



**Mercator**



**Annual report**

**2009**



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# Introduction



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## REPORT BY THE MANAGEMENT BOARD PRESIDENT

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We are looking back on an extremely exacting business year that presented us with numerous challenges. Economic conditions in all markets of our operations were harsher than expected. In the retail industry of the whole Southeastern Europe region, that was mostly reflected in consumer behavior. Customers have become more rational, and thus adjusted their purchase decisions in that direction. Consumer confidence indicator hit the lowest level of the last 20 years – not only in Slovenia, but also throughout the developed world. All of that had its impact on the range and structure of consumption, and consequently on sales revenues. The crisis also upset our financial management, as well as introduced new financial risks in the Southeastern Europe, namely the region of our operation and the region in which we remain the largest retailer of alimentary products. On one hand, these involve credit risks, which have increased as a result of growing payment indiscipline and shallower liquidity in the economy, and on the other, additional currency risks have appeared, to which we haven't been exposed in the past. Macroeconomic and political conditions in most West Balkan countries are challenging, what makes the general business conditions very burdensome and affects the operations of Mercator Group.

### **Timely "anti-crisis" measures**

In Mercator Group, as early as in mid-2008, we started with seriously preparing our response to the changes in economic conditions brought about by the global financial and economic crisis by devising two sets of measures: in the first set, we prepared measures for adjusting our offer for the consumers according to the new and changed circumstances; in the second set, we launched the measures for business rationalization. In year 2009 we added another set of measures aimed at increasing the business flexibility, in which framework we commenced and realized the reorganization of the whole Mercator Group, with the goal of increasing the focus and efficiency of our operations, enabling improved responsiveness to local customer demands and adjusting our operations to the growing complexity of international operations.

All these measures contributed to a stable business in year 2009. Net sales revenues at constant exchange rates have increased by 0.6 percent, and so have cash flows from operating activities before rental expense remained stable. Profit for the financial period reached somewhat over EUR 21 million and is approximately half the figure from the year before. On one hand, that is a consequence of the harsh economic conditions, on the other, it is also the consequence of the smaller scope of extraordinary business events, which influenced our business performance in year 2008. With the exclusion of extraordinary items, the income before taxes in year 2009 is only 20.5 percent lower than in 2008, which we estimate as relatively successful, taking into account the business circumstances.

In terms of business performance, it is to be stressed that our business results, bearing in mind the faced conditions, were successful on our two largest markets, namely Slovenia and Serbia, despite the substantial depreciation of the Serbian Dinar, which significantly affected the revenues of the Group. More troublesome were our operations on the markets of Croatia and Bosnia and Herzegovina. What contributed to the fall of revenues realized on the Croatian market, were the difficult economic conditions, as well as customers' response to the tightened relations between the two countries. This was impossible to compensate for in whole with the undertaken rationalization measures, thus it was reflected in the weakened business performance on that market. As a consequence of the hard living conditions on the market of Bosnia and Herzegovina, the pressure for lowering our margins was so high that,

despite the achieved revenue growth with our rationalisation measures, it was just as well impossible to be compensated for in whole, which was reflected in our business performance.

The rest of our markets, Montenegro, Bulgaria and Albania are still in their beginning phase of business development, whereby their business performance is influenced by entrance costs, pertaining to marketing and investment activities, as well as costs, pertaining to activating new large trade areas. Moreover, it needs to be noted that the changed economic conditions also influenced the dynamics of our investment projects in all the markets in the region. According to experience, new trade facilities, which were activated in 2008 and 2009, in the setting of changed consumption and generally difficult living circumstances, would require longer period of time to achieve a normal scope of operations and together with that the expected business results, than in the situation of good economic conditions. That has a negative influence on the business performance of the Group in the short term, but in the long run and alongside improved economic conditions, it represents a huge growth and development potential for the whole Mercator Group.

### **Intensive marketing activities**

Intensive and adapted marketing activities are crucial for maintaining the loyalty of our customers and the stability of revenues in times of crisis. Hard living conditions and consequently low level of consumer confidence affect consumers' behavior and their purchases. Consumers have become even more rational, psychological effects of uncertainty have also manifested in the economic sphere. Addressing these issues, already in the first quarter of 2009 and on the Slovenian market, which represents the largest market of the Mercator Group, we have permanently cut the prices of over 3,000 fast-moving consumer products most commonly purchased by Slovenian households. At the same time, besides our regular Tuesday discounts of 10%, we also introduced regular Thursday discounts of 10% for pensioners. Similar activities for assuring price advantage were undertaken on the rest of our markets. Simultaneously, we were intensively developing our private label line products on all markets, which offer the optimum price to quality ratio. Crucial for maintaining our customer loyalty is also our customer loyalty Pika card system, which was used even more intensively by our customers in 2009, due to the benefits it offers. Accordingly, the number of Pika card holders has increased and reached the level of 1.4 million card holders by the end of 2009. I evaluate our marketing and development activities as successful, as we succeeded to ensure profit growth of 0.6% at constant exchange rates compared to year 2008, despite declining consumption in practically all market programs.

### **Well thought continuance of development activities**

Even though the Group, in the framework of its anti-crisis measures, has limited the scope of its investment activities to a level that could be financed from our own sources, the development activities continued in a well thought-out way. In 2009 Mercator invested over EUR 150 million in the development of our retail network and through its own investments or operating and financial lease acquired more than 100,000 m<sup>2</sup> of sales area, thus at the end of year it operated with more than 1.0 million m<sup>2</sup> gross sales area. Furthermore, more than a third of revenues was generated on foreign markets.

Strategic activities in the scope of our planned internationalization continued. In 2009 Mercator completed the preparations for entrance and entered two new markets: the Bulgarian market, with the opening of the first store in Stara Zagora, and on the Albanian market, with the opening of a hypermarket and the sports store Intersport in a trade center in Tirana. For the entrance on those two markets we employed the concept of operating lease for the commercial premises, which demands lower investment and enables expansion to other markets, without diminishing the development plan for the rest of the markets.

We carried on with the strategic business combinations and alliances, and at the end of 2009 we realized a strategic alliance agreement with the Croatian trading company Getro, which was concluded in February 2009. By that, Mercator acquired 16 commercial premises from the Cash & Carry format on a long term operating lease and significantly improved its market position on the Croatian market. In November the Management Board adopted a resolution to commence with preparation proceedings for the issuance of up to 20 percent of new company share capital based on approved share capital, in case of any further strategic combinations and alliances. The crisis namely brings opportunities for business combinations and alliances, and we in Mercator want to be prepared to that and take advantage of those opportunities in largest extent possible and according to our outlined strategic goals.

### **Stable cash flows and smooth financial operation**

Stable revenues together with the measures of business rationalization assured also a stable realization of cash flows. The group generated EUR 196.6 million EBITDAR (gross operating cash flows before rental expenses) at constant exchange rates which is only 0.8 percent lower than what was achieved in 2008. Stable generation of cash flows from operating activities, even in the time of economic hardship, indicates great financial power, competitiveness, and business efficiency of the Group.

Throughout the whole year 2009 Mercator's financial operations went on without any difficulty. The Group refinanced all of its short term liabilities without any trouble. At the same time the Group acquired also significant additional long term financing sources, thus we concluded the year with an even more solid term structure of financing. The real estate position of the Mercator Group, which in addition to being the largest retailer in Slovenia is also the biggest real estate company in the region, remains solid at the end of 2009. More than EUR 1.7 million worth of unburdened real estate and more than EUR 800 million share capital, ensure financial strength and stability to all company stakeholders, from financial as well as operating aspect. Undisturbed financial operations, which further enabled undisturbed execution of development activities, was in substantial part a result of the mutual trust and partnership with our banking partners and other financial institutions, which is even more crucial in times of severe and harsh economic conditions.

### **Social responsibility**

Our endeavors for balanced and sustainable development, care for the employees and customers, as well as integration into our natural and social environment were combined in our corporate social responsibility projects. In 2009, our humanitarian activities spearheaded this line of our efforts, as in the beginning of the year the economic crisis immediately increased the number of people in social distress. In our central humanitarian action in Slovenia, in cooperation with the Red Cross and Caritas Slovenia, we helped more than one hundred thousand socially deprived persons. With similar activities we acted on the other markets where we are present. With sponsorships and donations, we further supported numerous humanitarian, sport, cultural, scientific, educational and other projects and organizations, which operate on the wider social environment.

Furthermore, we didn't neglect the other aspects of social responsibility, whereby we were awarded the ISO 14001 certificate for environmental management system. We are committed to improving our systems for economical management and rational use of energy, raw materials, and other natural resources.

### **60<sup>th</sup> anniversary of "The Best Neighbor"**

This year, 2009, Mercator celebrated its 60<sup>th</sup> anniversary. From a small wholesale trading company known by the name »Živila«, established in the post war period in the year 1949, in the sixties, it grew to be the leading retail company of alimentary products in the whole region of Southeastern Europe. The celebration of the 60<sup>th</sup> anniversary may have been, as

times require, somewhat modest; however, this was not to downplay its importance and its message: each generation of Mercator employees provides the foundations for the company's future success. Aware of this, we dedicate particular attention to continuous employee education and training, and transfer of knowledge – processes in which our in-house tutors and mentors play a notable role. We are also committed to promoting health and well-being of our employees as we strive unrelentingly to update and improve the efficiency of our services. I hereby thank everyone whose work contributed to Mercator's success in the past 60 years; upon these foundations, we will cope more easily with the challenges ahead of us.

### **Courageously into the future**

The medium term period ahead of us will be very strenuous for all companies. While we all wish the economic situation to improve as soon as possible, I do not feel that recovery is near. The first half of the year will certainly be harsh and stabilization in the region is only expected in the next year, which in turn will be followed by gradual improvement. We at Mercator are aware that the global financial crisis and economic recession will leave permanent consequences in the business environment. Thus we adjust our strategic goals to the newly arisen circumstances, which will shape the business world in the upcoming years. Operating adjustability and flexibility will represent the key competitive advantages and conditions for a long term successful performance, growth and development. In that scope, we have set forth ambitious business goals for the year 2010, which represent a continuation of the realization of the planned strategic goals of the Mercator Group.

I hereby would like to express my gratitude to all the shareholders of Mercator for their support and trust, and to its Supervisory board for its regardful and professional cooperation. I would like to add that the vision of Mercator remains clear and unchanged: more than 21 thousand of Mercator employees have the ability, knowledge and experience, to independently lead the way of the largest retailer in the whole region of Southeastern Europe further in the future!



Žiga Debeljak  
Management Board President

Ljubljana, February 18<sup>th</sup> 2010

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## MERCATOR GROUP PROFILE

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Mercator Group is one of the largest retail chains in the region of Southeastern Europe, the leading retail chain in Slovenia, and increasingly important player in the markets of Serbia, Croatia, Bosnia and Herzegovina, and Montenegro. In 2009, we entered two new markets: Bulgaria and Albania. Our vision remains unchanged – we wish to be the leading retail chain with FMCG program (market program) in Southeastern Europe.



**Current markets of our operations:** Slovenia, Serbia, Croatia, Bosnia and Herzegovina, Montenegro, Bulgaria, Albania.

**New target markets:** Republic of Kosovo, Macedonia.

## Company Profile

The company Poslovni sistem Mercator, d.d., is the controlling company of a group of associated companies (the Mercator Group), one of the largest corporate groups in Slovenia and the entire region of Southeastern Europe.

Full name	<b>Poslovni sistem Mercator, d.d.</b>
Abbreviated name	Mercator, d.d.
Activity	G 47.110 Retail in non-specialized food retail outlets
Identification number	5300231
VAT Tax Code	45884595
Court registry date	January 1 <sup>st</sup> 1990
Company share capital as at December 31 <sup>th</sup> 2009	EUR 157,128,514.53
Number of shares issued and paid-up as at December 31 <sup>th</sup> 2009	3,765,361
Share listing	Ljubljana Stock Exchange (Ljubljanska borza, d.d.) official market, prime market, trading code <b>MELR</b>
President of the Management Board & CEO	<b>Žiga Debeljak</b>
Management Board Members	Vera Aljančič Falež, Mateja Jesenek, Peter Zavrl
President of the Supervisory Board	<b>Robert Šega</b>
Deputy chairman of the Supervisory Board	Jadranka Dakič

## Mercator Group Activities

The most important and extensive business of the Mercator Group is **retail and wholesale** of fast-moving consumer goods (market program).

- ▶ Widely spread retail network with various store formats:
  - ▶ **market program:** hypermarkets, supermarkets, neighborhood stores, comfort stores, Hura! discount stores, and web store;
  - ▶ **specialized programs:** technical and furniture program, clothing program and drugstores, and sportswear stores.
- ▶ Numerous mutually complementing services aimed at satisfying the needs, wishes, and expectations of all our customers.

## Mercator Group Composition

As at December 31<sup>st</sup> 2009, Mercator Group included the following companies:

<b>TRADE SLOVENIA</b>			
<b>Poslovni sistem Mercator, d.d.</b> Slovenia	<b>Mercator IP, d.o.o.</b> 100.0% Slovenia	<b>M.COM, d.o.o.*</b> 100.0% Slovenia	
<b>TRADE SOUTHEASTERN EUROPE</b>			
<b>Mercator - H, d.o.o.</b> 99.9% Croatia	<b>Mercator - S, d.o.o.</b> 100.0% Serbia	<b>Mercator - Mex, d.o.o.</b> 81.0% Montenegro	
<b>Mercator - BH, d.o.o.</b> 100.0% Bosnia and Herzegovina	<b>M - BL, d.o.o.</b> 100.0% Bosnia and Herzegovina	<b>Mercator Makedonija, d.o.o.e.l.</b> 100.0% Macedonia	
<b>Mercator - B, e.o.o.d</b> 100.0% Bulgaria	<b>Mercator - A, sh.p.k.</b> 100.0% Albania	<b>Mercator - K, d.o.o.*</b> 100.0% Republic of Kosovo	
<b>REAL ESTATE</b>			
<b>M - nepremičnine, d.o.o.</b> 100.0% Slovenia	<b>Mercator - Optima, d.o.o.</b> 100.0% Slovenia	<b>Investment International, d.o.o.e.l.**</b> 100.0% Macedonia	
<b>Tomkon, d.o.o.**</b> 100.0% Serbia	<b>Tomveloping, d.o.o.**</b> 100.0% Serbia	<b>Tomsales, d.o.o.**</b> 100.0% Serbia	
<b>Šitireks, d.o.o.**</b> 100.0% Serbia	<b>Magnoreks, d.o.o.**</b> 100.0% Serbia		
<b>OTHER</b>			
<b>Intersport ISI, d.o.o.*</b> 100.0% Slovenia	<b>Eta, d.d.</b> 100.0% Slovenia	<b>Mercator - Emba, d.d.</b> 100.0% Slovenia	

\*The company has not yet commenced its business operations.

\*\*Project-based real estate companies not conducting business operations; they are to be merged with the parent companies in respective markets.

### Branch Offices

As at December 31<sup>st</sup> 2009, 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.

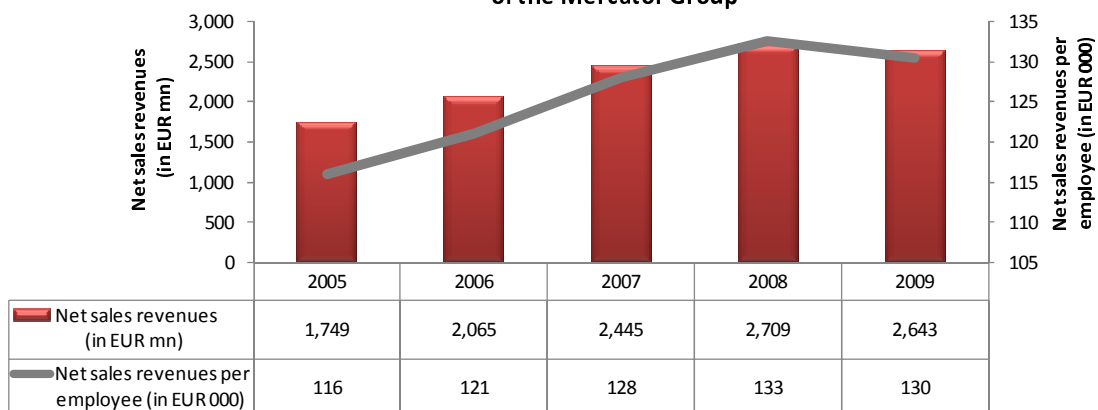
# FINANCIAL HIGHLIGHTS OF 2009

## Mercator Group Financial Highlights for 2009

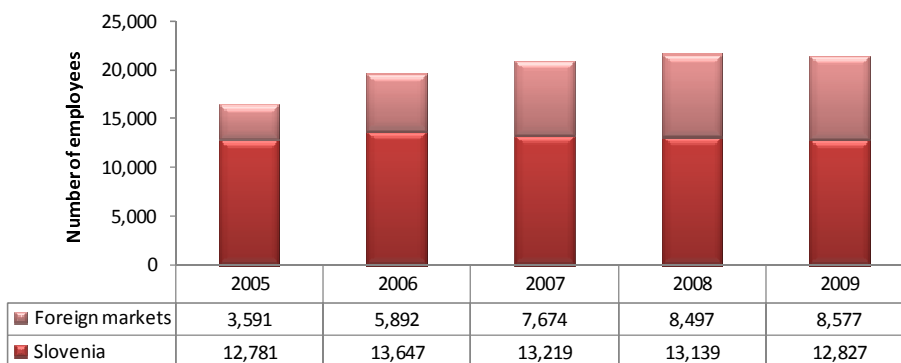
	2005	2006	2007	2008	2009	Index 2009/2008
<b>FINANCIAL DATA</b>						
Net sales revenues (in EUR 000)	1,749,206	2,064,583	2,445,258	2,708,560	2,643,315	97.6
Operating profit (in EUR 000)	30,401	50,776	91,335	100,327	71,842	71.6
Profit before income tax (in EUR 000)	20,588	36,724	54,475	49,993	25,196	50.4
Profit for the financial period (in EUR 000)	13,626	30,149	43,814	40,761	21,119	51.8
Gross cash flow from operating activities (in EUR 000)	111,129	135,394	162,046	176,773	167,296	94.6
Gross cash flow from operating activities before rental expenses (in EUR 000)	117,279	141,703	171,781	198,158	190,619	96.2
Equity (in EUR 000)	551,175	647,880	688,196	814,101	805,390	98.9
Total assets (in EUR 000)	1,533,457	1,861,175	2,070,473	2,540,122	2,476,348	97.5
<b>SELECTED FINANCIAL DATA, BASED ON CONSTANT EXCHANGE</b>						
Net sales revenues (in EUR 000)				2,708,560	2,724,010	100.6
Gross cash flow from operating activities (in EUR 000)				176,773	171,469	97.0
Gross cash flow from operating activities before rental expenses (in EUR 000)				198,158	196,604	99.2
<b>INVESTMENT ACTIVITIES</b>						
Capital expenditure (in EUR 000)	238,180	149,283	164,850	298,305	157,353	52.7
Long-term financial investments (in EUR 000)	39,646	117,467	49,221	15,104	4,801	31.8
<b>EMPLOYEES</b>						
Number of employees as at the end of the period	16,372	19,539	20,893	21,636	21,404	98.9
Number of employees based on hours worked	15,086	17,101	19,099	20,438	20,266	99.2
<b>FINANCIAL INDICATORS</b>						
Productivity (in EUR 000)	115.9	120.7	128.0	132.5	130.4	98.4
Value added per employee per hours worked (in EUR 000)	22.5	22.7	22.9	22.8	22.0	96.1
Return on sales	0.8%	1.5%	1.8%	1.5%	0.8%	53.1
Return on equity	2.7%	5.2%	6.8%	5.6%	2.6%	47.4
Gross cash flow from operating activities / net sales revenues	6.4%	6.6%	6.6%	6.5%	6.3%	97.0
Gross cash flow from operating activities before rental expenses / net sales revenues	6.7%	6.9%	7.0%	7.3%	7.2%	98.6
<b>SHAREHOLDERS INFORMATION</b>						
Market value per share as at the end of the period 31.12. (in EUR)	153.9	212.9	335.0	158.1	153.2	96.9
Dividend per share (in EUR)	1.30	2.50	4.00	4.25	4.50	105.9
Earnings per share (in EUR)	4.1	8.4	11.8	10.9	5.7	52.2
<b>NUMBER OF COMPANIES IN THE GROUP</b>						
Number of companies in the group as at the end of the period	18	13	16	20	23	115.0

# Mercator Group Development Indicators for the Period 2005 - 2009

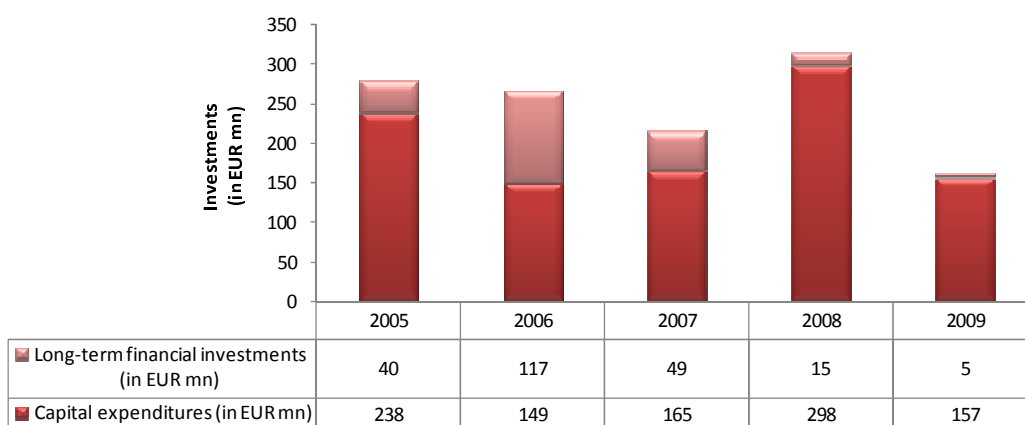
**Net sales revenues and productivity of the Mercator Group**



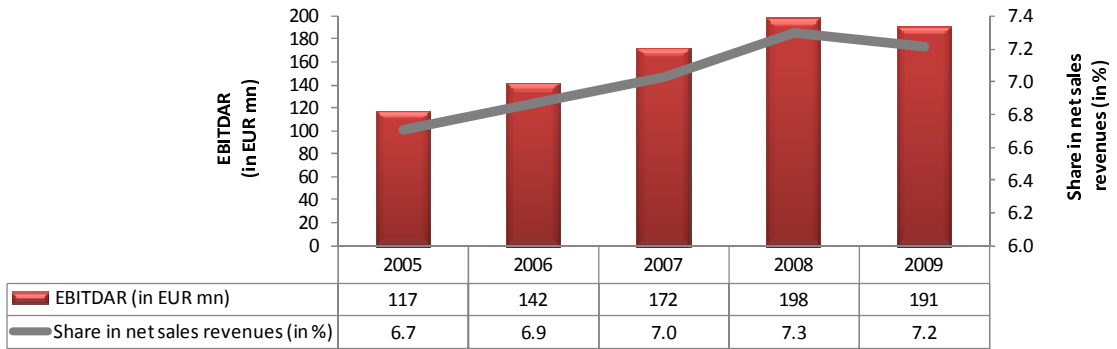
**Employees**



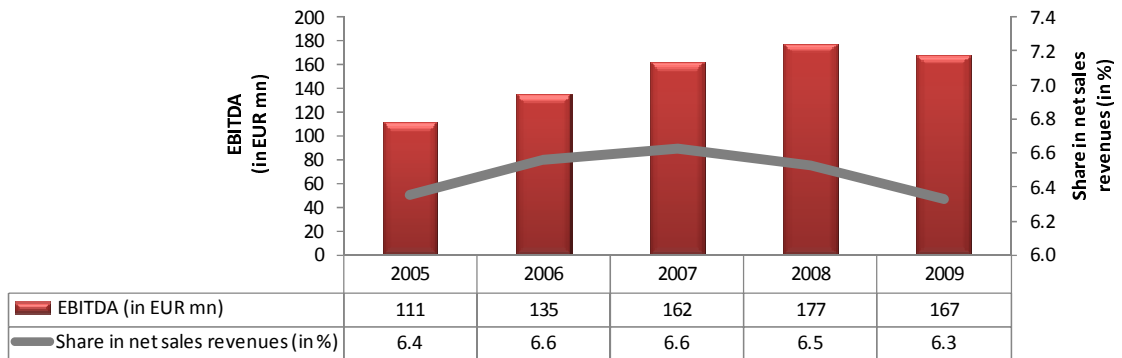
**Capital expenditure and long-term financial investment of the Mercator Group**



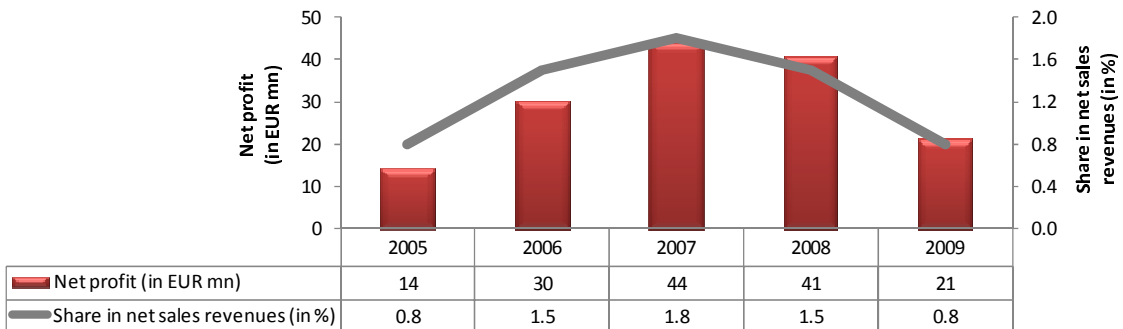
**Gross cash flow from operating activities before rental expenses  
and share in net revenues of Mercator Group**



**Gross cash flow from operating activities and share  
in net revenues of Mercator Group**



**Net profit and share in net revenues  
of Mercator Group**



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## KEY EVENTS

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### Major Events in 2009

#### RETAIL NETWORK DEVELOPMENT AND ENTRIES INTO NEW MARKETS

In **Slovenia**, we opened a hypermarket and Intersport store in Škofja Loka, a hardware, electronics, and construction store in Slovenska Bistrica, a Planina supermarket in Kranj, a superette in Primskovo in Kranj, a supermarket in Preddvor, and a supermarket in Pesnica.

Openings **abroad** include the following:

- ▶ in Serbia: Roda Center Šabac, Roda Center Senta, Roda Center Sombor, a supermarket in Ruma, seven superettes and a supermarket in Sombor, four superettes in Novi Sad, a superette in Zrenjanin, a supermarket in Belgrade, and a superette in Bačka Topola;
- ▶ in Croatia: Mercator Center Varaždin, a hypermarket and Intersport store in Zaprešić, a supermarket in Buje, and a supermarket in Zagreb;
- ▶ in Bosnia and Herzegovina: hypermarket, Intersport store, Modiana, and Beautique store in the shopping center Ilidža – Sarajevo, Mercator Center Banja Luka, a supermarket in Vogošća, and a supermarket in Mostar;
- ▶ in Montenegro: a hypermarket in Podgorica.

In 2009, Mercator entered two new markets. These entries included the following openings:

- ▶ **in Bulgaria:** a hypermarket in Stara Zagora.
- ▶ **in Albania:** a hypermarket and an Intersport store in Tirana.

In 2009, a total of 95,696 square meter of gross sales area were activated.

#### CHANGES IN MERCATOR GROUP COMPOSITION

- ▶ On January 1<sup>st</sup> 2009, the company Mercator – S, d.o.o., took over the activity of the company M – Rodić, d.o.o.; On December 25<sup>th</sup> 2009, the acquisition was completed.
- ▶ On April 9<sup>th</sup> 2009, the company Belpana, d.o.o., Croatia, was merged with the company Mercator - H, d.o.o.
- ▶ On April 16<sup>th</sup> 2009, the company Poslovni sistem Mercator, d.d., founded a new company Mercator - A, sh.p.k., Tirana, to conduct the operations in Albania.
- ▶ Based on the agreement on strategic combination in the field of trade activity, signed on October 19<sup>th</sup> 2006 by Holding Rodić M&B and Mercator, d.d., the company Poslovni sistem Mercator, d.d., purchased on May 29<sup>th</sup> 2009 an additional 12 percent share of the company M - Rodić, d.o.o., Novi Sad. Before the transaction, the company Mercator, d.d., Ljubljana, held 88 percent of the share capital of the company M - Rodić, d.o.o.; after the transaction, the company Mercator, d.d., Ljubljana holds 100 percent of the share capital of the company M - Rodić, d.o.o.
- ▶ On June 1<sup>st</sup> 2009, the companies Pekarna Grosuplje, d.d., and Evolution, d.d., were merged with the company Poslovni sistem Mercator, d.d.
- ▶ On July 31<sup>st</sup> 2009, the company Interier, d.o.o., was acquired with the company Poslovni sistem Mercator, d.d.

- ▶ On October 22<sup>nd</sup> 2009, the company Mercator - K, d.o.o., Priština, was founded in accordance with our strategy to enter Republic of Kosovo, in order to conduct our expansion to this market.
- ▶ On October 29<sup>th</sup> 2009, the company Poslovni sistem Mercator, d.d., acquired an additional 30 percent share in the company Mercator - Mex, d.o.o., Montenegro. After the transaction, the company Poslovni sistem Mercator, d.d., holds 81 percent of the share capital of the company Mercator - Mex, d.o.o.
- ▶ On December 15<sup>th</sup> 2009, the company Poslovni sistem Mercator, d.d., founded the company Intersport ISI, d.o.o. The activities and operations of Intersport will be transferred to this company.
- ▶ In 2009, the company Poslovni sistem Mercator, d.d., acquired 100 percent share of project-based real estate companies Tomkon, d.o.o., Tomveloping, d.o.o., Tomsales, d.o.o., Magnoreks, d.o.o., and Sitireks, d.o.o., which do not conduct any activities and which were acquired in order to obtain the landed property for construction of shopping centers. In the course of 2010, these companies will be merged with the parent companies in particular markets.

## STRATEGIC COMBINATIONS AND ALLIANCES

- ▶ On December 18<sup>th</sup> 2009, the companies Getro, d.d., and Mercator - H, d.o.o., signed an agreement on strategic alliance, pursuant to which Mercator - H will take over the trade activities of the company Getro in the market of the Republic of Croatia. The strategic alliance includes the purchase of the "Getro" brand and long-term operating lease of 16 Getro trade centers and other business facilities with a total area of over 110,000 square meter.

## MARKETING AND CORPORATE ACTIVITIES

- ▶ In 2009, Mercator celebrated its **60<sup>th</sup> anniversary**. Accounting for the current economic conditions, the festivities avoided any lavishness: traditional and regular corporate events were extended, and an event was organized for Mercator Group key employees, which also hosted the president of the Republic of Slovenia.
- ▶ In 2009, we also celebrated the **10<sup>th</sup> anniversary of the Mercator brand**, as well as the **10<sup>th</sup> anniversary of the Mercator Pika card**.
- ▶ In 2009, we pursued the establishment and development of **Mercator call center** in Slovenia and set up Mercator call centers in Serbia, Croatia, and Bosnia and Herzegovina. The customers throughout the region thus have the option to call a toll-free number to obtain all information on Mercator Pika card transactions, Mercator outlets, working hours, products, campaigns, and events at Mercator stores and shopping centers. The call centers also accept customers' opinions, propositions, and praises.
- ▶ In February, we carried out our traditional meeting with our business partners – the **10<sup>th</sup> Days of Marketing**. The event that took place in Cankarjev dom was attended by a record number of 464 suppliers and other business partners.



- ▶ In March 2009, we held the **9<sup>th</sup> Financial Partners Meeting**. Held in Cankarjev Dom, the event hosted representatives of commercial banks, leasing companies, and insurance companies to inform them of Mercator Group's business plans, performance, and financial policy for 2009.
- ▶ In May 2009, the first products of the **revamped Lumpi line** were launched in Mercator stores. The assortment of products is certified by the Pediatric Clinic in Ljubljana, and the Kranj Institute of Public Health. The Lumpi logo underwent a face lift and the entire line is now distinctive for its new lovable characters called Luki, Uma, Miki, Pia, and Iki. In August, we introduced the Lumpi Club, thus announcing the revision of the line and the launch of the [www.lumpi.si](http://www.lumpi.si) website.
- ▶ In September 2009, Mercator received the **Trusted Brand Award**, presented based on the results of a consumer survey by the Reader's Digest Magazine. The survey is conducted by Mediana, an independent market and media research institute. The key criteria of the survey are high quality of products and positive personal experience of the consumers. 
- ▶ In September 2009, the **3<sup>rd</sup> Mercator Human Resource Day** was held in Ljubljana. The central topic of the round table, held at Cankarjev Dom, was "Health – a Common Concern of the Employees, Employers, and the Government."
- ▶ 2009 also saw further development of the network of our own tourist offices. In Slovenia, a total of 11 **M Holidays** offices are now active.

## CORPORATE GOVERNANCE

- ▶ 2009 saw some **major changes in the ownership composition** of the company Mercator, d.d. Current major shareholders are listed in more detail in the section Mercator Share and Ownership Structure.
- ▶ The 15<sup>th</sup> regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., held on July 20<sup>th</sup> 2009, saw the adoption of the resolutions on the allocation of distributable profit, dividend payment, and granting discharge to the Management Board and Supervisory Board. A **new eight-member Supervisory Board** was appointed. Members of the Supervisory Board representing capital are Stefan Vavti, Robert Šega, Jadranka Dakič, and Kristjan Verbič. The Supervisory Board members shall assume their respective terms on October 31<sup>st</sup> 2009; pursuant to the company Articles of Association and Bylaws, the term lasts four years, i.e. until October 31<sup>st</sup> 2013. The Shareholders Assembly was informed that the Council of Employees also appointed representatives of employees for the Supervisory Board, who will assume their terms simultaneously with the representatives of capital. They are Mateja Širec, Jože Cvetek, Janez Strniša, and Ivica Župetič. The company KPMG Slovenija, podjetje za revidiranje, d.o.o., Železna cesta 8a, Ljubljana, was appointed as the authorized auditing company for the year 2009.
- ▶ At its meeting held on September 21<sup>st</sup> 2009, the Management Board of the company Poslovni sistem Mercator, d.d., adopted a resolution to launch preliminary preparation proceedings for the **issuance of up to 20 percent of new company share capital**, based on approved share capital, in order to secure in a timely manner additional financial funds to fuel any strategic combinations and alliances in the field of trade, real estate, or other activities.

## **PROCEEDINGS AT THE COMPETITION PROTECTION OFFICE**

- ▶ Completing and terminating the proceedings instituted against the companies Mercator, d.d., Spar Slovenija, d.o.o., and Engrotuš, d.d., on the grounds of allegedly concerted action between the said companies, the Competition Protection Office issued on May 7<sup>th</sup> 2009 a decision to accept the commitments proposed to the Office by the parties in the proceedings. The commitments are related to various aspects of managing relationships between retailers and suppliers of fast-moving consumer goods, and to reporting on such activities to the Office. They will be in effect for a period of five years.
- ▶ On June 26<sup>th</sup> 2009, the Competition Protection Office, completing the proceedings instituted due to alleged abuse of dominant position in the upstream market of fast-moving consumer goods, issued a decision to accept the commitments proposed by the company Mercator, d.d. The commitments are related to various aspects of managing the relations with the suppliers of fast-moving consumer goods, and to reporting on such activities to the Office. The commitments shall be in effect for a period of five years.

Thereby, both proceedings instituted by the Competition Protection Office against the company at the end of 2007, were completed.

## **Major Events Following the End of 2009**

- ▶ As of January 1<sup>st</sup> 2010, the new macro-organizational structure of the Mercator Group has been put in effect. The key reasons for the reorganization are the need for improved local responsiveness in all markets and improved adjustment to consumer needs, improved operating efficiency, adjustment of the organizational complexity of international operations, and preparation for the option of monetization of our trade property and facilities in order to accelerate our development cycle. The new organizational structure is presented in more detail in the section Organization and Quality of Operations.
- ▶ On January 4<sup>th</sup> 2010, the company Poslovni sistem Mercator, d.d., founded the company Modiana, d.o.o. The activities of clothing program and drugstores will be transferred to the newly founded company.
- ▶ On February 17<sup>th</sup> 2010, the companies Getro, d.d., and Mercator - H, d.o.o., completed their strategic alliance based on the agreement on the acquisition of trade activities of the Croatian trade company Getro, d.d., signed by the partners involved on December 18<sup>th</sup> 2009.

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## CORPORATE GOVERNANCE

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Governance of the company Poslovni sistem Mercator, d.d., and the group of associated companies is based on legislation, Corporate Governance Code for Publicly Traded Companies in Slovenia, internal rules and regulations laid out in compliance with the ISO standards, and sound business practice.

The company is managed by a four-member Management Board supervised by a Supervisory Board. The company has the following bodies of governance: Shareholder's Assembly, Supervisory Board, and Management Board.

### Shareholders Assembly

Shareholders Assembly is a body of governance through which the shareholders assert their rights with regard to the company affairs. As a rule, the company Management Board convenes the Shareholders Assembly of the Poslovni sistem Mercator, d.d., once per year. The convocation of the Assembly is announced in the Delo daily paper, and in the electronic information dissemination system of the Ljubljana Stock Exchange, d.d., called SEOnet, at least one month prior to the Assembly date.

In addition to the location and time of the Assembly, the convocation, or announcement defines the conditions for taking part in the assembly and asserting the voting right, as well as the agenda and proposed resolutions. A shareholder or a proxy may assert the voting right at the Assembly by presenting a written authorization. Convocation of the Assembly, agenda, proposed resolutions with the relevant explanations, and the Assembly resolutions, are also announced on the official company website at [www.mercator.si](http://www.mercator.si).

For the 15<sup>th</sup> Shareholders Assembly, the company took part in the collection of proxy authorizations from minority shareholders; the process was carried out by the Pan-Slovenian Shareholders' Association.

In 2009, 15<sup>th</sup> regular Shareholders Assembly took place with 67.28 percent of total shares with voting rights present. The Securities Market Agency had issued a decision that prohibited the companies Pivovarna Laško, d.d., Pivovarna Union, d.d., and Radenska, d.d., the assertion of their voting rights. The shareholders voted in favor of the proposal on the allocation of distributable profit and dividend payment, and granted discharge to the Supervisory Board and the Management Board. Furthermore, they appointed the Supervisory Board members representing the shareholders, and they were informed which Supervisory Board members were appointed by the Council of Employees. The shareholders appointed the auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., as the company auditor for 2009.

