Business Report of the Mercator Group and the company Poslovni sistem Mercator, d.d., for the period 1-3 2012

Poslovni sistem Mercator, d.d.
Management Board

May 2012

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SUMMARY

In the first quarter of the year, Mercator Group attained revenue growth of 3.6%; although this is consistent with the plan, negative effects of the economic crisis on performance persist.

In the first quarter of 2012, Mercator Group revenue amounted to EUR 676 million which is 3.6 percent more than in 2011. In Slovenia, revenue remained virtually the same (index 99.7); however, development activities yielded a solid 9.5-percent growth in foreign markets. Economic crisis and the effect thereof on the volume and composition of household consumption required additional investments into favourable offer for our consumers. Paired with negative macroeconomic effects, especially the changes in the Serbian dinar exchange rate and rampant payment defaults and delinquency in the region, this severely challenged the Group's performance. In the first quarter of the year, Mercator Group's results from operating activities amounted to EUR 19.5 million, and profit for the period stood at EUR 0.7 million. In addition to the counter-crisis measures already in place, the Management Board adopted a set of additional measures to alleviate the negative effects of the economic crisis in the region on the Group performance and to keep the Group on track towards the planned annual results.

<u>Economic crisis in all markets in the region</u>
In early 2012, Mercator is facing further aggravation of economic conditions in all markets of Group operations. Pronounced slowdown in economic growth, sluggish economic activity, rising unemployment, and a decrease in real income of households were reflected in a drop of consumption and in a change of its structure; furthermore, consumers have grown more price-sensitive and rational. Increase in the value-added tax rate in Croatia exerted negative pressure on consumption as well. Another hindrance to our performance was the depreciation of the Serbian dinar and worsening of payment defaults and delinquency throughout the region, which has particularly affected our wholesale operations. On the cost side, we have seen pressure resulting from the global increase in the prices of energy and some strategic resources. In such circumstances, Mercator Group continued to invest into even better offer. While such approach led to the attainment of the planned revenue, the effect on business performance was negative.

<u>High growth in international markets despite negative currency translation differences</u>
In the period 1-3 2012, Mercator Group generated EUR 676,101 thousand of revenue, which is 3.6 percent more than in the corresponding period last year. The revenue generated represents 22.8 percent of the figure planned for the entire year 2012, which is consistent with the interim dynamics as the first quarter of each year is traditionally the most sluggish in the retail business. With an index of 99.7, revenue in Slovenia remained virtually the same as last year. On the other hand, revenue in Mercator's international markets rose by as much as 9.5 percent as a result of strategic alliances forged as a part of the Group's development efforts, despite the negative currency translation effects.

<u>Strategic projects and development activities in progress as planned</u>
In the first quarter of 2012, the Group continued to conduct its strategic projects aimed at adjusting Mercator's offer to the changes in consumer behaviour. In Slovenia, the project of refreshment of fast-moving consumer goods was carried on; thus, offer has already been adjusted at 12 stores. The project of refreshment and restructuring of FMCG offer was also in progress in Croatia where the offer has already been adjusted at three stores. Both projects will be carried on in ensuing quarters of this year. Furthermore, the project to establish the technical consumer goods chain as an independent business entity was conducted in order to improve the offer and boost the operating efficiency at this program. In the first quarter of 2012, the project of optimizing the working capital management was also in progress at all companies of the Group.

In the period 1-3 2012, Mercator Group invested EUR 13,015 thousand into retail network development. Nearly 13 thousand square meters of new gross area was acquired in the period. In the first quarter of the year, key development activities included an update and modernization of the retail network in Slovenia and Croatia, which is a part of the strategic projects of refreshment of FMCG offer in these two markets. The project of real property monetization also remains on track as scheduled.

Employees

As at March 31, 2012, the number of employees at Mercator Group was 24,279 which ranks Mercator among the largest employers in the entire Southeastern European region; with over 12 thousand employees in Slovenia, it is also the largest corporate employer in Slovenia.

Mercator implements the provisions of the Code of Practice for the stakeholders in the agricultural and food industry chain with regard to supplier relations

Pursuant to the provisions of Article 7 of the Code of Practice for the stakeholders in the agrifood chain, adopted in 2011, Mercator Group changed on January 1, 2012 the way it manages its relations with majority of suppliers of fast-moving consumer goods in Slovenia, by implementing pricing according to net-net price system. Before, Mercator mostly managed its supplier relations according to the principle of manufacturer or wholesale prices. In the future, Mercator will continue to observe the provisions of the Code of Practice and implement them as much as possible in all markets of its operations.

Business performance

Despite the attainment of the planned revenue growth, the necessary additional investment into favourable offer for the consumers had a negative impact on business performance, despite the concurrent cost rationalization measures. Moreover, increased finance expenses, mostly pertaining to negative currency translation differences for Serbian dinar and measures for managing the refinancing risk, also bore a negative impact on performance as they resulted in a higher level of overall debt in the first quarter of 2012. Gross cash flows from operating activities before rental expenses stood at EUR 47 million (21.9% of annual plan); Group results from operating activities in the first quarter amounted to EUR 19.5 million (25.5% of the plan for the entire year 2012); and profit for the period reached EUR 0.7 million (4.6% of the plan for the entire year 2012).

