a five-year term of office.

At the **14th correspondence session held on April 9, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., decided to increase the number of Management Board members at the company Poslovni sistem Mercator, d.d., by one member so that the Management Board consists of 3 members, and appointed Draga Cukjati as a new Management Board member in charge of finance and IT, with a term of office from April 18, 2017, to April 6, 2022.

At the **extraordinary session held on April 14, 2017**, convened at the request of four Supervisory Board members, the Supervisory Board of the company Poslovni sistem Mercator, d.d., was presented the report on Mercator's purchasing policy and on signing of agreements with third-party suppliers or service providers in marketing services and investments, and found based on the relevant data from all reports that no irregularities had occurred in the operations in this respect. In addition, the Supervisory Board was presented the report by the Management Board president on the current and completed Management Board activities for the protection of all interests of the company and the Mercator Group with regard to the developments at the Agrokor Group, and tasked the company Management Board to examine all possibilities to offset or settle as soon as possible all and any mutual receivables and liabilities between Mercator Group companies and Agrokor Group companies that are not a part of the Mercator Group.

At the **14th regular session held on April 25, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., adopted the Annual Report of the company Mercator, d.d., and the Mercator Group for the year 2016, approved the wording of the Supervisory Board report on the 2016 Annual Report Audit; perused the report by an independent auditor on the relations with affiliated companies in 2016, and the statement of resignation by Ante Todorić and Ivan Crnjac, by which the two resigned from the position of Supervisory Board members of the company Poslovni sistem Mercator, d.d., as of April 25, 2017; approved the agenda for the 24th regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., the resolution proposals for the appointment of the authorized auditing company for the year 2017, and appointment of new Supervisory Board members; and appointed Matej Lahovnik as a member of the Supervisory Board's Audit Committee, replacing Darko Knez.

At the **15th regular session held on May 23, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., was presented the performance of the company Poslovni sistem Mercator, d.d., and the Mercator Group in the period 1–3, 2017; approved the revision of the Mercator Group plan for the year 2017; received information about the projects of Mercator nepremičnine (Mercator real estate) that the Supervisory Board had discussed and approved at the sessions in the period from September 1, 2014, to 2017, and the information about the completion of investments in the first quarter of 2017; and approved the investment proposal for the Mercator Group for the period by the end of 2017.

At the **16th regular session held on June 15, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., appointed Ante Ramljak as Supervisory Board chairman; appointed Vladimir Bošnjak as Audit Committee member, who thus joined Damir Kuštrak, Matej Lahovnik, and Sergeja Slapničar in the Audit Committee; and appointed a Human Resource Committee that includes Vesna Stojanović, Matej Lahovnik, and Ivica Mudrinić. In addition, the Supervisory Board was presented the performance of the Mercator Group in the period 1–5, 2017.

At the **15th correspondence session held on June 26, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., received information about the new macro organization of the company Poslovni sistem Mercator, d.d.

At the **16th correspondence session held on July 17, 2017**, the Supervisory Board of Poslovni sistem Mercator, d.d., agreed with return of Mercator's retail operations to the market of Bosnia and Herzegovina. At the session, the Supervisory Board was also presented the preliminary business results of the Mercator Group and the company Mercator, d.d., in the period 1–6, 2017.

At the **17th regular session held on August 30, 2017**, the Supervisory Board of Poslovni sistem Mercator, d.d., was presented the operations and performance of the Mercator Group and the company Mercator, d.d., for the period 1–6, 2017; the report on receivables collection activities within the Group, as prepared in accordance with the Lex Agrokor; and the Report on all transactions concluded with the majority shareholder, i.e. the company Agrokor, d.d., and companies affiliated to it, for the period from May 8, 2017, to August 8, 2017. Moreover, the

Supervisory Board of Mercator, d.d., was presented the Management Board's activities regarding the settlement, or offsetting, of receivables and liabilities between the company Mercator - BH, d.o.o., and Konzum BH, d.o.o., and the Management Board activities regarding the return of Mercator's retail operations to the market of Bosnia and Herzegovina. At the session, the Supervisory Board of Poslovni sistem Mercator, d.d., adopted the Rules of Procedure for the Human Resource Committee of Mercator, d.d., Supervisory Board, and the Rules of Procedure for the Audit Committee of Mercator, d.d., Supervisory Board; and appointed Matej Lahovnik as chairman of the Human Resource Committee of Mercator, d.d., Supervisory Board, and Vladimir Bošnjak as the chairman of the Audit Committee of Mercator, d.d., Supervisory Board.

#### **Major events following the end of period at hand**

At the **17th correspondence session on October 6, 2017**, the Supervisory Board of the company Poslovni sistem Mercator, d.d., unanimously approved upon proposal by the company Management Board the contractual solutions for termination of lease agreements for 83 commercial premises in Bosnia and Herzegovina as signed between the company Mercator - BH, d.o.o., Sarajevo, and the company Konzum, d.o.o., Sarajevo, settlement of outstanding amounts of rent with equipment at these stores to the benefit of Mercator - BH, d.o.o., Sarajevo, and for agreement on purchase of trade goods by Mercator - BH, d.o.o., Sarajevo.

## Mercator Group composition as at September 30, 2017



\* The company does not conduct business operations.

### Branch Offices

As at September 30, 2017, Mercator Group companies did not have any branch offices.

### Other Organizations

The company Poslovni sistem Mercator, d.d., is the founder of the Mercator Humanitarian Foundation whose purpose is provision of humanitarian aid to Mercator employees.

The company Mercator - S, d.o.o., is the founder of the Mercator Solidarity Foundation in Serbia, and Mercator - CG, d.o.o., is the founder of the Mercator Solidarity Foundation in Montenegro. The purpose of both is to provide solidarity aid to the employees in social or economic distress.



# MERCATOR GROUP KEY OBJECTIVES

We are fulfilling the six key initiatives:

**1. Revenue and profit margin**

We are pursuing the goal of optimizing our prices and promotions.

**2. New store concept**

We are updating our retail network and introducing a new store concept.

**3. Cost optimization**

We are optimizing costs, through the cost control system already in place.

**4. Cash flow**

We are focused on optimizing our working capital management, especially inventory, and on the divestment of non-core operations and real property out of use.

**5. Brand differentiation**

We are strengthening our brand identity by emphasizing local offer, freshness, and quality. We offer our customers the most for their money.

**6. Employees**

We care for development, training and education, rewards, and motivation of our employees.

# MERCATOR GROUP PERFORMANCE HIGHLIGHTS IN THE PERIOD 1–9, 2017

		1–9, 2017	1–9, 2016 continued <sup>1,2</sup>	Index 1–9, 2017/ 1–9, 2016 continued
INCOME STATEMENT	Revenue (in EUR 000)	1,730,139	1,777,798	97.3
	Results from operating activities (in EUR 000)	33,493	19,766	169.4
	Profit (loss) before income tax (in EUR 000)	14,596	845	1,726.6
	Profit (loss) for the year (in EUR 000)	9,941	-1,700	-
	Gross cash flow from operating activities (EBITDA) (in EUR 000)	89,208	77,823	114.6
	Gross cash flow from operating activities before rental expenses (EBITDAR) (in EUR 000)	142,855	132,811	107.6
ABILITY TO GENERATE CASH FLOW	Return on sales	0.6%	-0.1%	-
	Return on equity <sup>3</sup>	2.2%	-0.4%	-
	Gross cash flow from operating activities (EBITDA) / revenue	5.2%	4.4%	117.8
	Gross cash flow from operating activities before rental expenses (EBITDAR) / revenue	8.3%	7.5%	110.5
		1–9, 2017	1–9, 2016 <sup>2</sup>	Index 1–9, 2017/ 1–9, 2016
BALANCE SHEET	Total assets as at September 30 (in EUR 000)	2,105,663	2,217,466	95.0
	Equity as at September 30 (in EUR 000)	572,146	636,350	85.2
INVESTMENT ACTIVITIES	Capital expenditure (in EUR 000)	36,602	53,187	68.8
EMPLOYEES	Number of employees as at the end of the period September 30	20,795	21,757	95.6
	Number of employees based on hours worked	18,491	20,087	92.1

<sup>1</sup> Modiana and Intersport operations are excluded.





<sup>2</sup> As the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

<sup>3</sup> Indicator is adjusted to the annual level.

# KEY EVENTS

## Retail network development

In the period 1–9, 2017:

-  we invested EUR 36,602 thousand into property, plant, and equipment (CAPEX);
-  we divested EUR 12,193 thousand worth of property, plant and equipment;
-  we added 16 new units spanning a combined total of 15,003 m<sup>2</sup> of new gross retail area and 1 distribution centre (1,723 m<sup>2</sup> of new gross retail area), by construction of the Trade centre Bled, Supermarket Blok 63 in Beograd and operating lease.
-  took over from Konzum Sarajevo Mercator's former stores (83 units) and one distribution centre, which now again operate within Mercator's company in Bosnia and Herzegovina.

## Changes in the composition of the Mercator Group

On August 31, 2017, the company M - BL, d.o.o., Bosnia and Herzegovina, was founded.

## Changes in parent company governance

As of April 5, 2017, the term of office of Management Board president Anton Balažič was terminated, without any fault-based grounds or liability on the part of the Management Board president. At the same time, Tomislav Čizmić was appointed new President of the Management Board for a term of office of five years, as of April 6, 2017. The Supervisory Board appointed Draga Cukjati as the new Management Board member in charge of finance and IT. She commenced her term of office on April 18, 2017.

In April, Slovenian National Assembly adopted the Act on Conditions for Appointment of Extraordinary Management Board Member in Companies of Systemic Importance to the Republic of Slovenia (so-called Lex Mercator). The new Management Board member will only be in charge of transactions related to the majority owner and will not have any power or authority with regard to management of regular transactions. Based on the adopted Act, the government proposed Gregor Planteu for the position of the Management Board member, and the District Court of Ljubljana, consistently with its powers, appointed him, by the court's decision, as extraordinary Management Board member as of May 18, 2017. Thus, the Management Board of Poslovni sistem Mercator operates with the following composition: Tomislav Čizmić, President of the Management Board; and Management Board members Draga Cukjati, Igor Mamuza, and Gregor Planteu.

As of April 25, 2017, two Supervisory Board members at the company Poslovni sistem Mercator, d.d., – Ante Todorić as the Supervisory Board chairman and Ivan Crnjac as the Supervisory Board member – resigned from their respective positions. As of June 8, 2017, Darko Knez resigned from the position of a Supervisory Board member at the company Poslovni sistem Mercator, d.d.

On June 15, 2017, the Shareholders Assembly appointed Ante Ramljak, Vladimir Bošnjak, and Teo Vujčić as Supervisory Board members representing the interests of shareholders, for a four-year term of office starting with the day of appointment at the Shareholders Assembly.

At the Supervisory Board session held on June 15, 2017, Ante Ramljak was appointed new Supervisory Board chairman for the company Poslovni sistem Mercator, d.d. At the session held on June 28, 2017, members of the Works Council of Mercator, d.d., appointed Jože Lavrenčič as the new employee representative in the company Supervisory Board, as the term of the previous Supervisory Board member Veljko Tatić was to expire on November 4, 2017. At the same session, the workers also reappointed Vesna Stojanović as the Supervisory Board member of the company Poslovni sistem Mercator, d.d., for a new term of office that started as of July 4, 2017. On the same session, a resolution on the establishment of a Human Resource Committee was adopted. The Human Resource Committee includes Vesna Stojanović, Matej Lahovnik, and Ivica Mudrinić.

Two months later, the Supervisory Board of Poslovni sistem Mercator, d.d., appointed at the 17 regular session Matej Lahovnik as chairman of the Human Resource Committee of Mercator, d.d., Supervisory Board, and Vladimir Bošnjak as the chairman of the Audit Committee of Mercator, d.d., Supervisory Board.

### Changes in subsidiary management and governance

In September, Entoni Sošić was appointed new managing director of the company Mercator - S, d.o.o., replacing his predecessor Aleksandar Seratlić.

### Changes in the parent company ownership structure

On March 10, 2017, a share sale and purchase agreement was signed between Agrokor Investment B.V. and Agrokor, d.d., pursuant to which the company Agrokor Investment B.V. sold to Agrokor, d.d., 615,384 MELR shares. Thus, the shareholding held by the company Agrokor, d.d., increased from 59.47% to 69.57%, while the shareholding held by the company Agrokor Investments B.V. decreased from 28.64% to 18.53%.

In June 2017, the company Sberbank of Russia exercised their lien over 1,128,803 shares of the company Poslovni sistem Mercator, d.d., held by the company Agrokor Investment B.V. Thus, the company Sberbank of Russia became in the following month an 18.53% shareholder of the company Poslovni sistem Mercator, d.d.

### Entry into the market of Bosnia and Herzegovina

Mercator re-entered the market of Bosnia and Herzegovina. Transfer of possession and establishment of retail operations in 83 stores, of which 76 are active, took place in September 2017. Mercator's goal is to offer the local consumers a new store concept as developed by Mercator, and especially a broad assortment tailored as closely as possible to the needs and desires of the customers.

### Events, related to the developments at the Agrokor Group

In 2016, the companies Poslovni sistem Mercator, d.d., Mercator - H, d.o.o., and Mercator - BH, d.o.o., recognized impairments for receivables from the Agrokor Group companies that are not a part of the Mercator Group. At its extraordinary session held on April 14, 2017, the Supervisory Board instructed the Management Board to immediately examine all possibilities of settling or offsetting as soon as possible all mutual receivables and liabilities between the Mercator Group companies and Agrokor Group companies that are not part of the Mercator Group.

In March and April of 2017, the Management Board of the company Poslovni sistem Mercator, d.d., maintained regular contact with the company creditors with regard to avoidance of a breach of long-term financing contracts which could result from the events pertaining at the time to the company's majority shareholder, and which eventually resulted in the invocation of the so-called Lex Agrokor. On April 9, 2017, the Management Board requested a waiver from the creditor banks in order to avoid a potential cross default. The waiver that the company requested pertained to the potential cross default with regard to the company Agrokor, d.d., and its restricted subsidiaries as a result of the events taking place at that time regarding the company's majority shareholder. The company Poslovni sistem Mercator, d.d., did not receive any rejections of such requests, meaning it only received positive response – waivers by the majority of the creditor banks, so that the required two-thirds majority required for consent was reached.

In September 2017, a report by the extraordinary Management Board member for the period from May 8, 2017, to August 8, 2017, was released, which indicates that all transactions signed between the company Mercator, and Agrokor and the companies affiliated with it, complied with the principles of diligence, good management and credibility, and that the company did not sustain any loss or damage with regard to such transactions.

### Awards and other achievements

#### Slovenia

Mercator brand received the **Trusted Brand 2017 award** in two categories: shopping centre and environment protection. It also received a special Trusted Brand award for its 10th victory in the shopping centres category. The survey was conducted by the market and media research institute Mediana.



The bakery section of the Chamber of Agricultural and Alimentary Companies with the Slovenian Chamber of Commerce and Industry presented the highest award to **five Mercator baking products** and **fifteen products of the Grosuplje Bakery brand** available only at Mercator. The golden awards are proof that Mercator offers superior products in its bakery and dessert department, too.