### Supervisory Board

The fundamental function of the Supervisory Board is to supervise the management of company affairs. One half of the members, representing the interests of the shareholders, are appointed by the Shareholders Assembly, while the members who represent the interests

of the employees, are appointed pursuant to the Worker Participation in Management Act, by the Council of Employees.

Members of the Supervisory Board are elected for a four-year term and may be re-elected. Pursuant to the relevant legislation and the provisions of the Rules of Procedure of the Supervisory Board, the Supervisory Board must hold a meeting at least once per quarter, and at least once in each half of the year. In the company Poslovni sistem Mercator, d.d., the Supervisory Board holds at least five regular meetings per year.

The methods and organization of work, convocation of meetings, and other affairs relevant to the activities of the Supervisory Board of the company Poslovni sistem Mercator, d.d., are defined in the company Articles of Association and the Bylaws, and in the Rules of Procedure of the Supervisory Board. At its regular meeting held on June 27<sup>th</sup> 2007, the Shareholders Assembly adopted the resolution on monthly payments as of January 1<sup>st</sup> 2007: according to this resolution, Supervisory Board chairman shall receive EUR 2,500 per month, while the other members will receive EUR 1,500 per month. In 2009, Supervisory Board members also received meeting attendance fees in the net amount of EUR 200, while the net attendance fee for the Supervisory Board chairman amounted to EUR 350.

Pursuant to the provisions of the Companies Act, the Supervisory Board appointed at its 18<sup>th</sup> meeting held on November 11<sup>th</sup> 2008, the Audit Committee for the period until October 30<sup>th</sup> 2009. At the first meeting of new Supervisory Board appointed on November 19<sup>th</sup> 2009, the Audit Committee was appointed for the period until October 31<sup>st</sup> 2013.

## **Presentation Of The Supervisory Board Members**

As at December 31<sup>st</sup> 2009, the company Supervisory Board included eight members.

### **Supervisory Board Members – Representatives of capital**

#### **Robert Šega**, Supervisory Board Chairman

Education:

- BS and MS Electrical Engineering & Electronics

Employment:

- business consultant to the company Epakta, d.o.o., Škofja Loka

Membership in Supervisory or Management Boards of other companies:

- Supervisory Board member at Delo, d.d.

#### **Jadranka Dakič**, Deputy Chairwoman

Education:

- BA Economics

Employment:

- deputy mayor of the Municipality of Ljubljana – non-professional position
- director of the company Lanea, d.o.o., Ljubljana

Membership in Supervisory or Management Boards of other companies:

- Supervisory Board Chairwoman at Javni Holding Ljubljana, d.o.o.
- Supervisory Board Chairwoman at Termoelektrarna Toplarna Ljubljana, d.o.o.

### **Stefan Vavti**

Education:

- MA Economics

Employment:

- executive director for private banking in Central and Eastern European countries, UniCredit Bank Austria, AG

### **Kristjan Verbič**

Education:

- MA Sociology; professor of philosophy and sociology

Employment:

- President of the Pan Slovenian Shareholders Association

## **Supervisory Board Members – Representatives of Employees**

### **Jože Cvetek**

Education:

- BA Economics

Employment:

- head of financial-accounting sector at Eta, d.d.

### **Janez Strniša**

Education:

- BA Economics

Employment:

- head of department at Mercator, d.d.

### **Mateja Širec**

Education:

- BA Sociology

Employment:

- head of department at Mercator, d.d.

### **Ivica Župetić**

Education:

- BA Economics

Employment:

- advisor to the executive director of international development; employed at Mercator - H, d.o.o.

## **Management Board**

The company Poslovni sistem Mercator, d.d., is managed by the Management Board consisting of a president and three members. The president submits to the Supervisory Board a proposal for the appointment of the remaining Management Board members, and the Supervisory Board appoints the entire Management Board for a five year term, with unlimited entitlement for re-election. The number of Management Board members and their respective fields of work and responsibilities are defined as proposed by the president of the

Management Board and confirmed by the Supervisory Board with the adoption of the Management Board Act. The Management Board manages company affairs independently, responsibly, and to the benefit of the company.

Supervisory Board resolution dated December 13<sup>th</sup> 2005, appoints the members of the Management Board of the company Poslovni sistem Mercator, d.d., for a five-year term, starting on January 1<sup>st</sup> 2006. All Management Board members of the company Poslovni sistem Mercator, d.d., signed their respective fixed-term employment agreements with the company Poslovni sistem Mercator, d.d., for the period of five years, which is consistent with the duration of their term.

## **Presentation of the Management Board members**

As of January 1<sup>st</sup> 2006, the Management Board of the company Poslovni sistem Mercator, d.d., consists of the president and three members, appointed for a five-year term. Following is their brief presentation.

### **Management Board President - Žiga Debeljak**

Education:

- MScBA, BS Computer Engineering

Fields of responsibility:

- Coordination of Management Board and Group governance
- Development and investment
- IT
- Finance, controlling, accounting, internal audit, and investor relations

Other responsibilities:

- Member of the Administrative Committee of the Manager Association
- Member of the Council of the Faculty of Economics in Ljubljana
- Member of the Council of the National Gallery

Membership in other administrative or supervisory bodies of non-associated companies:

- Supervisory Board Chairman at the company Pokojninska družba A, d.d.
- Supervisory Board member at Petrol, d.d.

### **Management Board member in charge of human resources, organization, legal and general affairs - Vera Aljančič Falež**

Education:

- LL.M., LL.B.

Fields of responsibility:

- Human resource management
- Organization and quality
- Legal affairs
- General affairs

Other responsibilities:

- Member of the Administrative Board of the Slovenian Chamber of Commerce
- Deputy Chairwoman of the Council of the Institute of Innovation and Development of the University of Ljubljana
- Chairwoman of the Pension Plan Committee at Pokojninska družba A, d.d.
- Member of the Economic and Social Council
- Managing Board member at the Slovenian Association for Human Resource Management and Industrial Relations

## **Management Board member in charge of marketing and purchasing – Mateja Jesenek**

Education:

- MBA, BA Economics

Fields of responsibility:

- Product and service marketing
- Market research and development
- Purchasing and supplier relations
- Public relations

Other responsibilities:

- Marketing Board member at the Consumer Goods Forum, a global association of manufacturers and retailers
- Supervisory Board member at the Slovenian Marketing Association
- Honorary chairwoman of the Society for Promotion of Women in Culture - The City of Women ("Mesto žensk")
- President of the Program Council of the 14<sup>th</sup> Slovenian Marketing Conference 2009
- Member of the UNICEF Economic Council

## **Management Board member in charge of retail, wholesale, and logistics – Peter Zavrl**

Education:

- BA Economics

Fields of responsibility:

- Retail,
- Wholesale,
- Franchise system
- Logistics

Other responsibilities:

- Chairman of the Krim Mercator Handball Club,
- Head of the Supervisory Committee at the Kranj Radioclub

## **Audit Committee**

The activities of the Audit Committee are aimed at further improvement of performance of the supervisory function in the company.

The tasks of the Audit Committee include monitoring the process of financial reporting, monitoring the efficiency of internal control in the company, internal audit and risk management systems, monitoring the mandatory audit of annual and consolidated financial statements, reviewing and monitoring the independency of the auditor appointed to audit the company Annual Report, particularly in terms of providing additional non-audit services, proposing to the Supervisory Board the candidate to be appointed as the company Annual Report auditor, verifying the validity of financial information submitted by the company, appraisal of the Annual Report contents and composition, including submitting a proposal to the Supervisory Board, taking part in defining the key auditing areas, taking part in the preparation of a contract between the auditor and the company, performing other tasks defined either by Articles of Association and Bylaws or a Supervisory Board resolution, and working with the auditor during the company Annual Report audit.

The Audit Committee at the company Poslovni sistem Mercator, d.d., for the period until October 30<sup>th</sup> 2009 consisted of the president Mrs. Mateja Vidnar, (Supervisory Board member) and two members: Mr. Jože Cvetek (Supervisory Board member) and Mr. Peter Ribarič (independent expert on accounting and auditing). As of November 19<sup>th</sup> 2009, the Audit Committee consists of the president Mrs. Jadranka Dakič (Supervisory Board member) and two members: Mr. Jože Cvetek and Mr. Peter Ribarič.

The Audit Committee is performing its duties pursuant to the provisions of the Companies Act. Upon appointment of the Audit Committee, the Supervisory Board appointed the members and defined their respective compensations. The Members of the Committee receive an attendance fee of EUR 200 net per meeting, while the attendance fee for the president of the Audit Committee amounts to EUR 350 net. For performing her duties, the president of the Audit Committee shall in addition receive a monthly compensation in the gross amount of EUR 1,250, while gross monthly compensation for the two members amounts to EUR 750, which is equal to one half of the compensation of the chairman and members of the company Supervisory Board respectively.

## **Management of Subsidiaries**

Mercator Group consists of the parent company Poslovni sistem Mercator, d.d., and its subsidiaries in which the parent company holds, directly or indirectly, the majority interest or the majority of voting rights. Parent company controls its subsidiaries within a single Management Board.

The company Poslovni sistem Mercator, d.d., as the parent company of the Mercator Group, operates by the principles of improving business performance in each subsidiary and the Group as a whole, common harmonized development of the Group, optimal supply of fast-moving consumer goods and services in all markets of Group's operations, improving competitiveness, efficient allocation and coordination of material flows, harmonized and coordinated procurement and sales at home and abroad, financing current operations and development with common funds, and security, risk and liquidity management, and maximum returns in financial management.

In Slovenian and foreign subsidiaries incorporated as limited companies (d.o.o.), the parent company's Management Board performs the function of company Assembly; alternatively, the parent company's Management Board, either entirely or partially (with involvement of only some of its members), takes part in the work of the Supervisory Boards of these companies. The employees present in the bodies of governance at these companies do not receive any additional compensation for performance of such functions.

## **Audit**

In today's continuously changing environment, efficient and successful business operation requires accurate and prompt information. Whilst the management of the company is responsible for providing relevant financial information, the paramount task of internal and external audit is to minimize the risks related to the preparation as far as possible.

At Mercator Group, this is achieved by:

- ▶ clear and concise accounting practices and their strict implementation;
- ▶ completely synchronized accounting policy throughout the entire Group;

- ▶ comprehensive and extensive disclosures and explanations;
- ▶ timely preparation, detailed treatment, and suitable data selection in statements relevant for financial reporting;
- ▶ preparation of financial statements in line with the International Financial Reporting Standards (IFRS);
- ▶ regular monitoring of the accounting and controlling process, as well as other business processes within the internal and external auditing procedures.

## **Internal auditing**

The independent support function of internal audit has been introduced in the Mercator Group in the year 2000; since, it has been actively performed both within the parent company and at the Group level. Basic function of internal audit is perpetual development and monitoring of the internal control systems from the aspect of managing, or hedging, all sorts of operating and other risks to which the Mercator Group is exposed.

The aim of internal audit is to provide assistance to the top management and other levels of management in the improvement of Mercator Group asset management, enhancement of quality, economization and effective business operations within the scope of adopted strategies, business policies, and business and financial plans.

Internal audit includes regular and extraordinary auditing of particular areas of operations of the Mercator Group companies, as well as collaboration with external auditors. In 2009, regular audits included a review of the implemented measures and financial effects of the Mercator Group Operations Optimization Project, and monitored the implementation of cost rationalization measures at the Mercator Group. Internal audit of the non-trade goods and services within the SAP IT system was repeated. Furthermore, internal audits of the data warehouse at Mercator, d.d., of the entire process of the Mercator Pika card at the company Mercator, d.d., and of the measures for managing key risks at the Mercator Group, were also carried out.

In 2010, we will carry on the activities of auditing the implemented measures and the financial effects of the Mercator Group Business Operation Optimization projects and the measures of operating cost rationalization at the Mercator Group, and the measures for managing the key risks.

## **External auditing**

External auditing is carried out by a certified auditing company which, in addition to regular annual audit of the company's financial statements, also provides expert consulting including warnings and proposals for the improvement of the internal control systems for successful management of all types of risks.

Pursuant to the resolution adopted at the 15<sup>th</sup> regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., was appointed as the external auditor for the year 2009 as well.

## Communication with Shareholders and Reporting

The strategy of communicating with the shareholders, financial analysts and institutions, the media, and the general public, is based on the pursuit of transparency and clarity of our operations; this is achieved at Mercator by regular and timely announcement of information on the company status, as well as on major changes in company operations.

Implementation and development of the system of communication with shareholders and the financial community is the responsibility of the Strategic Controlling service which works closely with particular sectors responsible of providing relevant information, and the company's management. In the process, various communication tools are employed, including press releases and public announcements, press conferences, presentation publications, and various materials and announcements published on the company website. A considerable part of communication with the financial community takes place through announcements on the Ljubljana Stock Exchange website, within the SEOnet, the electronic information dissemination system, where we have been publishing all announcements simultaneously in Slovenian and English since 2005, and where all financial statements and reports for the company and the Group have since been published in compliance with the International Financial Reporting Standards.

In 2009, we held regular meetings with various members of the financial community. We also took part in the Days of Slovenian Capital organized by the Ljubljana Stock Exchange and the Central Securities Clearing Corporation in Ljubljana. At the event, Mercator Group was presented to various domestic and international portfolio issuing authorities. In March 2009, we met with our financial partners for the ninth consecutive year. We presented them the Mercator Group development policies for 2009, business performance in 2008, and the Group financial policy for 2009. We also took part in promotions organized by representatives of the capital market.

In 2009, we were also ranked among the few Slovenian companies in the competition for the Portal award – the award for the best investor and other interest group relations.

The strategy of communication with the shareholders and financial community is successfully complemented by our Annual Report. Each year, our efforts are invested into improving its form and contents while complying fully with the relevant legislation and taking into consideration the response from and requirements of the broader public. In 2009, we won the Best 2008 Annual Report competition organized annually by the Finance daily paper. Mercator also ranked at the top in the category of communication where transparency with a creative solution, intelligibility, the story of the annual report, and e-communication were rated.

An outline of the financial calendar, i.e. the schedule of major announcements and events for the current year, is also published at the end of each year for the year to follow, on SEOnet, the electronic information dissemination system of the Ljubljana Stock Exchange, d.d.

## **Declaration of Compliance with the Corporate Governance Code for Publicly Traded Companies**

The Management Board and the Supervisory Board of the company Poslovni sistem Mercator, d.d., headquartered at Dunajska cesta 107 in Ljubljana, hereby submit the Declaration of Compliance with the Corporate Governance Code for Publicly Traded Companies (hereinafter referred to as The Code, dated February 5<sup>th</sup> 2007) which constitutes a part of the Annual Report for the year 2009 and is available on the company website at [www.mercator.si](http://www.mercator.si).

The statement relates to the period from January 1<sup>st</sup> 2009 to December 31<sup>st</sup> 2009.

The governance of the company Poslovni sistem Mercator, d.d., is based on legal provisions, sound business practice, and the principles of the Corporate Governance Code for Publicly Traded Companies. The Code (dated February 5<sup>th</sup> 2007) is available on the Ljubljana Stock Exchange website at [www.ljse.si](http://www.ljse.si), in Slovenian and English language.

Management Board and Supervisory Board of the company Poslovni sistem Mercator, d.d., have reviewed the corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group, and the compliance thereof with the Code, and prepared a new statement which reflects the actual situation of corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group.

It was found that corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group is compliant with the provisions of the Corporate Governance Code for Publicly Traded Companies, except for a part of the provision in section 3.7.3. (President of the Audit Committee should not be a former member of the Management Board; if so, at least five years, must have passed since the end of her/his most recent term as a Management Board member). This provision of the Code will be fully complied with as of the end of 2010.

As of January 1<sup>st</sup> 2010, a new Corporate Governance Code for Publicly Traded Companies is in force, available at [www.ljse.si](http://www.ljse.si). The company Mercator, d.d., is in the process of preparing the relevant grounds and procedures to allow full compliance with the new Code.

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## MANAGEMENT RESPONSIBILITY STATEMENT

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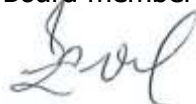
The company's Management Board is responsible for the compilation of the Annual Report for Poslovni sistem Mercator, d.d., and the Mercator Group for the year 2009, including all relevant financial statements which, to the best of the Management Board's knowledge, present truly and fairly the development and performance of the company's operations and the company's financial position, including the description of all significant types of risk to which the company, any other companies included in the consolidation, or the Group as a whole are exposed.

The Management Board confirms that the financial statements were compiled by applying duly and consistently the relevant accounting policies; that the accounting estimates were made on the principle of fair value, prudence and the principle of sound management; and that financial statements represent a true and fair view of the company's financial position, and of the results of its operations in 2009.

The Management Board is also responsible for appropriate and accurate accounting, and adoption of relevant measures to protect its property and other assets. The Management Board hereby confirms that the financial statements, including all and any notes, are compiled based on the going concern assumption and in compliance with relevant legislation and International Financial Reporting Standards as adopted by the European Union.

The company Management Board hereby adopts and confirms the Annual Report for the Company Poslovni sistem Mercator, d.d., and the Mercator Group for the Year 2009.

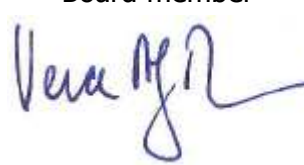
Peter Zavrl,  
Management  
Board member



mag. Mateja Jesenek,  
Management  
Board member



mag. Vera Aljančič Falež,  
Management  
Board member



mag. Žiga Debeljak,  
Management Board  
President



Ljubljana, February 18<sup>th</sup> 2010

# **Business report**



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# BUSINESS STRATEGY OF THE MERCATOR GROUP

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Strategic policies and strategic goals of the Mercator Group for the medium term period 2008 – 2012 were adopted in December 2007. A summary thereof was published on December 18<sup>th</sup> 2007 on SEOnet, the electronic information dissemination system of the Ljubljana Stock Exchange, d.d.

## Vision

**To be the leading retail chain with FMCG program (market program) in Southeastern Europe.**

## Mission

Our business is aimed at creating:

- ▶ benefit for the customers by providing excellent retail services, high-quality goods and competitive prices,
- ▶ benefit for employees by providing a safe and pleasant working environment and a possibility of personal and professional development,
- ▶ benefit for suppliers by taking part in the development of high-quality and innovative products and by providing the possibilities for growth in Slovenia and in emerging markets,
- ▶ benefit for shareholders by attaining a profitable growth of business operations, improving business efficiency, and increasing the company market value,
- ▶ benefit for wider environment by a responsible attitude towards our natural and social environment and by respecting the business ethics and social values in all fields of operation.

## Corporate culture values

We are bound by trust and mutual respect. Our values are:

- ▶ sound teamwork,
- ▶ sincere relationships,
- ▶ encouraging creativity,
- ▶ motivating the fellow workers.

Nobody knows the customer preferences better than we do. Our values are:

- ▶ unwavering education at home and abroad,
- ▶ constant transfer of knowledge,
- ▶ ensuring personal growth and development,
- ▶ excellent staff competitiveness.

Our operations are always diligent and transparent at all levels. Our values are:

- ▶ competitiveness as the foundation of any partnership,
- ▶ accessibility of key information,
- ▶ consistency and honesty.

We are expanding with a sound corporate culture. Our values are:

- ▶ training key human resources for assuming international tasks,
- ▶ understanding the differences and adapting to local environment.

## **Strategic policies**

1. LARGEST RETAILER IN SLOVENIA - To retain the leading market share of market program in Slovenia, primarily by the following activities:
  - ▶ improving the competitiveness of our offer,
  - ▶ developing the retail network.
2. LEADING RETAILER ON NEIGHBORING MARKETS OF SE EUROPE - To become the largest or second largest retailer with market program in the markets of Croatia, Serbia, and Bosnia and Herzegovina, by:
  - ▶ strategic combinations and alliances,
  - ▶ development of our own retail network.
3. ENTERING OTHER SE EUROPEAN MARKETS - To enter or enable the entrance to other markets in Southeastern Europe, where we could become one of the five leading retailers with market program; this will be attained by:
  - ▶ purchasing attractive locations,
  - ▶ development of our own retail network,
  - ▶ strategic combinations and alliances.
4. DEVELOPMENT OF NON-MARKET PROGRAMS - To develop non-market programs and supplementary programs that will:
  - ▶ enable reaping the potential of positive synergies with market program and/or
  - ▶ provide a concept for development of the second fundamental commercial program with a long-term potential of growth and profitability in the target markets,
  - ▶ foster the development of long-term competitive advantages.
5. PROFITABLE OPERATION - Ensure profitable operation by:
  - ▶ measures for retaining the level of trade margins,
  - ▶ measures for cost rationalization and increasing the productivity,
  - ▶ measures for increasing the productivity of invested capital.

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## ECONOMIC CONDITIONS IN 2009

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Business environment in 2009 was extremely challenging due to negative economic growth, credit crunch, and other effects of the global financial crisis. The level of economic activity was considerably lower than expected in all markets, which was in turn reflected in the changes of the volume and composition of consumer demand. In addition, nominal financing costs remained relatively high due to the effects of the global financial crisis, despite falling reference interest rate.

Macroeconomic position of numerous countries in the Western Balkans is troubled and the payment indiscipline, resulting from the restricted amount of credit available to enterprises and individuals, is posing another notable risk. Furthermore, the Republic of Serbia has seen considerable depreciation of its local currency whose average EURO exchange rate rose by 15.6 percent in 2009 compared to the year before. Another notable effect on Mercator's operations was a result of the drop in real purchasing power of the consumers in these countries.

In order to cope with the effective economic conditions, the Management Board of the Mercator Group has introduced two sets of measures:

- ▶ **Adjusting the offer for the consumers**, effected by:
  1. adjusting the sales assortment;
  2. price competitiveness;
  3. customer loyalty system upgrade.
- ▶ **Operating rationalization**, effected by:
  1. cost rationalization;
  2. restriction of investment volume;
  3. efficient risk management.

### ▶ Slovenia

According to first estimates, Slovenia's economy has shrunk by 7.3 percent in 2009, which is a notable drop in the rate of economic growth compared to 2008 (+3.5 percent). The decline of growth was brought about primarily by the collapse of international trade as Slovenia's GDP is significantly export-dependent. Average annual inflation rate in the country amounted to 0.9 percent in 2009. The average inflation rate is a result of low inflation throughout the year – in July and September, we even saw year-on-year deflation. In December 2009, year-on-year inflation amounted to 1.8 percent.

### ▶ Croatia

The first estimates for 2009 indicate a 6 percent decline in the Croatian economy in 2009. The shrinking of the economy is a result of a considerable fall in household consumption. In December 2009, year-on-year inflation amounted to 1.9 percent. In the first half of 2009, Croatian currency, the kuna, depreciated, only to bounce back in the second half, with the strongest appreciation in the beginning of the third quarter. Average annual exchange rate for Croatian kuna in 2009 amounted to HRK 7.34 per 1 EUR (HRK 7.22 per 1 EUR in 2008). As at December 31<sup>st</sup> 2009, the closing rate was HRK 7.30 per 1 EUR.

### ▶ **Serbia**

According to first estimates, economic growth in Serbia was negative in 2009, at 2.9 percent. The prime reason for the GDP drop was a decline in the processing industry, trade, and construction. In December 2009, year-on-year inflation amounted to 6.6 percent. The Serbian dinar saw strong depreciation in the beginning of 2009, prompting an intervention by the Serbian Central Bank aided by the International Monetary Fund which helped the currency maintain the level of RSD 93 per 1 EUR for the most of the year. Average annual exchange rate for Serbian dinar in 2009 amounted to RSD 93.79 per 1 EUR, which is 15.6 percent more than the average rate in 2008. As at December 31<sup>st</sup> 2009, the rate was RSD 95.03 per 1 EUR, which is 6.3 percent more than on December 31<sup>st</sup> 2008.

### ▶ **Bosnia and Herzegovina**

The first estimates for Bosnia and Herzegovina in 2009 also indicate a negative economic growth at 3.0 percent. In December 2009, Bosnia and Herzegovina saw a 0.3 percent year-on-year deflation. The recession is expected to extend into 2010 as domestic demand is expected to remain weak, fiscal policy austere, and unemployment higher. Exchange rate of the Convertible mark is pegged to the euro at the rate of BAM 1.95583 per 1 EUR.

### ▶ **Montenegro**

Lower domestic and foreign demand is estimated to result in a 4.0 percent drop in the Montenegrin economy in 2009. Economic and financial crisis also considerably reduced the inflow of foreign direct investment in 2009, a fuel of high economic growth in the previous years. In December 2009, year-on-year inflation amounted to 1.5 percent. The currency used in Montenegro is EUR.

### ▶ **Bulgaria**

According to first estimates, Bulgaria saw a 6.3 drop in the economic growth in 2009. The main reason for the slump was the decline in both exports and domestic demand, resulting mostly from the lower investment and household consumption. In December 2009, year-on-year inflation amounted to 0.6 percent. Exchange rate for the Bulgarian lev is pegged to the euro at the rate of BGN 1.9558 per 1 EUR.

### ▶ **Albania**

The first estimates by the Albanian government indicate a 4.0 percent economic growth in this country in 2009, making it one of the very few countries whose modest integration into the international monetary flows allowed a positive GDP growth in 2009. In December 2009, the year-on-year inflation rate amounted to 3.5 percent. Average annual exchange rate for the Albanian lek amounted to ALL 131.55 per 1 EUR in 2009. As at December 31<sup>st</sup> 2009, the closing rate was ALL 138.90 per 1 EUR.

## DEVELOPMENT AND INVESTMENTS

In 2009, Mercator Group's investment into property, plant, and equipment amounted to EUR 157,353 thousand, of which EUR 108,520 (69.0 percent) was invested abroad. The majority of funds, amounting to EUR 108,831 thousand, or 69.2 percent, were allocated for construction, acquisition, completion, and furnishing of shopping centers or landed property. Remaining funds were invested in new individual stores, refurbishments, distribution centers, and IT.

### Investment breakdown

Country	Capital expenditure 1-12 2009 (in EUR 000)	Structure in %
Slovenia	48,833	31.0%
Serbia	49,970	31.8%
Croatia	24,882	15.8%
Bosnia and Herzegovina	16,967	10.8%
Montenegro	4,059	2.6%
Bulgaria	6,376	4.0%
Albania	4,986	3.2%
Macedonia	1,280	0.8%
<b>TOTAL</b>	<b>157,353</b>	<b>100.0%</b>

### ► SLOVENIA

► On April 30<sup>th</sup> 2009, we opened a **hypermarket and Intersport** in **Škofja Loka**, including one supplementary service outlet (a café). The newly built facility extends over a total area of 3,516 square meter and it includes 113 parking spots.



► On December 10<sup>th</sup> 2009, we opened a **Hardware, electronics, and construction center** in **Slovenska Bistrica**. The facility has a total area of 1,903 square meter.

► **Other openings:** supermarket Planina in Kranj with a total area of 784 square meter, on February 5<sup>th</sup> 2009; extended and refurbished superette in Primskovo, Kranj, on May 23<sup>rd</sup> 2009; supermarket in Preddvor on November 27<sup>th</sup> 2009; supermarket in Pesnica on December 1<sup>st</sup> 2009.

### FOREIGN MARKETS

### ► CROATIA

► On May 21<sup>st</sup> 2009, **Mercator Center Varaždin** was opened, extending over a total area of 9,310 square meter and including 411 parking spots, of which 266 are located in the basement garage. The program mix is offered in a hypermarket (total area



of 3,037 square meter), Intersport, Modiana, café, and 21 outlets offering supplementary services.

▶ On November 12<sup>th</sup> 2009, **hypermarket and Intersport** were opened in the West Gate Shopping City in **Zaprešić** near Zagreb. The hypermarket has a total area of 7,444 square meter; that of the Intersport amounts to 2,437 square meter. Both outlets are leased.



▶ **Other openings:** supermarket in Buje on March 4<sup>th</sup> 2009 and superette Odra in Zagreb on October 15<sup>th</sup> 2009.

## ▶ SERBIA

▶ On February 25<sup>th</sup> 2009, we opened **Roda Center Šabac**, a facility with a total area of 14,646 square meter and 206 parking spots, of which 180 are roofed. The center includes a hypermarket with a total area of 4,379 square meter, Intersport, Modiana, Beautique, hardware and electronics store, and 39 outlets offering supplementary services. The center is subject to a long-term lease agreement signed by the company Mercator - S, d.o.o.



▶ On December 17<sup>th</sup> 2009, **Roda Center Senta** was opened. The facility has a total area of 3,268 square meter and 62 parking spots of which 52 are in a garage. In addition to the supermarket with a total area of 1,706 square meter, the center also includes 19 outlets leased to third-party providers of supplementary services.

▶ December 18<sup>th</sup> 2009 saw the opening of **Roda Center Sombor**, a facility with a total area of 5,390 square meter and 45 parking spots in a garage. The center includes a supermarket with a total area of 1,290 square meter, Intersport, Modiana, Beautique, hardware store, and 10 outlets offering supplementary services. The center is subject to a long-term lease agreement signed by the company Mercator - S, d.o.o.



▶ **Other openings:** On April 28<sup>th</sup> 2009, we opened a supermarket in Ruma; in the course of 2009, seven additional superettes and a supermarket were opened in Sombor (lease of the outlets of the food retail chain Prehrana, a.d.); four superettes in Novi Sad (lease of the Centroslavija outlets); a superette in Zrenjanin; supermarket Konjarnik in Belgrade; and a superette in Bačka Topola.

## ▶ BOSNIA AND HERZEGOVINA

▶ On April 16<sup>th</sup> 2009, we opened a **hypermarket, Intersport, Modiana, and Beautique** in the **Ilidža – Sarajevo** shopping center. Total area of the leased and fully furnished Mercator outlets amounts to 3,643 square meter, of which hypermarket extends over 2,690 square meter.



▶ On May 7<sup>th</sup> 2009, **Mercator Center Banja Luka** was opened. The facility has a gross area of 17,271 square meter, and a garage with 631 parking spots. The center includes a hypermarket (total area of 6,201 square meter), Intersport, Modiana, Beautique, and 51 outlets leased to third party service providers.



▶ **Other openings:** On December 10<sup>th</sup> 2009, Hayat supermarket was opened in Vogošća; on December 23<sup>rd</sup> 2009, supermarket Carinski most was opened in Mostar. Both outlets are subject to a long-term lease.

### ▶ MONTENEGRO

▶ On December 12<sup>th</sup> 2009, we opened a **hypermarket** in the Mall of Montenegro **in Podgorica**; the hypermarket has a total area of 4,349 square meter. An Intersport store is scheduled for opening in the same mall for March 2010.



### ▶ BULGARIA

▶ On October 7<sup>th</sup> 2009, the opening of a 3,002 square meter **hypermarket in Stara Zagora** marked our entry into a new market – Bulgaria.



### ▶ ALBANIA

▶ On December 19<sup>th</sup> 2009, the opening of a **hypermarket and an Intersport store** in City Park shopping center **in Tirana** marked our entry into a new market – Albania. The two facilities extend over an area of 4,494 and 1,022 square meter.



**In 2009, a total of 95,696 square meter of gross trade area was activated.**

Following is a breakdown of total gross operating area in the real estate, or real property, held by Mercator Group as at December 31<sup>st</sup> 2009.

Gross effective surface area (square meter)	Employed for own operations	Leased out	Total as at December 31st 2009
Trade area, own	756,944	146,125	903,069
Trade area, leased	229,444	59,960	289,404
<b>Trade area, total</b>	<b>986,389</b>	<b>206,084</b>	<b>1,192,473</b>
Warehouse area, own	140,074	-	140,074
Warehouse area, leased	3,698	-	3,698
<b>Warehouse area, total</b>	<b>143,773</b>	-	<b>143,773</b>
Office area, own	43,981	-	43,981
Office area, leased	3,658	-	3,658
<b>Office area, total</b>	<b>47,639</b>	-	<b>47,639</b>
<b>Effective surface area managed</b>	<b>1,177,801</b>	<b>206,084</b>	<b>1,383,885</b>
- of which own	940,999	146,125	1,087,124
- of which leased	236,800	59,960	296,760

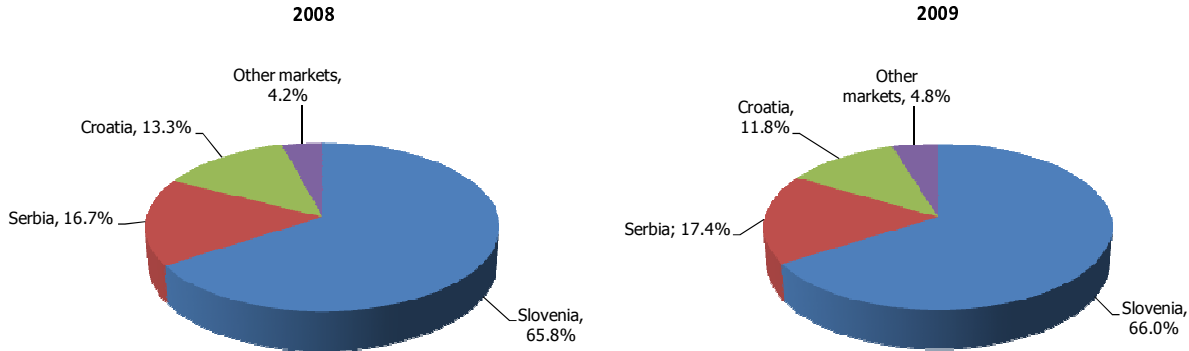
Fair value of real estate owned by the Mercator Group, with a total gross area of 1,087,124 square meter, amounts to EUR 1.7 billion as at December 31<sup>st</sup> 2009 (an average of EUR 1,554 per square meter); carrying amount, excluding revaluation effects, amounts of EUR 1.5 billion (an average of EUR 1,366 per square meter). These values include both land and buildings.

## SALES AND MARKETING

### Sales

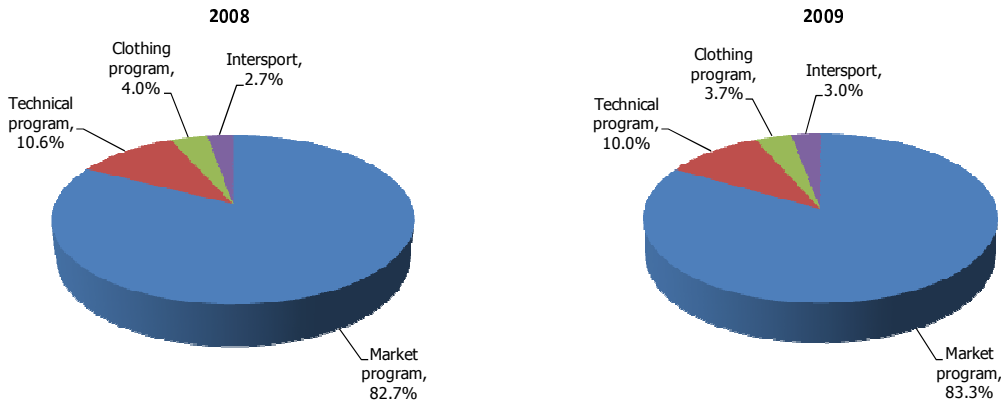
In 2009, Mercator Group generated a total of EUR 2,643 million of net sales revenues, which is 2.4 percent less than in 2008. Assuming constant exchange rates, net revenues from sales would have amounted to EUR 2,724 million, topping the 2008 figure by 0.6 percent.

Mercator Group net sales revenues by geographical segments:



In Slovenia, Mercator Group net sales revenues amounted to EUR 1,745 million in 2009, which is 2.1 percent less than in 2008. In foreign markets, EUR 899 million of net sales revenues was generated in 2009, which is 3.0 percent less than in the year before. Assuming constant exchange rates, revenues abroad would have amounted to EUR 979 million, exceeding the 2008 figure by 5.7 percent.

Mercator Group net sales revenues by programs:



In 2009, the majority of Mercator Group trade revenues resulted from sales of market program products as they accounted for 83.3 percent of total net sales revenues; revenues from other specialized programs amounted to 16.7 percent.



Mercator Group generated 85.4 percent of net sales revenues in retail in 2009, while wholesale and other activities accounted for the remaining 14.6 percent.

Mercator Group generated 99.2 percent of net sales revenues with trade operations in 2009; non-trade operations accounted for the remaining 0.8 percent of total net revenues from sales.

## Category Management

In 2009, category management in Slovenia was focused on improving the price competitiveness and perception in Slovenia. To this end, a pricing model was developed based on the price elasticity of each product, and other relevant economic criteria. Simultaneously, we launched the development of a promotional tool through simulation of marketing mix effects (product, price, promotion, place); the aim of this tool is to improve the effectiveness of our promotions. At the end of the year, we also started to develop an assortment model that will allow defining the assortment in each store according to the store format and the presence of a particular category.

In order to redefine the strategy of private label development, we have analyzed the sales and prices of all Mercator private label lines, and compared them to both competing private labels and equivalent branded products. In the process of hypermarket refurbishment, we also analyzed the effect of space on sales of particular programs in order to define the optimum space for each market program.

In 2009, we refreshed the planograms for the majority of categories at all hypermarkets, in order to improve our sales results, to optimize the profit margin, and to improve inventory turnover. At the same time, we conducted the preparation for further expansion of planograms to major supermarkets.

In Croatia, we set up market program organization in compliance with the principles of category management, and established a reporting system. In the second half of the year, we focused on improving price competitiveness and price perception, and on developing the strategies of select categories.

## Marketing Strategy and Market Share

By offering added value for the customer and providing a pleasant modern shopping experience, we wish to elevate Mercator to the position of the most competitive retailer in the market.

- ▶ Our customers will be offered services and products fitting today's modern way of life;
- ▶ We shall promote environmental responsibility and care for health;
- ▶ We shall have an innovative offer of products and services.

Changed social and economic conditions provided the guideline for our marketing and purchasing activities, as well as for the definition of our priorities, which include the following:

- ▶ Customer care and adjustment to the new market conditions: intensive adjustment of prices of the most commonly sold products;
- ▶ Upgrade of the Mercator Pika card customer loyalty system;
- ▶ Development of private label line products;
- ▶ Adjustment of the sales assortment and sales area;
- ▶ Rationalization of marketing activities, but not at the expense of the customer benefits;
- ▶ High level of service;
- ▶ Social accountability.

### Market Share

Mercator Group market shares in particular FMCG markets in 2009 are estimated as follows:

	Slovenia	Serbia	Croatia	Bosnia and Herzegovina	Montenegro
Market share	35-36 %	8-9 %	5-6 %	4-5 %	4-5 %

Source: Mercator estimates.

Due to notable changes in the volume and composition of consumption, resulting from the economic crisis, no reliable measurements of market shares are available for 2009. Mercator prepared these estimates based on in-house analyses and other available sources; market shares are estimated in intervals.