Measures to mitigate the negative impact of economic crisis

In December 2011, the Management Board adopted 12 sets of counter-crisis measures pertaining to the adjustment of offer to the changes in consumer behaviour and business rationalization. These measures also include the strategic projects of refreshment of FMCG offer in Slovenia, refreshment and restructuring of FMCG offer in Croatia, and establishment of the technical consumer goods chain. Responding to very harsh economic conditions and the effect thereof on performance in the first quarter, the Management Board adopted further counter-crisis measures in order to mitigate the risks and to come as close as possible to the planned results for the year.

INTRODUCTION

MERCATOR GROUP PROFILE

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	Poslovni sistem Mercator, d.d.
Abbreviated name	Mercator, d.d.
Activity	G 47.110 Retail in non-specialized food retail outlets
Registration number	5300231
VAT tax code	45884595
Court registry date	January 1, 1990
Company share capital as at March 31, 2012	EUR 157,128,514.53
Number of shares issued and paid-up as at March 31, 2012	3,765,361
Share listing	Ljubljana Stock Exchange, d.d., prime market, symbol MELR
President of the Management Board	Žiga Debeljak
Senior Vice Presidents	Melita Kolbezen, Vera Aljančič Falež, Peter Zavrl, Stanka Čurović
Supervisory Board Chairman	Matej Lahovnik
Deputy Supervisory Board Chairman	Rok Rozman

Mercator Group Composition

As at March 31, 2012, Mercator Group included the following companies:

MERCATOR GROUP	
MERCATOR OPERATIONS SLOVENIA	
Poslovni sistem Mercator, d.d., Slovenia	
Mercator IP, d.o.o., Slovenia (100.0 %)	M - Tehnika, d.d., Slovenia (100.0 %)
M.COM, d.o.o., Slovenia (100.0 %)*	· Mercator centar tehnike d.o.o. za trgovinu i usluge, Croatia (100.0 %)
M - Energija, d.o.o., Slovenia (100.0 %)	
MERCATOR OPERATIONS SOUTHEASTERN EUROPE	
Mercator - S, d.o.o., Serbia (100.0 %)	Mercator - B, e.o.o.d., Bulgaria (100.0 %)
Mercator - H, d.o.o., Croatia (99.9 %)	Mercator - A, sh.p.k., Albania (100.0 %)
Mercator - BH, d.o.o., Bosnia and Herzegovina (100.0 %)	Mercator Makedonija, d.o.o.e.l., Macedonia (100.0%)*
M - BL, d.o.o., Bosnia and Herzegovina (100.0 %)	Mercator - K, l.l.c., Republic of Kosovo (100.0 %)*
Mercator - CG, d.o.o., Montenegro (100.0 %)	
MERCATOR REAL ESTATE	
Investment Internacional, d.o.o.e.l., Macedonia (100.0 %)*	Argentum - D, d.o.o., Slovenia (100.0 %)**
Mercator - Optima, d.o.o., Slovenia (100.0 %)	Argentum - E, d.o.o., Slovenia (100.0 %)**
M - nepremičnine, d.o.o., Slovenia (100.0 %)	Argentum - F, d.o.o., Slovenia (100.0 %)**
Argentum - A, d.o.o., Slovenia (100.0 %)**	Argentum - G, d.o.o., Slovenia (100.0 %)**
Argentum - B, d.o.o., Slovenia (100.0 %)**	Argentum - H, d.o.o., Slovenia (100.0 %)**
Argentum - C, d.o.o., Slovenia (100.0 %)**	Argentum - I, d.o.o., Slovenia (100.0 %)**
OTHER OPERATING ACTIVITIES	
Intersport ISI, d.o.o., Slovenia (100.0 %)	Modiana, d.o.o., Slovenia (100.0 %)
· Intersport S-ISI, d.o.o., Serbia (100.0 %)	· Modiana, d.o.o., Serbia (100.0 %)
· Intersport H, d.o.o., Croatia (100.0 %)	· Modiana, d.o.o., Croatia (100.0 %)
· Intersport BH, d.o.o., Bosnia and Herzegovina (100.0 %)	· Modiana, d.o.o., Bosnia and Herzegovina (100.0 %)
Mercator - Emba, d.d., Slovenia (100.0 %)	

* The company has not yet commenced its business operations.
** Project-based real estate company, established for real property monetization purposes.

Corporate governance

Supervisory Board of the company Poslovni sistem Mercator, d.d., held two sessions in the first quarter of 2012.
At the 17th regular session held on January 19, 2012, Supervisory Board adopted the Business Plan of the Mercator Group and the company Mercator, d.d., for the year 2012. At their 18th regular session held on February 27, 2012, they adopted the Annual Report of the Mercator Group and the company Poslovni sistem Mercator, d.d., for 2011, and confirmed the Supervisory Board Report on the Annual Report audit, and the opinion on the allocation of distributable profit. Upon proposal of Mercator's senior vice president Mrs. Mateja Jesenek and President of the Management Board Mr. Žiga Debeljak, the Supervisory Board terminated as of February 29, 2012 the term of the senior vice president in charge of strategic marketing and global procurement, Mrs. Mateja Jesenek.