As a part of the Ljubljana Quality (LQ) project, taking place every two years in Ljubljana and the Central Slovenian Region, Ljubljana Tourism listed the **Maxim restaurant** as one of the six best-rated restaurants.

The company Mercator IP, d.o.o., received **five golden medals for products of the pastry shop Kranjski kolaček** in the 17th bakery section contest that rates the quality of bread and pastry under the auspices of the Slovenian Chamber of Commerce and Industry.



In August, the **55th International Agriculture and Food Fair** took place in Gornja Radgona. **Mercator IP, d.o.o.**, sent 10 products from meat, meat produce and fish product categories for assessment. All 10 products **won medals**: 5 products won gold, 3 products won silver, and 2 products won a bronze medal.

Based on the Rules and Regulations for rating the quality of milk and dairy products by the dairy interest group (GIZ) of Slovenia, **Mercator UHT-treated milk** scored an excellent quality score, receiving full marks – 20 out of 20.



Mercator is a proud recipient of the **Select Quality from Slovenia** certificate, awarded based on specification Select Quality for Fresh Beef, Veal, and Poultry by the IKC – Institute of Control and Certification of the University of Maribor. This sign of excellence guarantees quality, transparency and traceability of origin, and special marketing conditions.

The Ministry of Labour, Family, Social Affairs and Equal Opportunities offered symbolic support to employers who help maintain the hiring of disabled persons in the open labour market. Within the **Zmoremo (Yes, We Can)** project, special award was presented to five employers who **hired the most persons with disabilities** in 2016, including Mercator.

#### Foreign markets

**The IDEA format** is the recipient of the **Best Buy Award** for the best price to quality ratio in **Serbia for the period 2017/2018**, according to the results of an online survey conducted by the Swiss organization Icertias.

**IDEA Online in Serbia** is the recipient of the **Qudal Award for superior quality**. Thus, the IDEA Online Store reaffirmed its top ranking in the online store category, and the award stands witness to the quality and focus on customer needs.

**The IDEA website in Serbia** is the recipient of a top-five award in the eMarket category as presented by PC Press, proving that the site is neat and functional.



### Mercator's humanitarian activities

With the Slovenian Red Cross organization, we are collecting food for people in need at 35 major stores across Slovenia.

With the Lions Club Ljubljana Viva and Slovenian athletes, we prepared a charity auction for a signed jersey by our ski jumping champion Peter Prevc and other "eagles". The auction took place as a part of this year's campaign **I Run to Help**. The proceeds will be donated to blind and visually impaired children.

Mercator supports our eagles – both the national ski jumping team and their young successors. In the campaign **"Jump to Mercator, support our ski jumpers"**, Ski jumping club Ilirija from Ljubljana won the most votes of our customers and thus won the main prize – a Ford van.



Within the **Stop** project, we garnered 2,334 likes on our Facebook page. We turned the likes into minutes that our volunteer employees spent in late September doing good deeds, helping and socializing with elderly people.

# BUSINESS REPORT

## EFFECT OF ECONOMIC CONDITIONS AND COMPETITION ON MERCATOR GROUP OPERATIONS IN THE PERIOD 1–9, 2017

### Economic conditions in the period 1–9, 2017<sup>1</sup>

According to forecasts by international institutions, economic growth in the euro zone in the period 2017–2019 is anticipated between 1.5% and 1.9%. It will be fuelled by domestic and foreign spending. Private spending is expected to pick up pace as conditions in the labour market continue to improve; moreover, further recovery of investment is expected. Export growth will see a further increase, consistently with the expected growth of the global economy. Optimism regarding further growth and persistence of stimulative ECB policy have resulted in an improvement of lending terms for businesses and households, which in turn boosted the credit flows. Among major trade partners beyond the euro zone, favorable economic growth is expected to continue in Croatia, while in Russia growth of economic activity is expected to recover after last year's stagnation, driven especially by higher prices of raw materials. In this year, the amount of credit extended to businesses has started to increase, and the growth of credit to households has increased, too. Conditions in the banking system continue to improve.

### Slovenia

Economic growth, at 4.4%, will be even steeper in this year than it was in the previous years. In addition to further growth of exports and private spending, we are also expecting an increase in investment. Gross domestic product (GDP) in the first half of the year was up 4.7% year-on-year, and the available activity and confidence indicators point to continuation of positive developments in the second half of the year as well. One major factor for this year's higher economic growth is the export growth which is considerably higher than last year. In addition to the increase in foreign demand, we also ascribe this to improvement in export efficiency.

Employment increased notably in the first half of this year, which we ascribe to further broadly based economic growth and favorable economic outlook. There was a further increase in employment in the first six months of the year in most private sector industries. Hiring activities also saw further growth. Decrease in the number of registered unemployed in the first eight months of the year was even higher than last year, mostly as a result of the shift from the records of unemployed to the records of employed early in the year. Inflow into unemployment continues to gradually decrease as a result of both fewer terminations of employment and due to lower number of first job seekers.

Growth of salaries in the private sector will continue to be derived in the years ahead from the growth of economic activity and from a decrease of unemployment and the related restrictions in the search for well-trained employees in certain segments of the economy. In our estimate, however, the quest for maintenance of competitive position will continue to significantly impact private sector salaries (especially in the tradable sector) so that they are consistent with the development of productivity. In the government sector, salary growth will, considering the recent salary agreements, remain relatively high in this and the next year.

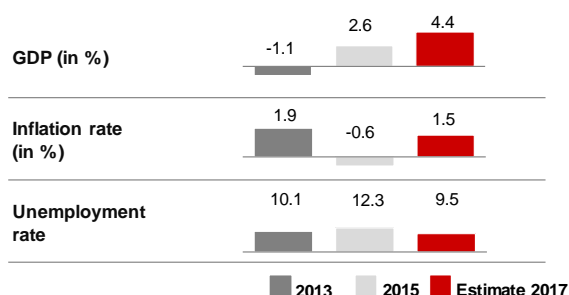
Inflation rate is expected to fluctuate around 2% in the coming years. After a period of low price growth or even deflation, growth in domestic and foreign spending will drive an increase especially in the price of services. Growth of the price of energy (fuels) and non-energy goods will, absent any raw material shocks from abroad, remain moderate.

<sup>1</sup> Economic conditions and competition are commented based on the following data sources: UMAR (Institute of Macroeconomic Analysis and Development of the Republic of Slovenia), ECB (European central bank), FED (Federal Reserve System), EBRD (European Bank for Reconstruction and Development), S&P (Standard&Poor's ratings services), statistical offices or respective countries, IMF (International Monetary Fund), market research company Nielsen, and EC (European Commission).

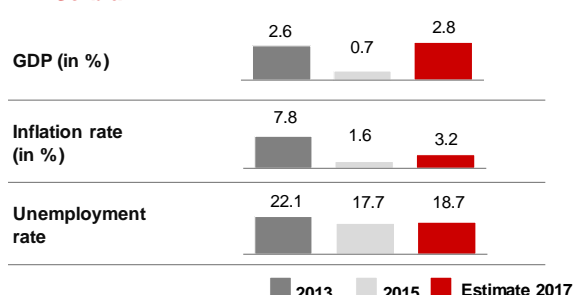
### Key macroeconomic indicators in the market of Mercator's operations

Following is a presentation of changes in three indicators: GDP growth, inflation rate, and unemployment rate for the years 2013 and 2015, and an estimate for 2017. The data pertains to the countries of Mercator Group operations.

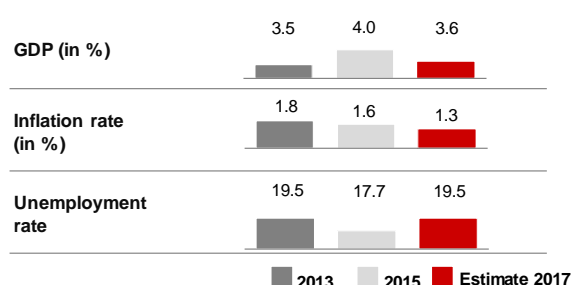
#### Slovenia



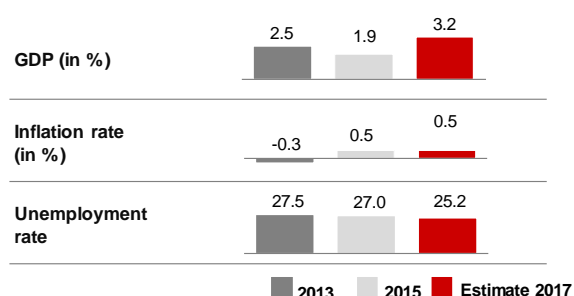
#### Serbia



#### Montenegro



#### Bosnia and Herzegovina



### Credit rating by markets

	Rating <sup>2</sup>	Outlook
Slovenia	A+	stable trend
Serbia	BB-	positive trend
Croatia	BB	stable trend
Bosnia and Herzegovina	B	stable trend
Montenegro	B+	negative trend

### Changes in consumer behaviour and effect of the market situation on consumption

Economic recovery continues in 2017 in all markets of Mercator's operations. In **Slovenia**, recovery of economic activity had a favourable effect on the conditions in the labour market. Improvement in the general economic situation and conditions in the labour market has had a positive effect on the growth of private spending and new investment.

Domestic consumption remains an important motor of economic growth. Household consumption will continue to be fuelled by growth of disposable income as the circumstances in the labour markets are positive, which in turn has a positive effect on consumer confidence. As the conditions in the labour market improve, consumer confidence is improving as well. This has recently been reflected in particular on the purchases of the durables: personal vehicles, home equipment, communication and computer devices, and services related to leisure time.

According to Nielsen data<sup>3</sup> consumer confidence in **Slovenia** in the second quarter of 2017 is considerably higher than in the last quarter of 2016, yet still below the European average. Less than one half of respondents believe the country is in a recession. Just over 66% of respondents believe that the country will not recover from the recession in the next 12 months. Their primary concerns include security of employment, their health and work-life balance.

<sup>2</sup> Rating agency Standard&Poor's

<sup>3</sup> Nielsen: Consumer Confidence Index, Q2 2017, Slovenia

According to economic growth forecasts, improvement of economic conditions is also anticipated in the markets of **Serbia and Montenegro**. Private spending will increase, and the rate of registered unemployment is forecast to decrease, although it will remain at a high level.

Consumer confidence in **Serbia** is slowly but constantly improving;<sup>4</sup> however, it remains below the European average. A high share of respondents (78%) believe the country is in a recession. Approximately 66% of respondents believe that Serbia will not recover from the recession in the next 12 months. Consumers' primary concerns include security of employment, health, and financial standing.

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<sup>4</sup> Nielsen: Consumer Confidence Index, Q2 2017, Serbia

# SALES AND MARKETING

## Sales

International institutions expect similar economic growth for the euro zone as in the previous year. Growth will be based in particular on high confidence level of businesses and consumers, while global trade will continue to be driven by private spending and an increase in investment.

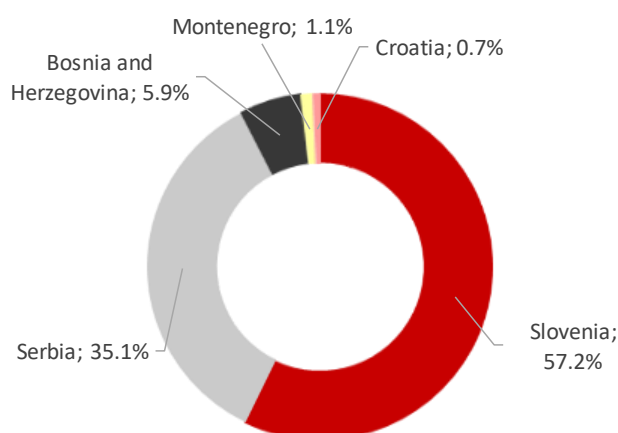
Exports remain the key motor of economic growth in Slovenia, driven by an increase in foreign demand and improvement in the competitive position of Slovenian companies. Positive conditions in the labour market, with growing employment rate and salaries, and further improvement of consumer confidence have contributed to an increase in private spending. Decrease of the number of registered unemployed continues to decrease, with a high hiring rate.

**Revenue from sales of goods in the core activity of retail is higher relative to the comparable period of the prior year in Slovenia and Montenegro, while in the Serbian market the revenue is lower especially on account of closing down the units in compliance with the market regulator's decision.**

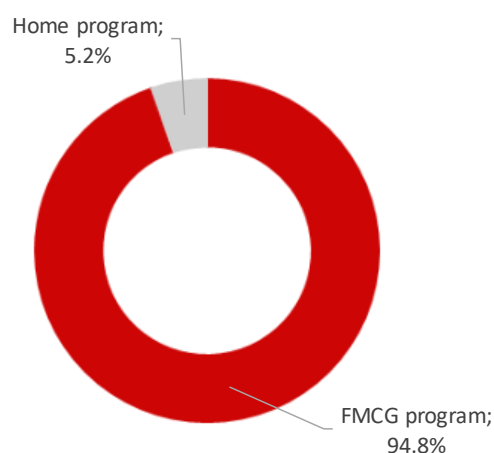
In the period 1–9, 2017, Mercator Group generated revenue of EUR 1,730.1 million, which is 2.7% less than continued operations in comparable period of the previous year. Core activity had a positive effect on the Mercator Group revenue. In the markets of Slovenia and Montenegro, our revenue from sales of goods was higher relative to the same period last year. In the Serbian market, retail revenue was lower, especially due to closing down the units in compliance with the market regulator's decision; however, the current trends are positive. The drop of overall revenue was affected especially by the optimization of wholesale channels.

Mercator Group successfully ended the period 1–9, 2017, with a net profit of EUR 9.9 million, which is EUR 11.6 million more than in 2016.

**Mercator Group revenue by geographical segments in the period 1–9, 2017:**



**Mercator Group revenue from trade operations by programs in the period 1–9, 2017:**





Mercator Group's core activity of fast-moving consumer goods retail generated 94.8% percent of total revenue in the period 1–9, 2017, which is more than in the equivalent period of last year, mostly as a result of the pursuit of strategy of divesting non-core operations. The share of sales revenue from specialized trade program of home products amounted to 5.2%.

## Store formats, customer segments, and category management

### Store Formats

Consumer shopping behaviour has changed considerably in recent years as a result of different impacts from the environment. This tends to increase the complexity of operations. Today's customer is defined by rapidly changing demographic conditions, lifestyle, and technological development. The consumers became even more demanding, more informed, and more aware. They look to get the most for their money and they are less loyal to a single retailer, which further increases the complexity of the business. Pressure on the retailers is mounting to move faster and more to the digital world and the online environment as consumers are willing to spend less and less of their time on shopping. The future of retail lies in further expansion of the number of sales channels and increasingly better integration across them.

Like most of the world's leading retailers, Mercator is seeking to adapt to these actual changes as much as possible by **diversifying its store formats**. They are intended to accommodate a variety of shopping needs, from major planned shopping sessions to minor daily, top-up, or occasional shopping for fast-moving consumer goods.