## Changes in Consumer Behavior and Effect of the Crisis on Consumption

The economic crisis has extended over the entire year 2009, weakening the purchasing power of the population. As the consumers are concerned about their financial status, they respond to the crisis by changing their consumption patterns and habits. Economic situation remains among the major worries of modern consumers who tend to control their spending more strictly, deciding on replacement purchases only when it is really necessary, and often opting for D.I.Y. ("Do It Yourself") rather than hiring costly services. When shopping, they

pay closer attention to the price, and the purchases are more planned and thought out as the customers are seeking the best ratio of value for money.<sup>1</sup>

The global trends reflected in some of Mercator's target markets and affecting the consumption during recession could be summarized as follows:

- ▶ The existing hierarchy of values has been shattered; consumers are much more price-aware which incites a shift towards more affordable products and private label products.
- ▶ Shopping is more rational and thought out, there is less impulse buying and less experimentation with previously unfamiliar products and innovations.
- ▶ Major purchases are postponed.
- ▶ The consumers increase their savings rate.
- ▶ Leisure time activities are changed, leading to a different lifestyle (eating out is less common; consumers prefer preparing their meals at home).
- ▶ Frequency of shopping trips: the consumers go shopping less often; when they do, the average basket is larger.
- ▶ Consumers are changing their shopping destinations: more shopping is done in discount stores.
- ▶ There is a shift in the importance of care for health and the environment.
- ▶ Increased use of the worldwide web, social networks, and technologies where "the information finds the user" or where the user generates the information, and which allow direct interaction between the company and the user.

According to the information provided by the Slovenian Marketing Association and the Valicon market research agency, Slovenian users most drastically reduced their expenditures for furniture and accommodation (55 percent of all consumers), major purchases and investments (54 percent of all consumers), clothing and footwear (52 percent of all consumers), tourist services (50 percent of all consumers), and consumer electronics and home appliances (49 and 47 percent of all consumers, respectively). 26 percent of all consumers have reduced their expenditures for alimentary products or fast-moving consumer goods.<sup>2</sup>

Economic crisis affected the shopping habits both in Slovenia and in Mercator's foreign target markets. According to the Shopper Trends 2009 research,<sup>3</sup> consumers respond to the crisis by purchasing lesser quantities of the same products, by actively seeking special offers, making use of the customer loyalty and benefit programs, and turning to private label products. The crisis also struck the Eastern European countries where the consumers mostly restrict their shopping to basic products and often look in several different stores to find the best prices.

In the second half of 2009, the decline in consumption was slightly mitigated. Although the consumers remain modest in their spending, they entered 2010 with more optimism than displayed in 2009.

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<sup>1</sup> Source: Consumer Insights / MGI Europe survey, McKinsey Global Institute EU Consumer Team analysis

<sup>2</sup> Source: Slovenian Marketing Association and Valicon, April 2009

<sup>3</sup> Source: ACNielsen 2009

## Mercator's Response to the Changes in the Economic Environment

Mercator responded to these changes with numerous campaigns and activities. Perhaps the most notable among them is the campaign **"we cut the prices of 2,800 products"** which started in February 2009 and continued throughout the year. The project was also set up in Croatia.



Responding to the rational behavior of the consumers, we also **expanded the generic line of our private label**. Related communication took place in April and already positive response to the campaign is perceivable as generic products have become the best-selling products in some categories.



Customers from the more threatened groups (pensioners, working class) are offered special discounts. As of September 2009, **members of the Slovenian Association of Free Trade Unions** are offered the following benefits when paying with the ZSSS-DH benefit card: 2 percent discount on the entire value of the purchase at all Mercator stores, eligibility for Special Pika Discounts under the same conditions as applicable to the Mercator Pika card holders, and 10 percent discount on the basket of 20 products, which is updated every three months.

## Customer Relations Management

### 10 Years of Mercator Pika Card Activities

Ten years of Mercator Pika card activities is a result of a solid and long-lasting partnership relation between Mercator and its customers. **Even during recession, the share of retail revenues generated by Mercator Pika card purchases is rising.** Mercator Pika card, due to being a credit card and offering benefits of Special Pika Discounts, as well as those provided through the network of our partner companies, has spread among the majority of active population in Slovenia, thus becoming a major asset of Mercator both in the highly competitive retail industry and in the segment of credit and debit cards.

### Mercator Pika card Customer Loyalty System

At the end of 2009, there is a total of **1,433,799 Mercator Pika card holders** in **four markets of our operations**.

Mercator Pika card holders	Slovenia	Serbia	Croatia	Bosnia and Herzegovina	Total
As at Dec 31 <sup>st</sup> 2008	836,851	129,017	213,418	92,551	1,271,837
<b>As at Dec 31<sup>st</sup> 2009</b>	<b>917,499</b>	<b>154,915</b>	<b>243,329</b>	<b>118,056</b>	<b>1,433,799</b>
New holders in 2009	80,648	25,898	29,911	25,505	161,962

In Slovenia, the **share of total retail revenues generated by purchases completed with Mercator Pika card** amounted to **54.6 percent** in 2009 (50.8 percent in 2008). In all markets of **Mercator operations** combined, this share amounted to **44.1 percent** (40.6 percent in 2008).

In cooperation with our partners in the Mercator Pika card system, we prepared the **Special Pika Discount** campaign each month. Two new partners were added to the Mercator Pika card customer loyalty system: **Kaval Group** and **Lipica Turizem**. To celebrate the **10<sup>th</sup> birthday** of the Mercator Pika system, a major prize competition was organized for all Mercator Pika card holders who responded to our collection of permissions for direct and targeted marketing.



## **Revision of the Mercator Pika Card Customer Loyalty System**

In addition to all basic advantages of the previously existing system, the new system delivers simplification of procedures, cost rationalization, higher level of services, and new possibilities for customer loyalty system upgrade which would allow adjusting the offer to the target segments.

### **Maxi Club**

The purpose of the Maxi Club is to provide a link between people who like shopping in the tranquil environment of the Maxi department store and who value the high quality of offer and expert service. At the end of 2009, Maxi club has a membership of 11 thousand.

### **M Mobil**

By launching the M Mobil service in 2006, Mercator became the first retailer in Slovenia to enter the mobile telephony market. Club members, also Mercator Pika card holders, are included in the M mobil benefit and bonus system.

### **Healthy Lifestyle Club**

In June 2009, the Healthy Lifestyle Club celebrated its 3<sup>rd</sup> anniversary. The club is intended for people of all generations who share the idea of a healthy lifestyle and who are seeking more information on wholesome nutrition, exercise, and quality leisure time. At the end of 2009, the club had a membership of 61 thousand.

### **Lumpi Club**

In May 2009, we founded the Lumpi Club to offer sage advice on upbringing, nutrition, care, education, play, and development of children. Advice is prepared in cooperation with renowned experts, while parents can share their personal experience. The website regularly informs the club members of club activities, events, and workshops for the children. The members are also offered discounts on products and services. At the end of 2009, Lumpi Club had 14 thousand members.



### **M Holidays**

In 2009, we continued to offer under the M Holidays brand our tourist arrangements. We also extended the network of our own tourist offices: eleven were newly opened in 2009. The offer of tourist arrangements are presented in Mercator special offer flyers and on our website found at [www.mholidays.si](http://www.mholidays.si).

### **Mercator Call Center**

In 2009, Slovenian call center was joined by call centers in Serbia, Croatia, and Bosnia and Herzegovina. Operators of the call centers are available at toll-free numbers 24 hours a day, every day of the year, ready to provide customers and Mercator Pika card holders with

information and answers to their questions. Thus far, over 400,000 calls were accepted in the entire region (Slovenia, Serbia, Croatia, and Bosnia and Herzegovina).

### **Mercator Web Store**

In 2009, we carried on our activities to prepare for the comprehensive upgrade of the Mercator web store offer. Despite the crisis, revenues generated by the Mercator web store have not declined in 2009.

### **Mercator Web Portal**

The web traffic at Mercator websites is growing each year: in 2009, it rose by nearly 40 percent compared to the year before. In addition to setting up the employment portal intended for both those seeking employment and current employees, we set up web presentations in Mercator's new markets, Bulgaria and Albania.

### **Mercator at Social Networking Sites**

In 2009, we have devised our strategy for presence at social networking sites and set up our profiles. Mercator ([www.facebook.com/Mercator](http://www.facebook.com/Mercator)) and Lumpi ([www.facebook.com/LUMPI](http://www.facebook.com/LUMPI)) profiles were set up on Facebook, and a prize competition was organized. On Twitter, we set up an account @mercator\_sl. Two channels were opened on YouTube, one for Mercator and the other one for the Lumpi brand. We also have a presentation page on LinkedIn and Wikipedia.

### **Customer Satisfaction Survey**

Each year, we conduct a customer satisfaction survey in each market of our operations; the surveys include customers of all store formats. The objective of the research is to identify any gaps between the level of customer satisfaction and the level of importance of particular elements of service and offer. Based on these findings, improvement proposals are made. Total average satisfaction rating for 2009 was **4.2** (on a scale from 1 to 5), which remains the same as last year.

### **Perception of Quality and Pricing**

Mercator is regularly monitoring the perception of quality and pricing among its customers. Mercator has the reputation of the retailer offering the highest quality of products, as well as a trustworthy retailer offering the customers the best quality for the price paid.

### **Operations in the Markets of Southeastern Europe**

In **Serbia**, the number of Mercator Pika card holders rose sharply in 2009, with the green card taking the highest share. In order to increase the number of card users, we have carried out in-store promotion activities and regularly informed the customers on novelties and benefits offered by the Mercator Pika card.

Customer relations management activities in **Bulgaria** in 2009 included a research on the attitude towards retail chains, and a research on current attitude to Mercator Stara Zagora among the current and potential customers.

In **Bosnia and Herzegovina**, we organized a competition among the cashiers / checkout assistants in signing new Mercator Pika card holders, rewarding those most successful. We also carried out several other activities to attract new Mercator Pika card holders.

In **Croatia**, various campaigns were carried out: Pika Day, Special Pika Discounts, Pika's Happy Week, double and triple Pika points, category discounts, and other campaigns. The




checkout assistant competition in signing new Pika members took place in Croatia as well, and the most successful checkout assistants were rewarded.

## Development of Private Label Lines and Exclusive Brands

In 2009, we continued to pursue our goals in the field of private label line and exclusive brand development. These goals include the following:

- ▶ preparing the strategies for development and future upgrade of Mercator private label lines and exclusive brands;
- ▶ improving the reputation and distinctiveness of the private label lines;
- ▶ motivating purchases by various target groups of consumers through sales promotion activities and innovative communication;
- ▶ growth of the share of private label products in total sales revenues and increasing the number of products offered under private label lines;
- ▶ developing new products by emphasizing safety and quality of products of all private label lines (in-house product testing and external testing at the Faculty of Biotechnology and the Institute of Public Health Kranj);
- ▶ launching the revised Lumpi line;
- ▶ new development concept for the cosmetics and body care products within the exclusive Trebnik Mansion ("Dvorec Trebnik") line.

### Private label and exclusive brands include the following product lines:

- ▶ **Mercator Line** includes alimentary products, products for households, and products of textile and hardware and electronics program. It seeks to offer the best price to quality ratio. To celebrate the 10<sup>th</sup> anniversary of the Mercator private label, we prepared special "gratis" product packages and a private label promotion flyer, and intensified our advertising efforts for special offers in the media.
- ▶ **Trebnik Mansion** ("Dvorec Trebnik") is a new exclusive line of high-quality cosmetics and body and facial care products. The products contain natural ingredients, and a selection of scents, fragrances, and other ingredients attuned to the most recent market trends. 
- ▶ **Grosuplje Bakery** line includes premium bread and pastry.
- ▶ **Ambient Line** includes high-quality products for interior decoration and daily household use.
- ▶ **Generic Line** includes FMCG whose target consumer groups are the most price sensitive, or price-aware, customers. Products of the generic line assure the lowest price at Mercator. In April, a special advertising campaign was carried out. 
- ▶ **Lumpi** includes food, cosmetics, and apparel for children aged up to 10 years, as well as toys, school stationery, and gift program. The products are currently in a stage of active revision. All new products are under the supervision of the Institute of Public Health, Kranj, and the Ljubljana Pediatric Clinic. 
- ▶ **Premium Line** is a newly conceived line intended for the customers with more exquisite taste. These high-quality products are made of the best ingredients, with less artificial additives; they are mostly of Slovenian origin.

- ▶ **The Wishing Table** includes products for the people who are short on time. It allows simple and fast preparation of a hearty meal. The offer includes individual products to be combined with others, products for immediate consumption, and refrigerated full meals that only require heating or cooking.
- ▶ **Healthy Living** includes products that contribute to the improvement of our customers' diets. The products meet at least one of the healthy food criteria: they are rich with fiber, have low fat content (particularly saturated fatty acids and cholesterol), low sugar and salt content, reduced caloric value.
- ▶ **The Kranj Cupcake** includes high-quality pastry products, emphasizing traditional hand-made delicacies. In 2009, we launched the redesign of the brand image and prepared a product catalogue.

### Presence of individual private label lines and exclusive brands in foreign markets

	Mercator Line	Generic Line	Healthy Living	The Wishing Table	Lumpi	Grosuplje Bakery	Total Body Care	Ambient	Premium	Trebnik Mansion	TOTAL NR. OF LINES
Slovenia	x	x	x	x	x	x	x	x	x	x	10
Serbia	x	x	x	x	x		x	x			7
Croatia	x	x	x	x	x		x	x		x	8
Bosnia and Herzegovina	x	x	x	x	x		x	x			7
Montenegro	x	x			x			x			4
Bulgaria	x							x			2

In **Serbia**, we focused on the development of new Mercator Line and Generic Line products to improve our pricing competitiveness in 2009. Our goal is to improve the distinction and recognition of private label products and to increase their share in total revenues. Activities in 2009 included: presenting the private label products in regular monthly campaigns and in a special catalogue; rewarding our customers with packages of private label products upon openings and other events.

In **Bulgaria**, the Mercator Line is already present with both alimentary and non-alimentary products, and the Ambient Line currently includes the products of the non-alimentary segment. Customers were presented with the private label products in a special flyer.

In the course of 2009, the following long-term goals were pursued in **Bosnia and Herzegovina**: improving the distinctiveness and recognition, and increasing the number of private label products, and increasing the share of private label product sales in total sales revenues.

## Sales promotion projects

### Long-term Sales Promotion Projects

- ▶ The projects "**Every Day Low Price**" and "**National Basket**" were carried out throughout the region in 2009.

- ▶ **Members of the Slovenian Association of Free Trade Unions** are offered special benefits when paying with their ZSSS-DH card.
- ▶ We carried on the "**YES! Coupon**" campaign which includes rewarding shoppers who purchase at least EUR 50 worth of products on Tuesdays, with a coupon for 10 percent discount valid on the following Tuesday. The project is also in progress in Serbia, Montenegro, Croatia, and Bosnia and Herzegovina.
- ▶ In April 2009, we introduced the **Thursday discount for retirees / pensioners**. When spending at least EUR 20, customers in retirement will be rewarded with a 10 percent discount valid on the following Thursday. The project is being carried out in Slovenia and Bosnia and Herzegovina. In Montenegro, **Pensioner's Discount** campaign was carried out several times. Retirees were awarded with four coupons in a total value of EUR 70, and they were offered payment in four installments.
- ▶ We also carried out three customer loyalty programs: "Dormeo", "Tefal", and "Collect and Choose Zwilling!" This time, customer loyalty was rewarded with a 70-85 percent discount on the silverware of the renowned brand Zwilling.
- ▶ In Serbia, Croatia, and Bosnia and Herzegovina, project "**Dormeo**" was carried out in 2009. Customers who collected a certain number of sticker coupons were granted 60 percent discount on Dormeo products. In Croatia, similar campaign took place in the first half of the year with **Tognana** tea or coffee sets.
- ▶ In January and February 2009 the campaign "**Five per Day**" took place in Slovenia, allowing the customers to exchange discounts and coupons for fresh fruit.
- ▶ Special projects during the summer included a prize competition called "**With Mercator to the Football World Championship**."
- ▶ In Bosnia and Herzegovina, special projects included a prize competition "**Win a Mercedes**". In addition to the main prize, a Mercedes B car, several minor prizes were presented.
- ▶ In Croatia, we carried out prize competitions "**Free Shopping for 12 Months**" and "**Super School**". The "**Super Wednesday**" campaign was also carried out.

### **Short-term Sales Promotion Projects**

Sales promotion communication was thoroughly revised. The main protagonists of the ads are our salespeople, who interact with the customers in a humorous way to present everyday situations at our stores.

- ▶ In 2009, the **Category Discount** activity was pursued further, offering at least 20 percent discount on a particular category from Friday to Monday. The campaign took place in Slovenia, Serbia, Croatia, Bulgaria, and Bosnia and Herzegovina.
- ▶ In April and May, activity "**Buy and Save!**" was carried out at hypermarkets. Each customer received a coupon for 5, 10, 25, 50, or 99 percent discount, effective for the current purchase. The campaign took place in Slovenia and Bosnia and Herzegovina.
- ▶ In May, we launched the campaign "**Special Weekend Offer**" which is carried out at the end of each month. The point of the campaign is to emphasize alimentary products

appropriate for a particular time or season, and to price them favorably. The campaign was carried out in Slovenia, Bulgaria, Croatia, and Bosnia and Herzegovina.

- ▶ In December 2009 and January 2010, customers spending EUR 30 or more received a 25 percent discount coupon for the purchase of a daily ski pass at ski resorts Vogel, Krvavec, Cerklno, and Rogla. The campaign took place in Slovenia.
- ▶ In Serbia, campaign "**10 Percent Off on Sunday**" took place starting in May at all Roda megamarkets. In October, November, and December we also carried out the campaign at the hardware and electronics departments at Roda Cash&Carry stores and those Roda supermarkets that have such department.
- ▶ In December, we carried out the campaign "**New Year's Coupon**" which included rewarding customers spending more than 3,000 Serbian dinars with a 10 percent discount coupon valid in the next year. In the same period, we also carried out the prize competition "**1001 Tales of Winter Magic**." The main prizes included 10 holidays for two in Venice, and three Hyundai automobiles.
- ▶ Immediately after our launch in Bulgaria, we started out "**Weekend at the Hypermarket**" campaign. In November, we also launched our **customer loyalty program** for "Magnifico glasses". Customers were presented with a pair of spectacles upon collecting a certain number of sticker coupons. At the end of the year, we launched the project "**New Year's Promotion**": children from daycare centers staged a puppet show and decorated 23 New Year's trees with toys of their selection. We also launched the "**Happy Hours**" project.
- ▶ In Bosnia and Herzegovina, we launched the "**Lock & Lock**" customer loyalty program in August, rewarding customers who spend more than 50 Convertible marks on Fridays. In December, we also carried out the "**Wednesday Coupon**" campaign, offering our customers discounts on selected products.

## Other Activities

- ▶ **Hardware and electronics program:** In 2009, we carried out sales promotion campaigns to improve the distinctiveness of our hardware and electronics program among the consumers and to establish a reputation as a retailer offering technologically advanced and attractive, competitively priced products in Slovenia and abroad.
- ▶ **Clothing program and drugstores:** In order to promote the sales of certain seasonal products, several activities were conducted in Slovenia. We offered the service of fashion consulting in our major stores, and carried out regular campaigns and makeup days. In addition, activities of related purchases were also introduced. **In Serbia**, we offered "Happy Hours", "Buy 3, Pay for 2", and category discount campaigns. Mercator Pika card holders were sent a coupon for 20 percent discount on the following purchase. **In Bosnia and Herzegovina**, regular campaigns were carried out at Beautique drugstores, in addition to special discounts on selected products, and discounts for Mercator Pika card holders. Sticker coupon collection campaign was also carried out. **In Croatia**, apparel and drugstore program included regular discount campaigns for particular groups of products, and our catalogues were advertised in magazines.
- ▶ **Intersport:** During the year, regular and additional campaigns took place in Slovenia in order to promote the sales of seasonal categories. We issued six program guides and four program catalogues. We carried out two international campaigns "Run Free Now" for the category of running, and sponsored selected events for amateur athletes. **In foreign markets**, we mostly focused on sales promotion projects: "Customers Win by 3:2",

category discount, and related purchases. We developed and upgraded the presentation at the [www.Intersport.si](http://www.Intersport.si) portal and set up a website at [www.intersport.rs](http://www.intersport.rs) in Serbia.

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## STORE FORMATS

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One characteristic feature of Mercator Group trade operations is the diversity of its retail network with various store formats both in the market program and in specialized stores of hardware and electronics, apparel and beauty, and sports program (Intersport).

As a response to the uncertain market conditions, changes in shopping habits of our customers, and changes in market trends, we started preparing a revision of Mercator hypermarket programs in Slovenia and abroad, which includes the following activities:

- ▶ redistributing the sales area among sales programs and categories;
- ▶ increasing sales area allocated for special offer goods (special offer aisles or islands within all programs, and final allocation of aisle compartments for targeted special offers);
- ▶ increasing the sales area intended for seasonal offer – establishing season-related aisles or islands where attractive season-related products can be promoted;
- ▶ more pronounced and effective labeling of special offers within regular and special offer sales areas.

### **Mercator Centers and Shopping Centers**

**Mercator centers** are shopping centers with a wide offer of all Mercator programs, as well as offer of other attractive service providers operating in leased outlets, and the offer of complementary services. Hence, our customers are offered everything at one place. These facilities are located in major urban centers.

**Roda centers** are a format of modern shopping centers that combine the benefits of shopping at Roda megamarkets or supermarkets with the offer of many other attractive service providers, as well as some specialized Mercator programs.



### **Market Program Store Formats**

**Mercator hypermarkets** are located in larger shopping centers where people not only do their major weekly shopping, but also socialize and spend their leisure time.



**Mercator supermarkets and neighborhood stores** are located in larger residential and commercial areas, and are intended for daily shopping.

**Mercator comfort stores** are located in central or, downtown areas of larger cities. Their program mix is adapted to the requirements of contemporary urban customers who are constantly in a rush. The emphasis is on fresh program and a wide assortment of ready-made food.



**Mercator web store** enables saving time and comfortable shopping without leaving your home.

**Mercator Cash & Carry** are conventional Cash & Carry stores selling only to companies, or only offering wholesale services. Assortment and sales area (larger, commercial packaging, larger quantities, units, and product packaging, functionality of store equipment, commissioning and delivery of the goods ordered, etc.) are adapted accordingly. These stores are located outside city centers, on the periphery of major cities; excellent traffic access is highly important for this store format.

At **discount stores**, customers are offered with rational shopping for basic FMCG, under the **Hura!** brand. The offer is based on the best ratio between price and quality, while providing the most competitive products in the market.

**Roda megamarkets** are larger stores offering affordably priced products, mostly to customers dosing their major weekly or monthly shopping. They are located in Roda centers where the offer of various supplementary service providers and complementary services allows socializing and enjoying leisure time.



**Roda supermarkets and markets** are located in major residential and commercial areas. They are intended primarily for daily shopping.

**Roda Cash & Carry** is an open-type Cash & Carry format serving for both legal persons and individuals (natural persons). Assortment and sales area are adapted accordingly. Open type Cash & Carry stores are located outside city centers, on the periphery of major cities; excellent traffic access and a large number of visitors are highly important for this store format.



## Specialized Store Formats

Specialized store formats are developed for the purpose of providing activities that supplement our core activity or FMCG retail.

**Hardware and electronics** includes construction centers, independent combined hardware and electronics stores, and interior design and equipment stores.



**Clothing program and drugstores** comprises the following formats of textile stores, which differ by size, and the scope and level of offer: Fashion Avenue ('Avenija mode'), Modiana, and Outlet stores. The offer of beauty program is presented under the Beautique label (drugstores and perfumeries).



Mercator Group is the license holder for **Intersport**, the world's largest global chain of sports equipment stores. The license applies to the markets of Slovenia, Croatia, Bosnia and Herzegovina, Serbia, Montenegro, and Albania. Intersport stores are available to customers both within Mercator Centers as well as independently, i.e. as City Shops located in the centers of major cities. In tourist resorts, we are developing the so-called Ski & Resort stores.



## Composition of Retail Units

Breakdown of the composition of Mercator Group retail units by types of stores, particular programs, and particular markets as at December 31<sup>st</sup> 2009

COUNTRY	SLOVENIA	SERBIA	CROATIA	BOSNIA AND HERZEGOVINA	MONTE-NEGRO	ALBANIA	BULGARIA	MERCATOR GROUP		
ACTIVITY	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Gross sales area	Net sales area
Hypermarkets	20	12	14	6	1	1	1	55	264,048	174,834
Supermarkets	130	24	29	12	4	-	-	199	226,101	145,847
Superettes	279	25	42	2	4	-	-	352	149,325	84,176
Neighbour stores	67	3	15	2	1	-	-	88	14,146	7,611
Cash & Carry	12	2	-	-	-	-	-	14	35,055	22,991
Hard discount stores	16	-	-	-	-	-	-	16	13,134	9,209
<b>TOTAL FMCG program</b>	<b>524</b>	<b>66</b>	<b>100</b>	<b>22</b>	<b>10</b>	<b>1</b>	<b>1</b>	<b>724</b>	<b>701,810</b>	<b>444,668</b>
Technical program	96	7	14	-	-	-	-	117	158,283	90,794
Technical program	64	3	14	-	-	-	-	81	121,997	63,681
Furniture program	32	4	-	-	-	-	-	36	36,286	27,113
Clothing program and drugstores	97	19	30	13	-	-	-	159	69,142	57,877
Clothing program	80	10	30	9	-	-	-	129	65,601	55,004
Drugstores and perfumeries	17	9	-	4	-	-	-	30	3,541	2,873
Intersport	30	10	24	8	1	1	-	74	44,125	34,090
Restaurants	19	6	-	12	-	-	-	37	12,832	7,580
Other	11	-	-	-	-	-	-	11	197	189
<b>TOTAL specialised programs</b>	<b>253</b>	<b>42</b>	<b>68</b>	<b>33</b>	<b>1</b>	<b>1</b>	<b>-</b>	<b>398</b>	<b>284,579</b>	<b>190,530</b>
<b>TOTAL</b>	<b>777</b>	<b>108</b>	<b>168</b>	<b>55</b>	<b>11</b>	<b>2</b>	<b>1</b>	<b>1,122</b>	<b>986,389</b>	<b>635,198</b>
Franchise stores	225	-	76	-	-	-	-	301	53,928	34,938
<b>TOTAL with franchise stores</b>	<b>1,002</b>	<b>108</b>	<b>244</b>	<b>55</b>	<b>11</b>	<b>2</b>	<b>1</b>	<b>1,423</b>	<b>1,040,317</b>	<b>670,136</b>

## **Development of New Technologies and Services**

In 2009, rollout of new technologies in our stores continued. In this year, self-service checkout cashiers were introduced in five Croatian hypermarkets and at hypermarket Škofja Loka. Tik Tak self-checkout cashiers are thus in operation in 29 Mercator hypermarkets and at two supermarkets. In Slovenia and Croatia combined, a total of 140 self-checkout cashiers are in operation, accounting for nearly 30 percent of all purchases.

## **Further Standardization of Store Formats**

The standardization project in 2009 included 49 newly drafted standards, confirmed by the Store Format Standardization Project Council; the standards relate to the formats of hardware and electronics stores, Intersport stores, and market program store formats.

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# **SUPPLIER RELATIONS AND LOGISTICS**

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## **Purchasing of Trade Goods and Supplier Relations**

In 2009, looking for new, more favorable procurement sources and adjustment of offer to various segments of our customers remained the focus of our supplier relations efforts. Current market conditions have further increased the importance of a careful selection of appealing, marketable, affordably priced, yet high-quality products. We expanded the offer of our products in all private label lines, mostly by selecting the most favorable offers and quotations collected in public tenders; thus, purchasing prices were pushed down.

Particular attention was paid to the selection of products in short-term sales promotion projects. Responding to the said market conditions, we worked with our suppliers in order to provide high-quality offer of fast-moving consumer goods with added value at the end of the year. In our permanent sales promotion projects such as "Every Day Low Price", particular care was devoted to the right selection of products, making sure that the top selling products of each category were made accessible to Mercator consumers at the most favorable price possible. We continued to decrease delivery failures, reduce inventories, and optimize our operations.

Upon our entry into the markets of Albania and Bulgaria, we negotiated with our suppliers to agree on attractive sales assortments; purchase agreements were signed with them.

Our supplier relations complied fully with the commitments accepted by the Competition Protection Office, Code on the Management of Trade Goods Supplier Relations, Working Instructions on Business Communication, and Working Instructions on Price Change Implementation, all of which were adopted as sound practice measures for providing compliance of company operations and its commercial transactions with the internal and external rules and regulations related to competition protection.

## **Logistics**

In 2009, our logistics operations included efficient and successful provision of the agreed level of logistics services for the entities requiring them. Strategic programs for improvement of competitiveness were focused on further progress of the logistics infrastructure optimization project, with the following activities being at the forefront in the period:

### In Slovenia:

- ▶ We have completed the first stage of implementing paperless operation and pursued the revision of fruit and vegetables distribution processes.
- ▶ In 2009, investment volume was decreased due to the economic crisis. As a result, activities related to the construction of the central logistics center in Želodnik were temporarily halted.

### In foreign markets:

- ▶ In Croatia, a technological plan was prepared according to the agreement on the lease of a distribution center in Velika Nedelja.
- ▶ In Bosnia and Herzegovina, logistics facilities were relocated from the Rajlovac location to the Kakanj location, mostly for economic reasons.

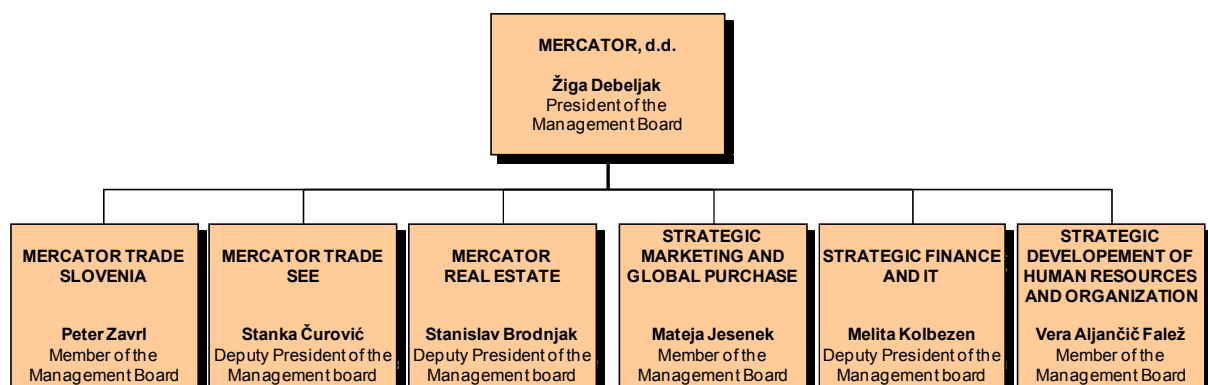
## ORGANIZATION AND QUALITY OF OPERATIONS

In 2009, a number of organizational changes took place at the Mercator Group. We successfully passed independent assessments and audits for the international quality standards and earned new certificates. We carried out the activities of internal control and further pursued the activities of the strategic project of general optimization of Mercator Group operations.

### Organizational Management

Organizational changes prompted by the transfer of retail and wholesale activities from the company M - Rodič, d.o.o., to the company Mercator - S, d.o.o. Companies Mercator - S, d.o.o., and Mercator - H, d.o.o., were reorganized. A part of the operations of the company Mercator - BH, d.o.o., was transferred to the newly founded company M - BL, d.o.o., Banja Luka. Micro-organization was laid out at the company Mercator - B, e.o.o.d., and a new trade company was founded in Albania: Mercator - A, sh.p.k. At Mercator, d.d., the first M Holidays offices were opened. Non-trade companies Pekarna Grosuplje, d.d., Evolution, d.d., Interier, d.o.o., and Belpana, d.o.o., Croatia were merged with their relevant parent companies. Job catalogue was revised and the Electronic Register of Rules and Regulations – Mercator Standards – was regularly updated.

At its meeting held on September 28<sup>th</sup> 2009, the Management Board of Mercator, d.d., adopted the new macro-organizational structure effective as of January 1<sup>st</sup> 2010. The main reasons for reorganization are the necessity to improve local responsiveness in all markets, better adaptivity to consumer needs, improved efficiency of our operations, the need to adapt the organizational complexity to international operations, and preparation for the option of monetization of our trade properties and facilities currently held in order to accelerate our development cycle.



## **Quality Standards**

In 2009, two new certificates were awarded to Mercator, d.d.: ISO 14001 for environmental management system, and ISO 22000 for food safety management system; at Mercator - S, d.o.o., certificate ISO 9001 for quality management system and the HACCP certificate for food safety management were obtained.

All planned independent and internal assessments and audits of the ISO 9001 quality management system were carried out at the companies Mercator, d.d., Mercator - H, d.o.o., and Mercator - BH, d.o.o., as well as QWeb at v Mercator, d.d. Independent audit at Mercator, d.d., was carried out as integrated audit in 2009 and was the most extensive to date.

Customs Administration of the Republic of Slovenia, authorized in Slovenia for certification in compliance with the criteria for awarding the AEO status, awarded the "Status of Authorized Economic Operator" to the company Mercator, d.d. The AEO status indicates that Mercator is recognized as a safe and reliable partner in international trade in the entire European Community, particularly with regard to customs operations; as a result, it is eligible for additional benefits throughout the Community.

Electronic application for paperless management of non-compliance, recommendations, and praises was introduced at Mercator, d.d. Further development of this application for optimizing and extending its use was also pursued. An application was developed to manage the electronic register of contracts and agreements, and the application for electronic management of councils was revised.

## **Internal Controls at Our Stores**

We followed closely the legislative changes in the processes of goods and services flow in trade industry, notified the users on requirements, provided advice to them, and introduced these changes to our internal standards. We carried out 594 regular and 59 extraordinary internal controls at our sales units, and kept track of the findings of inspections, as well as conducted provided training.

With regard to food safety, we carried out the corrective measures based on the findings of the first part of external certification audit, which was completed successfully in November as we were awarded the ISO 22000 certificate for food safety management system. We conducted or revised eight HACCP studies. An emergency task force was established, which is responsible for withdrawing the products during store working hours, outside the regular working hours of administrative workers. We also monitored withdrawals of goods and analyzed them according to the cause, sector, and the initiator of the withdrawal.

We carried out the activities to assume a new function of coordination and reporting in the field of monitoring. These activities include monitoring and reporting on the monitoring of private label products, products of our own production and butcher's departments, sampling in open departments (culinary islands) in retail, and national monitoring.

We compiled handbooks for coaches and mentors at all competency centers for checkout operation, and the handbooks of binding legislation. We are involved in all competency centers as members. Training was carried out for internal control based on the principles of the HACCP system, legislative requirements, and Mercator Academy for managers and

Coaches. With regard to functional training, all planned training for target groups was carried out, with a total duration of 324 hours.

## **Strategic Project of General Optimization of Operations**

Within the framework of the strategic project for general optimization of Mercator Group operations, we continued to work on improvement of efficiency and reduction of operating costs. We have developed a model for efficient retail unit and segment management, and prepared the implementation of a pilot project for Slovenia. In Slovenia, Serbia, and Croatia, we carried out continuous activities for disposing of unviable inventory at the stores. To attain the goals set with regard to inventory management at the stores, we additionally trained the relevant personnel, and worked individually with selected stores in Slovenia and Croatia. Consistently with the plan, we decreased the number of inventory turnover days at warehouses in Slovenia, as well as cut costs of purchasing non-trade goods at the Mercator Group. With regard to investment and maintenance of investment equipment, proposals of annual contracts were prepared for the Mercator Group, a list of common suppliers for all markets was drafted, and negotiations were commenced. With regard to optimization of logistics costs in Slovenia, we ensured the conditions for implementing the systemic solution of comprehensive optimization of goods delivery frequencies, which includes all Mercator stores and wholesale customers.

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## **IT AND TELECOMMUNICATIONS**

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Consistently with the **strategic project of IT system revision**, the following activities were carried out in 2009:

- ▶ As a part of the project of **support function IT system revision**, we completed the extension of the use of the basic SAP modules in the companies Mercator - H, d.o.o., Mercator - BH, d.o.o., M - BL, d.o.o., and Mercator - B, e.o.o.d. The extension of the use of these modules was carried on by introducing the basic SAP modules at the company Mercator - S, d.o.o., in Serbia; as of January 1<sup>st</sup> 2010, these modules, too, are in use. For the company Mercator, d.d., we also set up a HCM SAP module (a system that enables capturing and processing information on organization, human resources, time, and compensation, at a single place) and the PY SAP module (a system enabling to run the entire process of employee compensation calculation and reporting on the payment of employee personal income to public institutions).
- ▶ As a part of the project of **material operation IT system revision**, or the implementation of the G.O.L.D. software solution for operation management in retail, logistics, and wholesales, we carried out the following:
  - We have extended the use of G.O.L.D. CENTRAL module intended for editing and maintaining master data, managing procurement processes, and managing promotion activities;
  - We connected 200 market format outlets in Slovenia to the G.O.L.D. SHOP module (background operations at the store) by integrating the new POS trade system.
  - We provided support to material operation at the company Mercator - B, e.o.o.d.

The following activities were carried out in other fields:

- ▶ We continued to upgrade the **Mercator Pika card customer loyalty system**.

- ▶ With regard to IT support to **general operations optimization projects at the Mercator Group** we introduced the goods acceptance protocol at the Fruit & Vegetables warehouse, and continued to upgrade and expand the order generation system that employs distributors, automatic ordering system, and reporting system.
- ▶ **IT support to management and decision-making** included further activities within the program of category management, the project of Integral Material Operation Data Warehouse (inclusion of data from new markets and inclusion of units that have introduced G.O.L.D.).
- ▶ **IT support to retail, manufacturing, and catering services** included further qualitative upgrade of the POS trade systems, and unification of IT support, and extension of the self-check-out cashiers in Slovenia and Croatia. We also established IT support for tourist services.
- ▶ In the field of **infrastructure, telecommunication, and security**, we provided smooth operation and upgrade of the infrastructural environment (G.O.L.D. and other systems), established the infrastructural environment for M Holidays, completed the introduction of revised and revamped messaging system, carried on the implementation of the risk management system in the field of SAP authorizations (security), and completed the implementation of the revised communication network.
- ▶ With regard to the field of **information production support**, we set up a User Help Center, available during the progress of business processes, for the entire region.

In foreign markets, we carried on the unification of the infrastructure and the IT support to retail and wholesale in compliance with the standards of support to the companies of the Mercator Group. We established IT support for the companies M-BL, d.o.o., Mercator-B, e.o.o.d., and Mercator – A, sh.p.k.