The five-member Mercator Management Board, consisting of Mr. Žiga Debeljak, Mrs. Vera Aljančič Falež, Mrs. Melita Kolbezen, Mrs. Stanka Čurović, and Mr. Peter Zavrl submitted their resignation on

March 29, 2012. Until the appointment of a new Management Board, the current Board shall manage the company affairs with full power and authorizations.

On March 30, 2012, 18th regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., was held. The Shareholders Assembly confirmed the resolution proposal to change the number of Supervisory Board members to 9, of which 3 members shall represent the employees and 6 members shall represent the shareholders. Six new Supervisory Board members were appointed at the Assembly to represent shareholders: Mr. Matej Lahovnik, Mr. Rok Rozman, Mr. Boris Galić, Mrs. Marjeta Zevnik, Mrs. Mirjam Hočevar, and Mr. Zdenko Podlesnik. Furthermore, the Assembly proposed and confirmed the change in the amount of dividend to be paid out, to EUR 6.00 gross per ordinary share. On April 4, 2012, Mrs. Mirjam Hočevar submitted her irrevocable letter of resignation from the position of a Supervisory Board member. On April 6, 2012, Council of Employees held a session to terminate the terms of employee representatives in the Supervisory Board to Mr. Jože Cvetek, Mr. Janez Strniša, and Mr. Ivica Župetić.

On April 10, 2012, the new Supervisory Board of the company Poslovni sistem Mercator, d.d., met for their first, founding session. The eight-member Supervisory Board included:

- Mr. Matej Lahovnik, Mrs. Marjeta Zevnik, Mr. Zdenko Podlesnik, Mr. Boris Galić, and Mr. Rozman, representing shareholders; and
- Mr. Mateja Širec, Mr. Ivan Valand, and Mr. Sandi Leban, representing the employees.

The Supervisory Board appointed Mr. Matej Lahovnik as the Chairman and Mr. Rok Rozman as Deputy Chairman. They also appointed the Audit Committee and the HR Committee. Consistently with their powers and authorizations, the HR Committee shall prepare everything required for the appointment of a new Management Board.

On their second session held on April 24, 2012, the Supervisory Board appointed two independent Audit Committee members. The newly appointed Audit Committee thus consists of four members: two Supervisory Board members – Mrs. Marjeta Zevnik, Supervisory Board member and Audit Committee Chairwoman; and Mr. Rok Rozman, Deputy Chairman of the Supervisory Board – and two independent experts trained in accounting and auditing: Mrs. Sergeja Slapničar and Mr. Aleksander Igličar of the Faculty of Economics of the University of Ljubljana.

MERCATOR GROUP BUSINESS STRATEGY

Vision

To be the consumers' first choice when shopping for fast moving consumer goods and home products.

Mission

Mercator's mission is:

1) To provide optimum value for the consumers with our service and offer of fast moving consumer goods and home products.
2) To provide consumers with the best possible service in a pleasant shopping environment, by offering expert support of highly motivated employees.
3) To provide returns for our shareholders through growth and efficient operation.
4) To manage our operations in a way that improves the quality of life in our social and natural environment.

Corporate values

Following are Mercator's corporate values:

Responsibility	**Responsiveness**
Each employee is responsible for their work.	Prompt response is our advantage.
Integrity	**Learning**
We work honestly and fairly.	We build on our knowledge and experience.
Respect	**Cooperation**
Each individual matters and deserves respect.	What one person cannot do, we can accomplish together.

Strategic objectives

Following are Mercator Group's fundamental strategic goals:

1) In our **domestic market** (Slovenia):
    a. To retain the position of the leading fast moving consumer goods retailer.
    b. To consolidate the position of the second largest retailer of home products.
    c. To develop supplementary trade services related to our customer loyalty system.
2) In **existing foreign markets** (Serbia, Croatia, Bosnia and Herzegovina, Montenegro):
    a. To consolidate or attain the position of the second largest fast moving consumer goods retailer.
    b. To rank among the top three retailers of home products.
    c. To develop supplementary trade services related to our customer loyalty system.
3) In **new foreign markets** (Bulgaria, Albania, Macedonia, Republic of Kosovo):
    a. To rank among the top five retailers of fast moving consumer goods.

MAJOR EVENTS IN THE PERIOD 1-3 2012

Retail network development

In the period 1-3 2012, we:

- invested EUR 13,015 thousand,
- divested EUR 1,164 thousand,
- acquired 30 new units spanning 12,840 square meters of gross retail area on all our markets of operations, which includes real estate owned by Mercator and operating leases.

Strategic combinations

On February 23, 2012, the agreement on strategic combination based on which the company Poslovni sistem Mercator, d.d., increased its shareholding in the company Vesna, trgovsko podjetje (trade company), d.d., Ljutomer, from 45 percent to 100 percent, thus acquiring seven stores in Northeastern Slovenia, which operated as Mercator franchise units to date.