The year 2017 will also be one of **retail network updates** according to the new concept of trade. We will continue to focus on the consumers as we wish to offer them the best goods and services. We are looking to offer our customers a shopping environment with modern design, in as many locations as possible, with extended and richer offer of fast-moving consumer goods. Refurbished Mercator stores afford customers an even more pleasant shopping environment, while category structures and new services offered are adapted to the most recent trends.

In the period 1–9, 2017, **22 units** were opened or renovated in Slovenia. **29 units** were opened or renovated in Serbia, and **7** in Montenegro. In September, we took over **83 retail units** in the market of Bosnia and Herzegovina from the company Konzum, d.o.o., Sarajevo.

Among the renovated units in Slovenia, the **supermarket Lucija stands out in particular, with fresh design, expanded sales area, and numerous novelties in the offer**, such as:

- **fish department,**
- **new bakery department** that also offers pizza and an expanded offer of self-service small pastry,
- **warm food counter (roisserie),**
- **a large fruit and vegetables department** that also offers a juicer for self-service preparation of fresh orange juice.



In the first half of 2017, intensive **refurbishment of hypermarkets** also took place. The refurbishments are focused on strategic adjustment of the format to new conditions in the market. Thus, the relations and ratios between respective product categories were adjusted; the assortment was optimized with more stress on fresh program.

A lot of stress has been put on refurbishments of existing **supermarkets**, too. These are an upgrade to the neighbourhood stores, offering a broader and especially deeper offer of fast-moving consumer goods. Thus, the offer allows a full shopping session for both daily and weekly consumption, focusing on fresh produce. In the third quarter, a new fruit and vegetables department was introduced in many supermarkets, along with a new category layout for better clarity and easier passing through the store.

In 2017, we continue with refurbishments of smaller **neighbourhood stores** as Mercator carries on the tradition of coming closer to its customer in their local environment. At neighbourhood stores, we are looking to offer our customers a modern shopping environment with a select range of products and produce with continued focus on the home-made, local, and fresh, particular in categories such as fruit and vegetables, meat, and bread, as well as other fast-moving consumer goods.



### Composition of sales units as at September 30, 2017

COUNTRY	SLOVENIA	SERBIA			BOSNIA AND HERZEGOVINA	MONTENEGRO	MERCATOR GROUP		
	Mercator	Mercator	Roda	Idea	Mercator	Roda			
STORE FORMATS	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Gross area	Net sales area
Hypermarkets	22	2	31	3	5	2	65	292,135	194,556
Supermarkets	110	-	3	94	29	15	251	267,130	176,495
Neighbour stores	334	-	-	202	42	92	670	255,261	153,305
Comfort stores	1	-	-	1	-	-	2	6,296	3,776
Mini stores	1	-	-	-	-	-	1	159	83
Cash & Carry / VELPRO	13	-	-	6	-	3	22	63,750	35,366
Restaurants	8	-	-	-	-	-	8	2,070	1,379
Total FMCG program	489	2	34	306	76	112	1,019	886,801	564,960
Technical consumer goods	44	-	-	-	-	-	44	62,115	38,178
Total specialised programs	44	-	-	-	-	-	44	62,115	38,178
Total retail units under management	533	2	34	306	76	112	1,063	948,916	603,138
Franchise stores	199	-	-	-	-	-	199	43,326	28,314
<b>TOTAL</b>	<b>732</b>	<b>2</b>	<b>34</b>	<b>306</b>	<b>76</b>	<b>112</b>	<b>1,262</b>	<b>992,242</b>	<b>631,452</b>

### Customer segment

The needs and desires of our customers are highly diverse. We learn about them by analyzing their shopping behaviour, either through market research or shopping data analysis. Upon this basis, we can adjust the offer and the retail area accordingly, and plan our marketing activities. All major activities are approached with a three-dimensional mindset: offer, store (place), and customer. In 2017, we continue our activities for respective customer segments, with offer tailored to them as much as possible. The goal of some activities is to adjust

certain groups of products, while others are focused on the activities to maintain customer loyalty or on winning their confidence and strengthening their satisfaction.

### **Category management and procurement**

In 2017, we shall continue to actively support local supplier and promote local offer at Mercator stores. As to date, the focus will be on local fresh meat, local fruit and vegetables, and local dairy products. In addition, we shall further promote the offer of local growers and producers. We shall continue to train and educate our employees in the fresh meat departments in order to provide the maximum possible quality and convenience of offer, and especially friendly service. In the bread and pastry department, we shall continue our efforts to provide high-quality service with freshness of products and a varied offer, as well as friendly and professional service of our employees. The offer of fruit and vegetables will be based on promotion of seasonal produce, as well as on the quality of fruit and vegetables, and on introduction of proven market trends.

Key category management activities will remain focused on the pursuit of the following key goals:

- establish quality multi-level offer of branded and private label products of various lines;
- provide competitive prices of products for renowned brands and private labels, and attractive offer in sales promotion activities;
- efficiently manage the store area at a level of particular products or product or categories, and the store as a whole; and
- providing appropriate sales service in our stores (at the point of sales).

## **Marketing**

Our marketing activities are focused on market priorities and the dynamics of changes in the trade industry. In the period 1–9, 2017, we continued to exchange and roll out the best practices across markets.

### **Slovenia**

**We are pursuing the goal of creating value for the shareholder in the key areas.**

#### **We provide well-priced shopping**

We are pursuing the goal of offering our customers the most for their money. Therefore, we offer our customers many products and special prices every day. We provide further benefits to our loyal customers who can double their savings with the Pika card, receive immediate Pika discounts and bonus points. Thursdays are still reserved for retirees who can shop with an extra 10% discount on all products. Our loyal customers can also enjoy the benefit of a 25-percent Pika discount on the selected product, which is easily implemented with the Pika card on the cashier, on a monthly basis we are conducting the activity of double Pika points, allowing our customers to reach a certain benefit threshold sooner. Occasionally, we also offer a 10-percent discount on all products.



Our main tool of communication with the customers is the catalogue which we use to inform our customers on a weekly level about new special offers and quality products at favourable prices, novelties and specificities. Occasionally, we also issue additional catalogues in which we present the offer of non-food seasonal categories.



### With Pika, our customers save more

Advantages of the Pika customer loyalty system are now known to virtually every household in Slovenia. The customers can win and use their loyalty points for the entire offer. They are also offered **immediate Pika discounts for select products**. In addition, the card allows them to **defer the payment or to pay in up to 24 instalments at a zero interest rate**. Pika card affords the customers a number of benefits when shopping in Mercator's sales network and at partner companies. In addition to the Pika discounts on select products from the flyers, and double and triple Pika card bonus points which are available to all Pika card holders, additional discounts were offered in 2017 to all retirees who show their retiree card at the check-out counter.



For the segment of customers keen on shopping online, we also allow the **functionality of online payment** for alimentary products and technical consumer goods by Mercator Pika card. In addition we offer exclusive discounts and surprises for our customers. For the buyers who allowed us to look into their shopping behaviour, we also prepare customized offer. Golden Pika card holders also receive the Golden Letters with golden benefits.

In January, we successfully carried out the "vignette" activity in which customers who purchased the annual highway toll vignette received a coupon for 55 Pika points. Moreover, they were offered to pay in five instalments.

In April, we launched a mobile application **Moj M (My M)** that allows viewing the Pika accounts, transactions, store opening hours, an online grocery store, catalogues, shopping lists, and more.

### KitchenAid

In April 2017, we launched an interactive customer loyalty program KitchenAid in which we offered our customers top-class KitchenAid cookware with a discount of up to 71%. The program ended on July 31. Customers who have purchased any piece of cookware are also eligible for the main award – a KitchenAid kitchen robot.



### Tefal

In August 2017, we launched a new customer loyalty program Tefal. Customers were offered the purchase of top-class storage products and small domestic appliances with a discount of up to 60%. The program will last until November 5. In the week from August 17 to 23, we connected the customer loyalty program to the project My Brands, as we presented 5 additional stickers to customers who purchased My Brand products. The customers found the program very interesting, as evident in product sales.



### School

In the first half of August, we conducted sweepstakes under the slogan **Back to School Shopping** and presented the main prize: a family trip to Gardaland. Broad offer of school products was also presented in a special catalogue. Working with our supplier, we created unique backpacks. In the second half of August, we presented double Pika bonus points for products related to school, and presented gifts to our employees' children starting elementary school. At the end of August, our Mercator office building in Ljubljana held an Open Door Day for employees' children.



## My Brands

In the first half of June 2017, we launched a new project called **My Brands**. This project involves special marking of products of select and renowned brands that are especially exposed in Mercator stores and communication.

Cockta, Zlato polje, Alpsko mleko and Poli were the first brands to enter the project. They are our so-called premium partners with whom we are building long-term cooperation in advertising, sales, and other joint marketing activities. Thus, we are looking to bring both Mercator and renowned brands even closer to our customers, especially the younger generation. In the months ahead, we will include an increasing number and variety of renowned Slovenian brands in the project to show our customers the breadth of Slovenian offer available at Mercator.

The entire project is conceived as a 360° campaign, meaning it involves the entire advertising mix: catalogues, TV ads, social media ads, online ads, magazines, outdoor advertising etc. In the catalogues, the project is manifest through different stories and activities (sweepstakes, extra Tefal stickers upon purchase of My Brand products, related stories regarding school and marathon etc.).

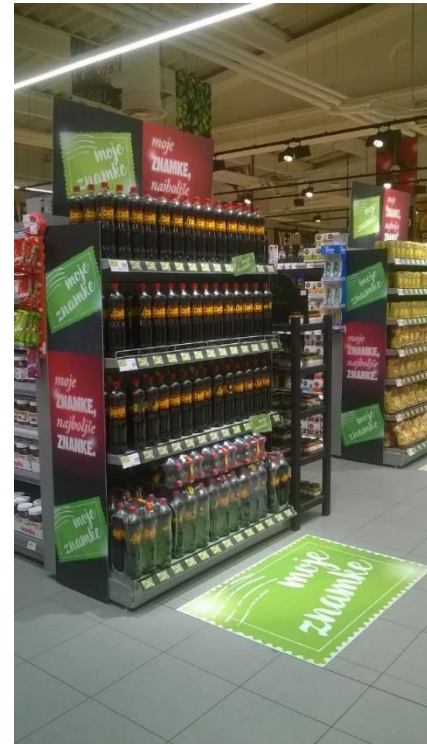
## We Love Local

The basic concept of the **We Love Local 2017** campaign includes monthly themes supported by home cooking with a modern twist. To this end, we enlisted the help of the master chefs **Tejani**. With their video recipes, adjusted to the weekly offer from the We Love Local flyer, they are increasing the interest and recognition in the digital channels. Thus, the campaign pursues the goal of bringing local food and local growers closer to our younger customers. The focus is on products, especially those from our new suppliers.

In the autumn, the focus in terms of contents is on select We Love Local products that we and our suppliers are particularly proud of. Day-in, day-out, we are building a relationship with small local suppliers, supporting and respecting their ideas as we understand the value of individual products, including niche products. We wish to show we are a retailer with an ear for the new, for high quality, and for sustainable development of local economies. Thus, we present in the autumn part of the media campaign under the umbrella slogan **"Good People behind Good Food"**, local growers who, with their know-how, hard work, and a good measure of innovativeness, launched products that are truly worth trying.

The project included our sponsorship of the popular Slovenian TV show **"Slovenski pozdrav"**, and the **Slovenian Polka and Waltz Festival** that also draws large crowds of visitors. As a part of the Magic Day, we hosted our youngest customers at the We Love Local farm. Working with Zavarovalnica Triglav (insurance company), we addressed the fans of Slovenian mountains; and we worked with Slovenian ski jumpers, musicians, and many other famous faces. We also took part in the selection of the best products or growers – Agrobiznis.

A part of the story of this campaign is also focused on the development of strategic partnership with cooperatives and small local growers; our goal is further improvement of our collaboration. We are looking to contribute to this goal by organizing events that allow cooperation between respective suppliers and participation in and support to activities improving recognition of both local growers and Mercator as a retailer offering local goods. One such example is the **We Love Local Academy**, closing with a fair at Mercator Šiška. The project included visits to 9 places across Slovenia, sharing our knowledge and opening the door to many local suppliers. At the fair, we offer the 29 suppliers who applied for the project the option to sell, promote, and connect.





### Mine. The best. Mercator

This spring, Mercator introduced a new communication campaign in Slovenia. It includes a **thorough revision of the strategy and refreshment of the tone of communication**. Mercator is looking to come closer to the new generations of customers, to consolidate the recognition of the communication platform, and to rejuvenate the Mercator brand identity. We are betting on freshness and quality, local origin, a cosmopolitan offer, and the best value for money. In addition, an **increasing number of Mercator stores are thoroughly updated or renovated**, and in the new campaign, especially the TV ad, **the main roles are played by our employees**: young, inquisitive, playful.

Creative solutions have been employed to update the store equipment as they moved to be among customers and employees, while their interactive character made ideal content for digital and social networks where especially the young intensively liked and shared the music, while employees and customers identified their "best neighbours", the employees starring in the ads.



Thus, Mercator used many elements to come closer to the younger, dynamic audience, as we are aware that the somewhat older and senior population has traditionally been the most loyal to Mercator. For the young, Mercator developed not only an energetic spring campaign with appealing ads and music; rather, the **offer and shopping paths** have been adjusted to them as well. Enriched offer of new products, online store, My M mobile application, lively activity in the social networks, and a range of other elements rounds off the convincing and inviting shopping experience at Mercator for the younger generations.

### Fresh category campaign

In the period 1–9, 2017, our umbrella campaign Mercator also included a fresh category campaign with a key emphasis on the offer of quality and fresh produce.

The campaign includes the offer of fresh meat, fruit and vegetables, and the dairy category in which the offer was focused on the products by our Mercator private label. The goal of the campaign was to present all aspects of our quality offer to the customers. Thus, the meat campaign included weekly stories presented in flyers to inform the customers about the advantages of purchasing the Mercator private label products and about the IFS standard. We also presented the story of our own meat products or pre-packed meat and quality control by the National Veterinary Institute, and several stories of our suppliers. We took the story about the quality of meat a step further in July when we became the first and only retailer to receive the **"Select Quality for Fresh Chicken Meat"** certificate. In September, we also received the certificate for **beef and veal**. Thus, Mercator is the only retailer in the market with an IK certificate for certified meat, which stands witness to higher quality, stricter control, and Slovenian origin of the meat.



At the end of May, we also launched a fruit and vegetable campaign in which we worked with the suppliers to inform the customers about the Global GAP certificate and offer of organic produce. Working with the Austrian laboratory Imprint Analytics, we carried out an origin test for the select fruits and vegetables. In this way, we checked whether the origin of the produce by our growers was indeed Slovenian. Tests were carried out for 12 products by different growers.

We also prepared two special reports for meat and for fruit and vegetables, presenting how all stakeholders in a supply chain work together to deliver freshness and quality.