## FINANCIAL MANAGEMENT

### Finance income and expenses

Favorable composition of debt financing sources, and a drop in reference rates had a positive effect on Mercator Group net financial performance.

in EUR 000	Mercator Group		Index	Poslovni sistem Mercator, d.d.		Index
	2008	2009	2009/2008	2008	2009	2009/2008
Finance income from interests	9,181	7,811	85.1	7,550	5,944	78.7
Finance expenses from interests	-58,127	-46,554	80.1	-50,173	-44,600	88.9
Net finance expenses from interest	-48,946	-38,743	79.2	-42,622	-38,656	90.7
Financial income from currency translation differences	2,555	100	3.9	1,020	28	2.8
Financial expenses from currency translation differences	-5,520	-4,224	76.5	0	0	-
Net financial expenses from currency translation differences	-2,965	-4,124	139.1	1,020	28	2.7
Other financial income	8,367	2,334	27.9	7,840	2,169	27.7
Other financial expenses	-6,790	-6,113	90.0	-2,370	-362	15.3
Net other financial expenses	1,577	-3,779	-	5,470	1,807	33.0
<b>Net finance expenses</b>	<b>-50,334</b>	<b>-46,646</b>	<b>92.7</b>	<b>-36,132</b>	<b>-36,821</b>	<b>101.9</b>

Mercator Group's finance income from interest amounted to EUR 7,811 thousand in 2009, which is 14.9 percent less than in 2008. Of this figure, EUR 5,381 thousand pertains to interest generated by activities of managing liquidity reserves or short-term investments. Remaining amount of EUR 2,430 thousand is a result of default interest charged to our wholesale customers.

Mercator Group's finance expenses in 2009 amounted to EUR 46,554 thousand, pertaining mostly to expenses for regular interests on borrowings from commercial banks, and financial lease. Relative to the year 2008, finance expenses dropped by 19.9 percent, which is mostly the result of lower reference rates and a more favorable composition of debt financing sources.

Finance expenses were notably affected by the currency translation differences in Serbia where the average RSD exchange rate in 2009 rose by 15.6 percent compared to the year before. This depreciation of the Serbian currency resulted in EUR 4.2 million of finance expenses due to currency translation differences.

Other net finance expenses of the Mercator Group in 2009 amounted to EUR 3,779 thousand, which is EUR 5,356 thousand more than in 2008. Other finance expenses in the amount of EUR 6.1 million mostly relate to adjustments of the carrying value of receivables, in compliance with the adopted accounting policies. EUR 5.5 million of the said sum is related to adjustments of trade receivables (receivables from Mercator Pika card holders, lessees, wholesale customers); EUR 0.2 million is related to the decrease in the fair value of financial investment; and EUR 0.4 million is related to other finance expenses.

**Financial Liabilities**

Financial liabilities of the Mercator Group as at December 31<sup>st</sup> 2009 amount to EUR 1,051 million, which is 1.5 percent more than at the end of 2008.

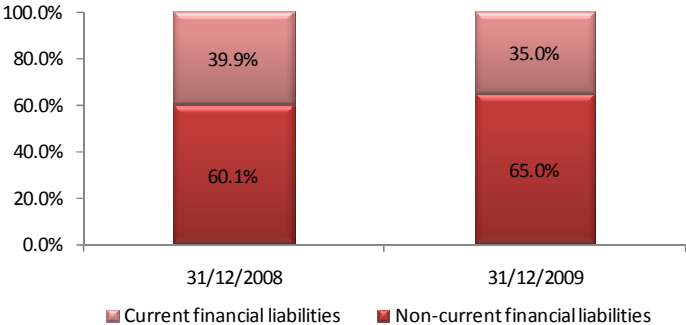
**Debt-to-Equity Ratio**

At the end of 2009, debt-to-equity ratio of the Mercator Group amounted to 1:1.25 (compared to 1:1.22 at the end of 2008). The ratio is a quotient between equity, which includes share capital as reported in financial statements and long-term provisions, and debt which includes long-term and short-term financial liabilities and long-term financial lease liabilities.

**Long-term Asset Coverage**

As at December 31<sup>st</sup> 2009, long-term coverage at Mercator Group, i.e. the ratio of non-current liabilities to non-current assets, amounted to 81.6 percent. Compared to the end of 2008, this indicator has improved by 0.3 percentage points, which is a result of the increase of long-term financing sources in the composition of liabilities.

**Ratio between Current and Non-Current Financial Liabilities**

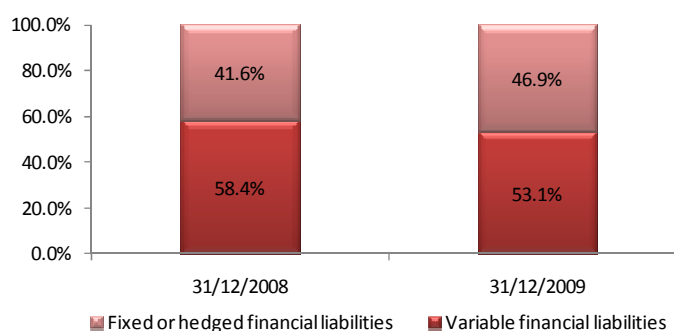


Regardless of the fact that banks mostly approved short-term loans in 2009, Mercator managed to improve the maturity composition of our financial liabilities, which is a sign of Mercator's financial stability and sound relations with our financing partners. Compared to 2008, the share of non-current financial liabilities rose by 4.9 percentage points.

### Obtaining Sources of Financing and Liquidity Reserves Management

- ▶ In 2009, Mercator obtained short-term, as well as long-term bilateral loans and signed long-term financial lease agreements.
- ▶ In 2009, we saw a notable upward pressure on the interest rate margins, which is mostly the result of diminished liquidity of commercial banks, and shattered confidence in the interbank market.
- ▶ Particularly abroad, the use of long-term operating lease of trade facilities constructed for Mercator by local real-estate partners was resorted to as an increasingly important form of financing our investments.

### Ratio between variable and fixed or hedged financial liabilities of the Mercator Group



At Mercator, we are using derivative financial instruments to hedge the risk of rising interest rates. As at December 31<sup>st</sup> 2009, the amount of borrowings hedged against the changes in variable interest rates amounted to EUR 350 million. Of this sum, EUR 150 million of borrowings were hedged with interest rate swaps, and EUR 200 million of borrowings were hedged with interest rate caps.

### Available liquidity sources as at December 31<sup>st</sup> 2009

As at December 31<sup>st</sup> 2009, companies of the Mercator Group had access to the following sources of liquidity with commercial banks:

EUR thousand	December 31 <sup>st</sup> 2009
Cash and cash equivalents	16,844
Bank deposits	12,983
Standby revolving credit lines	81,279
<b>Total</b>	<b>111,106</b>

# MERCATOR SHARE AND OWNERSHIP STRUCTURE

## Mercator Share

As at December 31<sup>st</sup> 2009, the **share capital of the company Poslovni sistem Mercator, d.d.**, was divided into 3,765,361 shares. Nominal value per share amounts to EUR 41.73.

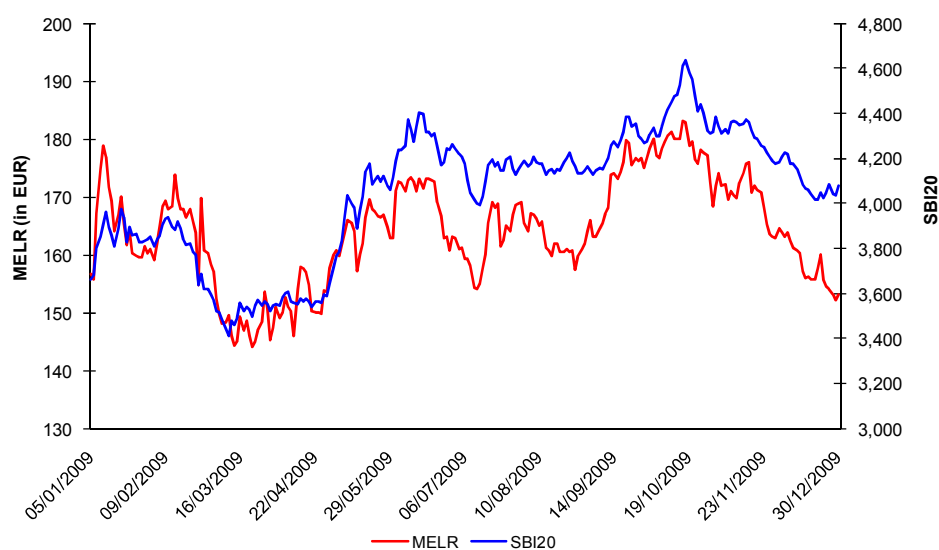
Shares of the company Poslovni sistem Mercator, d.d., are listed and traded in the **prime market of the Ljubljana Stock Exchange** (Ljubljanska borza, d.d.), under the trading code **MELR**.

On 2009, Mercator share was the second according to trading volume on the Ljubljana Stock Exchange, representing 23.57 percent of total stock market trading volume.

Pursuant to provisions of the Securities Market Act and the Rules and Regulations of the Ljubljana Stock Exchange, d.d., the company **regularly informs the public of the results of its operation and other relevant events**.

At its meeting held on September 21<sup>st</sup> 2009, the Management Board of the company Poslovni sistem Mercator, d.d., adopted a resolution to launch preliminary preparation proceedings for the **issuance of up to 20 percent of new company share capital**, based on approved share capital, in order to secure in a timely manner additional financial funds to fuel any strategic combinations and alliances in the field of trade, real estate, or other activities.

## Movement of average price per MELR share in 2009, compared to the movement of the SBI20 index



## Key information for the shareholders

	December 31 <sup>st</sup> 2009	December 31 <sup>st</sup> 2008	Index 2009/2008
Number of shares registered in Court Register	3,765,361	3,765,361	100.0
Number of treasury shares	42,192	42,381	99.6
Market capitalization (in EUR)	576,740,344	595,228,267	96.9
Market value of share (in EUR)	153.17	158.08	96.9
Book value per share (in EUR)	211.13	209.79	100.6
Annual low (in EUR)	144.03	148.29	97.1
Annual high (in EUR)	183.11	343.58	53.3
Weighted average market price, excluding block and cross trades (in EUR)	164.83	243.37	67.7
Earnings per share (in EUR)	5.2	8.6	60.0
Price/earnings ratio (P/E)	29.6	18.3	161.5
Capital gains yield (in %)	-3.11	-52.81	-
Dividend yield (in %)	2.85	1.27	224.4
Total yield (in %)	-0.26	-51.54	-

Equity market capitalization is calculated as the product of the number of shares entered into Court Register as at December 31<sup>st</sup>, and the market price per share as at December 31<sup>st</sup>.

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

Share book value is calculated as the ratio between the value of equity of the company Poslovni sistem Mercator, d.d., as at December 31<sup>st</sup>, and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.

Price/Earning ratio is calculated as ratio between market price per share as at December 31<sup>st</sup> and net profit per share.

Capital gains yield is calculated as the ratio between market price per share as at December 31<sup>st</sup> of the period at hand, and the market price per share as at December 31<sup>th</sup> of previous year.

Dividend yield is calculated as the ratio between dividend paid per share and the market price per share as at December 31<sup>st</sup>.

## Dividend policy

At its regular meeting held on April 17<sup>th</sup> 2007, the Supervisory Board of the company Poslovni sistem Mercator, d.d., adopted the company dividend policy for the period 2007 – 2010. The policy defines dividends in the following amounts: EUR 4.00 per share in 2007, EUR 4.25 per share in 2008, EUR 4.50 per share in 2009, EUR 4.75 per share in 2010.

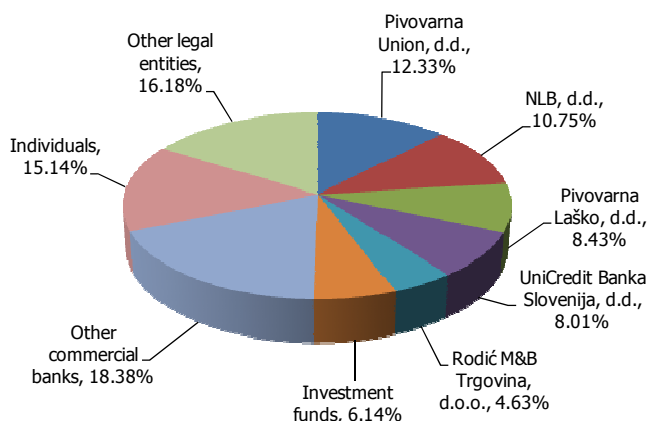
The actual amount of dividend is defined by the Shareholders Assembly each year. At the 15<sup>th</sup> regular Shareholders Assembly held on July 20<sup>th</sup> 2009, the resolution on the payment of dividends in the amount of EUR 4.50 per share was adopted.

Management Board and Supervisory Board believe that, due to the effects of the global financial crisis and harsh economic conditions, the medium-term dividend policy adopted in 2007 is no longer appropriate. This belief was considered in the proposal for the allocation of distributable profit for 2009, submitted by the Management and Supervisory Board.

## Ownership Structure

As at December 31<sup>st</sup> 2009, the **Share Register** of the company Poslovni sistem Mercator, d.d., indicated **17,079 shareholders** or 225 less compared to the situation as at December 31<sup>st</sup> 2008.

As at December 31<sup>st</sup> 2009, the **ownership structure of the company Poslovni sistem Mercator, d.d.**, was as follows:



## Major Shareholders

As at December 31<sup>st</sup> 2009, the following ten largest shareholders combined owned **60.51 percent** of the company:

Major shareholders	Country	Number of shares	Ownership share
1 Pivovarna Union, d.d.	Slovenia	464,390	12.33%
2 NLB, d.d.	Slovenia	404,832	10.75%
3 Pivovarna Laško, d.d.	Slovenia	317,498	8.43%
4 UniCredit Banka Slovenija, d.d.	Slovenia	301,437	8.01%
5 Rodič M&B Trgovina, d.o.o.	Serbia	174,517	4.63%
6 Banka Celje, d.d.	Slovenia	165,270	4.39%
7 Gorenjska banka, d.d.	Slovenia	142,920	3.80%
8 NFD 1 Delniški Investicijski Sklad, d.d.	Slovenia	107,211	2.85%
9 Abanka, d.d.	Slovenia	103,400	2.75%
10 Radenska, d.d.	Slovenia	96,952	2.57%
<b>Total</b>		<b>2,278,427</b>	<b>60.51%</b>

## Foreign shareholders

As at December 31<sup>st</sup> 2009, the share of foreign investors in the company Poslovni sistem Mercator, d.d., amounted to **12.48 percent**, which is 0.24 percentage points more than at the end of 2008.

## Shares held by Management Board members as at December 31<sup>st</sup> 2009

Name and surname	Number of shares	Ownership share
Žiga Debeljak	1,100	0.0292%
Vera Aljančič Falež	30	0.0008%
Mateja Jesenek	1,000	0.0266%
Peter Zavrl	60	0.0016%
<b>Total</b>	<b>2,190</b>	<b>0.0582%</b>

## Shares held by Supervisory Board members as at December 31<sup>st</sup> 2009

Name and surname	Number of shares	Ownership share
<b>President of Supervisory Board</b>		
1. Robert Šega	0	0.0000%
<b>Members of Supervisory Board (representatives of capital)</b>		
2. Jadranka Dakič, deputy president	0	0.0000%
3. Štefan Vavti	0	0.0000%
4. Kristjan Verbič	0	0.0000%
<b>Members of Supervisory Board (workers representatives)</b>		
5. Mateja Širec	36	0.0010%
6. Jože Cvetek	2,000	0.0531%
7. Janez Strniša	0	0.0000%
8. Ivica Župetič	0	0.0000%
<b>Total</b>	<b>2,036</b>	<b>0.0541%</b>

### Treasury shares

As at December 31<sup>st</sup> 2009, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares, which is 189 less than on December 31<sup>st</sup> 2008. In July 2009, the company Poslovni sistem Mercator, d.d., carried out a merger of the company Interier, d.o.o., with the company Poslovni sistem Mercator, d.d. In this transaction, 189 shares of the acquiring company were used as payment to minority shareholders, according to the exchange ratio defined in the merger agreement and audited by an independent auditor.

## RISK MANAGEMENT

In 2009, Mercator Group operations were conducted against a backdrop of harsher and more strenuous economic conditions than initially planned: GDP growth was negative in all key markets. This was reflected in a notable decrease in demand in retail, in all markets of our operations; in addition, negative effects of the global financial crisis persisted. In such conditions, deliberate and prudent management of the risks encountered, while conducting operations in a changed economic environment, is all the more important for the Mercator Group.

### Role, Principles, and Organization of the System

At Mercator, proactive risk management is the responsibility of the Mercator Group Risk Management Council; the Council is in charge of a systematic process of risk management.

Consistently with the need to monitor and analyze the risks from the aspects of several fields of expertise, The Risk Management Council includes the following three Committees for three key types of risk:

- ▶ **Business risks** related to company operation and its core activity;
- ▶ **Operational risks** related to executing and control of business processes and activities in the Mercator Group, and to the expenditures and costs incurred in the execution of business processes.

- ▶ **Financial risks** are those that may negatively affect the ability to generate cash flows, management of cash flows, maintaining the value of financial assets, and managing financial liabilities.

## **Risk management process**

In 2008, the risk management process at Mercator Group was thoroughly revised. In 2009, the measures adopted to manage the key risks were assessed with a special internal audit.

To this end, the following was carried out:

- ▶ risks were reclassified and re-identified;
- ▶ sensitivity analysis was conducted to find how a particular risk, in case of occurrence, affects the gross cash flow from operating activities;
- ▶ marginal value for defining key risks was defined;
- ▶ risk management measures were defined.

Following are the benefits of systematic risk management:

- ▶ selection of more appropriate and successful strategies and more efficient tactics for attaining our goals;
- ▶ anticipation, timely identification of negative trends and events, and timely response;
- ▶ interaction between various fields and multi-faceted character of each set of problems is more successfully accounted for in business decisions and measures;
- ▶ improved performance;
- ▶ lesser negative volatility, or variance, of future business performance;
- ▶ lesser probability of business or financial problems;
- ▶ better relations with company stakeholders – customers, suppliers, banks, shareholders, employees;
- ▶ better information for adopting business decisions;
- ▶ better quality of planning future operations.

When implementing the revised risk management process, respective committees identified all risks to which Mercator Group is exposed or may be exposed, according to our estimate, in the following year or in the upcoming medium term period. In addition, the assessments of Mercator's exposure to particular types of risk were prepared. The assessments were made based on the level of probability of occurrence, and expected damage in case a particular loss events actually took place. Risks were defined by applying descriptive and quantitative criteria.

The objective behind the process revision is quantification of the Mercator Group's exposure to particular identified risk types, based on the sensitivity analysis, which shows the percentage of decrease in gross operating cash flow at the Mercator Group level, or at an individual company level, when a certain loss event, analyzed within the framework of a particular risk, actually occurs. Risks have been classified according to the level of effect on the gross operating cash flow and tolerable risk limits have been defined. In line with the defined policies, particular proposals for the management of certain types of risk have been prepared, which have already been implemented into the day-to-day decision-making processes and operations in certain fields. The measures taken form a basis for the planning of internal auditing processes in terms of annual audits of risk management measures adopted by the Risk Management Council.

## Key Risks in 2009

At Mercator, we are constantly reexamining and analyzing the existing and potential new risks, as we devise and implement the measures for their management in daily operations. Particular attention is paid to the changes in economic conditions and their effect on individual areas of risk management. Following is a presentation of risks that were defined as key risks within their respective types, or groups of risks and were therefore most closely monitored in 2009.

Among the **business risks**, the following was defined as the key risk:

▶ Risk of a decline in the purchasing power:

As a result of harsh economic conditions, the risk of a decline in purchasing power remains high. Furthermore, changes in shopping habits and behavior of our customers have also been perceived, which affects the changes in both volume and composition of consumption. Bankruptcies and massive layoffs in some major systems considerably decreased the purchasing power of some segments of the population. In all markets, we have adapted the marketing activities to the new conditions in order to provide a favorable offer for our customers, and to retain our revenue level.

The following were defined as key risks among the **financial risks**:

▶ Foreign currency risk:

For Mercator Group, foreign currency risk, defined as the possibility of a loss of economic benefit due to a change in the exchange rate of a particular currency, appears in the markets of Serbia and Croatia; therefore, we are actively monitoring the macroeconomic background of the changes in exchange rates and attempt to adapt our operations so as to mitigate the exposure to the foreign currency risk, by responding to general trends and by adapting our operations to reduce the exposure to this risk through natural hedging. Foreign exchange risk is among the key risks, and the Group is looking to hedge it with appropriate business measures as far as viable.

▶ Credit risk:

Due to the aggravation of the economic crisis, exposure of companies to liquidity problems is increasing. Hence, credit risk in Mercator's wholesale is also increasing, as is the possibility that receivables will only be collected, or settled, partly or not at all. Activities conducted in 2009 in order to mitigate the credit risk resulted in notable decrease of receivables to wholesale customers and other business partners, while only slightly decreasing sales to wholesale customers. The activities that were focused on in 2009 included the following:

- ▶ closer supervision of exposure to a single customer;
- ▶ proactive collection of receivables;
- ▶ insurance of receivables.

▶ Refinancing risks

This risk could become a key risk, if the conditions in the international financial markets were to be further aggravated.

## Measures adopted to hedge the key risks at Mercator Group

At Mercator Group, the following measures were adopted to manage the key risks identified and described above.

### ▶ Measures adopted to manage the key risk of a decline in the purchasing power:

In order to manage the business processes and risks in a period of an economic slump and major oscillations in macroeconomic indicators, Mercator is carrying out measures in all fields in order to effectively manage its operations in these volatile conditions.

In terms of sales and purchasing, particular attention was paid to the markets of Slovenia and Croatia in 2009, as these are, in addition to Serbia, the key markets by revenues generated. Thus, we are working with the AT Kearney consulting company to establish a so-called pricing model. The model will take into account the macroeconomic changes in our environment (inflation, GDP, etc.), changes in the business environment (competitiveness, etc.), and other aspects in order to allow anticipating the effects on revenues generated by the retail network in Slovenia at several levels (product, category, entire network).

Introduction of business result modeling based on macro- and micro-economic criteria also enables greater reliability of forecasting the effects of changes in the macro and micro environment. Furthermore, it allows better flexibility of the company and adaptability of its retail pricing, which in turn results in better adaptability to the conditions in the environment, including a potential decline in consumer purchasing power. Last but not least, it allows control over the financial investment of cutting prices and profit margins – an investment that may be a required response to such event.

In marketing, operating activities are conducted with maximum commitment. High level of promotional activities and constant presence in the marketing mix allows us to provide the conditions for maintaining sales at the high levels from previous years. At the level of strategic marketing, we are making extra efforts in setting up the Customer Relationship Management system; using transaction databases, it will allow us a more accurate insight into the desires and needs of our customers. Simultaneously, support to commercial and marketing activities also includes setting up continuous monitoring of key consumer behavior indicators related to shopping for fast-moving consumer goods, in a form that will allow instant calculation of correlation between the said parameters.

### ▶ Measures adopted to manage foreign currency risk:

For Mercator, foreign currency risk is present in the markets of Serbia and Croatia. In other markets, legal tender is either euro or a currency pegged to it. In 2009, foreign currency risk was identified as a key risk; as a result, the following measures were adopted to manage it:

- ▶ constant monitoring of macroeconomic background of the changes in the exchange rate at hand, and other related macroeconomic indicators and trends;
- ▶ based on the general trends and expectations, we are looking to adapt our operations, as far as possible, in such way that it is naturally unexposed to foreign currency risk;
- ▶ in case of increased risk, we decided, given the estimated level of our exposure, to enter forward or option contracts by which the parent company Poslovni sistem Mercator, d.d., protects its subsidiaries from the foreign currency risk.

Foreign currency risk is particularly notable because our subsidiaries in Serbia and Croatia have financial liabilities denominated in euros. In order to financially evaluate the foreign currency risks, sensitivity analysis was carried out, measuring Mercator Group sensitivity to

the changes in exchange rates. Sensitivity analysis is presented in more detail in the financial part of the Mercator Group report (disclosure 29).

▶ Measures adopted to manage credit risk:

Due to the aggravation of the economic crisis, exposure of companies to liquidity issues is increasing. Simultaneously, credit risk of Mercator's wholesale is increasing. At Mercator, we responded to the changes in our environment by defining the measures to reduce the exposure to wholesale credit risk. In risk analysis for 2009, wholesale credit risk was defined as a key risk; therefore, the following risk management measures were adopted:

- ▶ Securing first-class credit insurance from customers with lower credit rating;
- ▶ Continuous monitoring of customers defaulting on their payments and restricting exposure to individual customers;
- ▶ reducing the number of days of default on payments after which further payments are blocked;
- ▶ proactive procedures of receivables collection - improved coordination between commercial and financial function;
- ▶ more active legal proceedings;
- ▶ promoting mutual and chain offsetting with customers, where possible.

Credit risk related to receivables from purchases with Mercator Pika card involves a significant probability that claims resulting from deferred payment, or customer crediting, will be settled only partly or not at all. Risk analysis for 2009 defined credit risk related to Mercator Pika card as a key risk.

The following measures were adopted to manage it:

- ▶ proactive collection of receivables from Mercator Pika card holders;
- ▶ introducing a new credit scoring model defining the opening limits to customers paying with the Mercator Pika card.

▶ Measures adopted to manage the key risk of refinancing:

In order to limit the refinancing risk, we agreed with all commercial banks already in the beginning of the year on refinancing the loans due for payment in 2009. We reached an agreement to convert a part of our short-term loans into long-term bilateral loans or long-term financial leases, thus reducing the refinancing risk. In the course of 2009, we also managed to improve the maturity composition of financing sources. Since 2008, we are actively managing our liquidity reserves, thus hedging the liquidity and refinancing risks.

## **Estimation of the risk exposure of Mercator Group**

The Management Board estimates that total exposure of Mercator Group to business, financing, and operational risks, as at December 31<sup>st</sup> 2009, considering the current assumption for further development of the aspects of economic environment in 2010, is at a **moderate level**.

It should furthermore be noted that there is a considerable uncertainty with regard to the following:

- ▶ conditions in financial markets;
- ▶ further effects of a sluggish economic recovery; and
- ▶ future macroeconomic situation in the countries of the Western Balkans.

Should any major changes occur, relative to the current expectations, with regard to the key aspects of our business and economic environment, as listed above, the exposure of Mercator Group to:

- ▶ risk of attaining the planned amount of revenues from sales, resulting from a decline in purchasing power;
- ▶ risk of refinancing of short-term financial liabilities;
- ▶ foreign currency risk, particularly in Serbia and Croatia;
- ▶ and/or any other risks.

could become considerable, or high, despite the measures introduced to hedge them.

Therefore, the company will update each quarter its assessment of exposure to risks, according to the development of the aspects of business and economic environment; these reassessments will be reported on in interim, or quarterly, business reports.

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## PERFORMANCE ANALYSIS

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**Despite extraordinarily challenging economic circumstances, Mercator Group operations were stable in 2009.**

Economic circumstances made 2009 a very challenging year that saw negative economic growth, a credit crunch, and other effects of the global financial crisis. The level of economic activity in all markets was far below the expected figures, which was in turn reflected in lower volume and a change in the composition of consumer demand.

Macroeconomic position of numerous countries in the Western Balkans has been and remains troubled and the payment indiscipline, resulting from the restricted amount of credit available to enterprises and individuals, is posing another notable risk. Furthermore, the Republic of Serbia has seen considerable depreciation of its local currency whose average EURO exchange rate rose by 15.6 percent in 2009 compared to the year before.

In order to cope with the effective economic conditions, the Management Board of the Mercator Group has introduced two sets of measures in 2009:

- ▶ Adjusting the offer for the consumers, which included adjusting the sales assortment, improving price competitiveness, and upgrading the customer loyalty system;
- ▶ Rationalizing our operations, which included cost rationalization, restriction of investment volume, and efficient management of key risks.

These measures ensured stable operations of the Mercator Group despite the extremely strenuous economic circumstances. Net revenues from sales, assuming constant exchange rates, reached EUR 2.7 billion, which is 0.6 percent more than in 2008. Gross cash flow from operating activities before rental expenses (EBITDAR) amounted to EUR 196.6 million, which is only 0.8 percent less than in 2008.

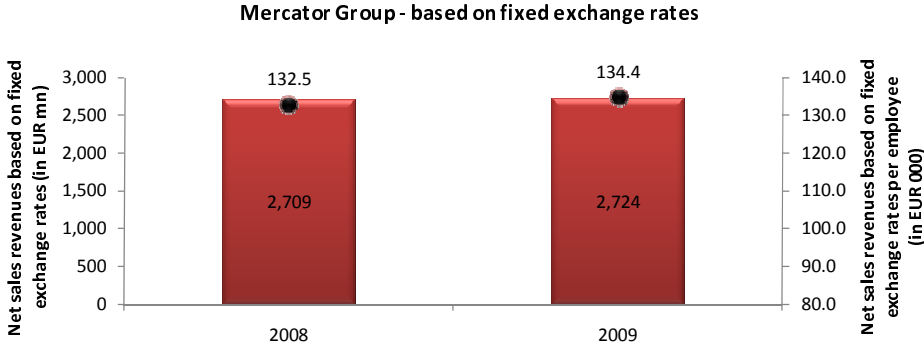
In 2009, Mercator Group continued to pursue its development activities, although investment volume was considerably decreased as a measure to counter the effects of the crisis. By investing approximately EUR 157.4 million, mostly into retail network development, the Group activated over 95.7 thousand square meter of gross sales area in 2009. Furthermore,

the Group pursued its internationalization strategy and entered Bulgaria and Albania, opening its first stores in these two markets. Moreover, an independent company was founded in Republic of Kosovo in 2009 to take the responsibility of Mercator's future expansion to this market as well. In order to consolidate and increase the market share in Croatia, a very important strategic alliance with the Croatian retailer Getro was agreed upon at the end of 2009 and effected in February 2010.

Following is an analysis of performance in 2009, focused on the Mercator Group. The company Poslovni sistem Mercator, d.d., has a double role in the Mercator Group: it is the parent company holding all ownership shares in the Group's subsidiaries; simultaneously, it is an operative company, carrying out all trade and other activities in Slovenia. Thus, employing the financial statements of the company Poslovni sistem Mercator, d.d., for economic analysis of Mercator Group's operations is inappropriate. For such analysis, it would be more reasonable to apply only the consolidated financial statements that represent the performance of the Mercator Group as a uniform business entity.

► **Sales and productivity**

Amounting to EUR 2,643,315 thousand, Mercator Group sales revenues in 2009 are 2.4 percent below the 2008 figure. Assuming constant exchange rates, the revenues in 2009 would have been 0.6 percent higher than in the year before.



In 2009, 34.0 percent of Mercator Group sales revenues were generated in foreign markets, which is 0.2 percentage points less than in 2008. Despite harsh economic conditions, operations were highly successful in Slovenian and Serbian market; Croatia and Bosnia and Herzegovina, however, were more severely affected by the negative effects of business and other conditions. In addition to the economic crisis, sales in Croatia were affected by the response of the consumers to new tensions in political relations with Slovenia, while in Bosnia and Herzegovina sales were strongly affected by the changes in the volume and composition of consumption, resulting from macroeconomic hardship. Other markets, i.e. Montenegro, Bulgaria, and Albania, are still in the early stages of development when sales are low, and their performance was consistent with this.

As a result of our efforts to optimize operations in all markets, labor productivity was further improved in 2009; assuming constant exchange rates, physical productivity of labor rose by 1.4 percent relative to the year 2008.

### ► **Operating costs and cost efficiency**

Mercator Group' measures adopted to counter the economic crisis included numerous activities intended for adjusting the offer to consumers in economic hardship, as well as many activities aimed at rationalizing the operations. Thus, the Group mitigated the pressures on the profit margin while still providing favorable offer and maintaining loyalty of its customer. However, cost savings could not fully compensate for the pressures on gross profit and as a result, it dropped by 4.6 percent in 2009 relative to the year before.

The Group was highly committed to cost rationalization with key types of costs. The sum of labor costs, and costs of material and services without rents in 2009 was nominally 2.4 percent lower than the sum of the same costs in 2008. The effects of cost rationalization are not fully manifested as the Group incurred considerable entry costs related to the preparation and launch of operations in two new markets in 2009 (Bulgaria and Albania). Costs of marketing services are a major category of cost of services and they played a key role in maintaining the loyalty of our consumers and retaining retail revenues. Moreover, relative cost efficiency was also affected by the drop in net sales revenues, as well as the additional time required to provide a normal volume of operating activities and for new investments to reach the breakeven point, which again is a result of exacting market conditions, particularly in foreign markets.

### ► **Ability to generate cash flows and returns**

In 2009, Mercator Group managed to retain stable cash flow generation with its operating activities, which gave the Group adequate financial power and furnished it with development potential.

Gross cash flow from operating activities before rents (EBITDAR) of the Mercator Group, assuming constant exchange rates, reached EUR 196,604 thousand in 2009, which is only 0.8 percent less than in 2008. Gross cash flow from operating activities, assuming constant exchange rates, amounted to EUR 171,469 thousand in 2009, which is 3.0 percent less than in the year before.

In 2009, Mercator Group's results from operating activities (operating profit) amounted to EUR 71,842 thousand, which is 28.4 percent less than in 2008. In 2008, the operating profit was notably affected by net proceeds from disposal of fixed assets (property, plant, and equipment), and other net revenues generated by extraordinary or non-recurring events (elimination of provisions). Excluding the extraordinary effects in both years, the comparable results from operating activities (operating profit) would have amounted to EUR 73,502 thousand, or 18.5 percent less than in 2008 (EUR 90,180 thousand).

Mercator Group's profit before income tax in 2009 amounted to EUR 25,196 thousand, which is 49.6 percent less than in 2008. In addition to the extraordinary effects described above, profit before income tax was also affected by net proceeds from disposal of financial assets, which were quite considerable in 2008 and almost negligible in 2009. Eliminating the extraordinary effects in both years, the comparable profit before income tax in 2009, amounting to EUR 27,056 thousand, is 20.5 percent lower than in 2008 (EUR 34,044 thousand).

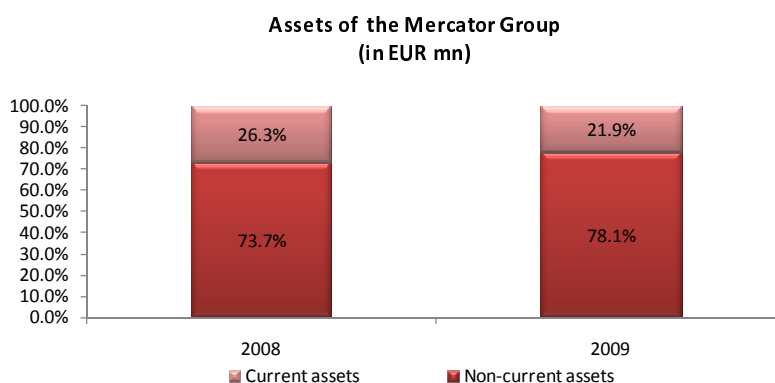
As for the profitability of operation in 2009, the Group generated a positive result in two of its largest markets: Slovenia and Serbia. Croatia and Bosnia and Herzegovina, however, presented some problems to the overall performance. In Croatia, revenues dropped both

because of harsh economic conditions and because of consumers' response to the political tension between that country and Slovenia since the end of 2008. This decline in revenues could not be fully compensated for by cost rationalization, the result was negative. Similar situation took place in Bosnia and Herzegovina where the revenues actually increased, but the pressures on profit margins due to the decline in consumption and the change in its composition were too strong to be fully compensated with cost rationalization. In addition, the company M - BL, d.o.o., just launched its operations by opening the first major shopping center in Banja Luka in 2009, and thus its performance was burdened by the startup costs. Performance in other markets (Montenegro, Bulgaria, and Albania) was also encumbered with high costs of entry into the market, and opening of a major format retail unit in Podgorica; given the low revenues, performance in the first year of operation was negative.

Performance in all market of our operations was also affected by the fact that the time required for normal activation of new retail facilities has extended as a result of harsh economic conditions. Given the new patterns of consumption and the decline thereof, new investments completed in 2008 and 2009 will require a longer startup period to reach the revenues that provide normal performance, than required during economic expansion.

### ► Composition of assets

As at December 31<sup>st</sup> 2009, Mercator Group balance sheet total amounts to EUR 2,476,348 thousand, which is 2.5 percent less than at the end of 2008.

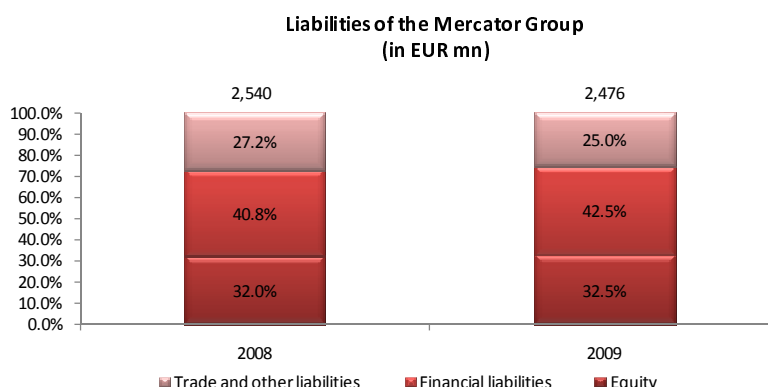


As at December 31<sup>st</sup> 2009, the value of Mercator Group **noncurrent assets** amounts to EUR 1,933,331 thousand, which is 3.2 percent more than at the end of 2008. The largest share among noncurrent assets is property, plant, and equipment, valued at EUR 1,863,291 thousand at December 31<sup>st</sup> 2009, or 5.2 percent more than at the end of 2008. The change in the value of Mercator Group noncurrent assets as at December 31<sup>st</sup> 2009 relative to the figure as at December 31<sup>st</sup> 2008 is mostly the result of investment into new retail facilities.

The value of **current assets** of Mercator Group as at December 31<sup>st</sup> 2009 amounts to EUR 543,017 thousand, which is EUR 123,794 thousand or 18.6 percent less than as at the end of 2008. The most notable effect causing the decline in value was the drop in trade and other receivables which dropped by 33.8 percent relative to the value as at December 31<sup>st</sup> 2008. Lower receivables are an effect of a decline in wholesale activities in some business segments, active management of working capital, and highly committed credit risk management activities. Within current assets, we saw an increase in inventories by 7.2 percent relative to the figure as at December 31<sup>st</sup> 2008, mostly as a result of opening several retail units in the last quarter of 2009: hypermarket and Intersport Zaprešič, Roda Center

Senta, Roda Center Sombor, hypermarket in Podgorica, hypermarket in Stara Zagora, hypermarket and Intersport in Tirana, etc.).