Corporate activities

In February 2012, the Mercator Group Management Board held an international press conference to present the Group operations and performance in 2011 and the business plans for this year.

Awards received

At the 12th competition of bread, pastry, and pasta, held by the Bakery Section of the Chamber of Agricultural and Food Companies with the Chamber of Commerce and Industry of Slovenia, Mercator's own bakery Pekarna Grosuplje received the highest possible rating for all nine zero-additive products submitted.

MERCATOR GROUP PERFORMANCE HIGHLIGHTS IN THE PERIOD 1-3 2012

	Mercator Group		
	1-3 2012	**Plan 2012 restated***	**Index 1-3 2012/ Plan 2012 restated***
Revenue (EUR thousand)	676,101	2,966,521	22.8
Results from operating activities (EUR thousand)	19,503	76,376	25.5
Profit before income tax (EUR thousand)	3,155	24,172	13.1
Profit for the financial period (EUR thousand)	716	15,708	4.6
Gross cash flow from operating activities (EUR thousand)	33,960	150,275	22.6
Gross cash flow from operating activities before rental expenses (EUR thousand)	47,030	214,264	21.9
Capital expenditure (EUR thousand)	13,015	88,452	14.7
Return on sales	0.1%	0.5%	20.0
Gross cash flow from operating activities / revenue	5.0%	5.1%	99.2
Gross cash flow from operating activities before rental expenses / revenue	7.0%	7.2%	96.3
Number of employees based on hours worked	22,983	23,350	98.4
Number of employees as at the end of the period	24,279	24,915	97.4

* Considering the changes in accounting policies, planned revenue was restated accordingly. Detailed explanation is provided in the financial report.

BUSINESS REPORT

EFFECT OF ECONOMIC CONDITIONS AND COMPETITION ON MERCATOR GROUP OPERATIONS IN THE PERIOD 1-3 2012

Economic conditions in the markets of Mercator operations in the period 1-3 2012

Global economic growth slowed down significantly in the second half of 2011. Real GDP fell by 0.3% in the euro zone in the last quarter of 2011, mostly as a result of a decline in economic activity in major countries and the fact that some countries slid back into recession. Also worsening the economic crisis in Europe are the macroeconomic imbalances between the countries, which had been present even before the onset of the recession, but were not an acute and problematic at the time. On the one hand, there are countries with a budget surplus; on the other hand, there are countries with budget deficits, which currently face the problem of implementing measures to counter and beat the crisis, as well as the problem of more or less ineffective approaches to balance out their budgets. Greece stood out as one of the most problematic countries in this regard; however, financial analysts increasingly point to Spain, Italy, and Ireland as well, underscoring their rampant unemployment and unstable banking systems. The problem with these countries is that much more severe as they represent a considerable share of the entire European economy and they are among the most important importers or exporters. Increased uncertainty in the financial markets resulting from lack of progress in resolving the financial crisis and issues of government impeded the access to financing. Geopolitical reasons pushed prices of oil skywards to new records; the same was seen with some other basic raw materials, which resulted in inflationary pressures. Various monetary measures were taken to maintain moderate rates of inflation. Subject to strict monitoring and balancing, these measures will contribute to stabilization and improvement in financial environment. Low economic activity also bears a negative impact on the labour market where conditions continue to worsen. Unemployment rate is rising and such trend is expected to continue in 2012. Low economic activity and falling real household income were reflected in a drop of consumption and limited possibilities of the supply side of the economy to increase downstream prices, although cost and pricing pressures have been mounting and despite the fact that this is paired with rampant payment defaults and delinquency. Adverse changes in the Serbian dinar exchange rate present another problem. The months ahead do not seem to bring any improvement in economic conditions as economic indicators for the future have grown worse in recent months. In March, growth forecast for the euro zone, especially as a result of bleak outlook in the labour market and uncertainty regarding the consolidation of public finances in some countries, was adjusted downwards to -0.4%; likewise, the consumer confidence index is falling as well.

Slovenian credit rating has been downgraded several times recently, which caused our shift from the group of stable euro zone countries to the group of countries of higher risk, facing major problems and, according to experts, affecting the entire euro zone. For this fact, and the fact that Slovenia is a relatively small country, access to international financial sources is additionally challenged.

Central banks have responded to the aggravation of economic conditions and they kept the key interest rates low. As at March 31, 2012, 6-month EURIBOR stood at 1.078%, which is more than 32% less than as at the beginning of the year 2012 (1.617% as at December 31, 2011). Average value of the 6-month EURIBOR in the first quarter of 2012 was 1.338%, which is 2.91% less than in the corresponding period last year.

Slovenia

Economic growth in Slovenia was negative in 2011 at -0.20%, which is much worse than in 2010 when it reached 1.40%. For 2012, the economy is anticipated to slump even harder than in 2011: GDP growth is expected to reach -0.90%. Inflation rate in 2011 was at 1.8 percent; in 2012, it is expected at 2.00%. In March, year-on-year inflation amounted to 2.30%.