In addition to fresh categories, particular attention was paid to the wine category. Since April, we have been conducting activities contributing to the improvement of the wine drinking culture in Slovenia. In addition to the **Wine of the Month** activity in which renowned wine experts recommend a certain type of wine, we also prepared a special wine guide for our stores to provide further information to our customers.

### Offer of private label products

Mercator private label lines offer a variety of products for all occasions, at all price segments.

In the first quarter, we conducted several activities related to our private labels. We presented an annual supply of **Lumpi diapers** to all children born on January 1, 2017, in Slovenia, which their mothers were very grateful for. This also resulted in Facebook communication in which mothers shared their experience with Lumpi diapers with us and others.

Our care for healthy diet of children was also manifest in organization of **Bio Zone** workshops with **Alenka Košir** at Mercator Šiška. Thus, we continued to communicate our Bio Zone product line. Bio Zone products were also promoted as a part of the "Žogarija" (Ball Game) project that encourages the young to do sports and to choose a healthy diet. This also included a **My Food, Natural is the Best** contest. At the end of June, we launched a refreshment campaign for the Bio Zone brand recall. This year, it was upgraded with interesting recipes based on the Bio Zone products, in cooperation with Alenka Košir, as well as with an interesting prize competition in which customers can win participation in workshops with Alenka Košir.

In February we received **golden medals from the Slovenian Chamber of Commerce and Industry for select pastries and biscuits of our Mercator line**. In March, we prepared an extensive **campaign for Mercator's dairy products** as we launched new product design and emphasized their Slovenian origin. In June, we upgraded our dairy product campaign with communication of labels for top quality awarded to Mercator dairy products at the tests conducted by the Faculty of Biotechnology. To support the communication of the quality of dairy products, we **also included our customers** with an interesting sweepstakes to invite the customers on a dairy tour in which they learned how to recognize the quality of milk and dairy products. The project resulted in a report and a TV ad.

### Slovenian Days at Mercator Šiška

In June, we prepared theme-oriented days at Mercator Šiška titled "**Dnevi Slovenije**" ("**Slovenia Days**") to present our country, its regions, and its delicacies. We prepared a special flyer presenting specific Slovenian regions and their most typical dishes. We also prepared tastings and promotions for our customers, so that hypermarket Mercator Šiška truly came to life in the spirit of the popular and lesser-known flavours of Slovenia.

## Serbia

Many joint marketing activities took place in the Serbian market in the period 1–9, 2017. Following are the most notable ones:

- The **Beer Rituals** campaign – taking place from May 25 to June 30, it included a catalogue presenting our current offer of beer, and how to pour, taste, and rate beer. We also presented the brewing machine to our customers.
- The "**Genije za režije**" campaign – in addition to doing their daily shopping, Idea customers can now pay their monthly bills from the companies SBB, VIP Mobile and Telekom Serbia. To date, the service is possible at 74 Idea stores, at all Roda stores, and at all Mercator hypermarkets across Serbia.
- The **Humanitarian Weekend** campaign – working with the "Bodi human" (Be Humane) Foundation, the company Mercator - S, d.o.o., organized the Humanitarian Weekend campaign at 339 Idea, Roda, and Mercator units. On the weekend of May 20 and 21, one dinar from each checkout was donated to the said campaign. The campaign raised 500,000 Serbian dinars in only two days.



- The campaign **Five Minutes to Get a Job** – the company Mercator - S, d.o.o., started a hiring project in which anyone interested can take part in a 5-minute job interview, which brings them a step closer to getting a job at an Idea, Roda, or Mercator unit anywhere in Serbia.

In the period 1–9, 2017, marketing activities also took place separately, by brands, as presented below.

### IDEA

For the second consecutive year, a workshop took place in January and February at four Belgrade municipalities as a part of the **Choose healthy, choose fresh** campaign. The workshop was intended for children and it focused on the importance of a healthy lifestyle and diet. Participation is upgraded by Idea and the Belgrade Marathon who signed a new three-year exclusive partnership agreement. Thus, Idea was once again a sponsor of the Belgrade Marathon attended by over 20,000 spectators.

For customers across Serbia, we organized a contest **Idea rewards with 1,000 bicycles** in which we gave away the said number of bicycles to the lucky winners.

The campaign **Belgrade, the City of your IDEAs** was launched in June. Eleven ideas were selected based on 500,000 votes, which will contribute to beautification of Belgrade. The first idea already put to action was called The People of Belgrade Read. It included promotion of culture through poetry with young poets reciting at 80 public transit stations or stops.



### RODA

Through the campaign **Where Happiness is 1,000 Times Bigger**, we organized a prize contest in January and presented the last 400 out of a total of 1,000 TV sets to lucky prize winners.

Moreover, we continued our activities of cooperating with the **Serbian Basketball Association** and together pursued the goal of development and promotion of basketball in the entire Serbia. This involved a number of trips in May.



With its Super Card, Roda prepared a customer loyalty program called **The Dreams Offer** in order to make it easier for parents to shop for baby equipment. The customers collect stickers for a 50-percent discount on the select products of the Chicco baby equipment range.



Roda is a proud partner of yet another competitive season of the unique contest **"Izađi mi na teglu"**. In the previous three seasons, the contest visited over 60 cities and attracted around 6,000 participants with 12,000 jars of ajvar made. In the fourth season, around 450 competitive teams with 3,000 participants will take part.

### MERCATOR

In order to offer a true shopping experience, the **Mercator Days** campaign took place for two weeks at the Mercator centre Belgrade and Novi Sad, which included a presentation of the breadth and exclusive selection of the most renowned brands.

**Scan in an instant** – Since Mercator customers appreciate simplicity, modern technology, and speed, we have already implemented the innovative service **"Sken za tren"** (Scan in an instant) at Mercator hypermarket in Belgrade and Novi Sad. The service allows the customers to scan their products and monitor the list and total amount, as well as savings.





## Montenegro

In the market of Montenegro, particular attention was paid to the introduction of new lines of local products through the campaign "**The Flavours of My Town**" launched in mid-March. This is a new campaign involving sale of local Montenegrin products at retail stores, in cooperation with 11 local producers. It is the goal of the campaign to make sure the consumers perceive IDEA brand as a retailer worthy of their consumer's confidence, and a retailer offering quality traditional products. Within the campaign, customers can choose from a range of healthy products prepared based on traditional production recipes. Thus, the products include local prosciutto, baklava, olive oil, wine etc.



As we seek to deliver the best quality, freshness, and a varied assortment, we held the **fruit and vegetables** campaign through 5 themes: citruses, exotic fruits, detox, vitamins, and salad. During the campaign, a giveaway was held under the slogan **Buy Oranges and Travel to Spain** which involved giving away 2 trips to Spain, 3 iPhones 7, and 100 fruit coupons.



In addition to regular pricing activities, we also launched at the end of March the camping **Phenomenal April** which lasted until the start of May and included 3 parts: spring cleaning, merry Easter, and I love grilling. The goal of the campaign was to keep the existing customers and win over new ones.

As of May 1, we launched a new customer loyalty program called **Super Card**. Super Card is a customer loyalty program that includes several partners, all of which rewards customer's shopping.



In April, we opened the **first Idea store in Šavnik**. In the first 2 days, we presented more than 1,000 presents to our customers, offered a 10% discount for every purchase, and gave away every 50th purchase.

In addition to regular pricing activities (regular catalogues, low price, super price, retirees), we carried out during the season a summer version of the campaign focused on **fresh produce**.

On August 1, we launched a new special offer, granting customers a 10-percent discount on their entire shopping session.

Upon the start of the new school year, we carried out the campaign "**Going back to School is Fun**" that included a catalogue for the period from August 21 to September 15. We also organized an event and workshop for schoolchildren.



# EMPLOYEES

In 2017, we continue the processes of restructuring and reorganization, started in 2014. The goal remains to establish a more efficient work processes. We are aware that the employees are at the heart of our operations. They contribute greatly to customer satisfaction and to success of the pursuit of Mercator's business goals.

As of January 1, 2017, new organizational structure came into effect at the company Mercator IP, d.o.o., at both macro and micro level. It allows faster and more efficient changes in organizational and work processes, and improved transparency of entire company operations.

Changes of macro and micro organization also took place at the company Mercator - S, d.o.o., as of February 1, 2017, and again as of June 1, July 1 and August 1, 2017, consistently with the relevant work processes and human resource changes.

As of March 15, 2017, a new Collective Labour Agreement came into effect at the company Poslovni sistem Mercator, d.d., which introduces alignment with the Employment Relationships Act (ZDR-1) and the industry collective labour agreement. There was a change in our macro and micro organizational structure as of August 1, 2017.

As of June 1, 2017, macro organizational structure at the company Mercator - CG, d.o.o., was changed; a month later, such change was also introduced at Mercator - H, d.o.o.

## Number of employees

	Number of employees as at September 30, 2017	Number of employees as at December 31, 2016	Index number of employees September 30, 2017/ December 31, 2016	Number of employees based on hours worked in the period 1–9, 2017
Slovenia	9,867	10,019	98.5	9,074
Serbia	8,229	8,830	93.2	7,953
Montenegro	1,456	1,436	101.4	1,367
Croatia	38	49	77.6	40
Bosnia and Herzegovina	1,205	20	6,025.0	56
<b>TOTAL</b>	<b>20,795</b>	<b>20,354</b>	<b>102.2</b>	<b>18,491</b>

## Hiring, caring for development, motivating, and connecting our employees

In the period at hand, Mercator Group devoted nearly 76,236 hours to training and education that involved 15,165 employees.

In 1–9 2017, in Slovenia, the **Mercator Humanitarian Foundation** provided aid to 81 employees of the companies Poslovni sistem Mercator, d.d., and Mercator IP, d.o.o., who were in need of help. We paid out humanitarian aid in the total amount of EUR 50,543. In Serbia, we provided humanitarian aid to 70 employees, in the total amount of EUR 20,933; in Montenegro, 32 employees received total aid of EUR 7,400; and in Croatia, one employee received aid of EUR 1,008.

### Poslovni sistem Mercator, d.d.

Modelled after the Shop Manager School, the **Deputy Shop Manager School** was launched at the parent company in mid-September. This year, **180 participants** will be enrolled in the training, while other deputy shop managers will attend the school in 2018. The purpose of the school is to boost key competences of the employees working as deputy shop managers. The program involves 5 days of training in which participants will learn about the topics related to motivation, positive attitude, processes, material operations projects, new developments in retail, business performance (or economics), trade legislation and HACCP, environment protection, and computer knowledge related to GOLD.

This year, **teambuilding workshops on Vogel** took place in the spring and autumn. Fifteen workshops held were attended by over **250 participants**.

**Poslovni sistem Mercator, d.d.**, is one of the first Slovenian companies to have introduced **internal coaching** in a systematic way, offering its employees who expressed the willingness to participate the possibility to work as coaches. Today, the group of active internal coaches includes 17 individuals. Internal coaching supports the succession programs in retail and wholesale, and the individuals who express their wish for internal coaching. In September, **internal coaches** exchange good practices and planned their activities as a part of the teambuilding session on Vogel.

In September, we held the second **"Butchery School"** (butcher training program) attended by **6 employees** who transferred to the meat departments from other departments in retail. In the theoretical part of the training, the participants learned about strategy in meat departments, selling skills, mandatory legislation and HACCP for meat departments. Then, they were assigned mentors who helped them apply their newly acquired knowledge in practice.

In September, 33 field sales agents started their sales training as a part of the **Wholesale Field Sales Agent School** (or training program). Working with a third-party service provider, they will visit two training sessions in this year and three more in the next year. They will apply their newly acquired skills in practice as they go, and improve their work in cooperation with the lecturer.

Sixty-two employees from the logistics department were enrolled in the **Logistics Management School**. They first took psychological tests and conducted a career interview. The purpose of the school is to boost competences that are of key importance for work of a logistics manager: feel for work with people, stress management, organization, and responsibility. The school lasts 7 training days and 52 educational hours. In addition to workshops, it will also include two team coaching sessions focused on contents highlighted by the participants. The School will be completed in February 2018.





In September, heads of key employees in administration took part in training for the **4th Development Dialogue**. Discussion on corporate climate, individual talent and individuals' competencies was logically followed up with a **discussion on learning**. At the training, the leaders were offered a broader insight into the field of learning, and instructions for dialogue and development of educational response resulting from the dialogue.

In July, we launched the project **Earn an Award with Your Candidate**. In the project, Mercator employees and agency workers propose candidates for hiring, which is aimed at improving our odds for recruiting scarce (excess-demand) human resources. We have already hired 24 new employees proposed as candidates by our employees. For each person newly hired at our company based on our human resource management procedures, and based on a proposal by a Mercator employee or agency worker, we shall pay out to the employee who proposed the candidate a gross bonus of EUR 100 to the salary, and EUR 100 of e-vouchers on the employee's Pika card, after the newly hired employee successfully completes the trial period.

*Imate znanca, ki si želi delati v trgovini?  
Ima prodajno žilico in rad dela z ljudmi?  
Smo vzbudili vašo pozornost?*

**POTEM PREDLAGAJTE SVOJEGA  
KANDIDATA ZA OBJAVLJENA PROSTA  
DELOVNA MESTA!**

Za vsakega novo zaposlenega, ki ga boste predlagali in ga bomo v skladu s kadrovalnimi postopki zaposlili v našem podjetju, boste prejeli nagrado, in sicer 100 EUR bruto dohodka k plačilu 100 EUR v obliki na vašo Pika kartico.

**PRISLUŽITE SI NAGRADO  
s svojim kandidatom!**

www.mercator.si



Before the start of the new school year, we held an **Open Door Day** for the children of employees from Ljubljana and its surroundings, and offered a relaxed day off at the company where their parents work. Thus, 53 children learned what it meant to "**work at a store**", and we also kept them amused with **singing hours**, by **learning to cook**, by working out in the **dance and movement workshops**, and by **developing their creativity**.



The **Health Promotion Project** and activities for **decrease of absenteeism** included visits by our human resource managers to 89 units (small formats), of which 59 units had absenteeism rates and 30 units had lower absenteeism rates than the average for the field of retail. The purpose of the visits was to present to shop managers the situation regarding absenteeism at their unit, to determine the reasons for high/low absenteeism, and to specify the measures to be introduced by the unit in order to cut its high, or to maintain its low, absenteeism rate. We also prepared Unit Health Cards for **health promoters and large format stores**, detailing the demographic data and information on

absenteeism. They will work with the leaders to prepare an action plan for maintaining health at their units.

#### Mercator IP, d.o.o.

In 2017, the company **Mercator IP, d.o.o.**, worked with the Slovenian Chamber of Commerce and Industry on certification of training programs for all vocations in the food industry, for which there is a scarcity of skilled workers.

At the end of the third quarter, the company Mercator IP, d.o.o., had 413 employees, of which 215, or 52.1%, were employees with a recognized category of disability.

#### Mercator - S, d.o.o.

At the company **Mercator - S, d.o.o.**, a new group of participants starting the **Trading Academy** program. This is a program of assessment and implementation of required knowledge in trade or retail.