## ► Equity and liabilities



As at December 31<sup>st</sup> 2009, debt-to-equity ratio of the Mercator Group amounted to 1:1.25 (compared to 1:1.22 at the end of 2008). The ratio is a quotient between equity which includes share capital as reported in financial statements and long-term provisions, and debt which includes long-term and short-term finance liabilities.

Financial liabilities of the Mercator Group amount to EUR 1,051,402 thousand. Compared to the beginning of 2009, they have increased by EUR 15,818 thousand, or 1.5 percent. In the composition of financial liabilities as at December 31<sup>st</sup> 2009, long-term (non-current) financial liabilities represent 65 percent, with the short-term (current) liabilities amounting to the remaining 35 percent of total liabilities. As at the end of 2008, long-term liabilities amounted to 60 percent and the short-term liabilities represented 40 percent of total liabilities. The change in the composition of financial assets as at December 31<sup>st</sup> 2009 compared to the composition as at the end of 2008 clearly points to the efficiency of our financial risk management efforts and a sound relationship with our financial partners. Both enabled our Group smooth financial operation even during the global financial crisis.

Trade and other payables of the Mercator Group declined by EUR 74,271 thousand compared to the end of 2008. The decrease in value of trade and other payables is predominantly the effect of lower payables related to investment in progress at the end of 2009 (EUR 46,593 thousand) compared to 2008 (EUR 107,940 thousand). The value of trade and other payables excluding those related to investment in progress as at December 31<sup>st</sup> 2009 amounts to EUR 481,340 thousand, which is 2.7 percent less than the comparable figure at the end of 2008; this is consistent with the dynamics of our operations.

## Key Financial Indicators

	Mercator Group		Poslovni sistem Mercator, d.d.	
	2008	2009	2008	2009
<b>Indicators of profitability</b>				
Return on equity	5.6%	2.6%	4.5%	2.5%
Return on sales	1.5%	0.8%	1.8%	1.1%
Gross profit margin	6.5%	6.4%	7.6%	7.6%
<b>Indicators of financial structure</b>				
Financial liabilities / equity	1.27	1.31	0.97	0.93
Equity and provisions to total equity and liabilities	33.3%	34.0%	39.8%	42.0%
Financial liabilities to total equity and liabilities	40.8%	42.5%	37.2%	37.4%
Trade and other payables to total equity and liabilities	23.6%	21.3%	20.9%	18.4%
<b>Indicators of operating efficiency and productivity</b>				
Labour costs per hours worked (in 000 EUR)	14.2	13.7	17.6	17.2
Net sales revenues / labour costs	9.3	9.5	8.4	8.6
Net sales revenues per employee per hours worked (in 000 EUR)	132.5	130.3	147.4	148.0
Value added per employee per hours worked (in 000 EUR)	22.8	22.0	27.3	27.4
Administrative expenses / net sales revenues	4.2%	4.1%	4.4%	4.4%
Gross cash flow from operating activities before rental expenses / net sales revenues	7.3%	7.2%	7.0%	7.3%

## CORPORATE SOCIAL RESPONSIBILITY

Socially accountable action has long surpassed the mere system of communication management of the values of the company and its stakeholders, to become a real value of the company, which is managed and developed through a wide array of corporate governance.

Sponsorship, donations, and participation in humanitarian campaigns are an important part of the strategy of comprehensive socially responsible conduct of the Mercator Group.

In Slovenia, our traditional central humanitarian campaign was dedicated to those who are unexpectedly facing social distress due to the effects of the global economic crisis. The campaign called "Kind Deeds Stem from Kind Words" collected one hundred thousand kind words as anyone was given the opportunity to symbolically support our campaign by selecting a kind word from Mercator webpage or special screens installed at Mercator shopping centers. The words most often selected were "kindness, safety, and love". We worked with our partners and suppliers to turn kind words into actions and provided actual aid for over one hundred thousand people. We donated half a million euros worth of food, school accessories for children, hygiene or body care products, and other essentials to Red Cross and Caritas Slovenia.

In addition, we supported numerous humanitarian, sports, culture, scientific, educational, and other projects and organizations engaging in socially responsible efforts in all markets of our operations.



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## CARE FOR THE ENVIRONMENT

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Mercator operations are conducted while bearing in mind the generations to come. We are aware that as Slovenia's largest company, which is furthermore increasingly becoming an international corporation, we are in a position to contribute substantially to the protection and preservation of the environment, even though our activities are not among those most harmful to it. As a **socially responsible enterprise aware of the importance of relieving the burden brought upon the environment**, we are continuously improving our business processes to make them more environmentally friendly.

The **activities of reducing the use of raw materials and energy** included the following in 2009:

▶ To reap maximum success from our efforts to preserve the clean environment and reduce the impact of our activities, Mercator, d.d., decided to introduce systemic management of environmental impact as provided by the environmental management system in compliance with the ISO 14001 standard. Our efforts were confirmed by awarding of the ISO 14001 certificate for environmental management system.

**Mercator, d.d., is the only trade company in Slovenia, engaging in wholesale or retail of fast-moving consumer goods, to be awarded the ISO 14001 certificate.**

- ▶ The company Poslovni sistem Mercator, d.d., received an award for ranking second among the finalists for the Slovenian Award of Social Accountability HORUS 2009 in the category of large companies.
- ▶ We have prepared a Waste Management Plan for the period 2009-2012, which also includes measures for preventing and reducing the generation of waste.
- ▶ We have established a waste battery management system and enabled the consumers to dispose of waste batteries (both dry-cell and wet-cell / car batteries) free of charge at our locations where such batteries are sold.
- ▶ In order to promote rational use of energy at our retail units, we compiled a Handbook of Efficient Energy Use for our managers and employees.
- ▶ In order to improve the efficiency of system management and maintenance, we compiled Maintenance Technician's Instructions for Efficient Use of Power and System Maintenance.
- ▶ By implementing the organizational measures for efficient use of energy in 2009 (optimization of lighting, heating, air conditioning, and refrigeration), we cut power consumption at locations under observation by approximately 3,000,000 kWh, thus indirectly reducing carbon dioxide emissions by 1,600 tons.
- ▶ By eliminating energy waste and implementing a change in power consumption groups, we cut our power costs.
- ▶ In order to reduce the use of fuels for heating, we are introducing central control systems at major Mercator centers.
- ▶ In order to comply with the provisions of the Regulation on Light Pollution and reduce the use of power, we prepared an internal lighting standard for lighting elements of complete graphical image of a company Poslovni sistem Mercator, d.d.
- ▶ As a result of the implementation of transport rout planning support, total number of kilometers clocked up in 2009 was reduced by 3.2 million compared to 2007. As a result, emissions of exhaust fumes into the air were also reduced.
- ▶ Reusable shopping bags were included in our regular offer in order to help our customers take a step towards a more environmentally friendly daily conduct.

- ▶ Mercator website was extended with information on environment protection and our activities related to the care for the environment.
- ▶ We hosted the meeting of the Slovenian Society of United Nations for Sustainable Development (United Nations Global Compact).

## **Environmental policy and our business partners**

Mercator Group has precisely defined its environmental policy which is being consistently pursued as one of the key principles of our operations. Thus, we have already made a commitment to continuously improve our environmental management, prevent pollution, as well to comply with all legislative provision relevant to the Group. Our environmental policy also represents a framework for cooperation with our business partners on the issues concerning environmental management.

Business partners of the company Mercator, d.d., were informed about our environmental policy and particularly on the following:

- ▶ we shall comply with the environment protection policies laid out in the company environmental program both with regard to existing activities, services, and products, and development of new ones;
- ▶ we shall include our business partners in our efforts for more environmentally friendly operations of our company; and
- ▶ we shall educate and raise the awareness among our employees and partners about their responsibility towards the environment and about the impacts of our activities on the environment.

Mercator is a member of the Slovenian Association of United Nations Global Compact (Slovenian society of UN for sustainable development); our business partners are also members of this Society. In 2008, we also signed the REAP (Retailers Environmental Action Plan) document within the European Chamber of Commerce). The aim of the initiative is to reduce the negative impact on the environment, exchange of best practices between European trading companies, as well as devising common views regarding the measures, propositions and motives of the European Commission, which affect the trade sector in that field.

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## **EMPLOYEE DEVELOPMENT**

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### **Number of employees**

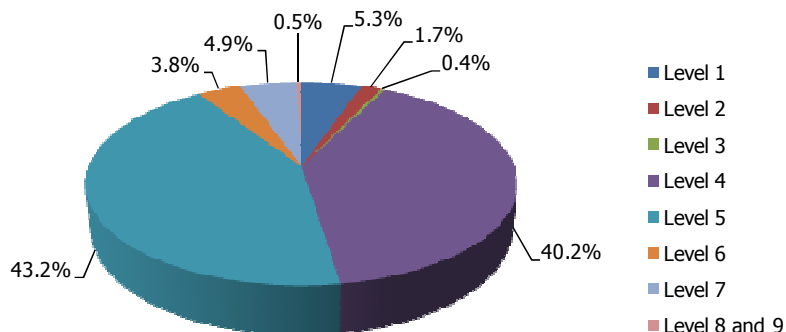
As at December 31<sup>st</sup> 2009, Mercator Group had 21,404 employees, of which 40.1 percent were employed abroad. The controlling company Poslovni sistem Mercator, d.d., employs 12,297 workers which is 57.5 percent of the Group's total.

## Number of employees:

	Number of employees as at December 31 <sup>st</sup> 2009	Number of employees based on hours worked in 2009	Number of employees as at December 31 <sup>st</sup> 2008	Number of employees based on hours worked in 2008
Poslovni sistem Mercator, d.d.	12,297	11,794	12,737	12,075
Mercator IP, d.o.o.	200	117	34	28
Mercator - S, d.o.o.*	3,714	3,722	1,009	992
M - Rodić, d.o.o.	-	-	2,664	2,675
Mercator - H, d.o.o.	3,023	2,823	3,347	3,055
Mercator - BH, d.o.o.	1,024	980	1,183	980
M - BL, d.o.o.	241	162	2	1
Mercator - Mex, d.o.o.	368	253	292	277
Mercator - B, e.o.o.d.	76	49	0	0
Mercator - A, sh.p.k.	131	34	-	-
Mercator - Optima, d.o.o.	21	20	22	19
Eta, d.d.	198	189	204	194
Mercator - Emba, d.d.	111	123	124	123
Interier, d.o.o.	-	-	17	18
Evolution, d.d.	-	-	1	1
Pekarna Grosuplje, d.d.	-	-	0	2
<b>MERCATOR GROUP</b>	<b>21,404</b>	<b>20,266</b>	<b>21,636</b>	<b>20,438</b>

\*Company Mercator - S, d.o.o., took employees of company M - Rodić, d.o.o.

## Breakdown by level of education



Most Mercator employees have completed fifth-degree education. Composition by education is improving, however, as progress is notable particularly with employees holding 6<sup>th</sup>, 7<sup>th</sup> and 8<sup>th</sup> degree education.

## Absenteeism due to illness

Total rate of illness-related absenteeism at Mercator Group in 2009 amounted to 5.26 percent, of which 2.88 percent was charged to the Group companies, and 2.38 percent was charged to Health Insurance Institutes. Total illness-related absenteeism rate was lower than in 2008 when it reached 5.34 percent. Total number of employee sick leave hours was 2,282,728 hours, which is less than in 2008 when the figure amounted to 2,295,537 hours.

At the company Poslovni sistem Mercator, d.d., where the average age of employees is the highest, total rate of illness-related absenteeism in the period at hand amounted to 6.17 percent, of which 3.47 was charged to the company and 2.70 percent was charged to the

Health Insurance Institute. Total rate of illness-related absenteeism is lower than in 2008. Total number of employee sick leave hours was 1,567,942, which is less than in 2008 when employees had a total of 1,603,442 sick leave hours. Reduced rate of absenteeism is the result of the project "Promoting Health at Mercator."

## Employment of disabled persons

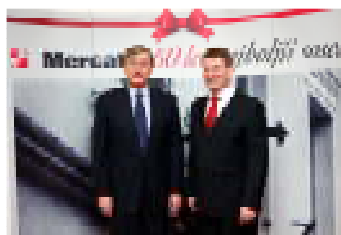
Mercator Group employs a total of 901 disabled persons, of which 781 are employed at the parent company, 112 in non-trade activities (out of which 90 in Mercator social enterprise), and 8 in foreign markets. The share of disabled persons in Mercator Group in year 2009 remained at the level of year 2008. The share of disabled persons employed at the controlling company amounts to 6.35 percent. The share required by the disabled person employment quota for trade industry is 2.0 percent.

## Employee Relations

### ▶ Talent development and career planning

In 2009, the year of crisis, talent development and career planning was adapted to the prevailing conditions.

▶ We organized a **key employee council** to celebrate Mercator's **60<sup>th</sup> anniversary**. The council, attended by over 1,700 key employees, also hosted the President of the Republic of Slovenia, Dr. Danilo Türk.



▶ In Croatia and Serbia, **store manager training** was carried out. In Slovenia, we provided a somewhat abridged program of **deputy store manager training** in which one third of deputies for market program were included.

▶ In Slovenia, we organized **business workshops for directors and heads of services or departments**. This time, workshops took place at our head offices in Ljubljana in order to save on travel expenses and lease of venues.

▶ **Mercator International Business Academy** hosted the third group of 29 promising employees. Highly talented employees from nontrade subsidiaries were included in the Academy for the first time.



▶ The scope of training, number of attendants and costs of training declined slightly in 2009; however, **all essential training requirements** in the Mercator Group were successfully met both with regard to formal education and training and with regard to mandatory and functional training and training for personal development.

▶ 316 executive, managerial, and expert employees, which are in every day relations with suppliers, attended the seminar "**Presentation of Commitments to the Competition Protection Office**".

- ▶ 1,107 employees from administrative services completed the training on **occupational health and safety** and **fire safety**, in the form of self-training which included pre-programd materials and a relevant test.
- ▶ We have carried on the selection process and training of new coaches for our **coaching and mentorship network** in retail. A total of 580 fully trained coaches are currently active in Mercator Group; in 2009, they trained a total of 9,771 sales employees. The coaches regularly update their training in cooperation with our suppliers.
- ▶ In Slovenia, we organized **training** for 144 employees from Bulgaria, Albania, Bosnia and Herzegovina, and Montenegro.
- ▶ 743 high school and university students were admitted for **practical training**.
- ▶ We also encourage formal education of our employees: 278 were enabled to attend **part time studies**.
- ▶ We organized the **9<sup>th</sup> meeting of in-house instructors** at Mercator, d.d. The meeting was attended by nearly 400 in-house instructors. 27 employees received awards for special achievements and for their work as mentors, lecturers, instructors, or coaches.

#### ▶ **Staffing and recruitment**

▶ Economic crisis profoundly affected staffing and recruitment at the company. Since hiring was scaled down and often completely halted, the number of employment applications soared. At the company Poslovni sistem Mercator, d.d., 8,413 job applications were received, and 823 applicants were newly employed, most of them in retail. In 2009, staffing was also focused on foreign markets: 814 people were hired in Bosnia and Herzegovina, Bulgaria, Albania, and Montenegro, combined.

▶ We have set up our **employment portal** at [www.mercator.si/kariera](http://www.mercator.si/kariera), and revised the HRM website in English. Thus, we cut costs of HRM advertising.



▶ We also adopted the **HRM standard** for the company Poslovni sistem Mercator, d.d.

#### ▶ **Motivation and compensation**

▶ Responding to the harsh economic conditions and a decline in the standard of living, the company Poslovni sistem Mercator, d.d., decided to implement a **solidarity redistribution of salaries** and performance bonuses from those with higher total rewards to those with lower ones. Hence, gross compensation of the Management Board President was cut by 25 percent, salary of Management Board members were cut by 15 percent, and salaries of other employees with individual employment contracts were reduced by 10 percent. Other employees in the highest salary categories saw their performance bonus cut by 3-5 percent, while the employees in the lower salary categories saw an increase in this bonus by 3-7 percent.

▶ Representatives of relevant trade unions were invited to take part in the **expert task force on total reward system**, whose purpose is constant monitoring and improvement of the total reward system at the parent company.

▶ An award ceremony was held in June. Twenty most distinguished employees were presented with the traditional "**Mercator Award**" for 2008.



▶ We completed or **motivation trips to Vogel** which were attended by 17 international teams of managers, or a total of 298 employees.

▶ We organized the third competition for **The Best Boss**, selecting 16 "best bosses" at the parent company for the year 2009.

▶ 2009 was a successful year for our HRM officers, as they received the following awards:

- **Human Resource Manager of the Year 2009**, awarded by the company Planet GV, was presented to Management Board member, Vera Aljančič Falež.
- Slovenian Institute for Adult Education presented an **Award for distinguished expert achievements** in the field of employee training and education at Mercator.
- Mercator project "Humanitarian Aspect of HRM Function at Mercator" received the **award for innovative human resource practice**, presented by the company Forum Media.
- HRM project **Promoting Health at Mercator** won the 2<sup>nd</sup> prize HRM projects in 2009; the prize is awarded by the company Planet GV.

### ▶ **Dialogue with the employees**

▶ From March 20<sup>th</sup> to June 26<sup>th</sup> 2009, **annual meetings** of leaders with all employees took place in all markets.

▶ In Slovenia, five regular and one special editions of our **internal magazine** were published. In Serbia and Croatia, five regular and two special editions were issued, and in Bosnia and Herzegovina and Montenegro, three editions were published.



▶ We have continued our regular monthly **meetings with representatives of relevant trade unions** and organized **meetings with the Management Board** upon discussions on quarterly business reports.

▶ Retail and human resource management visited several hypermarkets in Slovenia in the course of fall 2009, to **talk to the employees** on their work, possibilities of improvement, and work conditions.

### ▶ **Corporate culture and international development**

▶ At the end of May, traditional **Mercator sports games** took place.

▶ As a part of the **Mercator – family-friendly company**, two brochures were published: "Mercator, family-friendly company – benefits for the entire family", received by all employees; and "Things to Know When Expecting a Baby", presented to our female employees before going on maternity leave.

▶ Mercator's encouraging attitude towards the families of our employees was also reflected in an increase in **maternity leaves**. In 2009, their number **rose by 17 percent** compared to the year before.

▶ Mercator **standards and code of conduct for employees** were implemented and transferred in various ways and with various methods to the markets of Bulgaria and Albania.

▶ In Serbia, **Open Door Day** was held on September 1<sup>st</sup> for the **children of our employees**. The children, guided by our executive and expert employees, learned about the work of their parents.



▶ Due to the bleak economic conditions and outlooks, Mercator Day was not organized this year. Instead, employees at the company Poslovni sistem Mercator, d.d., were presented with e-coupons worth **EUR 60**.

### ▶ **Occupational health and safety**

▶ The project "**Promoting health at the company Mercator, d.d.**" involves various activities. We started off by organizing regular exercise for our employees; we launched the first Mercator regional exercise center; we hold discussions with the employees with most sick leave hours; we added the section on health to our internal magazine Časomer ("The Timekeeper"); we set up a phone number for medical advice; female employees aged over 45 are invited to attend seminars on breast cancer; and we appointed an ergonomics team to improve the working environment, making it more worker-friendly.



▶ On September 21<sup>st</sup> 2009, **3<sup>rd</sup> Mercator HRM Days** were held at Cankarjev Dom in Ljubljana. The central topic of the round table was "Health – a Common Concern of the Employees, Employers, and the Government".

▶ **Mercator hiking society**, with a membership of 320, organized 12 trips attended by a total of 963 hikers.

▶ In 2009, **Mercator Humanitarian Foundation** provided aid to 141 applicants.

### ▶ **Social enterprise**

▶ At the end of 2009, Mercator social enterprise had a total of 200 employees, of which 90 were persons with disabilities.

▶ Consistently with the Business Plan of expansion and transfer of some service activities from the parent company to the social enterprise, employees of the latter perform services of archiving, occupational health and safety tasks, fire safety tasks, decoration and flower arrangement services, mostly commissioned by the parent company.

▶ Manufacturing activity of the social enterprise includes development of cosmetics products and a line of interior decoration textile products under the brand **Dvorec Trebnik** (The Trebnik Mansion). As a result of the transfer of manufacturing activities, employees of the

social enterprise also prepare and pack fresh fruit and vegetables. In September, fresh program was extended with the activity of drying and packaging dried fruit. Their products are marketed mostly to the parent company.

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## ANTICIPATED ECONOMIC CONDITIONS AND PLANS FOR 2010

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Business and economic environment is expected to remain equally challenging in 2010 as it was in 2009. Sluggish recovery of economy will notably affect the composition and volume of consumption. Conditions in financial markets will leave the access to long-term financing sources restricted and the pressure on interest rate margins high. Macroeconomic situation in many countries in the region of Mercator Group operations will remain troubled. In 2010, low or negative GDP growth is expected in all relevant markets, paired with low inflation resulting from economic development in the global markets. Such circumstances will require further active management and hedging of key business and financial risks.

Net sales revenues of the Mercator Group are planned at EUR 2.75 billion for 2010. Planned revenue growth is influenced by the economic conditions, changes in consumption and lower investment activity. In 2010, no major changes in exchange rates are planned.

In 2010, Mercator Group is planning gross cash flow from operating activities before rental expenses – EBITDAR in the amount of EUR 202.6 million. Planned growth of gross cash flow is mainly the result of planned activities of business rationalization, reaping the economies of scale in all markets of our operation, and development and investment activities.

Mercator Group's net profit is planned to amount to EUR 21.9 million in 2010. As in 2009, performance in 2010 will be challenged by difficult economic conditions, changes in the volume and composition of consumption, and extensive investment into more competitive and favorable offer for the consumers.

Total investment at Mercator Group in 2010 is planned at EUR 120 million, which falls within the Group's own financing ability. Thus, net financial debt of the Group will not increase in 2010, according to plan.

By the end of 2010, Mercator Group is planned to have 22,167 employees. Of these, nearly 42 percent of all employees will work in markets outside Slovenia at the end of 2010.

In order to mitigate the negative effects of the economic crisis, Mercator Group prepared three sets of **measures** for 2010:

- ▶ adjusting our offer to the consumers:
  - by improving price competitiveness,
  - by adjusting our offer and assortment, and
  - by upgrading the customer loyalty system;
- ▶ business rationalization:
  - improving productivity and rationalizing costs,
  - restricting investment, and
  - risk management;

► improving flexibility:

- by reorganizing the Mercator Group,
- exploiting opportunities in the region, and
- preparing for the option of disposal/monetization of commercial real estate.

Close attention will also be paid to proactive financial risk management, particularly hedging credit risk, liquidity risk, and foreign exchange risk.

Considering the expectations of extremely harsh business conditions, and business and financial risks to which the Group is exposed, the company Management Board finds the 2010 Business Plan an ambitious agenda consistent with Mercator Group's pursuit of its strategic policies.

Due to high uncertainty with regard to the assumptions on the economic conditions and environment in the year 2010, the company Management Board will reevaluate the viability of the planned goals each quarter, while taking into account any deviations between the anticipated and actual influences from the economic environment; should such reevaluations be necessary, reports thereof will be included in the quarterly business reports.

Mercator Group Plan for 2010 does not include the effects of the strategic combination with the company Getro, d.d., effected on February 17<sup>th</sup> 2010.



# **Financial report**



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# **FINANCIAL REPORT OF THE MERCATOR GROUP**

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## Consolidated statement of financial position

As at 31 December

EUR thousand

	Note	2009	2008
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	15	1,863,291	1,771,963
Investment property	17	4,127	9,563
Intangible assets	16	51,995	78,196
Deferred tax assets	20	8,086	8,380
Trade and other receivables	22	359	384
Available-for-sale financial assets	18	5,473	4,824
		<b>1,933,331</b>	<b>1,873,310</b>
<b>Current assets</b>			
Inventories	21	292,050	272,391
Trade and other receivables	22	230,747	347,741
Current tax assets		2,639	809
Derivative financial instruments	19	737	-
Cash and cash equivalents	23	16,844	45,870
		<b>543,017</b>	<b>666,811</b>
<b>Total assets</b>		<b>2,476,348</b>	<b>2,540,121</b>
<b>EQUITY</b>			
	<b>24</b>		
Ordinary shares		157,129	157,129
Share premium		198,872	198,848
Treasury shares		(3,235)	(3,250)
Revenue reserves		270,194	267,640
Fair value reserve		186,029	188,751
Retained earnings		8,697	-
Profit for the period		21,232	24,682
Currency translation reserve		(33,782)	(21,708)
<b>Total equity attributable to equity holders of the Company</b>		<b>805,136</b>	<b>812,092</b>
<b>Non-controlling interest</b>		<b>254</b>	<b>2,008</b>
<b>Total equity</b>		<b>805,390</b>	<b>814,100</b>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Trade and other payables	28	2,872	2,271
Financial liabilities	26	683,547	622,787
Deferred tax liabilities	20	49,326	52,496
Provisions	27	37,188	31,415
		<b>772,933</b>	<b>708,969</b>
<b>Current liabilities</b>			
Trade and other payables	28	525,061	599,933
Current tax liabilities		164	724
Financial liabilities	26	367,855	412,797
Derivative financial instruments	19	4,945	3,598
		<b>898,025</b>	<b>1,017,052</b>
<b>Total liabilities</b>		<b>1,670,958</b>	<b>1,726,021</b>
<b>Total equity and liabilities</b>		<b>2,476,348</b>	<b>2,540,121</b>

## Consolidated income statement

EUR thousand	Note	2009	2008
Revenue	9	2,643,315	2,708,560
Cost of sales	11	(2,474,106)	(2,531,184)
<b>Gross profit</b>		<b>169,209</b>	<b>177,376</b>
Administrative expenses	11	(109,955)	(110,313)
Other income	10	12,588	33,264
<b>Results from operating activities</b>		<b>71,842</b>	<b>100,327</b>
Finance income	13	10,245	20,103
Finance expense	13	(56,891)	(70,437)
<b>Net finance expense</b>		<b>(46,646)</b>	<b>(50,334)</b>
<b>Profit before income tax</b>		<b>25,196</b>	<b>49,993</b>
Income tax expense	14, 20	(4,077)	(9,232)
<b>Profit for the period</b>		<b>21,119</b>	<b>40,761</b>
Profit attributable to:			
Owners of the Company		21,232	40,846
Non-controlling interest		(113)	(85)
Basic and diluted earnings per share (in EUR)	25	5.7	11.0

## Consolidated statement of comprehensive income

EUR thousand	2009	2008
Profit for the period	21,119	40,761
<b>Other comprehensive income</b>		
Foreign currency translation differences for foreign operations	(12,072)	(17,487)
Change in fair value of available-for-sale financial assets	841	(13,489)
Change in fair value of available-for-sale financial assets transferred to profit or loss	-	(3,997)
Effective portion of changes in fair value of cash flow hedges	(125)	(10,760)
Change in fair value of cash flow hedges transferred to profit or loss	(1,337)	1,391
Revaluation of property	-	181,295
Deferred tax	1,983	(29,069)
<b>Other comprehensive income for the period</b>	<b>(10,710)</b>	<b>107,884</b>
<b>Total comprehensive income for the period</b>	<b>10,409</b>	<b>148,645</b>
Attributable to:		
Owners of the Company	10,520	148,666
Non-controlling interest	(111)	(21)

## Consolidated statement of changes in equity

EUR thousand	Ordinary shares	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Currency translation reserve	Total equity attributable to equity holders of the Company	Non-controlling interest	Total
<b>Balance at 1 January 2008</b>	<b>157,129</b>	<b>198,848</b>	<b>(3,250)</b>	<b>243,309</b>	<b>68,078</b>	-	<b>26,047</b>	<b>(4,223)</b>	<b>685,938</b>	<b>2,258</b>	<b>688,196</b>
Restatement:											
Adjustment according to IAS 8.44	-	-	-	-	(1,248)	(3,905)	-	-	(5,153)	(8)	(5,161)
<b>Balance at 1 January 2008 (restated)</b>	<b>157,129</b>	<b>198,848</b>	<b>(3,250)</b>	<b>243,309</b>	<b>66,830</b>	<b>(3,905)</b>	<b>26,047</b>	<b>(4,223)</b>	<b>680,785</b>	<b>2,250</b>	<b>683,035</b>
Profit for the period	-	-	-	-	-	-	40,846	-	40,846	(85)	40,761
Other comprehensive income	-	-	-	-	121,921	3,384	-	(17,485)	107,820	64	107,884
<b>Total comprehensive income for the period</b>	-	-	-	-	<b>121,921</b>	<b>3,384</b>	<b>40,846</b>	<b>(17,485)</b>	<b>148,666</b>	<b>(21)</b>	<b>148,645</b>
<b>Transactions with owners, recorded directly in equity</b>											
<b>Contributions by and distributions to owners</b>											
Dividends to equity holders	-	-	-	-	-	(15,823)	-	-	(15,823)	-	(15,823)
Transfer of profit for the period to retained earnings	-	-	-	-	-	26,047	(26,047)	-	-	-	-
Allocation of disposable income following the Management / Supervisory Board resolution	-	-	-	16,164	-	-	(16,164)	-	-	-	-
Allocation of disposable income following the Shareholders' Assembly resolution	-	-	-	8,167	-	(8,167)	-	-	-	-	-
<b>Total contributions by and distributions to owners</b>	-	-	-	<b>24,331</b>	-	<b>2,057</b>	<b>(42,211)</b>	-	<b>(15,823)</b>	-	<b>(15,823)</b>
<b>Changes in ownership interests in subsidiaries that do not result in a loss of control</b>											
Acquisition of non-controlling interest	-	-	-	-	-	(1,536)	-	-	(1,536)	(221)	(1,757)
<b>Total transactions with owners</b>	-	-	-	<b>24,331</b>	-	<b>521</b>	<b>(42,211)</b>	-	<b>(17,359)</b>	<b>(221)</b>	<b>(17,580)</b>
<b>Balance at 31 December 2008</b>	<b>157,129</b>	<b>198,848</b>	<b>(3,250)</b>	<b>267,640</b>	<b>188,751</b>	-	<b>24,682</b>	<b>(21,708)</b>	<b>812,092</b>	<b>2,008</b>	<b>814,100</b>

## Consolidated statement of changes in equity (continued)

EUR thousand	Ordinary shares	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Currency translation reserve	Total equity attributable to equity holders of the Company	Non-controlling interest	Total
<b>Balance at 1 January 2009</b>	<b>157,129</b>	<b>198,848</b>	<b>(3,250)</b>	<b>267,640</b>	<b>188,751</b>	<b>-</b>	<b>24,682</b>	<b>(21,708)</b>	<b>812,092</b>	<b>2,008</b>	<b>814,100</b>
<b>Total comprehensive income for the period</b>											
Profit for the period	-	-	-	-	-	-	21,232	-	21,232	(113)	21,119
Other comprehensive income	-	-	-	-	(2,722)	4,084	-	(12,074)	(10,712)	2	(10,710)
<b>Total comprehensive income for the period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(2,722)</b>	<b>4,084</b>	<b>21,232</b>	<b>(12,074)</b>	<b>10,520</b>	<b>(111)</b>	<b>10,409</b>
<b>Transactions with owners, recorded directly in equity</b>											
<b>Contributions by and distributions to owners</b>											
Dividends to equity holders*	-	-	-	-	-	(16,754)	-	-	(16,754)	-	(16,754)
Treasury shares disposal	-	24	15	(15)	-	15	-	-	39	-	39
Transfer of profit for the period to retained earnings	-	-	-	-	-	24,682	(24,682)	-	-	-	-
Allocation of disposable income following the Shareholders' Assembly resolution	-	-	-	2,569	-	(2,569)	-	-	-	-	-
<b>Total contributions by and distributions to owners</b>	<b>-</b>	<b>24</b>	<b>15</b>	<b>2,554</b>	<b>-</b>	<b>5,374</b>	<b>(24,682)</b>	<b>-</b>	<b>(16,715)</b>	<b>-</b>	<b>(16,715)</b>
<b>Changes in ownership interests in subsidiaries that do not result in a loss of control</b>											
Acquisition of non-controlling interest	-	-	-	-	-	(761)	-	-	(761)	(1,643)	(2,404)
<b>Total transactions with owners</b>	<b>-</b>	<b>24</b>	<b>15</b>	<b>2,554</b>	<b>-</b>	<b>4,613</b>	<b>(24,682)</b>	<b>-</b>	<b>(17,476)</b>	<b>(1,643)</b>	<b>(19,119)</b>
<b>Balance at 31 December 2009</b>	<b>157,129</b>	<b>198,872</b>	<b>(3,235)</b>	<b>270,194</b>	<b>186,029</b>	<b>8,697</b>	<b>21,232</b>	<b>(33,782)</b>	<b>805,136</b>	<b>254</b>	<b>805,390</b>

\* The amount of dividends to equity holders differs from the amount declared by the Shareholders' Assembly, due to consideration of treasury shares in dividends calculation.

## Consolidated statement of cash flows

EUR thousand	Note	2009	2008
<b>Cash flows from operating activities</b>			
Profit for the period		<b>21,119</b>	<b>40,761</b>
Adjustments:			
Income tax expense	14	4,077	9,232
Depreciation of property, plant and equipment	15	85,463	82,467
Depreciation of investment property	17	211	262
Amortisation of intangible assets	16	10,338	11,325
Gain on sale of property, plant and equipment		(1,423)	(8,895)
Change in provisions, accruals and deferrals	22, 27, 28	4,737	(7,431)
(Gain) loss on sale and impairment losses of available-for-sale financial assets	13	178	(5,347)
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost	10	(371)	(67)
Net foreign exchange loss from borrowings	13	4,224	5,520
Interest received	13	(7,811)	(9,181)
Interest paid	13	46,554	58,127
<b>Gross cash flow from operating activities</b>		<b>167,296</b>	<b>176,773</b>
Change in inventories		(19,659)	(25,608)
Change in trade and other receivables		93,866	(63,075)
Change in trade and other payables		(78,067)	110,949
		<b>163,436</b>	<b>199,039</b>
Interest paid	13	(46,554)	(58,127)
Income tax paid	14	(4,844)	(7,997)
<b>Net cash from operating activities</b>		<b>112,038</b>	<b>132,915</b>
<b>Cash flows from investing activities</b>			
Acquisition of subsidiaries, net of cash acquired	8	(4,801)	(15,105)
Acquisition of property, plant and equipment and investment property	15, 17	(149,757)	(288,531)
Acquisition of intangible assets	16	(7,596)	(9,774)
Bank deposits made		(24,963)	(15,138)
Proceeds from sale of property, plant and equipment and investment property	15, 17	6,967	16,618
Proceeds from sale of intangible assets	16	36	46
Proceeds from sale of available-for-sale financial assets	18	-	7,268
Interest received	13	7,811	9,181
Dividends received	13	16	68
Bank deposits received		30,269	136
<b>Net cash used in investing activities</b>		<b>(142,018)</b>	<b>(295,231)</b>
<b>Cash flows from financing activities</b>			
Proceeds (repayments) from borrowings		14,032	201,627
Dividends paid		(12,366)	(15,647)
<b>Net cash from financing activities</b>		<b>1,666</b>	<b>185,980</b>

**Net (decrease) increase in cash and cash equivalents**

Cash and cash equivalents at the beginning of the year

Currency translation differences

**Cash and cash equivalents at the end of the year**

23

<b>(28,314)</b>	<b>23,664</b>
45,870	23,089
(712)	(883)
<b>16,844</b>	<b>45,870</b>

# Notes to consolidated financial statements

## 1. Reporting company

Poslovni sistem Mercator, d.d., (hereinafter referred to as Mercator, d.d.) is a company domiciled in Slovenia. The address of the company's registered office is Ljubljana, Dunajska cesta 107. The consolidated financial statements of the Company as at and for year ended 31 December 2009 comprise the company and its subsidiaries (together referred to as the "Mercator Group"). The predominant activity of the Mercator Group is retail and wholesale of fast-moving consumer goods.

## 2. Basis of preparation

### (a) Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU, and in compliance with the requirements of the Slovenian Companies Act.

The financial statements were approved by the Company Management Board on 1 February 2010.

### (b) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis, except for the items listed below, where fair value is considered.

- ▶ derivative financial instruments,
- ▶ available-for-sale financial assets,
- ▶ property by revaluation model.

The methods used to measure fair values are discussed further in Note 4.

### (c) Functional and presentation currency

These consolidated financial statements are presented in euro, which is the functional currency of Company Poslovni sistem Mercator, d.d. All financial information presented in euro has been rounded to the nearest thousand.

### (d) Use of estimates and judgements

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of uncertainty estimation and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is given below.

#### (i) Goodwill

Each year when compiling the financial statements, the Group conducts the goodwill impairment test. The recoverable amount of the cash generating unit is defined based on the calculations of value in use. The calculations include projections of cash flow that are based on operation plans for the successive year, as adopted by the Management Board, and the extrapolation of the growth rates for all successive periods. The Management Board has defined the gross margin based on the business performance record (history) and expectations with regard to development of the market. The discount rate employed is based on market rates adjusted to reflect specific risks related to particular business units.

#### (ii) Available-for-sale financial assets

The Group's long-term financial investments into equity of other companies, classified as available-for-sale financial assets, also include such assets that could not be valued at fair value. Shares of these companies are also not listed or traded in the stock market. The Group estimates that the costs of evaluating these long-term financial investments into equity of other companies by their fair value would be too high, while the evaluation would not affect significantly the correctness of financial statements; hence, these assets are valued at cost.

#### (iii) Trade and other receivables

The estimate is based on assumption, that trade and other receivables will be paid in recognised amount. Provision for the impairment of trade and other receivables is based on pending legal processes and previous years' experience. In the future the Group does not expect any events that would significantly influence accounting estimates.

#### (iv) Inventories

The carrying values of inventories approximate net realizable value in all material aspects. Allowances and write downs of inventories are based on previous years' experiences. In the future the company does not expect any events that would significantly influence accounting estimates.

#### (v) Provisions

Carrying values of provisions are measured as the present value of the expenditures expected to be required to settle the obligation. Estimates are given by experts or the values are based on original documentation. The outcome and the date of resolution of legal proceedings, which were the basis for recognition of provisions, are uncertain. In the future the company does not expect any events that would significantly influence accounting estimates.