Serbia

Economic growth in Serbia in 2011 is estimated to have amounted to 1.90%. In 2012, it is expected to increase somewhat to 3.00%. Inflation in 2011 was lower than in the year before, reaching 7.00% compared to 10.30% in 2010. Forecast for 2012 is inflation rate of 4.3 percent. In the first quarter of 2012, unemployment rate in Serbia stood at 23.70%. In the first quarter of 2012, the average exchange rate of the Serbian dinar was RSD 108.11 per 1 EUR (RSD 103.95 per 1 EUR in the first quarter of 2011). As at March 31, 2012, exchange rate for the Serbian dinar was at RSD 111.36 per 1 EUR (as at March 31, 2011: RSD 103.60 per 1 EUR).

Croatia

Gross domestic product growth in 2011 is estimated to have amounted to 0.20%; in 2012, it is expected to be negative at -1.00%. In March, year-on-year inflation amounted to 2.00%. Inflation in 2011 was 2.3 percent; for 2012, it is forecast at 2.50%. In March 2012, registered unemployment rate was 20.00%. Average exchange rate for Croatian kuna in the first quarter of 2012 amounted to HRK 7.56 per 1 EUR (first quarter of 2011: HRK 7.40 per 1 EUR). As at March 31, 2012, exchange rate for the Croatian kuna was at HRK 7.51 per 1 EUR (as at March 31, 2011: HRK 7.38 per 1 EUR). In 2012, consumption and trade in Croatia will be negatively affected by the increase in the VAT rate from 23 to 25 percent as of March 1, 2012.

Bosnia and Herzegovina

In the first quarter of 2012, GDP growth stood at 1.90%. In 2011, GDP growth is estimated to have amounted to 1.90%; in 2012, it is anticipated at 0.00%. Inflation rate in 2011 amounted to 3.60%; in 2012 it is expected at 2.30%. In March 2012, year-on-year inflation was at 1.90%. In the first quarter of 2012, Bosnia and Herzegovina saw extreme unemployment rate of 44.00%. The exchange rate of the convertible mark is pegged to euro at the rate of KM 1.95583 per 1 EUR.

Montenegro

GDP growth in 2011 reached 2.50%, and inflation in the same period was at 3.10%. In 2012, economic growth is expected at 2.00% while the inflation rate is anticipated at 2.50%. In March, year-on-year inflation amounted to 2.70%. In the first quarter of 2012, unemployment rate was at 13.50%. Montenegrin official currency is the euro.

Bulgaria

Economic growth in Bulgaria in 2011 reached 1.70%, while inflation rate in the same period was at 3.40%. According to forecasts by analysts, gross domestic product will grow by 1.20% in 2012, while inflation rate will be at 3.10%. Year-on-year inflation rate in March 2012 was at 1.70% (2.00% in February 2012). In the first quarter of 2012, unemployment rate in Bulgaria was 11.40%. The exchange rate of Bulgarian lev is pegged to euro at the rate of BGN 1.95583 per 1 EUR.

Albania

Economic growth in 2011 amounted to 3.10% while inflation reached a rate of 1.70%. In 2012, gross domestic product growth is forecast at 2.50% while the inflation rate is anticipated at 3.00%. In March 2012, year-on-year inflation amounted to 1.00%. In the first quarter of 2012, unemployment rate in Albania stood at 11.00%. Average annual exchange rate for Albanian lek in 2011 reached ALL 140.34 per 1 EUR; in 2012, it is expected at ALL 141.00 per 1 EUR. As at March 31, 2012, the closing rate for the Albanian lek was ALL 140.38 per 1 EUR (as at March 31, 2011: ALL 140.57). Average exchange rate in the first quarter of 2012 amounted to ALL 139.22 per 1 EUR (first quarter of 2011: ALL 139.46 per 1 EUR).

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

All markets of Mercator operations were severely struck by the global economic crisis which persists in 2012. **Unemployment in key Mercator markets reached record levels. Consumers have a high propensity to save and their purchasing power is stagnant. This is reflected in lower number of shopping sessions and lower value of each shopping basket.** Due to uncertainty and an entire set of effects from the environment, consumer shopping and consumption behaviour has taken a permanently conservative and rational turn.

Consumers **in Slovenia** have low confidence; they are pessimistic, cautious, and sensitive to pricing. Consumer confidence index is very low and it has dropped further in the first quarter of 2012. According to the Slovenski utrip (Slovenian pulse) survey, 54% of the respondents believe they are worse off than they were four years ago[1].
Slovenian fast-moving consumer goods market is consolidated and highly competitive. Changes in consumer behaviour are reflected in growth of discount retailers, shopping at several different retailers, and increased sales of private label products.
International markets of Mercator operations are not as consolidated; however, the competition there is very stringent. Many international, regional and local players are present in the region. Due to low economic growth, rising unemployment, and low personal income, consumer purchasing power remains low. Changes in consumer behaviour is reflected in lower number of shopping sessions (especially in Serbia and Bosnia and Herzegovina), lower value of the shopping basket (especially in Croatia and in Bosnia and Herzegovina), and development of discount retailers (in Croatia and Bulgaria). Price sensitivity of consumers is also reflected in increased shopping for private label products. In addition to deterioration of economic circumstances in 2012, purchasing power of Croatian consumers and consequently the retail industry was also hit by the increase in VAT rate from 23 to 25 percent as of March 1, 2012.