The project **Shop Manager Academy** is intended for all employees in retail working as sales assistant / cashier and head of department or section, who were identified as talent for promotion to the position of shop manager deputy shop manager. The program consists of two weeks of specialized training, three days of soft skill training, and six weeks of practical work in retail units under the supervision of a shop manager – mentor. The third generation will start their training in October.

The goal of the program **Academy for Meat Department Sales Assistants** is to re-train in a structured and systematic way the interested employees working in various departments for the job of a butcher which they can then independently perform. This two-month program is held in cooperation with the Technical School for Chemistry and Food Industry and it includes education and training, examination, and grading. The mentors are our best butchers who share their knowledge with their colleagues. We also continue our cooperation with high schools to provide dual education and practical training at our retail units.

**Case study competition (CSC)** is an interactive two-day competition organized by the Alumni Club IEDC Bled, in which teams from different companies show their talent and creativity in a limited period of time, through teamwork in analysis and resolution of a realistic business situation. This year's CSC took place on March 22 and 23, 2017, in Belgrade. The six-member team of young managers performed very well in the search for the best business solution, competing against other participating companies such as Coca Cola Hellenic Serbia, Delhaize, GGE, Hemofarm, and Triglav Osiguranje.



The goal of **coaching network in retail** is to train every newly hired retail employee for work in a certain department. Before starting work at her or his unit, every new employee undergoes 6 days of training for work at a school unit. Pilot projects were carried out in April and September. We continue the concept of **new employee induction process** for newly hired employees in administration, which includes the concept of play to present the company processes, thus cutting short the time new employees need to learn and adapt.

We held English language workshops for 56 employees in retail for easier communication with international customers.

A draft version for the model **Retail Management Program (RMP)** has been developed in order to implement the required skills in the business field of retail and logistics. Target participants include shop managers, heads of retail areas, and regional directors. The program will consist of several modules and a target group of participants will be defined for each module.

The project of disabled persons hiring included creating a new job sales assistant, with working environment adjusted to the special needs of individuals with disability. We hired 20 persons with disabilities by the end of September 2017.

At locations with higher fluctuation in Belgrade and Novi Sad, we carried out **mobile hiring** for retail jobs (shop assistant, cashier). To this end, we set up outdoor mobile offices near our stores and at city outdoor swimming pools, distributed flyers to passers-by, and immediately held interviews with any interested candidates.



#### **Mercator - CG, d.o.o.**

In February in **Mercator - CG, d.o.o.**, the Employee Talent Development Department held training for regional leaders and shop managers at all Idea business units, titled **Human Resources in Retail**. In order to improve the leadership skills, participants in training discussed the contents related to work satisfaction, management, leadership and communication etc. which they will use in their daily work.

During the month of April, we conducted training for 250 employees as we introduced a new Super Card that replaced the Pika card. Training participants included shop managers and selected cashiers who took part in the theoretical and practical training.

In the summer months from June to September, there was considerably more hiring to cover the needs of seasonal work at units in the coastal region, as over 200 seasonal employees did seasonal work at 50 retail units.



We launched a qualitative employee satisfaction survey. Target groups consisting of employees from a variety of retail segments discussed the factors of employee satisfaction and dissatisfaction, incentives for improved satisfaction, training and education, and business unit management. The results are used to devise a strategy for promoting care for the employees and putting in place mechanisms that improve the rate of satisfaction. Based on the analysis of data, the development of the plan for 2018 is in progress.

**Mercator - BH, d.o.o.**

At **Mercator - BH, d.o.o.**, the biggest human resource management challenge in September were the activities related to re-establishment of retail operations on the territory of BiH. Retail operations were re-established in BiH in the period from September 7 to 30, 2017. New employment contracts were signed with all employees, pursuant to the relevant legislation.

**Mercator - Emba, d.d.**

At the end of March, the company **Mercator - Emba, d.d.**, joined twenty-five other alimentary companies in the public tender KOC Food for co-financing of training and education in the next two years. The project is managed by the Chamber of Commerce of the Pomurje Region, working with the Chamber of Agricultural and Alimentary Companies. The project will include setting up an industry-wide competence centre or model, and co-financing for training and education that will contribute to improvement of competencies specified for respective job profiles.



# REAL ESTATE MANAGEMENT AND RETAIL NETWORK DEVELOPMENT

In the period 1–9, 2017, Mercator Group's priority in investment activities, consistently with the investment plan, was refurbishment of retail units and setting up new stores acquired through operating lease. The two exceptions in this case are the Trade Centre Bled for which construction started in September last year and it was opened in March 2017, and the Supermarket Blok 63 in Belgrade, opened in September this year. In the period 1–9, 2017, we opened a total of 16 new FMCG stores and one distribution centre.

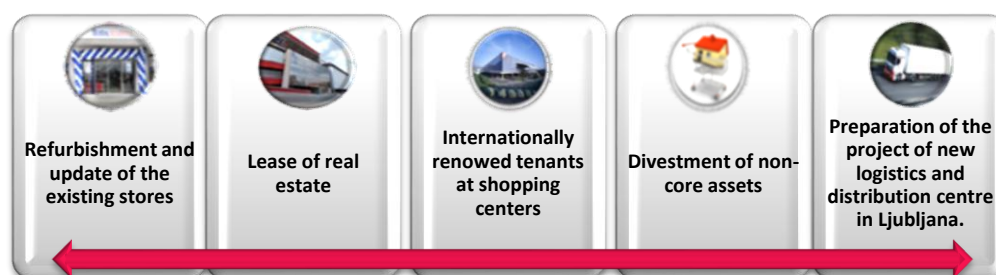
In September 2017, we took over Mercator's former stores (83 units) and one distribution centre from Konzum Sarajevo, which now again operate within Mercator's company in Bosnia and Herzegovina.

We also searched for and evaluated new potential locations to extend Mercator's retail network.

Mercator's greatest acquisitions in the period 1–9, 2017, are the newly constructed Trade Centre Bled with a supermarket and additional premises to be leased out to third parties, and Supermarket Blok 63 in Belgrade. There was no other own real estate development. Remaining investment funds were mostly used for renovation, acquisition of additional equipment, and investment maintenance of the existing retail network, and for investment into new leased stores.

Activities also took place with regard to divestment of non-core or non-operating assets, as well as with the investors willing to build or acquire retail area to suit Mercator's needs and then offer these facilities to Mercator on a lease.

Following are Mercator's key goals in real estate management:



## Investment and Divestment

In the period 1–9, 2017, Mercator Group's investment into property, plant, and equipment (CAPEX) amounted to EUR 36.6 million. Of this amount, 38.8% was used for investments in Slovenia and 61.2% was used for investments in international markets.

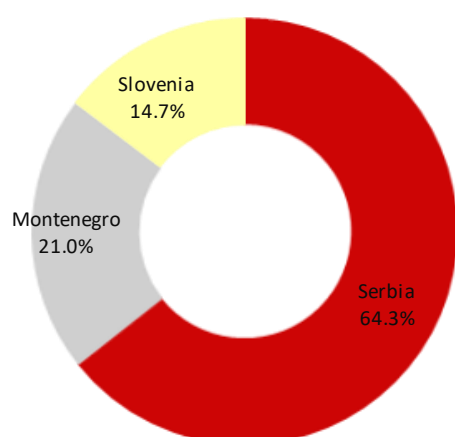
	Capital expenditure in 1–9, 2017 (in EUR 000)	Structure (in %)
Serbia	17,137	46.8%
Slovenia	14,129	38.6%
Montenegro	2,133	5.8%
Bosnia and Herzegovina	1,977	5.4%
Croatia	1,226	3.4%
<b>TOTAL</b>	<b>36,602</b>	<b>100.0%</b>

Investment into refurbishments of existing units accounted for 61.2%; expansion of retail area represented 19.2% of total investment; IT investments accounted for 11.3%; investments into distribution centers accounted for 4.7% and the remaining 3.6% was invested in non-trade activities.

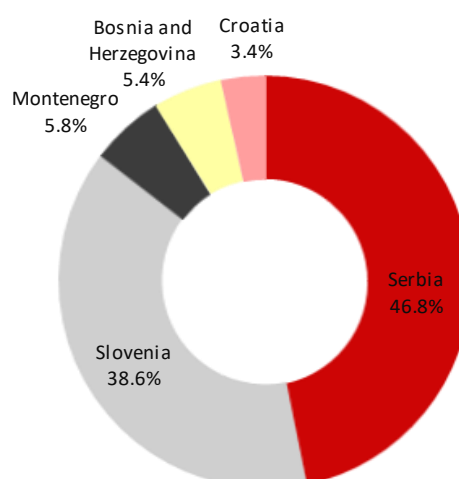
In the period 1–9, 2017, Mercator Group newly acquired 16,726 square meters of gross store area, of which 976 square meters was intended to be leased out to third party service providers. All new gross area, except for Trade Centre Bled and Supermarket Blok 63, Belgrade, was acquired by operating lease.

In the period 1–9, 2017, Mercator Group divested property, plant, and equipment worth EUR 12.2 million, of which EUR 11.4 million pertains to the divestment of property (real estate) and EUR 0.8 million pertains to plant and equipment.

#### Share of newly launched facilities by markets:



#### Share of investments by market:



#### Summary of total gross retail area as at September 30, 2017:

	Gross area in square meters			TOTAL
	Used for own operations	Leased out-Konzum	Leased out-third parties	
Owned retail area	541,323	83,853	318,902	944,078
Leased retail area	407,594	32,173	119,778	559,545
<b>Total retail area</b>	<b>948,917</b>	<b>116,026</b>	<b>438,680</b>	<b>1,503,623</b>
Owned warehouse capacity	130,578	661	17,032	148,271
Leased warehouse capacity	56,030	22,844	17,165	96,039
<b>Total warehouse capacity</b>	<b>186,608</b>	<b>23,505</b>	<b>34,197</b>	<b>244,310</b>
Owned commercial facilities	18,530	0	2,216	20,746
Leased commercial facilities	7,870	0	346	8,216
<b>Total commercial facilities</b>	<b>26,400</b>	<b>0</b>	<b>2,562</b>	<b>28,962</b>
<b>GROSS AREA UNDER MANAGEMENT</b>	<b>1,161,925</b>	<b>139,531</b>	<b>475,439</b>	<b>1,776,895</b>
- of which owned	690,431	84,514	338,150	1,113,095
- of which leased	471,494	55,017	137,289	663,800



## Retail unit, logistics, and distribution center openings by respective markets in the period 1–9, 2017

### SLOVENIA

**Area of new facilities:** 2,451 m<sup>2</sup>

Number of new units: 1

Openings: Trgovski center Bled

**Refurbishments:**

Number of refurbished units: 21

### SERBIA

**Area of new facilities:** 10,759 square metres (of which 9,036 square metres pertains to new retail units, and 1,723 square metres pertains to the logistics and distribution centre)

Number of new units: 8 retail units and 1 logistics and distribution centre (LDC)

Openings: Market Jurija Gagarina, Belgrade; Supermarket Višnjička, Belgrade; Market Mis Irbijeve, Belgrade; Market Petefi Šandora, Subotica; Market Goce Delčeva, Belgrade; Market Dorčol, Belgrade; Supermarket Blok 63, Belgrade; Market Lazarevac; LDC Ugrinovci

**Refurbishments:**

Number of refurbished units: 20

### MONTENEGRO

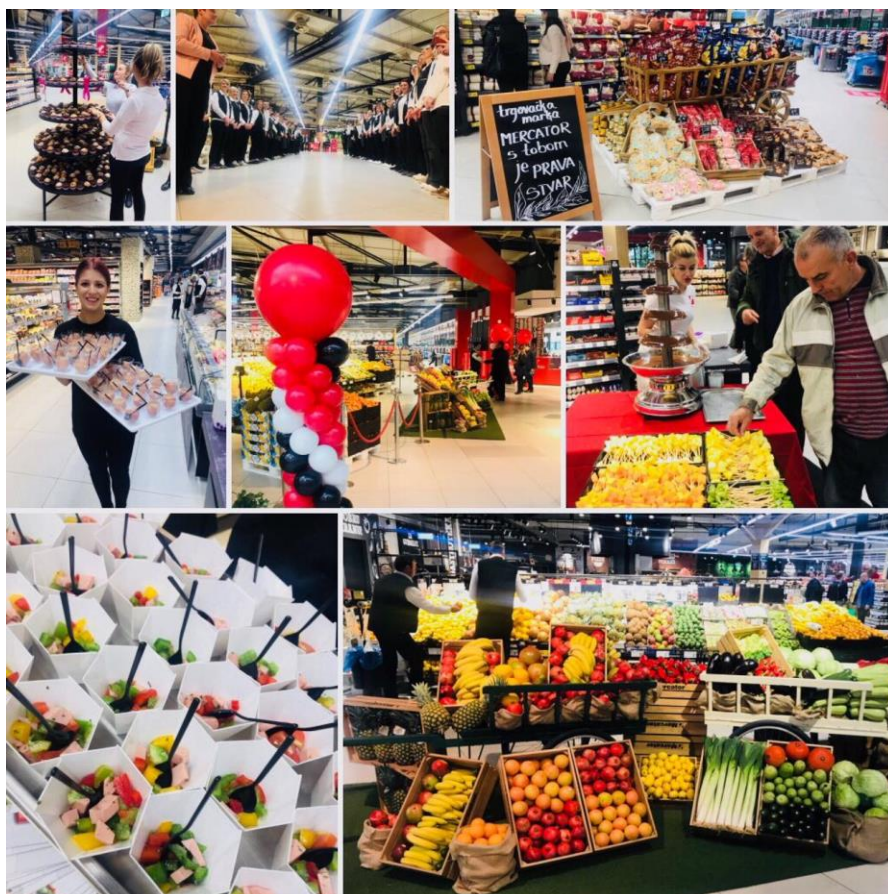
**Area of new facilities:** 3,516 m<sup>2</sup>

Number of new units: 7

Openings: Supermarket Idea Gold, Podgorica; Market Idea Trešnica, Podgorica; Market Idea Rafailovići, Budva; Market Idea Spuž, Podgorica; Market Idea Šavnik; Market Idea Zagorič 3, Podgorica; Market Idea Zagorič 4, Podgorica

### BOSNIA AND HERZEGOVINA

Mercator re-entered the market of Bosnia and Herzegovina. Transfer of possession and establishment of retail operations in 83 stores, of which 76 are active, took place in September 2017.





# RISK MANAGEMENT

Risk management is an important component of management which is conducted at Mercator in compliance with the new version of the quality management system standard ISO 9001:2015, and in compliance with the environmental management system ISO 14001:2015. In May 2016, the SIQ certification institute conducted the ISO 9001 and ISO 14001 audit at Poslovni sistem Mercator, d.d. The auditors praised the risk management system in place.

Risks are divided into 5 areas, or categories:

- strategic risks,
- financial risks,
- operative risks,
- support risks, and
- compliance risks.