Retirement benefits and jubilee premiums provisions refer to estimated payments of retirement benefits and long service awards presented to the employees who have been with the Group for a long period of time, as at the balance sheet date, discounted to present value. These provisions have been made for expected payments. The calculation of the figure also accounted for the expected growth of wages from the day of calculation until the day of retirement of a particular employee, as well as employee fluctuation. Wage growth consists of career promotion and the related wage inflation. To calculate the present value of retirement benefits and jubilee premiums provisions, a discount rate was used that is equal to the market yield on highly rated corporate bonds issued in euros. In the future the Group does not expect any events that would significantly influence accounting estimates.

#### (vi) Deferred taxes

Deferred income taxes are calculated on all temporary differences under the liability method using a principal domestic tax rate of individual consolidated entity's country. If the tax rate changes, the deferred income tax assets and liabilities will change appropriately. In the future the Group does not expect any events that would significantly influence accounting estimates.

### (e) Changes in accounting policies

#### (i) Presentation of financial statements

The Group applies revised IAS 1 *Presentation of Financial Statements (2007)*, which became effective as of 1 January 2009. As a result, the Group presents in the consolidated statement of changes in equity all owner changes in equity, whereas all non-owner changes in equity are presented in the consolidated statement of comprehensive income. Comparative information has been re-presented so that it also is in conformity with the revised standard. Since the change in accounting policy only impacts presentation aspects, there is no impact on earnings per share.

#### (ii) Accounting for borrowing costs

In respect of borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009, the Group capitalises borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Previously the Group immediately recognised all borrowing costs as an expense. This change in accounting policy was due to the adoption of IAS 23 *Borrowing Costs (2007)* in accordance with the transitional provisions of such standard; comparative figures have not been restated. The change in accounting policy had no material impact on earnings per share. Capitalisation of borrowing costs is carried out with respect to significant capital expenditures (capital expenditures, that at completion amount over 3% of the carrying amount of property, plant and equipment at the beginning of accounting period), that have started after 1 January 2009 and whose construction or preparation for use lasts over 6 months. In 2009 no single capital expenditure fulfils the above described criteria to be considered significant.

#### (iii) Determination and presentation of operating segments

As of 1 January 2009 the Group determines and presents operating segments based on the information that internally is provided to the CEO, who is the Group's chief operating decision maker. This change in accounting policy is due to the adoption of IFRS 8 *Operating Segments*. Previously operating segments were determined and presented in accordance with IAS 14 *Segment Reporting*. Apart from some additional disclosures, there are no significant changes from previous year. Comparative segment information has been re-presented in conformity with the transitional requirements of such standard. Since the change in accounting policy only impacts presentation and disclosure aspects, there is no impact on earnings per share.

### 3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities.

The Group has in the financial statements for 2009 reclassified some comparative information for 2008 due to change in allocation of certain income and expense items. In

2009 selling and marketing costs have been included in cost of sales, which also comprises cost of goods sold and production costs. In 2008 selling and marketing costs were presented as an independent item in the income statement. Also, comparative information was reclassified in Note 13 (Finance income and expense), where net Foreign currency translation differences from financing are disclosed separately. In Note 11 (Expenses by nature) costs of materials, costs of services, other expenses and change in inventories have been adjusted in 2008 for comparability with 2009.

## **(a) Basis of consolidation**

### **(i) Subsidiaries**

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

### **(ii) Acquisitions from entities under common control**

Business combinations arising from transfers of interests in entities that are under the control of the shareholder that controls the Group are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date when common control was established; for this purpose comparatives are restated. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the Group's controlling shareholder's consolidated financial statements. The components of equity of the acquired entities are added to the same components within Group equity except that any share capital of the acquired entities is recognised as part of share premium. Any cash paid for the acquisition is recognised directly in equity.

### **(iii) Transactions eliminated on consolidation**

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

## **(b) Foreign currency**

### **(i) Foreign currency transactions**

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss, except for differences arising on retranslation of available-for-

sale equity instruments, a financial liability designated as a hedge of the net investment in a foreign operation, or qualifying cash flow hedges, which are recognised directly in equity.

#### (ii) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to euro at exchange rates at the reporting date. The income and expenses of foreign operations, excluding foreign operations in hyperinflationary economies, are translated to euro at average exchange rates.

Foreign currency differences are recognised directly in equity. Since the Group's date of transition to IFRSs, such differences have been recognised in the foreign currency translation reserve (FCTR). When a foreign operation is disposed of, in part or in full, the relevant amount in the FCTR is transferred to profit or loss.

### (c) Financial instruments

#### (i) Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Non-derivative financial instruments are initially recognised at fair value. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

Costs of transaction are recognized among expenses in the income statement. The exception to this rule are investments in equity, where the transaction costs increase the fair value of the financial instrument.

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the cash flow statement.

Accounting for finance income and expenses is discussed in note 3(o).

#### Available-for-sale financial assets

The Group's investments in equity securities and certain debt securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see note 3(i)(i)), and foreign exchange gains and losses on available-for-sale monetary items (see note 3(b)(i)), are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to profit or loss.

Available-for-sale financial assets of the Group also include such assets whose fair value could not be evaluated. This mainly includes equity securities of companies that are not listed and traded in stock markets. The Group estimates that costs of evaluating the fair value of all these financial assets would have been too high, while the evaluation would not considerably affect the correctness of financial statements.

#### Other

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses.

## (ii) Derivative financial instruments

The Group holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures. Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss.

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, derivatives are measured at fair value, and changes therein are accounted for as described below.

### *Cash flow hedges*

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in equity to the extent that the hedge is effective. To the extent that the hedge is ineffective, changes in fair value are recognised in profit or loss.

If the hedging instrument no longer meets the criteria for hedge accounting, expires or is sold, terminated or exercised, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in equity remains there until the forecast transaction occurs. When the hedged item is a non-financial asset, the amount recognised in equity is transferred to the carrying amount of the asset when it is recognised. In other cases the amount recognised in equity is transferred to profit or loss in the same period that the hedged item affects profit or loss.

## (iii) Share capital

### **Ordinary shares**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognised as a deduction from equity, net of any tax effects.

### **Repurchase of share capital (treasury shares)**

When share capital recognised as equity is repurchased, the amount of consideration paid, which includes directly attributable costs, is net of any tax effects, and is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to capital reserves or retained earnings.

## (d) Property, plant and equipment

### (i) Reporting and measurement

Upon the initial recognition, property, plant and equipment are measured at cost, increased by expenses that can be ascribed directly to their commissioning / putting to use.

For measuring land and buildings, the Group employs the revaluation model. The fair values reported are based on periodical, but not less than three-year valuations by an external independent appraiser, less accumulated depreciation. Increases in carrying amount from land and building revaluation are reported in the increase of revaluation surplus in equity. Impairment of assets whose value was previously increased directly decrease the value of established revaluation surplus in equity; otherwise, they are recognized in the income statement. Depreciation charge based on revalued value of assets is recognised in the Income statement. Useful life and remaining value of buildings is evaluated / appraised

annually, by an internal committee of experts, based on events that indicate the need for revaluation of a particular asset.

The value of plant and equipment is determined using the cost model. Cost of plant and equipment is decreased by accumulated depreciation.

The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment. Borrowing costs related to the acquisition or construction of qualifying assets are capitalised, if they exceed 3 % of the carrying amount of property, plant and equipment at the beginning of the year, start after 1 January 2009 and construction or preparation for use lasts over 6 months. In 2009 the group has not made capital expenditures, which would meet the described criteria.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount. The Group shall recognise such gains and losses in the income statement, gains among 'other income', and losses among 'administrative expenses'. When revalued assets are sold, the amounts included in the revaluation surplus reserve are transferred to retained earnings.

#### (ii) Reclassification to investment property

If a property used by the company is reclassified to investment property, the value of such property shall be evaluated its cost, and the property shall be included among the investment property. The Group evaluates its investment property by the cost model. Only independent real estate units, entirely leased to a third party, are classified as investment property. If only a part of a building / facility is leased to a third party, it is not classified as investment property, as it can not be sold separately and because the other important part of the facility is being used for selling or producing goods.

#### (iii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within that part will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

#### (iv) Depreciation

Depreciation is calculated on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Leased assets are depreciated taking into account the lease term and their useful lives unless it is reasonably certain that the company will obtain ownership by the end of the lease term. Land is not depreciated.

For the part of the depreciation that relates to revalued property, plant, and equipment, the Group shall continuously eliminate the established revaluation surplus in retained earnings.

The estimated useful lives for the current and comparative periods are as follows:

- ▶ buildings 20 - 40 years,
- ▶ plant and equipment 3 - 15 years.

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

## **(e) Intangible assets**

### **(i) Goodwill**

Goodwill (negative goodwill) arises from the acquisition of subsidiaries, associates and joint ventures.

#### *Acquisitions as of the day of transition to IFRS*

For acquisitions on or after 1 January 2006, goodwill represents the excess of the cost of the acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess is negative (negative goodwill), it is recognised immediately in profit or loss.

### **(ii) Acquisitions of non-controlling interests**

All surpluses or difference between cost of interests and the carrying amount of assets are recognised in equity, at changes in equity interests that do not result in change of control.

### **(iii) Other intangible assets**

Other intangible assets that are acquired by the Group, which have finite useful lives, are measured at cost less accumulated amortisation and accumulated impairment losses.

### **(iv) Subsequent expenditure**

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including brands, is recognised in profit or loss as incurred.

### **(v) Amortisation**

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets, other than goodwill, from the date that they are available for use. The estimated useful lives for the current and comparative periods are as follows:

- ▶ patents, licenses, and brands      5-10 years.

## **(f) Investment property**

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services or for administrative purposes.

Only independent buildings / real estate units that are entirely leased to third parties are classified as investment property. If only a part of a building / facility is leased to third parties, it is not classified as investment property, as it cannot be sold separately and because other major part of the facility is used for producing or delivering goods or services (e.g. hypermarket within a shopping centre). Investment property is recorded by the cost model. Depreciation is calculated based on a linear method, so that the purchase value of assets is divided on their respective remaining values throughout the anticipated useful life which is the same as for property, plant and equipment.

When the use of a property changes so that it is reclassified as property, plant and equipment, the fair value of such asset is measured. Positive difference is recognized in the revaluation surplus, while the negative difference is recognized in the profit or loss.

## **(g) Leased assets**

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and, except for investment property, the leased assets are not recognised on the Group's statement of financial position.

## **(h) Inventories**

Inventories are measured at the lower of cost and net realizable value.

Following are the methods of calculating the cost of inventories and relevant expenses:

- ▶ FIFO method for merchandise,
- ▶ method of average purchase prices for raw materials and packaging; costs of inventory include purchase value, costs of production, transformation, and other costs incurred in bringing them to the current location and in the current condition; with both finished products and semi-products, the costs also include the relevant part of indirect production costs, under the assumption of normal use of means of production.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The estimation of net realisable value of inventory is conducted at least once per year, upon the compilation of regular annual inventory lists.

Write-offs and partial write-offs of damaged, expired and useless inventories are conducted regularly during the year on specific items. At the end of the year inventories are revalued as of 31 December on groups of related or connected items depending on their aging or obsolescence. They are impaired on the basis of previous years' experience.

## **(i) Impairment of assets**

### **(i) Financial assets**

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial asset is calculated by reference to its fair value.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar risk characteristics.

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in profit or loss. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

#### **(ii) Non-financial assets**

The carrying amounts of the Group's non-financial assets, other than investment property, inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, the recoverable amount is estimated at least once a year before completing the annual report.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to cash-generating units that are expected to benefit from synergies of the combination.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

#### **(j) Employee benefits**

##### **(i) Other long-term employee benefits – retirement benefits and jubilee premiums provisions**

In the balance sheet, the Group recognized long-term provisions deriving from future liabilities to employees for long service awards, calculated in compliance with the collective labour agreement for this activity / industry, and the mandatory retirement benefits as stipulated by the relevant act. The changes in retirement benefits and jubilee premiums provisions are recognized in the income statement. The provisions are determined based on actuarial calculations that are revised annually. Actuarial gains or losses are the effect of

changed facts that affect the actuarial calculation (e.g. change in legislation), or a change in actuarial assumptions.

#### **(ii) Short-term employee benefits**

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

#### **(k) Provisions**

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

#### **(i) Onerous contracts**

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with that contract.

#### **(l) Revenue**

##### **(i) Revenues from sales of goods, products, and material**

Revenue from the sale of goods, products and material is measured at the fair value of consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognised when the significant risks and rewards of ownership have been transferred to the buyer, recovery of consideration is probable, the associated costs and possible return of goods, products and material can be estimated reliably, there is no continuing management involvement with the quantity of goods sold, and the amount of revenue can be measured reliably.

Transfers of risks and rewards vary depending on the individual terms of the contract of sale. For wholesale of goods, transfer usually occurs when the product is received at the customer's warehouse; however, for some international shipments transfer occurs upon loading the goods onto the relevant carrier.

##### **(ii) Revenues from services rendered**

Revenue from services rendered is recognised in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

##### **(iii) Rental income**

Rental income is recognised in profit or loss on a straight-line basis over the term of the lease. Any discounts and benefits granted are recognised as an integral part of the total rental income.

### **(m) Government grants**

All types of government grants are recognised initially as deferred income when there is reasonable assurance that they will be received and that the Group will comply with the conditions associated with the grant. Grants that compensate the Group for expenses incurred are recognised in profit or loss on a systematic basis in the same periods in which the expenses are recognised. Grants that compensate the Group for the cost of an asset are recognised in profit or loss among other income on a systematic basis over the useful life of the asset.

### **(n) Finance lease**

Payments made under finance leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease discounts and benefits received are recognised as an integral part of the total lease expense.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

### **(o) Finance income and expenses**

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, changes in the fair value of financial assets at fair value through profit or loss, and gains on hedging instruments that are recognised in profit or loss. Interest income is recognised as it accrues in profit or loss, using the effective interest method. Dividend income is recognised in profit or loss on the date that the Group's right to receive payment is established, which in the case of quoted securities is the ex-dividend date.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions, impairment losses recognised on financial assets, and losses on hedging instruments that are recognised in profit or loss. All borrowing costs are recognised in profit or loss.

### **(p) Corporate income tax**

Income tax expense for the year comprises current and deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences:

- ▶ the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating

to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future,

- ▶ initial recognition of goodwill.

Deferred tax liabilities are measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

### **(q) Net earnings per share**

The Group calculates basic earnings per share by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. The Group has no preference shares, nor does it have any ordinary shares that would represent convertible bonds and stock options; hence, the Group does not calculate dilutive earnings and dilutive earnings per share.

### **(r) Customer loyalty programme**

The Group issues Mercator Pika credit cards to its customers, who collect bonus points for each purchase. The cycle for collecting bonus points lasts six months. First cycle in the year lasts from 1 February until 31 July, while the second cycle lasts from 1 August until 31 January of the following year. In each cycle the customers collect bonus points. Depending on the amount of purchases and consequently the number of collected points, the customers can gain 3 to 6 % discount. During the year the Group defers potential discounts on the basis of given bonus points, while based on data from previous bonus periods it defers income from unrealized bonus points. Notwithstanding, that the second bonus period ends on 31 January the following year, the Group ensures, that recognised revenues correspond to expenses, which were necessary for realization of revenues.

### **New standards and interpretations not yet adopted**

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2009, and have not been applied in preparing these consolidated financial statements:

- ▶ Revised IFRS 3 *Business Combinations* (effective for annual periods beginning on or after 1 July 2009). The scope of the revised Standard has been amended and the definition of a business has been expanded. The revised Standard also includes a number of other potentially significant changes including:

- All items of consideration transferred by the acquirer are recognised and measured at fair value as of the acquisition date, including contingent consideration.

- Subsequent change in contingent consideration will be recognized in profit or loss.
- Transaction costs, other than share and debt issuance costs, will be expensed as incurred.
- The acquirer can elect to measure any non-controlling interest at fair value at the acquisition date (full goodwill), or at its proportionate interest in the fair value of the identifiable assets and liabilities of the acquiree, on a transaction-by-transaction basis.

As the revised Standard should not be applied to business combinations prior to the date of adoption, the revised Standard is expected to have no impact on the financial statements with respect to business combinations that occur before the date of adoption of the revised Standard.

▶ Revised IAS 27 *Consolidated and Separate Financial Statements* (effective for annual periods beginning on or after 1 July 2009). In the revised Standard the term minority interest has been replaced by non-controlling interest, and is defined as "the equity in a subsidiary not attributable, directly or indirectly, to a parent". The revised Standard also amends the accounting for non-controlling interest, the loss of control of a subsidiary, and the allocation of profit or loss and other comprehensive income between the controlling and non-controlling interest. The Group has not yet completed its analysis of the impact of the revised Standard.

▶ Amendment to IAS 32 *Financial Instruments: Presentation – Classification of Rights Issues* (effective for annual period beginning on or after 1 February 2010). The amendment requires that rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency, are equity instruments if the entity offers the rights, options or warrants pro rata to all of its existing owners of the same class of its own non-derivative equity instruments. The amendments to IAS 32 are not relevant to the Group's financial statements as the Group has not issued such instruments at any time in the past.

▶ Amendment to IAS 39 *Financial Instruments: Recognition and Measurement – Eligible Hedged Items* (effective for annual periods beginning on or after 1 July 2009). The amended Standard clarifies the application of existing principles that determine whether specific risks or portions of cash flows are eligible for designation in a hedging relationship. In designating a hedging relationship the risks or portions must be separately identifiable and reliably measurable; however inflation cannot be designated, except in limited circumstances. The Group has not yet completed its analysis of the impact of the amendments to the Standard.

▶ IFRIC 12 *Service Concession Arrangements* (effective for first annual reporting period beginning on or after 1 April 2009). The Interpretation provides guidance to private sector entities on certain recognition and measurement issues that arise in accounting for public-to-private service concession arrangements. IFRIC 12 is not relevant to the Group's operations as none of the Group entities have entered into any service concession arrangements.

▶ IFRIC 15 *Agreements for the Construction of Real Estate* (effective for annual periods beginning on or after 1 January 2010). IFRIC 15 clarifies that revenue arising from agreements for the construction of real estate is recognised by reference to the stage of completion of the contract activity in the following cases:

- the agreement meets the definition of a construction contract in accordance with IAS 11.3;
- the agreement is only for the rendering of services in accordance with IAS 18 (e.g., the entity is not required to supply construction materials); and

- the agreement is for the sale of goods but the revenue recognition criteria of IAS 18.14 are met continuously as construction progresses.

In all other cases, revenue is recognised when all of the revenue recognition criteria of IAS 18.14 are satisfied (e.g., upon completion of construction or upon delivery). IFRIC 15 is not relevant to the Group's financial statements as the Group does not provide real estate construction services or develop real estate for sale.

▶ IFRIC 16 *Hedges of a Net Investment in a Foreign Operation* (effective for annual periods beginning on or after 1 July 2009). The Interpretation explains the type of exposure that may be hedged, where in the group the hedged item may be held, whether the method of consolidation affects hedge effectiveness, the form the hedged instrument may take and which amounts are reclassified from equity to profit or loss on disposal of the foreign operation. IFRIC 16 is not relevant to the Group's financial statements as the Group has not designated any hedges of a net investment in a foreign operation.

▶ IFRIC 17 *Distributions of Non-cash Assets to Owners* (effective prospectively for annual periods beginning on or after 1 November 2009). The Interpretation applies to non-reciprocal distributions of non-cash assets to owners acting in their capacity as owners. In accordance with the Interpretation a liability to pay a dividend shall be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity and shall be measured at the fair value of the assets to be distributed. The carrying amount of the dividend payable shall be remeasured at each reporting date, with any changes in the carrying amount recognised in equity as adjustments to the amount of the distribution. When the dividend payable is settled, the difference, if any, between the carrying amount of the assets distributed and the carrying amount of the dividend payable shall be recognised in profit or loss. As the Interpretation is applicable only from the date of application, it will have no impact on the financial statements for periods prior to the date of adoption of the interpretation. Further, since it relates to future dividends that will be at the discretion of the board of directors/shareholders, it is not possible to determine the effects of application in advance.

▶ IFRIC 18 *Transfers of Assets from Customers* (effective prospectively for annual period beginning on or after 1 November 2009). The Interpretation requires an entity that receives a contribution in the scope of the Interpretation to recognize the item as an asset at its fair value if the transferred item meets the criteria for property, plant, and equipment in IAS 16, *Property, Plant and Equipment*. The Interpretation also requires the entity to recognize the amount as revenue; the timing of revenue recognition depends on the facts and circumstances of the particular arrangement. IFRIC 18 is not relevant to the Group's financial statements as the Group does normally receive contributions from customers.

#### **4. Determination of fair values at business combinations**

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and / or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

##### **(a) Property, plant, and equipment**

The fair value of property, plant and equipment recognised as a result of a business combination is based on market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing

buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. Plant, equipment, fixtures and fittings are measured at cost.

#### **(b) Intangible assets**

The fair value of patents and trademarks acquired in a business combination is based on the discounted estimated royalty payments that have been avoided as a result of the patent or trademark being owned. The fair value of other intangible assets is based on the discounted cash flows expected to be derived from the use and eventual sale of the assets.

#### **(c) Investment property**

The fair values in business or strategic combinations are based on market values, being the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion (arm's length transaction).

In the absence of current prices in an active market, the valuations are prepared by considering the aggregate of the estimated cash flows expected to be received from renting out the property. A yield that reflects the specific risks inherent in the net cash flows then is applied to the net annual cash flows to arrive at the property valuation.

Valuations reflect, when appropriate: the type of tenants actually in occupation or responsible for meeting lease commitments or likely to be in occupation after letting vacant accommodation, and the market's general perception of their creditworthiness; the allocation of maintenance and insurance responsibilities between the Group and the lessee; and the remaining economic life of the property. When rent reviews or lease renewals are pending with anticipated reversionary increases, it is assumed that all notices, and when appropriate counter-notices, have been served validly and within the appropriate time.

#### **(d) Inventories**

The fair value of inventories acquired in a business combination is determined based on its estimated selling price in the ordinary course of business less the estimated costs of completion and sale, and a reasonable profit margin based on the effort required to complete and sell the inventories.

#### **(e) Investments in equity and debt securities**

The fair value of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets in business or strategic combinations is determined by reference to their quoted bid price at the reporting date. The fair value of held-to-maturity investments is determined for disclosure purposes only.

#### **(f) Trade and other receivables**

The fair value of trade and other receivables, excluding construction work in progress, in business or strategic combinations is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

## **(g) Derivatives**

The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds).

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

## **(h) Non-derivative financial liabilities**

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. In respect of the liability component of convertible notes, the market rate of interest is determined by reference to similar liabilities that do not have a conversion option. For finance leases the market rate of interest is determined by reference to similar lease agreements.

# **5. Financial risk management**

## **(a) Overview**

The Group is constantly monitoring various types of financial risks to which it is exposed through its operations. Among these risks are the following: interest rate risk, foreign exchange risk, credit risk and liquidity risks. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

In the Mercator Group, there is a special body that deals with risk management, i.e. the Risk Management Council. The Council evaluates the level of exposure to risks and lays down the principles for comprehensive risk management, as well as risk management policies for particular areas. The Group has introduced a consistent policy of risk management that covers various types of risk. The policy consists of analysis of the Group's exposure to risk, evaluation of the level of risk, and the measures for reducing, or mitigating. In 2009 credit and refinancing risk have been identified as key risks. Following is a short summary of the risk management policy.

## **(i) Credit risk**

Credit risk represents the possibility that trade receivables towards customers and other business partners, caused by deferred payment, will be only partly paid or even remain unpaid. In the Mercator Group we assessed the credit risk in two segments, the sale on deferred payment of the wholesale buyers and the deferred payment of Mercator Pika credit card holders. In order to control wholesale credit risk Mercator Group is deriving premium insurance from customers with poor credit standing, monitoring poor payers and enhancing exposure limit to individual customers. Mercator Group has already reduced number of days of delays, introduced regular proceedings for the recovery of receivables and performed mutual and chain netting of receivables.

In order to control credit risk of Mercator Pika card the Group is actively performing the recovery process and monitoring bad payers.

#### (ii) Liquidity risk

The Group actively manages liquidity risk by:

- ▶ operating a centralized cash management system,
- ▶ statistically supported forecasting of cash flows,
- ▶ daily contact with its largest wholesale customers, thereby increasing the predictability of its cash flows,
- ▶ operating a centralised cash pooling system.

Due to worsened situation on financial markets and decreased liquidity of financial institutions Mercator Group has estimated increased liquidity risk in 2009. A new type of risk is emerging, namely that banks will not be able to refinance all existing financial liabilities, that companies have towards banks. In response, the Group has, in addition to activities that have been carried out previously for managing liquidity risk, systematically approached to refinance existing financial liabilities, promote compensations with customers and suppliers, perform more actively the process of collecting receivables, optimize the volume of purchase orders and search for alternative sources of financing.

#### (iii) Market risks

##### **Interest rate risk**

Interest rate risk of the Group derives from financial liabilities. Financial liabilities expose the Group to cash flow interest rate risk.

Interest rate risk deriving from the possible growth of financing cost for the sources related to the variable / floating interest rate, is adequately managed by the Group. The policy on interest rate risk management includes analyses of increased exposure in case of net borrowing at floating interest rate, insurance of a part of financial liabilities with appropriate derivative financial instruments, and the possibility of issuing debt at fixed interest rate.

##### **Currency risk**

Mercator's operations in an international environment necessarily involve exposure to currency risk. Mercator Group is facing currency risk in the markets of Serbia and Croatia; exposure to risk has increased on these two markets according to estimate.

In case of increase in exposure to this type of risk, the Group has prepared a general policy of risk management that involves the following two steps:

- ▶ constant monitoring of macroeconomic background against which the movement of a particular exchange rate is taking place, and the related macroeconomic aspects and trends,
- ▶ adapting the operations based on the general trends and expectations, towards lesser exposure to currency risk.

In case of increased risk, the Group will decide on implementing any further measures based on the estimated level of exposure; needless to say, such measure will only be implemented following a thorough analysis and with consideration of the 'cost-benefit' principle. The type of measure will depend on its appropriateness or viability, the nature of exposure, planned Group operations, and anticipated economic effects.

## **(b) Capital management**

Policy of the Group is oriented to achieve adequate amount of capital so as to maintain investor, creditor and market confidence and to sustain future development of the business. Management Board therefore monitors on an ongoing basis the return on capital and capital structure.

The target capital structure ratio of the Group is 1:1.5 between equity and provisions, and financial liabilities.

Dividend policy is adopted for the period until 2010; actual amount of dividends in each year is determined by the Shareholders' Assembly.

As of 31 December 2009 the company Poslovni sistem Mercator, d.d., holds 42,192 treasury shares (31 December 2008: 42,381 treasury shares). In July 2009 the company designated 189 treasury shares as purchase consideration for 2,4 percent ownership interest in the company Interier, d.o.o.

## **(c) Accounting for derivative financial instruments**

The Group has signed several agreements on interest rate swaps and interest rate caps, exclusively for the purposes of hedging; all criteria related to such purposes are met. The instruments employed are intended for cash flow hedging and are highly effective in managing the cash flows related to Group's borrowings.

Upon completion of a transaction, Mercator Group documents the relation between derivative financial instruments and hedged items, as well as the goal of its risk management and strategy for effecting various hedging transactions. This process also includes relating all derivative financial instruments to the portfolio of borrowings, or to particular borrowings.

The Group also documents every estimate it makes, both upon the completion of a transaction, as well as later, with regard to the effectiveness of derivative financial instruments employed for hedging in managing the cash flow from borrowings.

The Group employs derivative financial instruments for hedging purposes and recognizes them initially at fair value. If the cash flow hedge is effective, the changes in fair value are recognized directly in equity; otherwise, they are recognized in the profit or loss for the current period. The method for recognizing the profit or loss related to these instruments does not depend on the form of the hedged item.

## **(d) Fair value estimation**

The fair value of interest rate swaps has been calculated as the present value of the estimated future cash flows and deferred in a 'hedging reserve' in equity. Calculation of the fair value changes of each instrument is assessed on a semi-annual basis and recognised in the income statement when the hedged transaction affects the income statement.

## 6. Tax policy

### (a) Slovenia

Tax statements (financial statements for tax authorities) of the company Poslovni sistem Mercator, d.d., and the companies of the Mercator Group in Slovenia, are prepared in accordance with International Financial Reporting Standards and the Corporate Income Tax Act.

In 2009 Corporate Income Tax Act was not revised, therefore at income tax calculation the same provisions as the previous year were adhered to.

Corporate income tax rate is 21%. Pursuant to the corporate Income Tax Act Company's taxable base is the profit as the surplus of revenues over expenses, where the basic criteria for recognition, or inclusion, in a tax statement are still the revenues and expenses as shown in the income statement, defined pursuant to the legislation or accounting standards.

In 2009, Mercator Group companies in Slovenia recognized and derecognized deferred taxes related to the following aspects:

- ▶ differences between business and tax recognised depreciation,
- ▶ impairment of receivables,
- ▶ write-down of inventories,
- ▶ provisions made,
- ▶ change in fair value of derivative financial instruments,
- ▶ revaluation of property, plant and equipment,
- ▶ property, plant and equipment, whose value does not exceed EUR 500 and whose useful life is longer than one year,
- ▶ change in fair value of available-for-sale financial assets.

The company must provide documentation on transfer prices; general documentation can be common to a group of related entities as a whole.

### (b) Serbia

Tax statements of the company Mercator-S, d.o.o., are prepared in compliance with International Financial Reporting Standards and the relevant Corporate Income Tax Act ("Zakon o porezu na dobit preduzeća").

Corporate income tax rate amounts to 10%.

In the assessment of corporate income tax, the following tax reliefs can be exercised:

- ▶ investment relief for newly hired, that are employed for indefinite time period;
- ▶ investment relief in the amount of 20% of the sum invested in the current year (but not over 50% of levied tax);
- ▶ investment relief for hiring handicapped persons in the amount of their proportionate share in the total number of employees.

In 2009, the company Mercator-S, d.o.o., recognised deferred tax liabilities for the differences between depreciation as calculated for business purposes, and tax depreciation, calculated exclusively for the tax statement.

### **(c) Croatia**

Tax statements of the company Mercator-H, d.o.o., are prepared in compliance with International Financial Reporting Standards and the Corporate Income Tax Act ("Zakon o porezu na dobit").

Taxable base is the profit calculated in compliance with accounting principles, from which tax recognized or costs are subtracted, or to which unrecognized costs are added. The company may, among other, decrease its taxable base by the revenues from dividends or share in profit of other companies, and by depreciation that was not recognized as expense during the transitory periods.

Corporate income tax rate is 20%.

In the assessment of corporate income tax, companies can exercise the following tax reliefs:

- ▶ investment relief for promoting investments (under terms stated in the relevant act);
- ▶ investment relief for training (in part);
- ▶ investment relief for taxpayers in areas under special government protection.

In 2009 company Mercator – H, d.o.o., has derecognized deferred tax liabilities due to depreciation and disposal of revalued property.

### **(d) Bosnia and Herzegovina**

Tax statements of the companies Mercator-BH, d.o.o., and Mercator – BL, d.o.o., are prepared in compliance with International Financial Reporting Standards and the Corporate Income Tax Act ("Zakon o porezu na dobit").

Corporate income tax rate is 10%.

In the assessment of corporate income tax, companies can exercise the following tax reliefs:

- ▶ investment relief for investments in production on the territory of Bosnia and Herzegovina (taxpayers that invest 5 years successively at least BAM 20 mn);
- ▶ investment relief for exports;
- ▶ investment relief for hiring handicapped persons.

In 2009 company Mercator – BH, d.o.o., has derecognized deferred tax liabilities due to depreciation and disposal of revalued property.

### **(e) Montenegro**

Tax statements of the company Mercator-Mex, d.o.o., are prepared in compliance with International Financial Reporting Standards and the Corporate Income Tax Act ("Porez na dobit pravnih lica").

Corporate income tax rate is 9%.

In the assessment of corporate income tax, companies can exercise the following tax reliefs:

- ▶ investment relief for newly hired, that are employed for indefinite time period, in the amount of their wages;
- ▶ investment relief for the acquisition of assets that increase energy efficiency (tax base is decreased for 50% of completed investments).

In 2009 company Mercator – Mex, d.o.o., has not recognised deferred tax assets or liabilities.

## **(f) Bulgaria**

Tax statements of the company Mercator-B, e.o.o.d., are prepared in compliance with International Financial Reporting Standards and the Corporate tax on the annual taxable profit (loss).

Corporate income tax rate is 10%.

In the assessment of corporate income tax, companies can exercise the following tax reliefs:

- ▶ investment relief for hiring handicapped persons;
- ▶ investment relief for taxpayers in areas, which are less developed (under terms stated in the relevant act);
- ▶ investment relief for newly hired employees (under terms stated in the relevant act).

In 2009 company Mercator – B, e.o.o.d., has not recognised deferred tax assets or liabilities.

## **(g) Albania**

Tax statements of the company Mercator-A, sh.p.k., are prepared in compliance with International Financial Reporting Standards and the Corporate Tax on Income.

Corporate income tax rate is 20%.

Tax reliefs that could be used at determination of Income Tax are not foreseen.

In 2009 company Mercator – A, sh.p.k., has not recognised deferred tax assets or liabilities.

## **7. Business segments**

For the purpose of reporting by segments, the Mercator Group defined two segments by considering various sets of activities or services performed by the companies within the Group.

Market prices are used for selling goods, products and services between the segments.

The Group is organised into two main business segments:

- ▶ Trade, which consists of retail and wholesale of fast moving consumer goods, apparel goods, hardware and electronics, sportswear and sporting equipment. Fast moving consumer goods trade represents the core business of the Mercator Group.
- ▶ Non-trade, which consists of food processing, hospitality and other services.

## Information about reportable segments

EUR thousand	Trade		Non-trade		Total	
	2009	2008	2009	2008	2009	2008
<b>Total segment revenues</b>	<b>2,624,196</b>	<b>2,687,026</b>	<b>44,419</b>	<b>45,776</b>	<b>2,668,615</b>	<b>2,732,802</b>
Inter-segment revenues	2,391	2,620	22,909	21,622	25,300	24,242
Interest income	7,721	9,073	205	165	7,926	9,238
Interest expense	46,140	57,551	529	633	46,669	58,184
Depreciation and amortisation	93,918	90,064	2,094	3,990	96,012	94,054
<b>Total segment results from operating activities</b>	<b>69,798</b>	<b>97,863</b>	<b>2,393</b>	<b>2,464</b>	<b>72,191</b>	<b>100,327</b>
Assets	2,431,516	2,534,135	53,738	68,749	2,485,254	2,602,884
Liabilities	1,651,819	1,708,185	28,045	26,491	1,679,864	1,734,676
Capital expenditure	151,073	291,789	6,280	6,516	157,353	298,305
Reversal of impairment loss of property, plant and equipment	-	3,676	-	-	-	3,676

## Reconciliations of reportable segment revenues, results from operating activities, assets and liabilities and other material items

### Revenues

EUR thousand	2009	2008
Total segment revenues	2,668,615	2,732,802
Elimination of inter-segment revenues	(25,300)	(24,242)
<b>Consolidated revenue</b>	<b>2,643,315</b>	<b>2,708,560</b>

### Results from operating activities

EUR thousand	2009	2008
Total segment results from operating activities	72,191	100,327
Elimination of inter-segment profits	(349)	-
<b>Consolidated results from operating activities</b>	<b>71,842</b>	<b>100,327</b>

### Assets

EUR thousand	2009	2008
Total assets for reportable segments	2,485,254	2,602,884
Inter-segment elimination	(8,906)	(62,763)
<b>Consolidated total assets</b>	<b>2,476,348</b>	<b>2,540,121</b>

### Liabilities

EUR thousand	2009	2008
Total liabilities for reportable segments	1,679,864	1,734,676
Inter-segment elimination	(8,906)	(8,655)
<b>Consolidated total liabilities</b>	<b>1,670,958</b>	<b>1,726,021</b>

## Other material items 2009

EUR thousand	Reportable segment totals	Inter-segment eliminations	Consolidated totals
Interest income	7,926	(115)	7,811
Interest expense	46,669	(115)	46,554
Depreciation and amortisation	96,012	-	96,012
Capital expenditure	157,353	-	157,353

## Other material items 2008

EUR thousand	Reportable segment totals	Inter-segment eliminations	Consolidated totals
Interest income	9,238	(57)	9,181
Interest expense	58,184	(57)	58,127
Depreciation and amortisation	94,054	-	94,054
Reversal of impairment loss of property, plant and equipment	3,676	-	3,676
Capital expenditure	298,305	-	298,305

## Geographical segments

Although the Group's business segments are managed centrally, they operate in two main geographical areas:

- ▶ Slovenia, the location of the parent company, which is also the largest business unit of the Group. Areas of operation in Slovenia are: trade (retail and wholesale), food processing, hospitality and services.
- ▶ Foreign countries, including Serbia, Croatia, Bosnia and Herzegovina, Montenegro, Bulgaria, and Albania. Operations in these countries are carried out in the business segment of trade.

EUR thousand	Revenues from external customers		Non-current assets	
	2009	2008	2009	2008
Slovenia	1,744,603	1,781,921	1,097,439	1,060,908
Foreign countries	898,712	926,639	835,892	812,402
<b>Total</b>	<b>2,643,315</b>	<b>2,708,560</b>	<b>1,933,331</b>	<b>1,873,310</b>

Revenues from any individual customer do not reach 10% of total revenues of the Group.