DEVELOPMENT AND REAL ESTATE MANAGEMENT

In the period 1-3 2012, Mercator Group efforts in real estate development and management remained geared towards meeting the goals laid down in the adopted development strategy. Our key task is to acquire new retail area. Consistently with the medium-term investment plan, we favour lease of retail area, thus deviating to a considerable extent from the principle of mostly own construction which was predominant in the past. In addition to acquisition of new retail area mostly through lease, we allocate a considerable share of our investment efforts into refurbishment or update of our own retail network.

One key project in this regard which has been commenced by Mercator Group in 2011 is Refreshment of Mercator's FMCG Offer which is to provide the conditions for introducing a new sales concept. Hence, we refreshed the offer at 12 supermarkets in Slovenia and 3 supermarkets in Croatia in the first quarter of 2012.

Furthermore, we carried out in the period at hand various development activities to optimize Mercator's real estate management, and analyzed the possibilities to update the concept of Mercator's shopping centers, to improve the mix of products and services there, to improve composition of third-party providers, and to establish strategic partnerships with renowned international tenants/brands.

[1] Slovenski utrip (Slovenian pulse) survey, FUDŠ, April 2012.

Following are Mercator key goals in real estate management:

Investment and Divestment

In the period 1-3 2012, Mercator Group's investment into property, plant, and equipment (CAPEX) amounted to EUR 13,015 thousand. 56.1 percent of these funds were invested in Slovenia; 42.5 percent was invested in existing foreign markets (Serbia, Croatia, Bosnia and Herzegovina, and Montenegro); and 1.4 percent was invested in new foreign markets (Bulgaria).

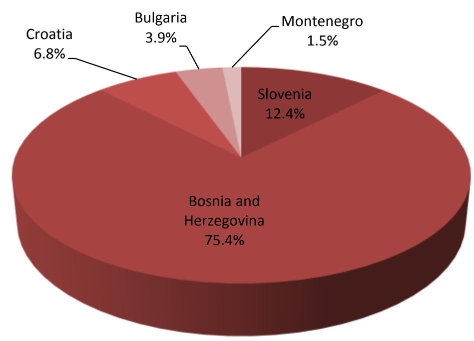
	Capital expenditure 1-3 2012 (EUR thousand)	Composition (in %)
Slovenia	7,304	56.1%
Serbia	1,033	7.9%
Croatia	1,649	12.7%
Bosnia and Herzegovina	2,143	16.5%
Montenegro	698	5.4%
Bulgaria	188	1.4%
TOTAL	**13,015**	**100.0%**

Investments in development of retail facilities (Mercator centers, trade centers, Roda centers, individual stores, and stores within other shopping centers) represent 54.9% of total investments; 25.5% was allocated for refurbishment of the existing facilities; and the remaining 19.6% was invested into logistics, IT, and non-trade activities.

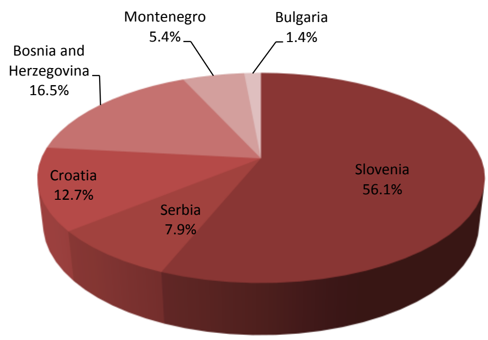
In the period 1-3 2012, the company acquired 12,840 m^2 of new gross area, of which 87.6% was by operating lease and 12.4% was by acquisitions and construction, or extension of existing facilities.

In the period 1-3 2012, Mercator Group divested EUR 1,164 thousand worth of property, plant and equipment.

Share of newly launched facilities by markets



Share of investments by markets



Summary of retail unit launches by markets

Slovenia

Area of new facilities: 1,593 m^2

Number of retail units: 2

Openings: Modiana Outlet in Ljubljana (Šmartinska 102) and Tehnika Outlet in Maribor (Tržaška 14)

Croatia

Area of new facilities: 875 m^2

Number of retail units: 1

Openings: Modiana in City Center One East in Zagreb

Bosnia and Herzegovina

Area of new facilities: 9,685 m^2

Number of retail units: 25

Openings: Stores of the company Drvopromet on total area of 9,685 m^2

Montenegro

Area of new facilities: 186 m^2

Number of retail units: 1

Openings: Superette Dobrota in Kotor

Bulgaria

Area of new facilities: 501 m^2

Number of retail units: 1

Openings: Superette Dianabad in Sofia

Summary of total gross retail area as at March 31, 2012

Gross retail area in m^2	Used for own operations	Leased out	Total
Owned retail area	812,944	174,750	987,694
Leased retail area	395,937	22,611	418,549
Total retail area	**1,208,882**	**197,361**	**1,406,243**
Owned warehouse capacity	140,065	65	140,130
Leased warehouse capacity	51,879	0	51,879
Total warehouse capacity	**191,944**	**65**	**192,009**
Owned commercial facilities	27,156	2,566	29,722
Leased commercial facilities	6,581	114	6,695
Total commercial facilities	**33,737**	**2,680**	**36,417**
GROSS AREA UNDER MANAGEMENT	**1,434,563**	**200,106**	**1,634,669**
- of which owned	980,165	177,381	1,157,546
- of which leased	454,398	22,725	477,123

Activities of Real Property Monetization

Reaping the growth potential laying in real property is highly important for successful operations of the Mercator Group. In comparison to its European competitors, Mercator's balance sheet includes a huge amount of real estate or assets which could, were they monetized, be used to reduce debt.