In total there are 509 identified risks in the Mercator Group risk register. Key risks for the Mercator Group were selected among them. A key risk for Mercator Group is a risk that meets at least one of the following criteria:

- key risks to be addressed and managed at the Mercator Group level include all risks that exceed 1% of Mercator Group EBITDA in value terms or
- a particular risk shall be deemed a key risk if such risk is the highest within a particular risk group or category that exceeds 1% of Mercator Group EBITDA.

## Strategic risks

Strategic risks pertain to development and implementation of the company strategy, stability of ownership, integration processes, management or governance of the company, compliance with the ethics code, flow of information, company reputation, sustainability of operations etc. These risks pertain to the questions of what will our customers, procurement sources, services, and sales channels be like in the medium run. Strategic risks pertain to occurrence of loss as a result of flawed business decisions, vision, mission, or values.

Key strategic risks include the following risk categories:

- **corporate governance risks** in which the risk of the laying down the right strategy and its execution is the most recognizable;
- **risk of competitiveness and customer satisfaction**, with the risk of a drop in market share as a result of new store openings by the competition being the most recognizable;
- **risks of development of the offer of goods and services**, among which the risk of poor price competitiveness related to pricing management is the most recognizable, as inefficient price management can lead to loss of revenue, profit margin, and poorer consumer perception; and
- **sales channels development risk.**

## Financial risks

Financial risks pertain to financial management. They involve credit, interest rate, currency, liquidity, inflation, price, and other similar risks. The most important among these are the **credit risks** that are managed via a central credit limit system, sending notices for late payments, monthly receivables monitoring, contacting the customers regarding payments etc. Moreover, we are successfully managing our **liquidity risks** as a part of the centralized cash management put in place and based on the management of liquidity reserve through revolving lines, accurate cash flow planning, standardized daily reporting systems, and efficient working capital management.

## Operational risks

Operational risks can threaten the operations in category management and purchasing, production, logistics, retail, and wholesale. Key operational risks include the following two risk categories:

- **risk of category management and procurement**, with regard to which the risks of an increase in tradable commodity prices and seasonal effects are the most pronounced. With regard to the latter, we carefully plan our ordering of seasonal products and follow the weather forecasts, analyze our sales in the preceding year and the challenges of the current year,
- **risks of wholesale operations in which the** risk of loss of franchise partners and third-party customers is the most pronounced.

## Support risks

Key support risks include the following risk categories:

- **human resource risks** which involve in particular the risks of lack of human resources,
- **legal risks**,
- **risks of real property and equipment management** which includes renovations and updates to our units,
- **IT risks**, with regard to which the key risk is the risk of central IT system failure (SAP, GOLD, Login, Hubie, e-mail etc. and
- **loss risks** pertaining to potential earthquakes and fires.

## Compliance risks

Compliance risks pertain to compliance with the requirements of the accounting legislation and standards, tax requirements, occupational health and safety, requirements regarding health compliance and safety of food in production and trade, and risks related to identified environmental aspects.

Key compliance risks include **environmental risks** in which employees are informed on a quarterly basis on the measures for efficient use of energy; in addition, control of the use of energy is already in place on a monthly level for respective units of the company Poslovni sistem Mercator, d.d.

# FINANCIAL MANAGEMENT

## Stable Financial Operations

As at September 30, 2017, Mercator Group net financial debt amounted to EUR 794,193 thousand, which is 1.4% more than as at the end of 2016, and 5.9% less than as at September 30, 2016. In the last year, Mercator Group continued its stable financing activities.

in EUR 000	September 30, 2016	December 31, 2016	September 30, 2017	Indeks September 30, 2017/ December 31, 2016	Indeks September 30, 2017/ September 30, 2016
Non-current financial liabilities	755,986	738,354	754,432	102.2	99.8
Current financial liabilities	142,818	133,241	100,373	75.3	70.3
<b>Financial liabilities</b>	<b>898,804</b>	<b>871,595</b>	<b>854,805</b>	<b>98.1</b>	<b>95.1</b>
Cash and cash equivalents	15,537	26,318	30,232	114.9	194.6
Available-for-sale financial assets	471	462	462	100.0	98.0
Loans and deposits	38,749	39,495	29,918	75.8	77.2
<b>Financial assets</b>	<b>54,757</b>	<b>66,275</b>	<b>60,612</b>	<b>91.5</b>	<b>110.7</b>
<b>Net financial debt</b>	<b>844,047</b>	<b>805,320</b>	<b>794,193</b>	<b>98.6</b>	<b>94.1</b>

## Financing costs

In the period 1–9, 2017, the 6-month EURIBOR averaged at -0.256%. At the end of the period, it was at -0.273%. Compared to the equivalent period of the year before when the 6-month EURIBOR averaged at -0.149%, this rate fell by 0.12 percentage point.

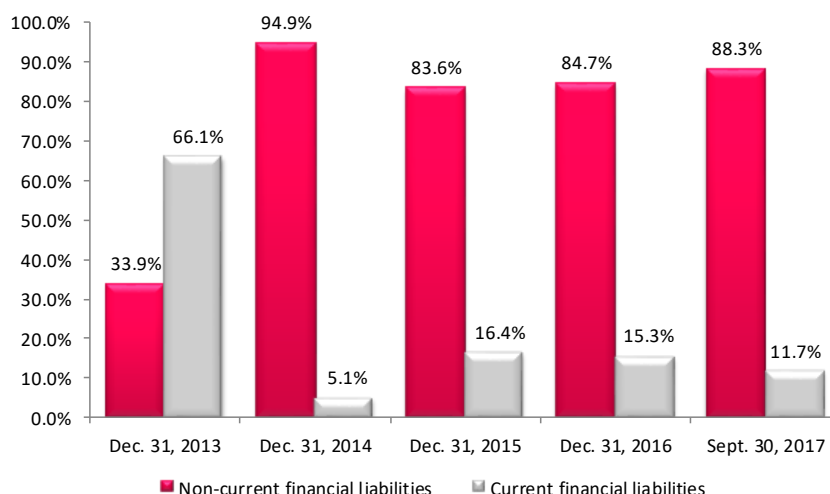
## Security of bank loans

Restructuring of Mercator Group's financial liabilities included securing such liabilities with mortgages on Mercator's own real property, with financial investments into subsidiaries, receivables, inventories, and funds/deposits in bank accounts.

## Debt to equity and financial liability ratio

As at September 30, 2017, Mercator Group attained a debt-to-equity (capital structure) ratio of 1:1.4. The ratio is a quotient between equity and net financial debt.

As at September 30, 2017, the share of Mercator Group's non-current financial assets was at 88.3%, which is consistent with a sustainable maturity profile of financial liabilities.



**Available liquidity lines as at September 30, 2017**

As at September 30, 2017, Mercator Group had access to the following liquidity lines:

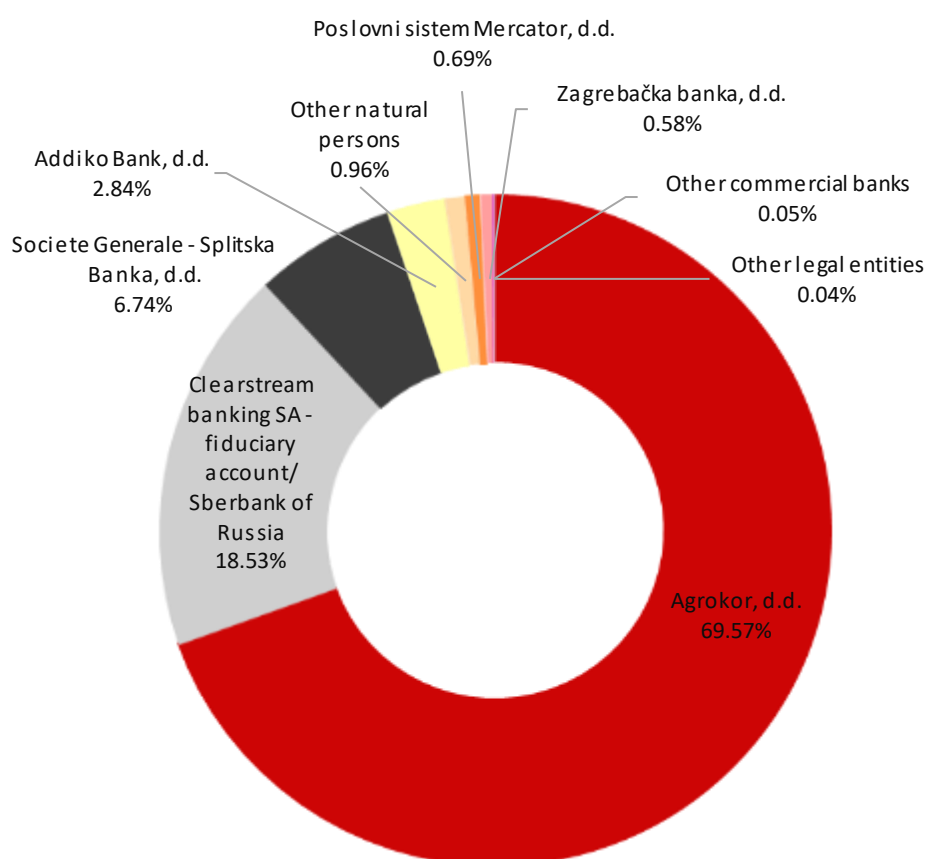
in EUR 000	September 30, 2017
Cash and cash equivalents	30,232
Standby revolving credit lines	10,145
<b>Total</b>	<b>40,377</b>

# MERCATOR SHARE AND INVESTOR RELATIONS

Basic information on the share of the company Poslovni sistem Mercator, d.d., as at September 30, 2017:

Code / Symbol	MELR
Type	Common share
Listing	Prime market of Ljubljana borza, d.d.
Share capital	EUR 254,175,051.39
Number of shares	6,090,943
Number of treasury shares	42,192
Number of shareholders	1.630

Ownership structure of the company Poslovni sistem Mercator, d.d., as at September 30, 2017:





### Major Shareholders

As at September 30, 2017 the following ten largest shareholders held a combined share of 98.67% of the company.

	Country	Number of shares	Share
1 Agrokor, d.d.	Croatia	4,237,376	69.57 %
2 Clearstream banking SA – fiduciary account/ Sberbank of Russia	Netherlands / Russia	1,128,945	18.53 %
3 Societe Generale - Splitska Banka, d.d.	Croatia	410,339	6.74 %
4 Addiko bank, d.d. - fiduciary account	Croatia	173,164	2.84 %
5 Zagrebačka Banka, d.d. - fiduciary account	Croatia	35,393	0.58 %
6 Galić Josip	Croatia	21,525	0.35 %
7 Banque Pictet and CIE SA- fiduciary account	Switzerland	1,107	0.02 %
8 Splitska banka, d.d.- Ucits client account	Croatia	953	0.02 %
9 Horvat Jože	Slovenia	770	0.01 %
10 Fortunat Miloš	Slovenia	575	0.01 %
<b>Total</b>		<b>6,010,147</b>	<b>98.67 %</b>

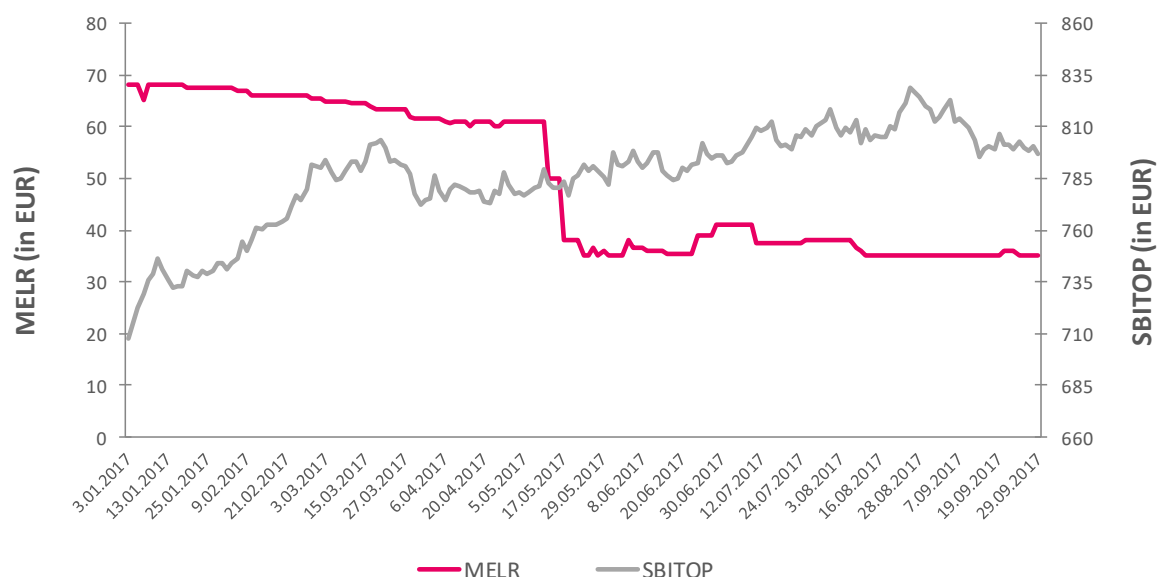
### Shares held by Management and Supervisory Board Members as at September 30, 2017

Management Board and Supervisory Board Members did not own shares of the company Poslovni sistem Mercator, d.d., as at September 30, 2017.

### Foreign shareholders

As at September 30, 2017, the share in the company Poslovni sistem Mercator, d.d., held by foreign investors amounted to **98.70%**, which is 0.20 percentage point more than as at September 30, 2016.

### Movement of closing price per MELR share in the period 1–9, 2017, compared to the movement of the SBITOP index



Key information for the shareholders <sup>5</sup>

	September 30, 2016	September 30, 2017	Indeks September 30, 2017/ September 30, 2016
Number of shares registered in Court Register	6,090,943	6,090,943	100.0
Number of treasury shares	42,192	42,192	100.0
Market capitalization (in EUR)	426,366,010	213,183,005	50.0
Market value of share (in EUR)	70.00	35.00	50.0
Book value per share (in EUR)	105.51	93.71	88.8
Minimum close rate in the period (in EUR)	68.00	35.00	51.5
Maximum close rate in the period (in EUR)	85.00	68.00	80.0
Average close rate in the period (in EUR)	78.65	49.62	63.1
Earnings per share (in EUR) <sup>3,4</sup>	1.31	3.37	212.4

<sup>3</sup> Data vary from published data 1–9, 2016 in 2016, as the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

<sup>4</sup> The indicator is adjusted to the annual level.

## Dividend policy

The company Poslovni sistem Mercator, d.d., does not plan dividend payment for 2017.

## Treasury shares

As at September 30, 2017, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares. In the period 1–9, 2017, the company Poslovni sistem Mercator, d.d., neither acquired nor disposed of treasury shares.

## Investors

The company Poslovni sistem Mercator, d.d., communicates important information and major changes in company operations or performance to all stakeholders regularly and in a timely fashion. Such information is conveyed via the website at [www.mercatorgroup.si](http://www.mercatorgroup.si), and the Ljubljana Stock Exchange electronic information dissemination system SEOnet where Mercator is publishing releases in Slovenian and English.

Shareholders holding shares of the same class are treated equally by Mercator. Furthermore, they are motivated to actively and responsibly assert their rights.