Mercator Group consists of the following companies as at 31 December 2009 (data in EUR thousand):

<b>TRADE</b>			
<b>Poslovni sistem Mercator, d.d.</b> Slovenia	<b>100.0%</b>	<b>Intersport ISI, d.o.o.*</b> Slovenia	<b>100.0%</b>
Equity	<b>786,088</b>	Equity	<b>10,004</b>
Profit for the period	<b>19,281</b>	Profit for the period	<b>4</b>
Revenue	<b>1,745,129</b>	Revenue	<b>0</b>
Number of employees	<b>12,297</b>	Number of employees	<b>0</b>
<b>Mercator - S, d.o.o.</b> Serbia	<b>100.0%</b>	<b>Mercator - H, d.o.o.</b> Croatia	<b>99.9%</b>
Equity	<b>226,077</b>	Equity	<b>239,079</b>
Profit for the period	<b>7,989</b>	Profit for the period	<b>-3,693</b>
Revenue	<b>461,580</b>	Revenue	<b>315,022</b>
Number of employees	<b>3,714</b>	Number of employees	<b>3,023</b>
<b>Mercator - BH, d.o.o.</b> Bosnia and Herzegovina	<b>100.0%</b>	<b>Mercator - B, e.o.o.d.</b> Bulgaria	<b>100.0%</b>
Equity	<b>34,803</b>	Equity	<b>-158</b>
Profit for the period	<b>-583</b>	Profit for the period	<b>-2,159</b>
Revenue	<b>16,795</b>	Revenue	<b>696</b>
Number of employees	<b>241</b>	Number of employees	<b>76</b>
<b>M - BL, d.o.o.</b> Bosnia and Herzegovina	<b>100.0%</b>	<b>Mercator - Mex, d.o.o.**</b> Montenegro	<b>100.0%</b>
Equity	<b>3,057</b>	Equity	<b>4,703</b>
Profit for the period	<b>-416</b>	Profit for the period	<b>-978</b>
Revenue	<b>543</b>	Revenue	<b>19,365</b>
Number of employees	<b>130</b>	Number of employees	<b>368</b>
<b>Mercator - A, sh.p.k.</b> Albania	<b>100.0%</b>	<b>Mercator - K, d.o.o.*</b> Kosovo	<b>100.0%</b>
Equity	<b>3,057</b>	Equity	<b>1</b>
Profit for the period	<b>-416</b>	Profit for the period	<b>0</b>
Revenue	<b>543</b>	Revenue	<b>0</b>
Number of employees	<b>130</b>	Number of employees	<b>0</b>
<b>Tomkon, d.o.o.**</b> Serbia	<b>100.0%</b>	<b>Mercator Makedonija, d.o.o.e.l.</b> Macedonia	<b>100.0%</b>
Equity	<b>3,651</b>	Equity	<b>-199</b>
Profit for the period	<b>0</b>	Profit for the period	<b>-87</b>
Revenue	<b>0</b>	Revenue	<b>0</b>
Number of employees	<b>0</b>	Number of employees	<b>0</b>
<b>Tomveloping, d.o.o.**</b> Serbia	<b>100.0%</b>	<b>Tomsales, d.o.o.**</b> Serbia	<b>100.0%</b>
Equity	<b>1,950</b>	Equity	<b>1,589</b>
Profit for the period	<b>0</b>	Profit for the period	<b>0</b>
Revenue	<b>0</b>	Revenue	<b>0</b>
Number of employees	<b>0</b>	Number of employees	<b>0</b>
<b>Sitireks, d.o.o.**</b> Serbia	<b>100.0%</b>	<b>Magnoreks, d.o.o.**</b> Serbia	<b>100.0%</b>
Equity	<b>4,654</b>	Equity	<b>3,028</b>
Profit for the period	<b>0</b>	Profit for the period	<b>0</b>
Revenue	<b>0</b>	Revenue	<b>0</b>
Number of employees	<b>0</b>	Number of employees	<b>0</b>
<b>NON-TRADE</b>			
<b>Eta, d.d.</b> Slovenia	<b>100.0%</b>	<b>Mercator - Emba, d.d.</b> Slovenia	<b>100.0%</b>
Equity	<b>9,319</b>	Equity	<b>6,755</b>
Profit for the period	<b>1,362</b>	Profit for the period	<b>289</b>
Revenue	<b>20,965</b>	Revenue	<b>17,839</b>
Number of employees	<b>198</b>	Number of employees	<b>111</b>
<b>Mercator IP, d.o.o.</b> Slovenia	<b>100.0%</b>	<b>M - Nepremičnine, d.o.o.</b> Slovenia	<b>100.0%</b>
Equity	<b>872</b>	Equity	<b>3,947</b>
Profit for the period	<b>26</b>	Profit for the period	<b>-25</b>
Revenue	<b>4,122</b>	Revenue	<b>434</b>
Number of employees	<b>200</b>	Number of employees	<b>0</b>
<b>Mercator - Optima, d.o.o.</b> Slovenia	<b>100.0%</b>		
Equity	<b>2,351</b>		
Profit for the period	<b>110</b>		
Revenue	<b>1,237</b>		
Number of employees	<b>21</b>		

\* The company does not perform any activities yet.

\*\* Project real estate companies, which do not perform any activities and will be merged to parent companies on individual markets.

\*\*\* As at 31 December 2009, Mercator, d.d., held 81-percent ownership interest of the company Mercator Mex, d.o.o.; however 100-percent ownership interest is taken into account for consolidation purposes, due to the recognition of financial liability deriving from contractual obligation to purchase the remaining 19-percent ownership interest.

## 8. Acquisitions of subsidiaries and non-controlling interests

### Business combinations

In 2009, the Group acquired 100 percent ownership share in project real-estate companies Tomkon, d.o.o., Tomveloping, d.o.o., Tomsales, d.o.o., Sitireks, d.o.o., and Magnoreks, d.o.o., in Serbia. Upon the inclusion of the companies Tomkon, d.o.o., Tomveloping, d.o.o., and Tomsales, d.o.o., into the consolidated financial statements, excess of acquirer's interest over cost of the business combination in the amount of EUR 371 thousand was established and recognised in the income statement. Upon the inclusion of the companies Sitireks, d.o.o., and Magnoreks, d.o.o., into the consolidated financial statements, goodwill in the amount of EUR 18 thousand was established.

The acquisition of the companies Tomkon, d.o.o., Tomveloping, d.o.o., and Tomsales, d.o.o., had the following effect on the assets and liabilities of the Mercator Group on the day of acquisition:

EUR thousand	Note	Pre-acquisition carrying amounts	Fair value adjustments	Recognized values on acquisition
Property, plant and equipment	15	5,199	2,209	7,408
Cash and cash equivalents		3	-	3
Deferred tax liabilities	20	-	(221)	(221)
<b>Net identifiable assets and liabilities</b>		<b>5,202</b>	<b>1,988</b>	<b>7,190</b>
<b>Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost</b>	10			<b>(371)</b>
Consideration				6,819

The acquisition of the companies Sitireks, d.o.o., and Magnoreks, d.o.o., had the following effect on the assets and liabilities of the Mercator Group on the day of acquisition:

EUR thousand	Note	Pre-acquisition carrying amounts	Fair value adjustments	Recognized values on acquisition
Property, plant and equipment	15	1,570	6,770	8,340
Cash and cash equivalents		18	-	18
Deferred tax liabilities	20	-	(676)	(676)
<b>Net identifiable assets and liabilities</b>		<b>1,588</b>	<b>6,094</b>	<b>7,682</b>
<b>Goodwill</b>	16			<b>18</b>
Consideration				7,700

On 16 April 2009, the Group established the company Mercator - A, sh.p.k., Albania, with contribution of share capital in the amount of EUR 1 thousand.

On 22 October 2009, the Group established the company Mercator - K, d.o.o., Kosovo, with contribution of share capital in the amount of EUR 1 thousand.

## Acquisition of non-controlling interests

On 29 May 2009, the Group has purchased last 12 percent ownership share of the company M – Rodić, d.o.o., based on the agreement on strategic combination between Holding Rodić M&B, d.o.o., and Mercator, d.d., as at 19 October 2006, for agreed amount of EUR 10,765 thousand, of which EUR 3,000 thousand was paid in cash by the end of 2009. Before the transaction the group was holding 88.0% ownership share in the company M - Rodić, d.o.o., whereas after the transaction the Group owns 100.0% ownership share in the company M - Rodić, d.o.o. In 2009 the company M - Rodić, d.o.o., was merged to company Mercator - S, d.o.o.

On 29 October 2009, the Group acquired additional 30 percent ownership share in the company Mercator - Mex, d.o.o., in the amount of EUR 1,801 thousand and thereby increased its ownership from 51.0% to 81.0 %. The Group recognized a decrease in non-controlling interest in the amount of EUR 1,595 thousand, and decrease of retained earnings in the amount of EUR 206 thousand. In addition to this the Group has obliged itself to purchase an additional 19.0% ownership share in the company Mercator - Mex, d.o.o., until 2013. The price will be defined at time of purchase, depending on several economic / business elements. Since this forward contract represents a financial liability pursuant to IAS 32, the Group recognized the liability in the amount of EUR 803 thousand, which represents the best estimate of this liability's present value. Any changes in this estimate are recognised in the income statement.

In 2009, Mercator Group acquired with treasury shares an additional 2.4 percent ownership share in the company Interier, d.o.o., in the amount of EUR 39 thousand; hence, the Group increased its ownership share from 97.6% to 100.0%. The Group recognized a decrease in non-controlling interest in the amount of EUR 48 thousand, and increase of retained earnings in the amount of EUR 9 thousand. In 2009 the company Interier, d.o.o., was merged to company Mercator, d.d.

## 9. Revenue

Breakdown of revenue by categories

EUR thousand	2009	2008
Sales of goods	2,410,674	2,473,151
Sales of services	211,559	214,240
Sales of products	25,913	25,471
Sales of materials	532	421
Expenses for given early payment discounts	(5,363)	(4,723)
<b>Total</b>	<b>2,643,315</b>	<b>2,708,560</b>

Sales of goods are also reduced for discounts given to customers, holders of Mercator Pika card.

## 10. Other income

EUR thousand	2009	2008
Net gain on sale of property, plant and equipment	2,096	6,997
Reversal of provisions	1,794	6,957
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost	371	67
Reversal of impairment loss of property, plant and equipment	-	3,676
Other operating income	8,327	15,567
<b>Total</b>	<b>12,588</b>	<b>33,264</b>

Other operating income refers to income from insurance compensations and other compensations, and income from benefits for employment of the disabled.

## 11. Expenses by nature

EUR thousand	2009	2008
Depreciation of property, plant and equipment	85,463	82,467
Amortisation of intangible assets	10,338	11,325
Depreciation of investment property	211	262
Employee benefit expenses	278,273	290,107
Costs of materials	73,598	75,084
Costs of services	178,544	170,234
Cost of provisions	4,877	2,029
Other expenses	13,321	11,980
Loss on sale of property, plant and equipment	673	1,778
Change in inventories	3,268	3,487
Other operating expenses	7,491	3,996
Cost of goods sold	1,928,004	1,988,748
<b>Total cost of goods sold, selling and marketing costs and administrative expenses</b>	<b>2,584,061</b>	<b>2,641,497</b>

In 2009 production costs amounted to EUR 33,870 thousand (2008: EUR 33,885 thousand), selling and marketing costs amounted to EUR 504,741 thousand (2008: EUR 504,555 thousand) and administrative expenses amounted to EUR 109,955 thousand (2008: EUR 110,313 thousand).

Costs of services include rental expenses in the amount of EUR 23,323 thousand (2008: EUR 21,385 thousand).

In 2009 other operating expenses increased due to increase of indemnity expenses, which amounted to EUR 3,458 thousand (2008: EUR 207 thousand).

In 2009, the Group's costs of services also include the costs of audit in the amount of EUR 289 thousand. The auditors also provided other services for the Group in the amount of EUR 4 thousand, which do not comprise consulting services.

## 12. Employee benefit expenses

EUR thousand	2009	2008
Wages and salaries	204,043	213,284
Pension insurance costs	19,961	18,210
Health insurance costs	12,366	15,253
Other payroll costs	41,903	43,360
<b>Total</b>	<b>278,273</b>	<b>290,107</b>
Number of employees as at 31 December	21,404	21,636

Average number of employees in the Group during the year (calculated based on hours worked) amounts to 20,266 (2008: 20,438).

## 13. Finance income and expense

### Recognised in profit or loss

EUR thousand	2009	2008
Interest income	7,811	9,181
Gain on disposal of available-for-sale financial assets	-	6,886
Net operating foreign currency translation differences	100	2,555
Dividend income	16	68
Other finance income	2,318	1,413
<b>Finance income</b>	<b>10,245</b>	<b>20,103</b>
Interest expense	(46,554)	(58,127)
Loss on disposal and impairment of available-for-sale financial assets	(178)	(1,539)
Impairment of trade and other receivables	(5,528)	(3,726)
Net finance foreign currency translation differences	(4,224)	(5,520)
Other finance expense	(407)	(1,525)
<b>Finance expense</b>	<b>(56,891)</b>	<b>(70,437)</b>
<b>Net finance expense recognised in profit or loss</b>	<b>(46,646)</b>	<b>(50,334)</b>

## Recognised in other comprehensive income (net)

EUR thousand	2009	2008
Foreign currency translation differences on consolidation	(12,072)	(17,487)
Effective portion of changes in fair value of cash flow hedges	(1,206)	(8,613)
Net change in fair value of available-for-sale financial assets	664	(10,519)
Net change in fair value of available-for-sale financial assets transferred to profit or loss	-	(3,118)
<b>Finance (expense) income recognised in other comprehensive income</b>	<b>(12,614)</b>	<b>(39,737)</b>
Attributable to:		
Equity holders of the Company	(12,616)	(39,735)
Non-controlling interest	2	(2)
<b>Finance (expense) income recognised in other comprehensive income</b>		
Recognised in:		
Fair value reserve	(542)	(22,250)
Currency translation reserve	(12,074)	(17,485)
Non-controlling interest	2	(2)
<b>Total</b>	<b>(12,614)</b>	<b>(39,737)</b>

## 14. Income tax expense

EUR thousand	2009	2008
Current tax expense	4,844	7,997
Deferred tax expense (Note 20)	(767)	1,235
<b>Total</b>	<b>4,077</b>	<b>9,232</b>

In 2009 income tax liability of the companies in the Mercator Group amounts to EUR 4,844 thousand.

According to IAS 12 current tax and deferred tax are recognised as revenue or expense and are included in profit or loss. If tax relates to items recognised in equity, deferred tax is also recognised directly in equity.

## Reconciliation between tax expense and the product of accounting profit multiplied by the applicable tax rate

EUR thousand	2009	2008
Profit for the period	21,119	40,761
Income tax expense	(4,077)	(9,232)
Profit before income tax	25,196	49,993
Tax calculated at 21% tax rate (2008: 22%)	5,093	10,998
Increase (decrease) of income subject to taxation	(1,244)	(3,155)
Decrease (increase) of expenses deductible for tax purposes	2,235	3,632
Utilisation of tax reliefs	(2,007)	(2,243)
<b>Total income tax expense</b>	<b>4,077</b>	<b>9,232</b>

## Income tax recognised in other comprehensive income:

EUR thousand

	<b>2009</b>		
	Before tax	Tax (expense) benefit	Net of tax
Change in fair value of available-for-sale financial assets	841	(177)	664
Effective portion of changes in fair value of cash flow hedges	(1,462)	256	(1,206)
Revaluation of property*	-	1,904	1,904
Foreign currency translation	(12,072)	-	(12,072)
<b>Other comprehensive income</b>	<b>(12,693)</b>	<b>1,983</b>	<b>(10,710)</b>

EUR thousand

	<b>2008</b>		
	Before tax	Tax (expense) benefit	Net of tax
Revaluation of property**	181,295	(33,674)	147,621
Change in fair value of available-for-sale financial assets	(13,489)	2,970	(10,519)
Change in fair value of available-for-sale financial assets transferred to profit or loss	(3,997)	879	(3,118)
Effective portion of changes in fair value of cash flow hedges	(9,369)	756	(8,613)
Foreign currency translation	(17,487)	-	(17,487)
<b>Other comprehensive income</b>	<b>136,953</b>	<b>(29,069)</b>	<b>107,884</b>

\* Revaluation of property refers to disposal and depreciation of revalued property and change in tax rate.

\*\* Revaluation of property refers to change in fair value of property, disposal and depreciation of revalued property and change in tax rate.

## 15. Property, plant and equipment

EUR thousand	Land and buildings	Production equipment	Office and other equipment	Construction in progress	Total
<b>At 1 January 2008</b>					
Cost or valuation	1,595,519	165,919	177,841	107,490	2,046,769
Accumulated depreciation	(395,542)	(121,268)	(127,561)	-	(644,371)
<b>Carrying amount</b>	<b>1,199,977</b>	<b>44,651</b>	<b>50,280</b>	<b>107,490</b>	<b>1,402,398</b>
<b>Year ended 31 December 2008</b>					
<b>Opening carrying amount</b>	<b>1,199,977</b>	<b>44,651</b>	<b>50,280</b>	<b>107,490</b>	<b>1,402,398</b>
Effect of movements in exchange rates	(19,045)	(1,080)	(1,405)	(1,148)	(22,678)
Acquisitions through business combinations	4,788	19	6	-	4,813
Additions	123,155	15	2,878	162,472	288,520
Transfers	94,945	20,233	31,337	(139,360)	7,155
Disposals	(9,356)	(352)	(1,041)	-	(10,749)
Depreciation charge	(48,414)	(13,879)	(20,174)	-	(82,467)
Revaluation surplus	184,971	-	-	-	184,971
<b>Closing carrying amount</b>	<b>1,531,021</b>	<b>49,607</b>	<b>61,881</b>	<b>129,454</b>	<b>1,771,963</b>
<b>At 31 December 2008</b>					
Cost or valuation	2,048,978	181,122	199,224	129,454	2,558,778
Accumulated depreciation	(517,957)	(131,515)	(137,343)	-	(786,815)
<b>Carrying amount</b>	<b>1,531,021</b>	<b>49,607</b>	<b>61,881</b>	<b>129,454</b>	<b>1,771,963</b>
<b>Year ended 31 December 2009</b>					
<b>Opening carrying amount</b>	<b>1,531,021</b>	<b>49,607</b>	<b>61,881</b>	<b>129,454</b>	<b>1,771,963</b>
Effect of movements in exchange rates	(11,260)	(1,029)	(778)	(358)	(13,425)
Acquisitions through business combinations	15,748	-	-	-	15,748
Additions	57,218	9,748	6,010	76,757	149,733
Transfers*	149,165	39,109	280	(159,260)	29,294
Disposals	(3,984)	(105)	(470)	-	(4,559)
Depreciation charge	(48,353)	(18,534)	(18,576)	-	(85,463)
<b>Closing carrying amount</b>	<b>1,689,555</b>	<b>78,796</b>	<b>48,347</b>	<b>46,593</b>	<b>1,863,291</b>
<b>At 31 December 2009</b>					
Cost or valuation	2,222,815	251,282	162,159	46,593	2,682,849
Accumulated depreciation	(533,260)	(172,486)	(113,812)	-	(819,558)
<b>Carrying amount</b>	<b>1,689,555</b>	<b>78,796</b>	<b>48,347</b>	<b>46,593</b>	<b>1,863,291</b>

\* Transfers are related to transfers between groups. Closing balance is related to transfer of investment property to property, plant and equipment in the amount of EUR 4,314 thousand, transfer from intangible assets to property, plant and equipment in the amount of EUR 20,277 thousand, and other transfers in the amount of EUR 4,703 thousand. Advance payments are included in construction in progress in the amount of EUR 7,329 thousand.

Carrying amount of land and buildings refer to land in the amount of EUR 605,763 thousand and to buildings in the amount of EUR 1,083,792 thousand.

Additions of property, plant and equipment (CAPEX) in the amount of EUR 149,773 thousand, is related to:

EUR thousand	<b>2009</b>
Additions of property, plant and equipment (new facilities)	127,337
Refurbishment of retail and wholesale units	16,807
Other	5,589
<b>Total</b>	<b>149,733</b>

Disposals of property, plant and equipment in the amount of EUR 4,559 thousand are related to the disposal of commercially unviable assets.

All land and buildings of the Mercator Group were last appraised in 2008, except for land and buildings pertaining to the merged subsidiary Presoflex, d.o.o., which were last appraised on 31 July 2007. Appraisal was prepared on the basis of fair market value determined by independent authorized appraiser.

Depreciation of property, plant and equipment in the amount of EUR 85,463 thousand is included among production costs in the amount of EUR 2,607 thousand, among the selling and marketing costs in the amount of EUR 78,598 thousand, and among the administrative expenses in the amount of EUR 4,258 thousand.

Bank borrowings are not secured by land and buildings at 31 December 2009.

If land and buildings were stated on the historical cost basis, the amounts would be as follows:

EUR thousand	<b>2009</b>	<b>2008</b>
Cost	1,848,358	1,664,753
Accumulated depreciation	(362,992)	(365,245)
<b>Carrying amount</b>	<b>1,485,366</b>	<b>1,299,508</b>

Carrying amount of property, plant and equipment held under financial leases amounts to EUR 215,373 thousand (2008: EUR 162,022 thousand) and refers to land and buildings.

## 16. Intangible assets

EUR thousand	Goodwill	Trademarks, rights and licenses	Total
<b>At 1 January 2008</b>			
Cost	9,669	96,531	106,200
Amortisation and impairment losses	-	(25,947)	(25,947)
<b>Carrying amount</b>	<b>9,669</b>	<b>70,584</b>	<b>80,253</b>
Adjustment of initial accounting for business combination:			
- acquisition of company Presoflex, d.o.o.	4,540	-	4,540
- acquisition of company Interier, d.o.o.	(1,629)	-	(1,629)
<b>Carrying amount</b>	<b>12,580</b>	<b>70,584</b>	<b>83,164</b>
<b>Year ended 31 December 2008</b>			
<b>Opening carrying amount</b>	<b>12,580</b>	<b>70,584</b>	<b>83,164</b>
Effect of movements in exchange rates	(6)	(3,022)	(3,028)
Acquisition through business combinations	367	396	763
Additions	-	9,774	9,774
Disposals	-	(46)	(46)
Transfers	-	(1,106)	(1,106)
Amortisation charge	-	(11,325)	(11,325)
<b>Closing carrying amount</b>	<b>12,941</b>	<b>65,255</b>	<b>78,196</b>
<b>At 31 December 2008</b>			
Cost	12,941	93,994	106,935
Amortisation and impairment losses	-	(28,739)	(28,739)
<b>Carrying amount</b>	<b>12,941</b>	<b>65,255</b>	<b>78,196</b>
<b>Year ended 31 December 2009</b>			
<b>Opening carrying amount</b>	<b>12,941</b>	<b>65,255</b>	<b>78,196</b>
Effect of movements in exchange rates	92	(3,206)	(3,114)
Acquisition through business combinations	18	-	18
Additions	-	7,596	7,596
Disposals	-	(36)	(36)
Transfers	-	(20,277)	(20,277)
Impairment	(50)	-	(50)
Amortisation charge	-	(10,338)	(10,338)
<b>Closing carrying amount</b>	<b>13,001</b>	<b>38,994</b>	<b>51,995</b>
<b>At 31 December 2009</b>			
Cost	13,001	103,178	116,179
Amortisation and impairment losses	-	(64,184)	(64,184)
<b>Carrying amount</b>	<b>13,001</b>	<b>38,994</b>	<b>51,995</b>

Intangible assets in development as at 31 December 2009 amount to EUR 198 thousand.

Intangible assets as at 31 December 2009, include rights, patents, licenses, trademarks, and investments into software, in total amount of EUR 20,973 thousand (2008: EUR 28,837 thousand); rights to lease property in the company Mercator-S, d.o.o., in the amount of EUR

18,021 thousand (2008: EUR 36,418 thousand); and goodwill in the amount of EUR 13,001 thousand (2008: EUR 12,941 thousand).

Goodwill in the amount of EUR 13,001 thousand, which arose in previous years, is related to: acquisition of the company Presoflex, d.o.o., Croatia, in 2007 in the amount of EUR 10,509 thousand; acquisition of the companies Era Tornado, d.o.o., Croatia, and Trgohit, d.o.o., Croatia, in 2005 in the amount of EUR 1,630 thousand; acquisition of the company Interier, d.o.o., in 2007 in the amount of EUR 457 thousand; acquisition of the companies Evolution, d.d., and Mercator IP, d.o.o., in 2008 in the amount of EUR 405 thousand; and other acquisitions of non-controlling interest in previous years.

Amortisation in the amount of EUR 10,338 thousand was included among the production costs in the amount of EUR 48 thousand; among the selling and marketing costs in the amount of EUR 5,681 thousand; and among the administrative expenses in the amount of EUR 4,609 thousand.

### Impairment testing of goodwill

Goodwill in the amount of EUR 1,630 thousand, which was created in 2005 upon the acquisition of the companies Era Tornado, d.o.o., and Trgohit, d.o.o., in Croatia was allocated to cash-generating units of the Group, defined according to the store format; on 31 December 2009, it was tested for impairment.

Goodwill in the amount of EUR 10,509 thousand, which was created upon the acquisition of the company Presoflex, d.o.o., Croatia was allocated to cash-generating units of the Group, defined according to the store format, and tested for impairment on 31 December 2009.

Remaining goodwill in the amount of EUR 862 thousand, which relates to various smaller transactions, was not allocated to cash-generating units and was not impaired, because we estimate that the recoverable amount of acquired assets exceeds their carrying amount, including the goodwill.

A summary of the goodwill allocation and impairment is presented below:

EUR thousand	Effect of movements		Identified in 2009	Impairment in 2009	31 December 2009
	31 December 2008	in exchange rates			
Hypermarkets	1,117	8	-	-	1,125
Supermarkets	10,088	76	-	-	10,164
Markets	827	6	-	-	833
Other stores	16	1	-	-	17
Unallocated	893	1	18	(50)	862
<b>Total</b>	<b>12,941</b>	<b>92</b>	<b>18</b>	<b>(50)</b>	<b>13,001</b>

When testing goodwill for impairment with regard to the acquisition of the companies Era Tornado, d.o.o., and Trgohit, d.o.o., the recoverable amount of cash-generating unit was determined based on the calculations of value in use. The calculations are based on cash flow projections prepared against the background of business plans for the following year, and projected forwards upon appropriate assumptions. Following are the main assumptions used when calculating the values in use: revenue growth rate of 2% and discount rate of 9%. The gross margin is based on operation and performance history, structure of sales, and

its expectations on the development of the market. The discount rate applied is based on market rates, adjusted to reflect the specific risks related to the business units. It was determined that the recoverable amount of cash-generating units exceeds their carrying amount, including the goodwill, therefore goodwill was not impaired.

When testing goodwill for impairment with regard to the acquisition of the company Presoflex, d.o.o., the recoverable amount of cash-generating unit was determined based on the calculations of value in use. The calculations are based on cash flow projections prepared against the background of business plans for the following year, and projected forwards upon appropriate assumptions. Following are the main assumptions used when calculating the values in use: revenue growth rate of 3% and discount rate of 9%. The gross margin is based on operation and performance history, structure of sales, and its expectations on the development of the market. The discount rate applied is based on market rates, adjusted to reflect the specific risks related to the business units. It was determined that the recoverable amount of cash-generating units exceeds their carrying amount, including the goodwill, therefore goodwill was not impaired.

When testing goodwill for impairment with regard to the assets of the company Belpana, d.o.o., it was established that the recoverable amount of cash-generating units does not reach their carrying amount, including the goodwill. Therefore goodwill was impaired in the amount of EUR 50 thousand.

## 17. Investment property

EUR thousand	2009	2008
<b>Balance at 1 January</b>	<b>9,563</b>	<b>16,476</b>
Additions	24	11
Transfer to property, plant and equipment	(4,314)	(6,609)
Disposals	(935)	(53)
Depreciation charge	(211)	(262)
<b>Balance at 31 December</b>	<b>4,127</b>	<b>9,563</b>
<b>Balance at 31 December</b>		
Cost	8,047	13,362
Accumulated depreciation	(3,920)	(3,799)
<b>Carrying amount</b>	<b>4,127</b>	<b>9,563</b>

Fair value of investment property as at 31 December 2009, amounts to EUR 6,557 thousand (2008: EUR 10,144 thousand).

The following amounts were recognized in the income statement with regard to investment property:

EUR thousand	2009	2008
Rental income	304	626
Direct operating expenses arising from investment properties that generate rental income	(286)	(548)
<b>Total</b>	<b>18</b>	<b>78</b>

Depreciation in the amount of EUR 211 thousand was included among the cost of sales.

## 18. Available-for-sale financial assets

EUR thousand	2009	2008
<b>Balance at 1 January</b>	<b>4,824</b>	<b>24,235</b>
Effect of movements in exchange rates	2	(4)
Changes in fair value	841	(13,489)
Impairment	(194)	(1,527)
Disposals	-	(4,391)
<b>Balance at 31 December</b>	<b>5,473</b>	<b>4,824</b>

The Group's available-for-sale financial assets also include assets that could not be valued at fair value; thus, these assets are measured at cost.

EUR thousand	2009	2008
<b>Equity securities and shares in insurance companies:</b>		
Zavarovalnica Triglav, d.d.	3,660	2,199
<b>Equity securities and shares in other companies</b>	1,813	2,625
<b>Total</b>	<b>5,473</b>	<b>4,824</b>
Of which:		
Available-for-sale financial assets measured at cost	802	1,193
Available-for-sale financial assets measured at fair value	4,671	3,631
<b>Total equity securities and shares</b>	<b>5,473</b>	<b>4,824</b>

As at 31 December 2009, the Group does not hold any financial assets at fair value through profit or loss, or held-to-maturity investments.

## 19. Derivative financial instruments

EUR thousand	2009	2008
<b>Assets</b>		
Interest rate caps	737	-
<b>Total</b>	<b>737</b>	<b>-</b>
<b>Liabilities</b>		
Interest rate swaps	(4,945)	(3,157)
Zero cost collars	-	(441)
<b>Total</b>	<b>(4,945)</b>	<b>(3,598)</b>

The carrying amounts of derivative financial instruments equal fair values.

The amount of borrowings hedged from interest rate risk as at 31 December 2009, amounted to EUR 350,000 thousand; where Mercator held interest rate swaps in the amount of EUR 150,000 thousand (contracted interest rates varied from 3.74% to 3.787%) and interest rate caps in the amount of EUR 200,000 thousand with strike price of 4%. On 31 December the applicable floating rates, i.e. the 3m and 6m Euribor amounted to 0.75% and 1.02%, respectively. Held derivative financial instruments are designated for cash flow hedging and are very effective at regulating cash flows from borrowings.

As of 31 December 2009, the Group did not hold any derivative financial instruments designated as fair value hedges.

Other than interest rate swaps and interest rate caps the Mercator Group did not hold other contracts with third parties that represent derivative financial instruments as at 31 December 2009. Mercator Group manages financial risks in the framework of adopted policy centrally at parent company level, which enters into interest rate swap and currency forward contracts with subsidiaries on market terms based on specific policies for managing specific risks. Such derivative financial instruments are accounted for adequately.

## 20. Deferred taxes

Deferred taxes are calculated based on temporary differences under the liability method, by applying the tax rate effective in individual countries of the Mercator Group's operations.

The movement in the deferred income tax account is as follows:

EUR thousand	2009	2008
<b>At beginning of year – net deferred tax assets (liabilities)</b>	<b>(44,116)</b>	<b>(9,864)</b>
Adjustment of initial accounting	-	(3,635)
<b>At beginning of year - restated</b>	<b>(44,116)</b>	<b>(13,499)</b>
Effect of movements in exchange rates	185	149
Acquired in a business combination	(897)	(941)
Recognised in profit or loss	767	(1,235)
Recognised in other comprehensive income	1,983	(29,069)
Recognised in liabilities	838	479
<b>At end of year – net deferred tax assets (liabilities)</b>	<b>(41,240)</b>	<b>(44,116)</b>

The deferred tax assets and liabilities are attributable to the following items:

### Deferred tax liabilities

EUR thousand	Revaluation of property, plant and equipment	Change in fair value of available-for-sale financial assets	Depreciation of property, plant and equipment under EUR 500	Difference between tax recognised and business depreciation	Total
<b>At 31 December 2008</b>	<b>48,800</b>	<b>49</b>	<b>908</b>	<b>2,739</b>	<b>52,496</b>
Effect of movements in exchange rates	(115)	-	-	(70)	(185)
Acquired in a business combination	897	-	-	-	897
Recognised in profit or loss	(105)	-	(20)	(1,259)	(1,384)
Recognised in other comprehensive income	(1,904)	244	-	-	(1,660)
Recognised in liabilities	(838)	-	-	-	(838)
<b>At 31 December 2009</b>	<b>46,735</b>	<b>293</b>	<b>888</b>	<b>1,410</b>	<b>49,326</b>

## Deferred tax assets

EUR thousand	Provisions not recognised for tax purposes	Impairment of trade receivables	Impairment of inventory	Differences between tax recognised and business depreciation	Change in fair value of available-for-sale financial assets and derivatives	Other	Total
<b>At 31 December 2008</b>	<b>3,641</b>	<b>1,818</b>	<b>135</b>	<b>1,122</b>	<b>983</b>	<b>681</b>	<b>8,380</b>
Recognised in profit or loss	(268)	(463)	(65)	466	-	(287)	(617)
Recognised in other comprehensive income	-	-	-	-	323	-	323
<b>At 31 December 2009</b>	<b>3,373</b>	<b>1,355</b>	<b>70</b>	<b>1,588</b>	<b>1,306</b>	<b>394</b>	<b>8,086</b>

In 2009 companies of Mercator Group have recognised deferred tax liabilities as well as deferred tax assets. Deferred tax liabilities charged to the income statement decrease tax bases of individual companies of the Group in 2009, whereas the deferred tax assets credited to the income statement in 2009 increase them.

Deferred tax assets and liabilities are not offset in the balance sheet.

## 21. Inventories

EUR thousand	2009	2008
Raw materials	4,978	6,812
Work in progress	4,370	3,187
Finished goods	1,597	1,519
Merchandise	297,979	276,298
Less: write-down of inventories	(16,874)	(15,425)
<b>Total</b>	<b>292,050</b>	<b>272,391</b>

Inventories of raw materials and merchandise as at 31 December 2009, amounted to EUR 292,050 thousand, which represents an increase by 7.2% compared to the beginning of the year; this is mostly the result of opening of new retail units in the last quarter of 2009.

## 22. Trade and other receivables

EUR thousand	2009	2008
Trade receivables	202,815	305,785
Deferred costs	2,431	6,080
Accrued revenues	2,786	7,215
Deposits in banks	12,983	18,669
Loans	10,091	10,376
<b>Total trade and other receivables</b>	<b>231,106</b>	<b>348,125</b>
Of which non-current trade and other receivables	359	384

Trade receivables have decreased by EUR 102,970 thousand, which is mostly the result of decrease in receivables to wholesale customers and other business partners as a result of reduced volume of wholesale activities in certain business segments, active management of working capital and performing activities for limiting risks in this area.

As of 31 December 2009, Mercator Group does not have any trade and other receivables from related parties.

Accrued revenues refer to transactions with Pika card, accrued revenues from gain of disposal of property under finance lease and accrued revenue from interest of derivative financial instruments.

Deposits in the amount of EUR 12,983 thousand (2008: EUR 18,669 thousand) refer to current deposits in banks.

Loans in the amount of EUR 10,091 thousand (2008: EUR 10,376 thousand) refer to current loans to companies, which are building or built shopping centres in Serbia, in the amount of EUR 9,526 thousand, and non-current loans granted to employees in previous years. Loans for construction of shopping centres are secured by mortgages. Effective interest rates as at the balance sheet date for loans amount to 3.27%.

Carrying amounts of all trade and other receivables are in materially relevant sums consistent with their respective fair values. Receivables and loans are measured at amortised cost.

The amount of provision for the impairment of receivables as at 31 December 2009 amounted to EUR 30,860 thousand (2008: EUR 31,202 thousand). Movements of the provision for impairment of trade receivables are presented in Note 29 (Financial instruments).

## 23. Cash and cash equivalents

EUR thousand	<b>2009</b>	<b>2008</b>
Cash at bank and on hand	16,844	45,870

Cash in the amount of EUR 16,844 thousand includes cash in banks, cash in transit (daily proceeds of retail units), cash in hand, and foreign currency letters of credit.

## 24. Equity

### *Share capital*

Share capital of the company Mercator, d.d., amounts to EUR 157,128,514.53. It is divided into 3,765,361 ordinary shares.

### *Approved capital*

Pursuant to the resolution adopted at the 13th Shareholders' Assembly of the company Poslovni sistem Mercator, d.d., the Management Board may, subject to previous consent of the Supervisory Board, in five years after the entry of changes to the company Articles of Association and Bylaws into the court register, increase the share capital by up to 20% of the share capital entered on the day of adoption of this resolution at the 13th regular Shareholders' Assembly of the company Poslovni sistem Mercator, d.d., by issuing new

shares; preemptive right of the existing shareholders may be waived under the following conditions:

- ▶ The newly issued shares are used to acquire shares or shareholdings in other companies, or business assets within strategic alliances and combinations;
- ▶ Waiver of preemptive right is approved by the company Supervisory Board;
- ▶ Prior to the issuing of new shares, the company Management Board must inform the shareholders of the reasons for the emission and reasons for omission of the preemptive right; these explanations should be published on the stock market's information dissemination system;
- ▶ Within individual strategic alliances, no individual recipient of newly issued shares, or a group of associated recipients of newly issued shares, shall acquire more than 10% of the company share capital;
- ▶ An independent financial advisor shall issue a positive opinion on the fairness of the issue of new shares from the aspect of shareholders and the company. The Management Board should inform the shareholders of such opinion by publishing it on the stock market's information dissemination system no later than 30 days after entering into a binding commitment or agreement on the issue of new shares.

#### *Conditional capital increase*

Shareholders' Assembly of the company Poslovni sistem Mercator, d.d., can adopt a resolution on capital increase on the basis of provisions stated in 46th article of the company Articles of Association and Bylaws; such possibility has not been realized so far.

#### *Treasury shares*

As at 31 December 2009, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares in the amount of EUR 3,235 thousand (2008: 42,381 treasury shares; EUR 3,250 thousand).

#### **Reserves**

Reserves consist of the share premium, revenue reserves, fair value reserve and currency translation reserve. None of those types of reserves can be used for the payment of dividends or other participations in profit.

*Share premium*, amounting to EUR 198,872 thousand as at 31 December 2009, increased for EUR 24 thousand due to excess of sales value of disposed treasury shares over cost in year 2009.

*Revenue reserves*, amounting to EUR 270,194 thousand as at 31 December 2009, include legal reserves and other revenue reserves.

As at 31 December 2009, the Group holds legal reserves in the amount of EUR 13,404 thousand. Share premium and legal reserves can be used in surplus amount to increase the share capital from company assets, and for covering the net loss of the business year, or to cover the carried forward net loss, if revenue reserves are not used simultaneously to pay dividends to the shareholders.

As at 31 December 2009, the Mercator Group held 42,192 treasury shares in the amount of EUR 3,235 thousand. In the year 2009 the number of treasury shares decreased by 189 due to acquisition of interest in the company Interior, d.o.o. The reserve for treasury shares is reported among other revenue reserves.

*Other revenue reserves* as at 31 December 2009 amount to EUR 253,555 thousand. They include residuals of retained earnings from previous years. They can be used for any purpose, except for the amount of the reserve for treasury shares within other revenue reserves.

*Currency translation reserve* has in 2009 decreased by EUR 12,074 thousand, which is related to a decrease due to currency translation differences that occurred upon the integration of financial statements of foreign subsidiaries into the consolidated financial statements.

*Fair value reserve* which amounts to EUR 186,029 thousand as at 31 December 2009, includes the revaluation reserve of property, measured by the revaluation model, changes to the fair value of available-for-sale financial assets, and changes to the value of effective cash flow hedges.