As early as in 2011, the monetization project included an international tender to select an internationally renowned consultant, the global real estate consultancy Cushman & Wakefield from Great Britain; thus, the activities to carry out the project were commenced. In the first quarter of 2012, we worked with the consultancy to define the portfolio of real estate to be offered for sale to international investors, and to hold an international tender to select from a range of global legal consultants the law firm Schoenherr in cooperation with the law firm SJ Berwin as the best bidder of legal services. We also founded nine project companies through which the monetization of real property will be effected, consistently with the prevailing international practice.

In line with the goals laid down in the medium term Business Plan of the Mercator Group, 2012 will see the selection of investors, and sale and lease-back of a part of the real estate portfolio in Slovenia with the planned value of EUR 250 million. Proceeds from monetization will be allocated for the reduction of debt.

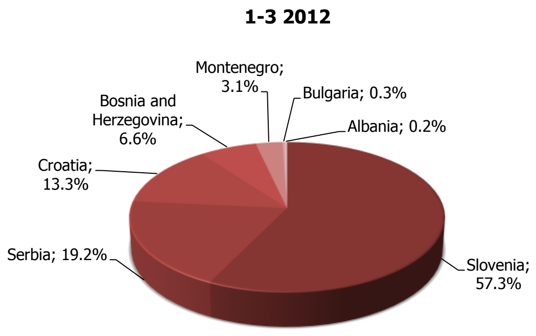
Final decision on the scope and timing will be adopted when all terms and conditions of the monetization are specified, given the market conditions and investor interest.

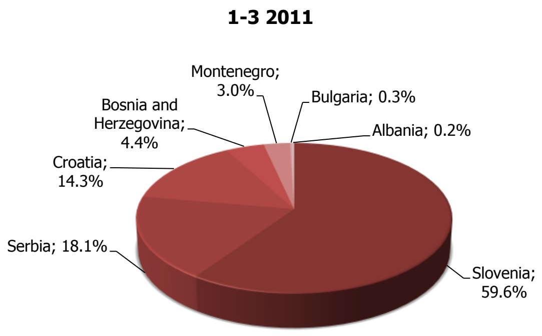
SALES AND MARKETING

Sales

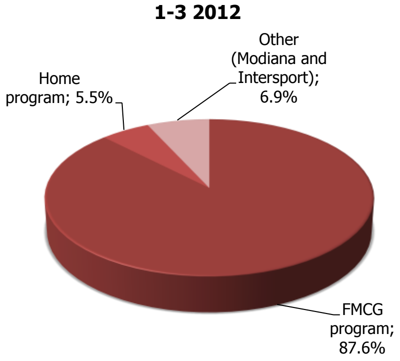
In the period 1-3 2012, Mercator Group generated EUR 676,101 thousand of revenue, which is 3.6 percent more relative to the period 1-3 2011. Majority of Group revenue is generated by sales of goods, material, and products, mostly retail and wholesale of trade goods. Revenue in Slovenia remained virtually the same with an index of 99.7; in foreign markets, revenue growth reached 9.5 percent.

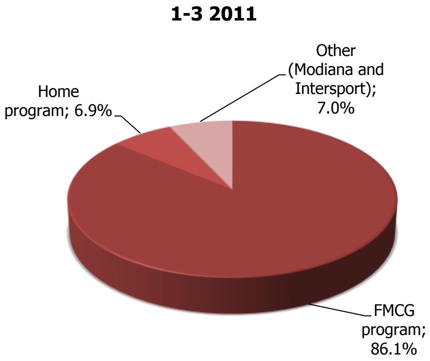
Mercator Group revenue by geographical segments:





Mercator Group revenue from trade operations by programs:





In the period 1-3 2012, the majority of Mercator Group revenue resulted from sales of fast-moving consumer goods as they accounted for 87.6 percent of the total figure; revenue from other specialized programs amounted to 12.4 percent.

Marketing

Mercator Group's vision, mission, and operating strategies place the consumers at the heart of our efforts. In 2012, we shall continue to conduct the planned activities to pursue our vision. Following are our key policies:

1. Mercator is providing **competitively priced offer**.
2. Mercator is developing **high-quality private label products**.
3. Shopping offered by Mercator is **transparent**, **simple**, and **well-priced**.
4. Mercator is committed to **sustainability** for the benefit of the consumer and the environment.