<sup>5</sup> Market capitalization is calculated by multiplying the number of shares entered into the court register as at September 30, with market price per share as at September 30.

Share book value is calculated as the ratio between the value of the equity of the company Poslovni sistem Mercator, d.d., as at September 30, and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.

Earnings per share is calculated as the ratio between net profit of the company Poslovni sistem Mercator, d.d., and weighted average number of ordinary shares in the period at hand, excluding the treasury shares.

# FINANCIAL REPORT

## ACCOUNTING POLICIES

All financial statements of the Mercator Group and the company Poslovni sistem Mercator, d.d., for the period 1–9, 2017, are drawn up in compliance with the International Financial Reporting Standards and they are unaudited.

## CONDENSED CONSOLIDATED FINANCIAL STATEMENTS OF THE MERCATOR GROUP

Poslovni sistem Mercator, d.d. (hereinafter referred to as Mercator, d.d.), is a company headquartered in Slovenia. The address of its registered head office is Ljubljana, Dunajska cesta 107. Condensed consolidated financial statements for the period 1–9, 2017, include the company Poslovni sistem Mercator, d.d., and its subsidiaries, as follows:

- in Slovenia: Mercator - Emba, d.d., Mercator IP, d.o.o., M - Energija, d.o.o.,
- abroad: Mercator - H, d.o.o., Croatia; Mercator - S, d.o.o., Serbia; Mercator - BH, d.o.o., Bosnia and Herzegovina; M - BL, d.o.o., Bosnia and Hercegovina; Mercator - CG, d.o.o., Montenegro; Mercator Macedonia, d.o.o.e.l., Macedonia; Investment Internacional, d.o.o.e.l., Macedonia.

(hereinafter jointly referred to as the "Mercator Group"). Mercator Group's predominant operating activity is retail and wholesale of fast-moving consumer goods.

# Condensed consolidated statement of financial position

EUR thousand	September 30, 2017	December 31, 2016	Index Sept. 30, 2017/ Dec. 31, 2016
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	1,555,912	1,569,905	99.1
Investment property	10,189	9,899	102.9
Intangible assets	22,178	21,963	101.0
Deferred tax assets	19,620	23,529	83.4
Loans and deposits	28,022	31,385	89.3
Available-for-sale financial assets	462	462	100.0
	<b>1,636,384</b>	<b>1,657,143</b>	<b>98.7</b>
<b>Current assets</b>			
Disposal groups	4	-	-
Inventories	212,185	224,328	94.6
Trade and other receivables	223,981	205,707	108.9
Current tax assets	981	1,230	79.8
Loans and deposits	1,896	8,110	23.4
Cash and cash equivalents	30,232	26,318	114.9
	<b>469,279</b>	<b>465,693</b>	<b>100.8</b>
<b>Total assets</b>	<b>2,105,663</b>	<b>2,122,836</b>	<b>99.2</b>
<b>EQUITY</b>			
Share capital	254,175	254,175	100.0
Share premium	207,523	286,772	72.4
Treasury shares	(3,235)	(3,235)	100.0
Revenue reserves	41,685	41,686	100.0
Fair value reserve	104,065	104,541	99.5
Retained earnings	44,746	37,515	119.3
Profit (loss) for the period	9,970	(72,463)	-
Currency translation reserve	(86,943)	(91,720)	94.8
<b>Total equity attributable to equity owners of the company</b>	<b>571,986</b>	<b>557,270</b>	<b>102.6</b>
<b>Non-controlling interests</b>	<b>160</b>	<b>106</b>	<b>151.1</b>
<b>Total equity</b>	<b>572,146</b>	<b>557,376</b>	<b>102.6</b>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Trade and other payables	49,762	45,183	110.1
Borrowings and other financial liabilities	754,432	738,354	102.2
Deferred tax liabilities	31,286	31,356	99.8
Provisions	24,946	26,818	93.0
	<b>860,426</b>	<b>841,711</b>	<b>102.2</b>
<b>Current liabilities</b>			
Trade and other payables	572,256	590,021	97.0
Current tax liabilities	461	488	94.5
Borrowings and other financial liabilities	100,373	133,241	75.3
	<b>673,090</b>	<b>723,750</b>	<b>93.0</b>
<b>Total liabilities</b>	<b>1,533,516</b>	<b>1,565,460</b>	<b>98.0</b>
<b>Total equity and liabilities</b>	<b>2,105,663</b>	<b>2,122,836</b>	<b>99.2</b>

## Condensed consolidated income statement

EUR thousand	1–9, 2017	1–9, 2016 continued*	Index 1–9, 2017/ 1–9, 2016 continued
Revenue	1,730,139	1,777,798	97.3
Cost of goods sold and selling costs	(1,652,309)	(1,714,985)	96.3
Administrative expenses	(56,011)	(55,196)	101.5
Other income	11,674	12,149	96.1
<b>Results from operating activities</b>	<b>33,493</b>	<b>19,766</b>	<b>169.4</b>
Finance income	6,500	4,321	150.4
Finance expenses	(25,397)	(23,244)	109.3
<b>Net finance expenses</b>	<b>(18,897)</b>	<b>(18,922)</b>	<b>99.9</b>
<b>Profit (loss) before tax</b>	<b>14,596</b>	<b>845</b>	<b>1,726.6</b>
Tax expense	(4,655)	(2,545)	182.9
<b>Profit (loss) for the period</b>	<b>9,941</b>	<b>(1,700)</b>	<b>-</b>

Profit (loss) for the period attributable to:

Owners of the parent company	9,970
Non-controlling interests	(29)

\* Operations of Modiana and Intersport are excluded. Revenue from sales of continued operations include also revenue from internal rents, that Mercator Group received from Intersport during the period when it was legal entity, in 2016 amounted to EUR 3.357 thousand.

As the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability with 2017, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.



# Condensed consolidated statement of comprehensive income

EUR thousand	1-9, 2017	1-9, 2016*	Index 1-9, 2017/ 1-9, 2016
<b>Profit (loss) for the period</b>	<b>9,941</b>	<b>3,427</b>	290.1
<b>Other comprehensive income</b>	-	-	-
<b>Items that will not be reclassified subsequently to profit or loss</b>	-	-	-
<b>Items that may be reclassified subsequently to profit or loss</b>	<b>4,830</b>	<b>(1,483)</b>	-
Foreign currency translation differences - foreign operations	4,777	(1,272)	-
Deferred tax	96	112	85.8
Other changes	(43)	(323)	13.2
<b>Other comprehensive income for the period</b>	<b>4,830</b>	<b>(1,483)</b>	-
<b>Total comprehensive income for the period</b>	<b>14,771</b>	<b>1,944</b>	759.7
<b>Total comprehensive income for the period attributable to:</b>			
Owners of the parent company	14,717	1,968	747.7
Non-controlling interests	53	(24)	-

\* Data vary from published data 1-9, 2016 in 2016, as the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1-9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

## Condensed consolidated statement of changes in equity

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings (loss)	Profit (loss) for the year	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interests	Total equity
<b>Balance as at January 1, 2016</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>41,686</b>	<b>108,865</b>	<b>15,365</b>	<b>20,245</b>	<b>(89,668)</b>	<b>634,205</b>	<b>228</b>	<b>634,433</b>
<b>Total comprehensive income for the period</b>											
Profit (loss) for the period*	-	-	-	-	-	-	3,427	-	3,427	(27)	3,400
Other comprehensive income	-	-	-	-	112	(322)	-	(1,276)	(1,486)	3	(1,483)
<b>Total comprehensive income for the period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>112</b>	<b>(322)</b>	<b>3,427</b>	<b>(1,276)</b>	<b>1,941</b>	<b>(24)</b>	<b>1,917</b>
<b>Transactions with owners directly recognized in equity</b>											
Transfer of profit for previous year to retained earnings	-	-	-	-	-	20,245	(20,245)	-	-	-	-
<b>Balance as at September 30, 2016</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>41,686</b>	<b>108,977</b>	<b>35,288</b>	<b>3,427</b>	<b>(90,944)</b>	<b>636,146</b>	<b>204</b>	<b>636,350</b>

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings (loss)	Profit (loss) for the year	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interests	Total equity
<b>Balance as at January 1, 2017</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>41,685</b>	<b>104,541</b>	<b>37,514</b>	<b>(72,463)</b>	<b>(91,720)</b>	<b>557,269</b>	<b>107</b>	<b>557,376</b>
<b>Total comprehensive income for the period</b>											
Profit (loss) for the period	-	-	-	-	-	-	9,970	-	9,970	(29)	9,941
Other comprehensive income	-	-	-	-	(476)	446	-	4,777	4,747	82	4,829
<b>Total comprehensive income for the period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(476)</b>	<b>446</b>	<b>9,970</b>	<b>4,777</b>	<b>14,717</b>	<b>53</b>	<b>14,770</b>
<b>Transactions with owners directly recognized in equity</b>											
Transfer of profit for previous year to retained earnings	-	-	-	-	-	6,786	72,463	-	79,249	-	79,249
Distribution of profit for the year pursuant to the Management Board decision	-	(79,249)	-	-	-	-	-	-	(79,249)	-	(79,249)
<b>Balance as at September 30, 2017</b>	<b>254,175</b>	<b>207,523</b>	<b>(3,235)</b>	<b>41,685</b>	<b>104,065</b>	<b>44,746</b>	<b>9,970</b>	<b>(86,943)</b>	<b>571,986</b>	<b>160</b>	<b>572,146</b>

\* Data vary from published data 1–9, 2016 in 2016, as the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

# Condensed consolidated cash flow statement

EUR thousand	1-9, 2017	1-9, 2016	Index 1-9, 2017/ 1-9, 2016
<b>Cash flows from operating activities</b>			
<b>Gross cash flows from operating activities</b>	<b>84,713</b>	<b>79,622</b>	<b>106.4</b>
Change in inventories	12,143	5,015	242.1
Change in trade and other receivables	(18,025)	(21,465)	84.0
Change in trade and other payables	(20,156)	1,872	-
	<b>58,675</b>	<b>65,044</b>	<b>90.2</b>
Interest paid	(24,330)	(22,191)	109.6
Income tax paid	298	(2,443)	-
<b>Net cash from (used in) operating activities</b>	<b>34,643</b>	<b>40,410</b>	<b>85.7</b>
<b>Cash flows from investing activities</b>			
Acquisition of property, plant and equipment and investment property	(33,817)	(45,610)	74.1
Acquisition of intangible assets	(2,785)	(7,577)	36.8
Loans and bank deposits made	-	(80)	-
Proceeds from sale of property, plant and equipment and investment property	12,193	14,163	86.1
Loans and bank repayments received	9,577	-	-
Proceeds from sale of available-for-sale financial assets	-	2,500	-
Dividend received	-	281	-
Interest received	706	1,151	61.3
	-	-	-
<b>Net cash used in investing activities</b>	<b>(14,126)</b>	<b>(35,172)</b>	<b>40.2</b>
<b>Cash flows from financing activities</b>			
Proceeds (repayment) in borrowings	(16,790)	(8,628)	194.6
<b>Net cash from (used in) financing activities</b>	<b>(16,790)</b>	<b>(8,628)</b>	<b>194.6</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>3,727</b>	<b>(3,390)</b>	<b>-</b>
Cash and cash equivalents at the beginning of the year	26,318	18,998	138.5
Effect of exchange rate fluctuations on cash and cash equivalents held	187	(71)	-
	-	-	-
<b>Cash and cash equivalents as at the end of the period</b>	<b>30,232</b>	<b>15,537</b>	<b>194.6</b>

# Notes to Mercator Group condensed consolidated financial statements<sup>6</sup>

## Notes to condensed consolidated income statement

### Revenue

In the period 1–9, 2017, Mercator Group generated EUR 1,730.1 million of revenue, which is 2.7% decrease compared with the same period of the previous year. Core activity had a positive effect on the Mercator Group revenue. In the markets of Slovenia and Montenegro, our revenue from sales of goods was higher relative to the same period last year. In the Serbian market, retail revenue was lower, especially due to closing down the units in compliance with the market regulator's decision; however, the current trends are positive. The drop of overall revenue across markets was affected especially by optimization of wholesale channels.

### Cost of goods sold and selling costs

Mercator Group cost of goods sold and selling costs which include the cost of goods sold, production costs, selling and other expenses, amounted to EUR 1,652,309 thousand in the period 1–9, 2017, which is a 3.7% decrease compared with the same period of the previous year.

### Administrative expenses

Mercator Group's administrative expenses in the period 1–9, 2017, amounted to EUR 56,011 thousand, which is 1.5% more compared with the equivalent period of the previous year.

Total expenses by nature amounted to EUR 442,626 thousand in the period 1–9, 2017, which is on a par with the figure for the equivalent period of last year.

### Result from operating activities

In the period 1–9, 2017, Mercator Group's result from operating activities reached EUR 33,493 thousand, which is 69.4% more compared with the equivalent period of the previous year.

### Net finance expenses

Net finance expenses in the period 1–9 2017, amounted to EUR 18,897 thousand, while they amounted to EUR 18,922 thousand in the previous year.

### Profit before income tax

In the period 1–9, 2017, Mercator Group's profit before income tax amounted to EUR 14,596 thousand.

### Profit for the financial period

Mercator Group net profit for the period 1–9, 2017, amounts to EUR 9,941 thousand, which is EUR 11,641 thousand more compared with the equivalent period of the previous year.

### EBITDA

Mercator Group EBITDA in the period 1–9, 2017, amounted to EUR 89,208 thousand, which is 14.6% more than in the same period of the previous year.

### EBITDAR

EBITDAR amounts to EUR 142,855 thousand for the period 1–9, 2017, which is 7.6% more than in the same period of the previous year.

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<sup>6</sup> Notes relate to continued operations.

## Notes to condensed consolidated statement of financial position

### Assets

Mercator Group assets as at September 30, 2017, amounted to EUR 2,105,663 thousand, which is EUR 17,173 thousand less than at the end of 2016.

As at September 30, 2017, the value of Mercator Group's non-current assets amounted to EUR 1,636,384 thousand, which is EUR 20,759 thousand less than as at December 31, 2016. Fixed assets represent the largest share of non-current assets at 97.1% (EUR 1,588,279 thousand), which is EUR 13,488 thousand less than as at the end of 2016.

As at September 30, 2017, the value of Mercator Group's current assets amounted to EUR 469,279 thousand, which is EUR 3,586 thousand more than as at the end of 2016. Trade and other receivables represent the largest portion of total current assets (47.7%), followed by inventories (45.2%).

### Equity and liabilities

As at September 30, 2017, Mercator Group total equity amounted to EUR 572,146 thousand, which is EUR 14,770 thousand more than as at the end of 2016. The change pertains to net profit in the amount of EUR 9,941 thousand, and other comprehensive income amounting to EUR 4,830 thousand.