Changes in fair value reserve are shown below:

EUR thousand	Revaluation reserve of property	Fair value reserve of available- for-sale financial assets	Hedging reserve	Total
<b>At 1 January 2008</b>	<b>47,651</b>	<b>14,656</b>	<b>5,771</b>	<b>68,078</b>
Adjustment according to IAS 8.44	(1,248)	-	-	(1,248)
<b>At 1 January 2008 (restated)</b>	<b>46,403</b>	<b>14,656</b>	<b>5,771</b>	<b>66,830</b>
Revaluation of property	181,223	-	-	181,223
Disposal and depreciation of revalued property	(4,124)	-	-	(4,124)
Effective portion of changes in fair value of cash flow hedges	-	-	(9,369)	(9,369)
Change in fair value of available-for-sale financial assets	-	(13,489)	-	(13,489)
Change in fair value of available-for-sale financial assets transferred to profit or loss	-	(3,997)	-	(3,997)
Deferred tax	(32,928)	3,849	756	(28,323)
<b>At 31 December 2008</b>	<b>190,574</b>	<b>1,019</b>	<b>(2,842)</b>	<b>188,751</b>
<b>At 1 January 2009</b>	<b>190,574</b>	<b>1,019</b>	<b>(2,842)</b>	<b>188,751</b>
Disposal and depreciation of revalued property	(3,112)	-	-	(3,112)
Effective portion of changes in fair value of cash flow hedges	-	-	(1,462)	(1,462)
Change in fair value of available-for-sale financial assets	-	841	-	841
Deferred tax	931	(177)	257	1,011
<b>At 31 December 2009</b>	<b>188,393</b>	<b>1,683</b>	<b>(4,047)</b>	<b>186,029</b>

### Dividends

Shareholders' Assembly adopted a resolution to pay dividends in 2009 in total amount of EUR 16,944 thousand (2008: EUR 16,003 thousand), or 4.5 EUR of gross dividend per share (2008: 4.25 EUR gross per share). Because the company disposed only part of treasury shares, precisely 189 treasury shares, while the rest 42,192 treasury shares were considered in calculation of dividends payout, the amount of EUR 190 thousand related to treasury shares was transferred back to retained earnings. Therefore undistributed profit of the period for the purposes of dividend payout was actually decreased to EUR 16,754 thousand (2008: EUR 15,823 thousand).

The proposed payment of dividends for 2010 amounts to EUR 27,111 thousand (EUR 7.2 per share); this proposal is yet to be confirmed by the Shareholders' Assembly.

Retained earnings have decreased by EUR 761 thousand due to the purchase of additional ownership shares of the companies M - Rodić, d.o.o., Mercator – Mex, d.o.o., and Interier, d.o.o.

## 25. Earnings per share

Basic earnings per share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year, excluding the average number of treasury shares.

	2009	2008
Profit attributable to shareholders (EUR thousand)	21,232	40,846
Weighted average number of ordinary shares	3,723,169	3,722,980
<b>Basic earnings per share (in EUR)</b>	<b>5.7</b>	<b>11.0</b>

Weighted average number of ordinary shares:

	2009	2008
Issued ordinary shares at 1 January	3,765,361	3,765,361
Effect of treasury shares	(42,192)	(42,381)
<b>Weighted average number of ordinary shares at 31 December</b>	<b>3,723,169</b>	<b>3,722,980</b>

Weighted average number of ordinary shares is calculated by the following formula:  
(Number of ordinary shares at the beginning of period + number of additional ordinary shares in the period) × time weight factor

The time weight factor represents the number, or share, of days when the shares are exercised, i.e. as of the day when cash was due for payment.

Since the Group does not have any preference shares or convertible bonds, diluted earnings per share are the same as basic earnings per share.

## 26. Financial liabilities

EUR thousand	2009	2008
<b>Non-current financial liabilities</b>		
Bank borrowings	442,845	430,268
Finance lease liabilities	203,329	155,417
Bonds	36,540	36,540
Borrowings from other companies	30	-
Other financial liabilities*	803	562
<b>Total</b>	<b>683,547</b>	<b>622,787</b>
<b>Current financial liabilities</b>		
Bank borrowings	190,948	256,904
Borrowings from other companies	1,873	1,528
Current portion of finance lease liabilities	12,044	6,605
Current portion of bank borrowings	155,225	137,558
Current portion of other financial liabilities*	7,765	10,202
<b>Total</b>	<b>367,855</b>	<b>412,797</b>
<b>Total financial liabilities</b>	<b>1,051,402</b>	<b>1,035,584</b>

\*Other financial liabilities are related to the liabilities for purchase of 12% ownership share in the company M - Rodić, d.o.o., and forward purchase of the 19% ownership share in the company Mercator - Mex, d.o.o.

In 2004, the company Poslovni sistem Mercator, d.d., issued 365,400 bonds with nominal value of EUR 100 per bond. Bonds are freely transferable, subject to relevant effective regulations and rules laid out by the Central Securities Clearing Corporation (KDD). The fixed interest rate on these bonds is 4.80% per annum. Interest payments are due each year on 27 September for the previous year, until the maturity of the bond. Face value is due for payment entirely upon the maturity of the bond, i.e. on 27 September 2011.

As at 31 December 2009, the Group's financial liabilities related to issued bonds are reported in total amount of EUR 36,540 thousand.

Effective interest rates as at the balance sheet date:

	2009	2008
Bank borrowings	4.09%	4.19%
Other borrowings	3.60%	4.80%

As at 31 December 2009, the Group does not have any pledged property.

Floating interest rates are mostly interest rates related to Euribor. Fixed interest rates are mostly related to borrowings from domestic banks, with fixed nominal interest rate, and interest rate on bonds. Financial liabilities are hedged with the use of derivative financial instruments, i.e. by interest rate swaps and caps.

As of 31 December 2009, Mercator Group met all financial covenants and other terms, stated in loan agreements with banking partners. Mercator Group does not have a contracted clause in any of its loan agreements on loan becoming due in case of important change in ownership (Change of Control Clause).

## Finance lease liabilities

Finance lease liabilities – minimum lease payments:

EUR thousand	2009	2008
Less than one year	16,862	12,029
Between one and five years	92,407	50,399
More than five years	133,358	139,143
<b>Total</b>	<b>242,627</b>	<b>201,571</b>
Future finance charges on finance leases	27,254	39,549
<b>Present value of finance lease liabilities</b>	<b>215,373</b>	<b>162,022</b>

The present value of finance lease liabilities is as follows:

EUR thousand	2009	2008
Less than one year	12,044	6,605
Between one and five years	76,570	31,017
More than five years	126,759	124,400
<b>Total</b>	<b>215,373</b>	<b>162,022</b>

Carrying amounts of all financial liabilities approximate their fair values. The share of non-current financial liabilities in total financial liabilities as at 31 December 2009 amounted to 65% (60% as at 31 December 2008).

## 27. Provisions

EUR thousand	Restitution claims	Restructuring provisions	Legal claims	Retirement benefits and jubilee premiums provisions	Other provisions	Total
<b>At 31 December 2008</b>	<b>1,943</b>	-	<b>9,477</b>	<b>19,848</b>	<b>147</b>	<b>31,415</b>
Increase	1,332	488	2,898	3,302	1,601	9,621
Utilisation	-	-	(110)	(2,159)	(1,231)	(3,500)
Reversal	(3)	-	(307)	-	-	(310)
Effect of movements in exchange rates	-	-	15	(54)	1	(38)
<b>At 31 December 2009</b>	<b>3,272</b>	<b>488</b>	<b>11,973</b>	<b>20,937</b>	<b>518</b>	<b>37,188</b>

### *Provisions for restitution claims*

Restitution claims as at 31 December 2009 amount to EUR 3,272 thousand. Provision has increased for EUR 1,332 thousand compared to previous year, while a reversal of provision was debited in the amount of EUR 3 thousand.

### *Provisions for restructuring costs*

As at 1 December 2009 the Group closed down 8 organisational units. Based on that event a process of terminating employment contracts with a larger number of employees has started

according to The Labor Code. In line with the provisions of Article 99 of The Labor Code the Group adopted a programme of reducing redundant employees, which entails: grounds for reduced need of workforce, measures for preventing or restrictions of reductions in employment of workers, whereby the Group examined the possibility of continued employment under different terms, list of redundant employees, measures and criteria for selection of measures to mitigate the adverse effects of reducing redundant employees. The programme for reducing redundant employees is coordinated with representative unions in the company Poslovni sistem Mercator, d.d. The programme was financially evaluated. The Group has recognised a provision in the amount of EUR 488 thousand.

#### *Legal claims*

In 2009 provisions for legal claims have been reversed in the amount of EUR 307 thousand. In 2009 legal claims have been paid out as a debit to provisions in the amount of EUR 110 thousand. On the basis of received legal claims and legal opinion the Group recognised additional provisions in the total amount of EUR 2,898 thousand, where also newly recognised provisions for reimbursing transportation costs of former employees in the amount of EUR 175 thousand are included. Total recognised provisions for reimbursing transportation costs of former employees therefore amount to EUR 1,041 thousand. Payment of these legal claims begun in 2008. Former employees can claim reimbursement of expenses also for the years 2005 and 2006. As at 1 January 2007 a new Collective Agreement of the Retail Industry came into force and from that date the reimbursement of transportation costs is not in dispute.

#### *Retirement benefits and jubilee premiums provisions*

As of 31 December 2009 retirement benefits and jubilee premiums provisions amount to EUR 20,937 thousand. Provisions have increased for EUR 3,302 thousand compared to previous year. The difference is included in other operating expenses of the current year. In 2009 payment of severance and jubilee bonuses has been debited to provisions in the total amount of EUR 2,159 thousand.

#### *Other provisions*

Increases and decreases in other provisions in net amount of EUR 371 thousand are in large part related to the provisions of the companies Mercator, d.d., and Mercator IP, d.o.o. Other provisions have increased on behalf of provisions made for improvement of working conditions of the disabled in the amount of EUR 1,601 thousand. In 2009 provisions for improvement of working conditions of the disabled have been used in the amount of EUR 1,231 thousand, by replacing increased costs due to higher sick leave of disabled workers.

## **28. Trade and other payables**

EUR thousand	<b>2009</b>	<b>2008</b>
Trade payables	468,996	524,932
Social security and other taxes	27,527	34,860
Other payables	7,512	9,888
Accrued costs	14,791	13,901
Deferred revenues	9,107	18,623
<b>Total</b>	<b>527,933</b>	<b>602,204</b>

In 2009 trade and other payables have decreased by EUR 55,963 thousand, which is the result of decrease in trade payables to equipment and construction service suppliers.

As at 31 December 2009, Mercator Group does not have any liabilities towards the members of the Supervisory Board, while towards Management Board and other employees it has liabilities on account of recognised undisbursed compensation for December 2009.

## 29. Financial instruments

### *Credit risk*

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

EUR thousand	2009	2008
Trade and other receivables	208,032	319,080
Deposits in banks	12,983	18,669
Loans	10,091	10,376
<b>Total</b>	<b>231,106</b>	<b>348,125</b>

Trade receivables derive from wholesale of goods, material, and services, and sale of goods to individuals, Mercator Pika card holders. Both wholesale and retail customers are dispersed; hence, there is no major exposure to an individual customer. The Group is also constantly monitoring customer payment defaults and checks the rating of external customers and Mercator Pika card holders.

Measures prepared in case of a considerable increase in risk include above all obtaining appropriate security, introduction of more strict control of customers in default, more active collecting procedures, and, if required, establishment of an expert rating department that would evaluate and monitor credit risk systematically.

The maximum exposure to credit risk for trade and other receivables at the reporting date by geographic region was:

EUR thousand	2009	2008
Slovenia	141,949	254,813
Foreign countries	89,157	93,312
<b>Total</b>	<b>231,106</b>	<b>348,125</b>

The maximum exposure to credit risk for trade and other receivables at the reporting date by type of customer was:

EUR thousand	2009	2008
Retail partners	50,050	75,711
Wholesale and other partners	181,056	272,414
<b>Total</b>	<b>231,106</b>	<b>348,125</b>

In the category of retail partners the Group included receivables from individuals related to purchases in company retail units with Mercator Pika card; the category of wholesale and other partners includes all receivables from sale of goods, material, and services, to legal/corporate entities, and receivables from employees and state/government bodies.

Security of trade and other receivables (in gross amounts, without the allowance for impairment):

EUR thousand	2009	2008
Secured receivables	107,680	27,948
Unsecured receivables	154,286	351,379
<b>Total</b>	<b>261,966</b>	<b>379,327</b>

### *Impairment of receivables*

The aging of trade and other receivables at the reporting date was:

EUR thousand	Gross Impairment		Gross Impairment	
	2009	2009	2008	2008
Not past due	193,725	-	331,146	-
Past due 0-60 days	33,532	-	20,498	4,601
Past due 61-74 days	2,082	851	2,243	1,161
Past due 75-89 days	1,494	1,131	1,422	1,422
More than 90 days	31,133	28,878	24,018	24,018
<b>Total</b>	<b>261,966</b>	<b>30,860</b>	<b>379,327</b>	<b>31,202</b>

The movement in the allowance for impairment in respect of trade and other receivables:

EUR thousand	2009	2008
<b>Balance at 1 January</b>	<b>31,202</b>	<b>30,587</b>
Effect of movements in exchange rates	(49)	(293)
Impairment loss recognised during the year	3,784	4,370
Collected receivables written off during the year	(1,861)	(2,480)
Decrease of allowance for impairment during the year	(2,216)	(982)
<b>Balance at 31 December</b>	<b>30,860</b>	<b>31,202</b>

### *Liquidity risk*

The following are the maturities of liabilities:

31 December 2009

EUR thousand	Carrying amount	Contractual cashflow	1 year or less	1-2 years	2-5 years	Over 5 years
<b>Non-derivative liabilities</b>						
Bank borrowings	789,018	931,869	508,610	177,128	213,792	32,339
Bonds	36,540	40,048	1,754	38,294	-	-
Borrowings from other companies	1,903	2,221	-	606	1,615	-
Finance lease liabilities	215,373	242,627	16,862	16,506	75,901	133,358
Other financial liabilities	8,568	8,568	7,765	-	803	-
Trade and other payables and current tax liabilities	528,097	528,097	528,097	-	-	-
<b>Total</b>	<b>1,579,499</b>	<b>1,753,430</b>	<b>1,063,088</b>	<b>232,534</b>	<b>292,111</b>	<b>165,697</b>

31 December 2008

EUR thousand	<b>Carrying amount</b>	<b>Contractual cashflow</b>	<b>1 year or less</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>Over 5 years</b>
<b>Non-derivative liabilities</b>						
Bank borrowings	824,730	860,853	411,639	173,609	238,215	37,390
Bonds	36,540	41,802	1,754	1,754	38,294	-
Borrowings from other companies	1,528	1,532	528	-	-	1,004
Finance lease liabilities	162,022	201,564	12,029	12,428	37,964	139,143
Other financial liabilities	10,764	10,764	10,202	-	562	-
Trade and other payables and current tax liabilities	602,928	602,928	602,928	-	-	-
<b>Total</b>	<b>1,638,512</b>	<b>1,719,443</b>	<b>1,039,080</b>	<b>187,791</b>	<b>315,035</b>	<b>177,537</b>

The following table indicates the periods in which the cash flows associated with derivatives that are cash flow hedges are expected to occur and their impact on profit or loss.

2009

EUR thousand	<b>Carrying amount</b>	<b>Contractual cashflow</b>	<b>1 year or less</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>Over 5 years</b>
<b>Interest rate swaps and caps</b>						
Assets	737	-	-	-	-	-
Liabilities	(4,945)	(6,207)	(3,404)	(2,803)	-	-

2008

EUR thousand	<b>Carrying amount</b>	<b>Contractual cashflow</b>	<b>1 year or less</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>Over 5 years</b>
<b>Interest rate swaps and zero cost collars</b>						
Assets	-	1,948	1,948	-	-	-
Liabilities	(3,598)	(11,976)	(7,990)	(3,986)	-	-

## ***Currency risk***

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows:

31 December 2009

EUR thousand

	<b>EUR</b>	<b>HRK</b>	<b>RSD</b>	<b>BAM</b>	<b>BGN</b>	<b>ALL</b>
Trade and other receivables	146,203	16,630	63,576	4,358	1,817	1,161
Available-for-sale financial assets	5,271	202	-	-	-	-
Cash and cash equivalents	3,271	282	11,141	1,133	4	1,013
Financial liabilities	(1,050,396)	-	-	(1,006)	-	-
Trade and other payables	(346,590)	(57,140)	(103,887)	(14,418)	(1,509)	(4,553)
<b>Balance sheet exposure</b>	<b>(1,242,241)</b>	<b>(40,026)</b>	<b>(29,170)</b>	<b>(9,933)</b>	<b>312</b>	<b>(2,379)</b>
Forward exchange contracts	-	-	-	-	-	-
<b>Net exposure</b>	<b>(1,242,241)</b>	<b>(40,026)</b>	<b>(29,170)</b>	<b>(9,933)</b>	<b>312</b>	<b>(2,379)</b>

\* HRK (Croatian kuna), RSD (Serbian dinar), BAM (convertible mark). BGN (Bulgarian lev), ALL (Albanian lek).

Mercator Group does not hold any derivative financial instruments for currency risk hedging (forward exchange contracts) as at 31 December 2009.

31 December 2008

EUR thousand

	<b>EUR</b>	<b>HRK</b>	<b>RSD</b>	<b>BAM</b>
Trade and other receivables	225,671	28,613	55,219	8,622
Available-for-sale financial assets	4,433	391	-	-
Cash and cash equivalents	703	1,841	12,098	31,228
Financial liabilities	(1,017,177)	-	(9,331)	(9,076)
Trade and other payables	(404,088)	(61,438)	(91,947)	(44,731)
<b>Balance sheet exposure</b>	<b>(1,190,458)</b>	<b>(30,593)</b>	<b>(33,961)</b>	<b>(13,957)</b>
Forward exchange contracts	-	-	-	-
<b>Net exposure</b>	<b>(1,190,458)</b>	<b>(30,593)</b>	<b>(33,961)</b>	<b>(13,957)</b>

The following significant exchange rates applied during the period:

Units per EUR	Average rate		Reporting date spot rate	
	2009	2008	2009	2008
HRK	7.341	7.224	7.300	7.356
RSD	93.785	81.119	95.025	89.372
BAM, BGN	1.956	1.956	1.956	1.956
ALL	131.547	-	138.900	-

#### Sensitivity analysis

A 5 percent appreciation of the Euro against the following currencies at 31 December would have increased (decreased) profit or loss and equity by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2008.

EUR thousand	Profit or loss	Equity
<b>2009</b>		
HRK	(8,145)	(11,385)
RSD	(5,169)	(10,766)
BAM, BGN	(2,388)	(3,462)
ALL	20	(146)
<b>2008</b>		
HRK	(8,563)	(11,478)
RSD	(4,264)	(11,047)
BAM	(1,228)	(3,438)

A 5 percent depreciation of the Euro against the above currencies at 31 December would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

#### **Interest rate risk**

##### Exposure

The following table presents the Group's exposure to interest rate risk:

EUR thousand	2009	2008
<b>Fixed rate instruments</b>		
Financial assets	2,761	19,751
Financial liabilities	(150,230)	(80,733)
<b>Total</b>	<b>(147,469)</b>	<b>(60,982)</b>
<b>Variable rate instruments</b>		
Financial assets	20,313	9,294
Financial liabilities	(901,172)	(954,851)
<b>Total</b>	<b>(880,859)</b>	<b>(945,557)</b>

### *Fair value sensitivity analysis for fixed rate instruments*

The Group does not hold any fixed rate financial instruments at fair value through profit or loss, nor derivative financial instruments designated as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

### *Cash flow sensitivity analysis for variable rate instruments*

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2008.

EUR thousand	Profit or loss		Equity	
	100 bp increase	100 bp decrease	100 bp increase	100 bp decrease
<b>2009</b>				
Variable rate instruments	(8,809)	8,809	-	-
Interest rate swaps and caps	-	-	1,500	(1,500)
<b>Cash flow sensitivity (net)</b>	<b>(8,809)</b>	<b>8,809</b>	<b>1,500</b>	<b>(1,500)</b>
<b>2008</b>				
Variable rate instruments	(9,563)	9,563	-	-
Interest rate swaps and caps	-	-	2,815	(3,500)
<b>Cash flow sensitivity (net)</b>	<b>(9,563)</b>	<b>9,563</b>	<b>2,815</b>	<b>(3,500)</b>

### *Fair values*

Fair values of assets and liabilities and carrying amounts shown in the balance sheet:

EUR thousand	31 December 2009		31 December 2008	
	Carrying amount	Fair value	Carrying amount	Fair value
Derivative financial instruments	(4,208)	(4,208)	(3,598)	(3,598)
Trade and other receivables	231,106	231,106	348,125	348,125
Available-for-sale financial assets	5,473	5,473	4,824	4,824
Cash and cash equivalents	16,844	16,844	45,870	45,870
Fixed rate bank borrowings	(104,841)	(104,841)	(32,434)	(32,434)
Floating rate bank borrowings	(684,177)	(684,177)	(792,296)	(792,296)
Bonds	(36,540)	(36,905)	(36,540)	(35,392)
Borrowings from other companies	(1,903)	(1,903)	(1,528)	(1,528)
Other financial liabilities	(8,568)	(8,568)	(10,764)	(10,764)
Finance lease liabilities	(215,373)	(215,373)	(162,022)	(162,022)
Trade and other payables	(527,933)	(527,933)	(602,204)	(602,204)

Fair value of bonds is for purposes of reporting calculated on the basis of last available quoted price of Mercator bond on the Ljubljana Stock Exchange before date of reporting, whereas their yield to maturity was 4.27%. Fair values of other non-derivative financial

liabilities are not determined, as the carrying amount represents a reasonable approximation of fair value.

#### *Fair value hierarchy*

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- ▶ Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- ▶ Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
- ▶ Level 3: inputs for the asset or liability that are not based on observable market data.

### **2009**

EUR thousand	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Available-for-sale financial assets	4,671	-	802	5,473
Derivative financial instruments - assets	-	737	-	737
Derivative financial instruments - liabilities	-	(4,945)	-	(4,945)

### **30. Operating leases**

Operating lease liabilities (Mercator group as lessee) – minimum lease payments:

EUR thousand	<b>2009</b>	<b>2008</b>
Less than one year	11,107	18,415
Between one and five years	41,679	73,025
More than five years	110,237	155,701
<b>Total</b>	<b>163,023</b>	<b>247,141</b>

### **31. Capital commitments**

Capital expenditures (into property, plant and equipment), defined in contracts and agreements, which were not yet recognised in the financial statements as at the balance sheet date:

EUR thousand	<b>2009</b>	<b>2008</b>
Property, plant and equipment	35,358	26,651

### **32. Contingencies**

EUR thousand	<b>2009</b>	<b>2008</b>
Coupons	6,316	5,828
Merchandise in consignment	5,582	937
Guarantees	11,482	11,498
Other	3,992	8,434
<b>Total</b>	<b>27,372</b>	<b>26,697</b>

As at 31 December 2009, the Group does not have any mortgages or pledged property.

Tax authorities may, in the period of five or ten years after the tax return date, review the operation of the companies in the Group, which may result in additional taxation, including the liability of default interest payment and penalty related to corporate income tax or other taxes and duties. The companies of the Group are not aware of any circumstances that could cause such material liability.

In a case of a collective labour dispute, the Supreme Court of the Republic of Slovenia has ruled that the Collective Labour Agreement for Catering and Tourism Industry includes a definition of the minimum commute allowance (allowance for transport to and from work) while the tariff appendix to the sale Collective Labour Agreement expressly states the actual amount of this allowance as being equal to the upper threshold of untaxed amounts (in compliance with the tax decree), i.e. to the amount of 100%. Based on this decision, several individual labour disputes were instituted as claims were asserted for the recovery or reimbursement of the difference in the commute allowance paid out in the period until 31 December 2006. Lower courts have followed the decision of the Supreme Court of the Republic of Slovenia and ruled in favour of the parties appealing for the reimbursement of commute allowances up to 100%. The company Mercator, d.d., disagrees with such decision as both the Collective Labour Agreement effective for the relevant industry and the Company Collective Labour Agreement clearly stipulate that commute allowance shall be reimbursed in the amount of 60 percent. For all existing lawsuit claims, the company Mercator, d.d., established adequate provisions as at 31 December 2009. The volume and probability of any additional liabilities potentially deriving from this affair could not be reliably estimated as at 31 December 2009; therefore, the company Mercator, d.d., did not establish additional provisions with regard to this affair. The company Mercator, d.d., will use all available legal means for protection of its legal and economic interests in this affair.

### 33. Related party transactions

Related parties of the Group are its management personnel. Included in the management personnel are members of Management Boards and Supervisory Boards in the companies of Mercator Group.

In 2009, the Group paid out the following compensation in gross amounts to Management Board members and Supervisory Board members of group companies:

EUR thousand	2009		2008	
	Amount	Number of recipients	Amount	Number of recipients
Members of Management Boards of companies in Mercator Group	2,273	18	2,033	14
- basic salaries	1,683		1,318	
- performance bonuses	483		617	
- other employment benefits	107		98	
Members of Supervisory Boards of companies in Mercator Group	247	16	213	10
<b>Total</b>	<b>2,520</b>	<b>34</b>	<b>2,246</b>	<b>24</b>

Members of Supervisory Boards in Mercator Group subsidiaries do not receive any compensation for their work, therefore the disclosed amounts refer solely to the parent company.

Gross payments to Management Board and Supervisory Board members of companies in Mercator Group represent 0.9% of total employee benefit expenses (2008: 0.8%).

### **34. Events after the balance sheet date**

- ▶ As of 1 January 2010, the new macro-organizational structure of the Mercator Group has been put in effect. The key reasons for the reorganization are the need for improved local responsiveness in all markets and improved adjustment to consumer needs, improved operating efficiency, adjustment of the organizational complexity of international operations, and preparation for the option of monetization of our trade property and facilities in order to accelerate our development cycle.
- ▶ On 4 January 2010, the company Poslovni sistem Mercator, d.d., founded the company Modiana, d.o.o. The activities of clothing program and drugstores will be transferred to the newly founded company.
- ▶ On 17 February 2010, the companies Getro, d.d., and Mercator - H, d.o.o., completed their strategic alliance based on the agreement on the acquisition of trade activities of the Croatian trade company Getro, d.d., signed by the partners involved on 18 December 2009.

# Independent auditor's report



## Independent Auditor's Report

To the Shareholders of Poslovni sistem Mercator, d.d., Ljubljana

We have audited the accompanying consolidated financial statements of the company Poslovni sistem Mercator, d.d. and its subsidiaries (the Mercator Group) which comprise the consolidated statement of financial position as at 31 December 2009, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### *Management's responsibility for the financial statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements prepared in accordance with International Financial Reporting Standards, as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### *Auditor's responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Mercator Group as at 31 December 2009, its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

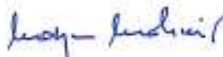
### *Report on other legal and regulatory requirements*

As required by the Slovenian Companies Act we herewith confirm that the information in the management report is in conformity with the accompanying financial statements.

  
Danilo Bukovec, B.Sc.Ec.  
Certified Auditor

Ljubljana, 18 February 2010

KPMG SLOVENIJA,  
podjetje za revidiranje, d.o.o.

  
Marjan Mahnič, B.Sc.Ec.  
Certified Auditor  
Partner

KPMG Slovenija, d.o.o.

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**AUDITED FINANCIAL STATEMENTS  
OF THE COMPANY  
POSLOVNI SISTEM MERCATOR, D.D.**

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# Statement of financial position

As at 31 December

EUR thousand

	2009	2008
<b>ASSETS</b>		
<b>Non-current assets</b>		
Property, plant and equipment	1,011,915	1,002,958
Investment property	4,127	9,563
Intangible assets	10,870	11,159
Deferred tax assets	8,174	8,430
Trade and other receivables	315	312
Investment into equity of subsidiaries	587,177	564,019
Available-for-sale financial assets	4,972	4,213
	<b>1,627,550</b>	<b>1,600,654</b>
<b>Current assets</b>		
Inventories	178,091	180,819
Trade and other receivables	136,408	250,330
Current tax assets	2,028	541
Derivative financial instruments	737	-
Cash and cash equivalents	2,457	-
	<b>319,721</b>	<b>431,690</b>
<b>Total assets</b>	<b>1,947,271</b>	<b>2,032,344</b>
<b>EQUITY</b>		
Ordinary shares	157,129	157,129
Share premium	198,872	198,848
Treasury shares	(3,235)	(3,250)
Revenue reserves	238,013	235,459
Fair value reserve	168,156	173,341
Retained earnings	7,872	3,444
Profit for the period	19,281	16,070
	<b>786,088</b>	<b>781,041</b>
<b>LIABILITIES</b>		
<b>Non-current liabilities</b>		
Trade and other payables	2,872	2,271
Financial liabilities	447,100	411,959
Deferred tax liabilities	38,051	39,055
Provisions	32,131	27,222
	<b>520,154</b>	<b>480,507</b>
<b>Current liabilities</b>		
Trade and other payables	355,811	423,490
Financial liabilities	280,273	343,708
Derivative financial instruments	4,945	3,598
	<b>641,029</b>	<b>770,796</b>
<b>Total liabilities</b>	<b>1,161,183</b>	<b>1,251,303</b>
<b>Total equity and liabilities</b>	<b>1,947,271</b>	<b>2,032,344</b>

## Income statement

EUR thousand	2009	2008
Revenue	1,745,129	1,780,222
Cost of sales	(1,612,996)	(1,644,710)
<b>Gross profit</b>	<b>132,133</b>	<b>135,512</b>
Administrative expenses	(77,459)	(79,211)
Other income	6,827	20,559
<b>Results from operating activities</b>	<b>61,501</b>	<b>76,860</b>
Finance income	8,141	16,410
Finance expense	(44,962)	(52,543)
<b>Net finance expense</b>	<b>(36,821)</b>	<b>(36,133)</b>
<b>Profit before income tax</b>	<b>24,680</b>	<b>40,727</b>
Income tax expense	(5,399)	(8,588)
<b>Profit for the period</b>	<b>19,281</b>	<b>32,139</b>
Basic and diluted earnings per share (in EUR)	5.2	8.6

## Statement of comprehensive income

EUR thousand	2009	2008
<b>Profit for the period</b>	19,281	32,139
<b>Other comprehensive income:</b>		
Change in fair value of available-for-sale financial assets	728	(12,330)
Change in fair value of available-for-sale financial assets transferred to profit or loss	-	(3,996)
Effective portion of changes in fair value of cash flow hedges	(125)	(10,760)
Change in fair value of cash flow hedges transferred to profit or loss	(1,337)	1,391
Change in fair value of investment into equity of subsidiaries	(18)	(3,390)
Revaluation of property	-	133,898
Deferred tax	1,942	(23,123)
Acquisition of companies	1,291	-
<b>Other comprehensive income for the period</b>	<b>2,481</b>	<b>81,690</b>
<b>Total comprehensive income for the period</b>	<b>21,763</b>	<b>113,829</b>

## Statement of changes in equity

EUR thousand	Ordinary shares	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Total
<b>Balance at 1 January 2008</b>	157,129	198,848	(3,250)	214,979	94,915	2,705	17,709	683,035
<b>Total comprehensive income for the period</b>								
Profit for the period	-	-	-	-	-	-	32,139	32,139
Other comprehensive income	-	-	-	-	78,426	3,264	-	81,690
<b>Total comprehensive income for the period</b>	-	-	-	-	<b>78,426</b>	<b>3,264</b>	<b>32,139</b>	<b>113,829</b>
<b>Transactions with owners, recorded directly in equity</b>								
<b>Contributions by and distributions to owners</b>								
Dividends to equity holders	-	-	-	-	-	(15,823)	-	(15,823)
Treasury shares disposal	-	-	-	-	-	-	-	-
Transfer of profit for the period to retained earnings	-	-	-	-	-	17,709	(17,709)	-
Allocation of disposable income following the Management / Supervisory Board resolution	-	-	-	16,070	-	-	(16,070)	-
Allocation of disposable income following the Shareholders' Assembly resolution	-	-	-	4,411	-	(4,411)	-	-
<b>Total contributions by and distributions to owners</b>	-	-	-	20,481	-	(2,525)	(33,779)	(15,823)
<b>Total transactions with owners</b>	-	-	-	20,481	-	(2,525)	(33,779)	(15,823)
<b>Balance at 31 December 2008</b>	<b>157,129</b>	<b>198,848</b>	<b>(3,250)</b>	<b>235,459</b>	<b>173,341</b>	<b>3,444</b>	<b>16,070</b>	<b>781,041</b>

## Statement of changes in equity (continued)

EUR thousand	Ordinary shares	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Total
<b>Balance at 1 January 2009</b>	157,129	198,848	(3,250)	235,459	173,341	3,444	16,070	781,041
<b>Total comprehensive income for the period</b>								
Profit for the period	-	-	-	-	-	-	19,281	19,281
Other comprehensive income	-	-	-	-	(5,185)	7,666	-	2,481
<b>Total comprehensive income for the period</b>	-	-	-	-	<b>(5,185)</b>	<b>7,666</b>	<b>19,281</b>	<b>21,762</b>
<b>Transactions with owners, recorded directly in equity</b>								
<b>Contributions by and distributions to owners</b>								
Dividends to equity holders*	-	-	-	-	-	(16,754)	-	(16,754)
Treasury shares disposal	-	24	15	(15)	-	15	-	39
Transfer of profit for the period to retained earnings	-	-	-	-	-	16,070	(16,070)	-
Allocation of disposable income following the Shareholders' Assembly resolution	-	-	-	2,569	-	(2,569)	-	-
<b>Total contributions by and distributions to owners</b>	-	24	15	2,554	-	(3,238)	(16,070)	(16,715)
<b>Total transactions with owners</b>	-	24	15	2,554	-	(3,238)	(16,070)	(16,715)
<b>Balance at 31 December 2009</b>	<b>157,129</b>	<b>198,872</b>	<b>(3,235)</b>	<b>238,013</b>	<b>168,156</b>	<b>7,872</b>	<b>19,281</b>	<b>786,088</b>

\* The amount of dividends to equity holders differs from the amount declared by the Shareholders' Assembly, due to consideration of treasury shares in dividends calculation.

## Proposal for the allocation of distributable profit

The distributable profit for the year 2009 consists of the following components:

EUR	
<b>Net profit for the year 2009</b>	19,281,204.96
Retained earnings	7,872,219.42
<b>Distributable profit for the year</b>	<b>27,153,424.38</b>

The proposal for the allocation of distributable profit, which amounted to EUR 27,153,424.38 as at 31 December 2009, is as follows:

- ▶ a part of the distributable profit in the amount of EUR 27,110,599.20 shall be allocated for the payment of dividends in gross value of EUR 7.20 per ordinary share,
- ▶ the remaining part of the distributable profit in the amount of EUR 42,825.18 remains unallocated.

3,765,361 ordinary shares which were entered into the court registry as at 31 December 2009, were considered for the proposed dividend payment, while dividends will not be paid for the amount of treasury shares of the company.

## Statement of cash flows

EUR thousand	2009	2008
<b>Cash flows from operating activities</b>		
Profit for the period	19,281	32,139
Adjustments:		
Income tax expense	5,399	8,588
Depreciation of property, plant and equipment	51,630	46,668
Depreciation of investment property	211	262
Amortisation of intangible assets	3,020	3,070
Gain on sale of property, plant and equipment	(1,291)	(2,266)
Change in provisions, accruals and deferrals	4,042	(7,802)
Gain on sale and impairment losses of available-for-sale financial assets	(16)	(5,887)
Interest received	(5,944)	(7,550)
Interest paid	44,600	50,173
<b>Gross cash flow from operating activities</b>	<b>120,932</b>	<b>117,395</b>
Change in inventories	2,767	(13,585)
Change in trade and other receivables	97,513	33,656
Change in trade and other payables	(84,323)	137,476
Interest paid	(44,600)	(50,173)
Income tax paid	(4,825)	(7,420)
<b>Net cash from operating activities</b>	<b>87,464</b>	<b>79,883</b>
<b>Cash flows from investing activities</b>		
Acquisition of subsidiaries	(29,013)	(70,360)
Acquisition of property, plant and equipment and investment property	(44,801)	(163,792)
Acquisition of intangible assets	(3,248)	(5,962)
Bank deposits made	(16,000)	(16,662)
Proceeds from sale of property, plant and equipment and investment property	6,265	8,984
Proceeds from sale of intangible assets	30	3
Proceeds from sale of available-for-sale financial assets	-	7,233
Interest received	5,944	7,550
Dividends received	14	65
Bank deposits received	34,305	76
<b>Net cash used in investing activities</b>	<b>(46,504)</b>	<b>(232,865)</b>
<b>Cash flows from financing activities</b>		
Proceeds (repayments) from borrowings	(26,138)	168,341
Dividends paid	(12,366)	(15,647)
<b>Net cash from (used in) financing activities</b>	<b>(38,504)</b>	<b>152,694</b>

**Net increase (decrease) in cash and cash equivalents**

Cash and cash equivalents at the beginning of the year

**Cash and cash equivalents at the end of the year**

<b>2,457</b>	<b>(288)</b>
-	288
<b>2,457</b>	-

# Independent auditor's report



## Auditor's Report for Public Reporting purposes

We have audited the financial statements and the related notes of the company Poslovni sistem Mercator, d.d., Ljubljana for the year ended 31 December 2009, prepared in accordance with the International Financial Reporting Standards as adopted by the European Union, from which the summarized financial statements are derived, in accordance with International Standards on Auditing. As stated in our Auditor's Reports of 18 February 2010, the financial statements with notes, used for the preparation of the summarized financial statements, give a true and fair view of the Company's operations in 2009.

In our opinion, the attached summarized financial statements comply, in all material aspects, with the financial statements and the notes thereto from which they originate and on which we have expressed an unqualified audit opinion.

For a better understanding of the financial position of Poslovni sistem Mercator, d.d., Ljubljana as of 31 December 2009, the results of its operations, and its cash flows for the year then ended, and the scope of our audit, it is necessary to read the summarized financial statements together with the financial statements and the notes thereto, and our audit report on these financial statements.

The Annual Report of the Poslovni sistem Mercator, d.d., Ljubljana has not yet been presented to the institution which is authorised for the processing and publishing of data.

**KPMG SLOVENIJA,**  
podjetje za revidiranje, d.o.o.

A handwritten signature in black ink, appearing to read 'Marjan Mahnič'.

Marjan Mahnič, B.Sc.Ec.

*Certified Auditor*

*Partner*

*KPMG Slovenija, d.o.o.*

Ljubljana, 25 February 2010



# Contacts



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### **Mercator Trade Slovenia**

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### **Mercator Trade Southeastern Europe**

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