As at September 30, 2017, total financial liabilities amounted to EUR 854,805 thousand, which is EUR 16,790 thousand less than as at the end of 2016. Net financial debt of the Mercator Group, calculated as the difference between Mercator Group financial liabilities and financial assets, amounted to EUR 794,193 thousand as at September 30, 2017 (December 31, 2016: EUR 805,320 thousand). The share of long-term financial liabilities as at September 30, 2017, was at 88.3% (84.7% as at December 31, 2016).

As at September 30, 2017, provisions amounted to EUR 24,946 thousand. Compared to the end of 2016, provisions have decreased by EUR 1,872 thousand.

Trade and other payables as at September 30, 2017, amounted to EUR 622,018 thousand, which is EUR 13,186 thousand less than at the end of 2016, especially on account of current trade and other payables.

As at September 30, 2017, coverage of non-current assets with non-current liabilities at the Mercator Group was at 87.5%, which is by 3.1 percentage point more than as at the end of 2016.



# CONDENSED FINANCIAL STATEMENTS OF THE COMPANY POSLOVNI SISTEM MERCATOR, D.D.

Poslovni sistem Mercator, d.d., is a company headquartered in Slovenia. The address of its registered head office is Ljubljana, Dunajska cesta 107. The company Poslovni sistem Mercator, d.d., is the controlling company of a Group of associated companies headquartered in Slovenia, Serbia, Croatia, Bosnia and Herzegovina, Montenegro, and Macedonia.

The company has a double role: it is predominantly engaged in retail and wholesale of fast-moving consumer goods; however, it also performs various group-related corporate tasks for the companies included in the Mercator Group. Hence, employing the financial statements of the company Poslovni sistem Mercator, d.d., for economic analysis of Mercator Group's operation is inappropriate. For such analysis, it is more sensible to apply above all the consolidated financial statements that present an account of the performance of the Mercator Group as a uniform business entity.

# Condensed statement of financial position

EUR thousand	September 30, 2017	December 31, 2016	Index Sep. 30, 2017/ Dec. 31, 2016
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	850,679	867,726	98.0
Investment property	3,128	3,237	96.6
Intangible assets	13,654	13,455	101.5
Deferred tax assets	17,112	21,218	80.6
Trade and other receivables	426	25,664	1.7
Loans and deposits	126,434	125,202	101.0
Equity investments in Group companies	306,377	270,758	113.2
Available-for-sale financial assets	296	296	100.0
	<b>1,318,107</b>	<b>1,327,554</b>	<b>99.3</b>
<b>Current assets</b>			
Inventories	110,264	121,783	90.5
Trade and other receivables	81,652	78,786	103.6
Current tax assets	-	300	-
Loans and deposits	969	999	97.0
Cash and cash equivalents	20,523	13,344	153.8
	<b>213,408</b>	<b>215,212</b>	<b>99.2</b>
<b>Total assets</b>	<b>1,531,515</b>	<b>1,542,766</b>	<b>99.3</b>
<b>EQUITY</b>			
Share capital	254,175	254,175	100.0
Share premium	207,523	286,772	72.4
Treasury shares	(3,235)	(3,235)	100.0
Revenue reserves	16,624	16,624	100.0
Fair value reserve	75,721	76,196	99.4
Retained earnings	735	(1,802)	-
Profit (loss) for the period	15,287	(77,447)	-
<b>Total equity</b>	<b>566,830</b>	<b>551,283</b>	<b>102.8</b>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Trade and other payables	30,191	27,198	111.0
Borrowings and other financial liabilities	535,174	508,047	105.3
Deferred tax liabilities	25,034	25,229	99.2
Provisions	21,351	23,041	92.7
	<b>611,750</b>	<b>583,514</b>	<b>104.8</b>
<b>Current liabilities</b>			
Trade and other payables	285,520	315,082	90.6
Current tax liabilities	-	-	-
Borrowings and other financial liabilities	67,415	92,886	72.6
	<b>352,935</b>	<b>407,968</b>	<b>86.5</b>
<b>Total liabilities</b>	<b>964,685</b>	<b>991,483</b>	<b>97.3</b>
<b>Total equity and liabilities</b>	<b>1,531,515</b>	<b>1,542,766</b>	<b>99.3</b>

## Condensed income statement

EUR thousand	1–9, 2017	1–9, 2016 continued*	Index 1–9, 2017/ 1–9, 2016 continued
Revenue	962,056	987,348	97.4
Cost of goods sold and selling costs	(911,847)	(950,633)	95.9
Administrative expenses	(27,393)	(26,833)	102.1
Other income	7,448	6,079	122.5
<b>Result from operating activities</b>	<b>30,264</b>	<b>15,961</b>	<b>189.6</b>
Finance income	4,540	6,820	66.6
Finance expenses	(15,303)	(14,856)	103.0
<b>Net finance expenses</b>	<b>(10,763)</b>	<b>(8,036)</b>	<b>133.9</b>
<b>Profit (loss) before tax</b>	<b>19,501</b>	<b>7,925</b>	<b>246.1</b>
Tax expense	(4,213)	(1,994)	211.3
<b>Profit (loss) for the period</b>	<b>15,287</b>	<b>5,931</b>	<b>257.7</b>

\* Operations of Modiana are excluded. As the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

## Condensed statement of comprehensive income

EUR thousand	1–9, 2017	1–9, 2016 adjusted	Index 1–9, 2017/ 1–9, 2016 adjusted
<b>Profit (loss) for the period</b>	<b>15,287</b>	<b>7,198</b>	<b>212.4</b>
<b>Other comprehensive income</b>			
<b>Items that will not be reclassified subsequently to profit or loss</b>	<b>259</b>	<b>-</b>	<b>-</b>
Deferred taxes	302	-	-
Other changes	(42)	-	-
<b>Items that may be reclassified subsequently to profit or loss</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Other comprehensive income for the period</b>	<b>259</b>	<b>-</b>	<b>-</b>
<b>Total comprehensive income for the period</b>	<b>15,547</b>	<b>7,198</b>	<b>216.0</b>

## Condensed statement of changes in equity

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Net profit (loss) for the year	Total equity
<b>Balance as at January 1, 2016</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>16,624</b>	<b>79,869</b>	<b>619</b>	<b>(3,800)</b>	<b>631,024</b>
<b>Total comprehensive income for the period</b>								-
Profit (loss) for the period*	-	-	-	-	-	-	7,198	7,198
Other comprehensive income	-	-	-	-	(1,252)	1,252	-	-
<b>Total comprehensive income for the period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(1,252)</b>	<b>1,252</b>	<b>7,198</b>	<b>7,198</b>
<b>Transactions with owners directly recognized in equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Transfer of profit for previous year to retained earnings	-	-	-	-	-	(3,800)	3,800	-
<b>Balance as at September 30, 2016</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>16,624</b>	<b>78,617</b>	<b>(1,929)</b>	<b>7,198</b>	<b>638,221</b>

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Net profit (loss) for the year	Total equity
<b>Balance as at January 1, 2017</b>	<b>254,175</b>	<b>286,772</b>	<b>(3,235)</b>	<b>16,624</b>	<b>76,196</b>	<b>(1,802)</b>	<b>(77,447)</b>	<b>551,283</b>
<b>Total comprehensive income for the period</b>								
Profit (loss) for the period	-	-	-	-	-	-	15,288	15,288
Other comprehensive income	-	-	-	-	(475)	735	-	259
<b>Total comprehensive income for the period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(475)</b>	<b>735</b>	<b>15,288</b>	<b>15,547</b>
<b>Transactions with owners directly recognized in equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Transfer of profit for previous year to retained earnings	-	-	-	-	-	1,802	77,447	79,249
Distribution of profit for the year pursuant to the Shareholders Assembly decision	-	(79,249)	-	-	-	-	-	(79,249)
<b>Balance as at September 30, 2017</b>	<b>254,175</b>	<b>207,523</b>	<b>(3,235)</b>	<b>16,624</b>	<b>75,721</b>	<b>735</b>	<b>15,288</b>	<b>566,830</b>

\* Data vary from published data 1–9, 2016 in 2016, as the monetization project at the company Poslovni sistem Mercator, d.d., was stopped, assets available for disposal were re-classified at the end of 2016 back to non-current assets, and we resumed their depreciation and amortization. Therefore, business results for the period 1–9, 2016, are, for comparability, adjusted for the extra depreciation pertaining to the assets reclassified back to non-current assets as at the end of 2016.

# Condensed cash flow statement

EUR thousand	1-9, 2017	1-9, 2016	Index 1-9, 2017/ 1-9, 2016
<b>Cash flows from operating activities</b>			
<b>Gross cash flows from operating activities</b>	<b>50,506</b>	<b>41,718</b>	<b>121.1</b>
Change in inventories	11,518	(783)	-
Change in trade and other receivables	(2,566)	(11,743)	21.9
Change in trade and other payables	(27,499)	3,685	-
	<b>31,959</b>	<b>32,877</b>	<b>97.2</b>
Net foreign exchange gains from financing activities	46	16	287.5
Interest paid	(14,223)	(13,520)	105.2
Income tax paid	-	(327)	-
<b>Net cash from (used in) operating activities</b>	<b>17,782</b>	<b>19,046</b>	<b>93.4</b>
<b>Cash flows from investing activities</b>			
Acquisition of subsidiaries and business operations, net of cash acquitted	(35,620)	(2,000)	1,781.0
Acquisition of property, plant and equipment and investment property	(11,282)	(21,675)	52.1
Acquisition of intangible assets	(1,946)	(5,289)	36.8
Loans and bank deposits made/received	24,035	(7,274)	-
Proceeds from sale of subsidiaries, net of cash disposed of	-	2,500	-
Proceeds from sale of property, plant and equipment and investment property	8,347	7,822	106.7
Proceeds from sale of available-for-sale financial assets	-	149	-
Interest received	4,205	4,156	101.2
Dividend received	-	2,282	-
<b>Net cash used in investing activities</b>	<b>(12,261)</b>	<b>(19,329)</b>	<b>63.4</b>
<b>Cash flows from financing activities</b>			
Proceeds (repayment) in borrowings	1,657	(4,333)	-
<b>Net cash from (used in) financing activities</b>	<b>1,657</b>	<b>(4,333)</b>	<b>-</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>7,178</b>	<b>(4,616)</b>	<b>-</b>
Cash and cash equivalents at the beginning of the year	13,344	10,046	132.8
<b>Cash and cash equivalents as at the end of the period</b>	<b>20,523</b>	<b>5,430</b>	<b>378.0</b>



# Notes to condensed financial statements of the company Poslovni sistem Mercator, d.d.<sup>7</sup>

## Notes to condensed income statement

### Revenue

In the period 1–9, 2017, the company Poslovni sistem Mercator, d.d., generated EUR 962,056 thousand of revenue, which is 2.6% less relative to the period 1–9, 2016. Core activity had a positive effect on the company Poslovni sistem Mercator, d.d. Revenue from sales of goods was higher relative to the same period last year. The drop of overall revenue was affected especially by optimization of wholesale channels.

### Cost of goods sold and selling costs

Costs of sales of the company Poslovni sistem Mercator, d.d., which include the cost of goods sold, selling costs, and other expenses, amounted to EUR 911,847 thousand in the period 1–9, 2017, which is 4.1% decrease on the same period of last year.

### Administrative expenses

The company's administrative expenses in the period 1–9, 2017, amounted to EUR 27,393 thousand, which is 2.1% more than in the equivalent period last year.

Total expenses by nature amounted to EUR 241,851 thousand in the period 1–9, 2017, which is 2.4% less than in the equivalent period of last year.

### Results from operating activities

In the period 1–9, 2017, results from operating activities of the company Poslovni sistem Mercator, d.d., reached EUR 30,264 thousand, which is 89.6% more than in the same period of last year.

### Net finance expenses

Net finance expenses in the period 1–9, 2017, amounted to EUR 10,763 thousand, while they amounted to EUR 8,036 thousand in the previous year.

### Profit before income tax

The company's profit before income tax for the period 1–9, 2017, amounted to EUR 19,501 thousand, which is EUR 11,576 thousand more than in the same period of 2016.

### Profit for the financial period

The company's net profit for the period 1–9, 2017, amounted to EUR 15,287 thousand, which is 9,356 thousand more than in the equivalent period of last year.

### EBITDA

EBITDA of the company Poslovni sistem Mercator, d.d., in the period 1–9, 2017, amounted to EUR 54,697 thousand which is 25.8% more than in the comparable period of last year.

### EBITDAR

EBITDAR of the company Poslovni sistem Mercator, d.d., in the period 1–9, 2017, amounted to EUR 61,639 thousand which is 21.6% more than in the comparable period of last year.

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<sup>7</sup> Notes relate to continued operations.

## Notes to condensed statement of financial position

### Assets

Assets of the company Poslovni sistem Mercator, d.d., as at September 30, 2017, amounted to EUR 1,531,515 thousand, which is EUR 11,251 thousand less than at the end of 2016.

As at September 30, 2017, the value of the company's non-current assets amounted to EUR 1,318,107 thousand, which is EUR 9,447 thousand less than as at December 31, 2016. Property, plant, and equipment represent the largest share of non-current assets at 65.8% (EUR 867,461 thousand), which is EUR 16,957 thousand less than at the end of 2016.

As at September 30, 2017, the value of company current assets amounted to EUR 213,408 thousand, which is EUR 1,804 thousand less than at the end of 2016. The decrease pertains largely to inventories, and cash and cash equivalents. Inventories account for the largest share of current assets with 51.7%, while trade and other receivables account for 38.3%.

### Equity and liabilities

As at September 30, 2017, total equity of the company Poslovni sistem Mercator, d.d., amounted to EUR 566,830 thousand, which is EUR 15,547 thousand, or 2.8%, more than as at the end of 2016. The increase is primarily a result of net profit in the period 1–9, 2017.

As at September 30, 2017, total financial liabilities amounted to EUR 602,589 thousand, which is EUR 1,656 thousand more than as at the end of 2016.

As at September 30, 2017, provisions amounted to EUR 21,351 thousand. Compared to the end of 2016, provisions decreased by EUR 1,690 thousand.

Trade and other payables as at September 30, 2017, amounted to EUR 315,711 thousand, which is EUR 26,569 thousand less than at the end of 2016, especially on account of current trade and other payables.

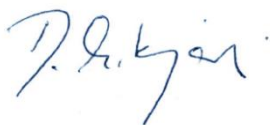
## MANAGEMENT RESPONSIBILITY STATEMENT

The Management Board of the company Poslovni sistem Mercator, d.d., hereby confirms that the summary of the financial report of the company Poslovni sistem Mercator, d.d., and the Mercator Group for the period ended on September 30, 2017, to their best knowledge, is compiled in compliance with the International Financial Reporting Standards and that it presents a true and fair account of assets and liabilities, financial position, and the net income of the company Poslovni sistem Mercator, d.d., and other companies included in the consolidated statements. The Management Board also declares that the transactions between associated entities within the Mercator Group were conducted based on the signed sale and purchase agreements, according to arm's length principle.

Ljubljana, October 25, 2017



Tomislav Čizmić  
President of the Management Board



Draga Cukjati  
Member of the Management Board



Igor Mamuza  
Member of the Management Board



Gregor Planteu  
Extraordinary Member of the Management Board