1. Mercator is providing competitively priced offer.

The world is changing and Mercator is changing with it. This though was a maxim in mapping out the **new corporate campaign** which ends with the thought, or commitment, that Mercator will remain the best neighbour. At Mercator, we are aware that despite the effects of the crisis and preference of cheaper products, including those by discount retailers, product origin still matters for the majority of consumers. This is particularly true for fresh products. Therefore, we are doing our best to provide as much Slovenian produce as possible, and to provide small farmers and growers an opportunity to sell their products at Mercator stores. Despite the changes in consumer behaviour, we put the needs and desires of our customers before anything else. Hence, we are adjusting our offer accordingly, justifying the slogan **"So Slovenian, so Mercator"**.

In order to allow our customers the most favourable shopping in a time when they are cutting back on their spending, we introduced many sales promotion activities. These included offering products of renowned brands in the "buy one, get one free" and "buy two, get one free" campaigns, offering products at attractive rounded prices, and promoted examples of family meals at very good prices in our flyers.

Mercator is carefully adjusting its sales promotion activities to the local characteristics of individual markets of operations. Key activities in the markets of Mercator's operations in the first quarter of 2012 included the following:

Country	Key activities
Slovenia	• Revised regular and theme-oriented flyer; issued every two weeks; each week, households receive a different flyer. • Flyer presenting private label products. • Tuesday's Yes! (To!) discounts and Thursday retiree discounts, and awarding double Pika bonus points in refurbished stores on the opening day. • 20% discount coupon for selected product in the regular flyer. • 1+1 free and 2+1 free campaigns for branded products and the "Rounded prices" activity. • Five per day project – get a bagful of fruit and vegetables at half price. • Weekend offers and theme-oriented category discounts. • Dormeo and M holidays customer loyalty campaigns.
Serbia	• Regular campaign Mercator and Roda. • Tuesday's Yes! (To!) discounts at Mercator hypermarkets. • 10% weekend discount at Roda megamarkets, and Wednesday's retiree discounts at all Roda store formats. • "Super offer, super price" activity at Wednesdays and Thursdays. • Exclamation mark activity. • Discount on technical consumer goods from Monday to Friday. • Delimano customer loyalty program.
Croatia	• Regular weekly Mercator flyer and the bi-weekly Getro flyer. • Thursday's discount for retirees at Mercator stores, and Tuesday's retiree discount at Getro stores. • Saturday's 10-percent discount on purchases over HRK 100 at Mercator and Getro stores. • Saturday's HRK 30 coupon awarded for purchases over HRK 300 at Getro centers (Getro friend card). • Weekend offers and category discounts. • Flyer presenting private label products. • Five per day project, Exotic days at hypermarkets. • Linked purchase – issuing coupons for 10-percent discount in January to be used in February. • M Tehnika (technical consumer goods) special offer flyer.
Bosnia and Herzegovina	• Regular campaign Mercator and DP Marketi. • Tuesday's YES! discount and Thursday's retiree discount at Mercator stores. • Tuesday's discount for DP card holders at DP Marketi stores. • Weekend campaigns at the Mercator and DP Marketi stores. • Customer loyalty program Delimano at Mercator stores.
Montenegro	• Regular campaign Mercator and Roda. • Tuesday's Yes! discounts at Mercator and Thursday's retiree discounts at Mercator and Roda stores. • Weekend campaigns at Roda and Mercator stores. • Sales promotion activities at critical locations. • "Presenting the supplier" campaigns. • Exclamation mark activity at Roda formats. • Delimano customer loyalty program.

Country	Key activities
Bulgaria	• Regular Roda campaign. • Fortnight offer of the most favourably priced products "Top 10-19". • 10-percent weekend discount for purchases above BGN 80 at megamarkets. • "Input price" project –assortment of input products at low prices. • Valentine's Day catalogue and special offer flyer for products of non-market (non-FMCG) program. • Delimano customer loyalty program.
Albania	• Regular campaign. • "Happy Thursday" 10-percent discount. • Special weekend campaigns. • Delimano customer loyalty program.

In Slovenia, we regularly conducted in the first quarter of 2012 our corporate campaigns of awarding **double Pika bonus points** at food stores, Hura stores, franchise stores, M holidays and hospitality services, Modiana stores, Intersport stores, and Beautique drugstores, and **triple Pika bonus points** at M Tehnika, M Gradnja (construction), M Pohištvo (furniture), and M Tehnika (technical consumer goods) web store.

At M Tehnika, we introduced a new activity called "**magnetic products**", which includes discounts on popular or attractive products by 30 percent or more relative to the regular prices for that product in the market.

2. Mercator is developing high-quality private label products.

The family of Mercator private label products is constantly expanding. Thus, our customers are offered **thirteen private label lines** which include alimentary products, household products, apparel, technical consumer goods, cosmetics, child care products, toys, ready-made food, pastry, and products for a healthy diet.

Number of Mercator's private label lines by countries of Mercator's operations as at March 31, 2012:

Country	Number of lines
Slovenia	13
Serbia	9
Croatia	11
Bosnia and Herzegovina	9
Montenegro	6
Bulgaria	4
Albania	7

We renamed and revised the appearance of the "Healthy living" line; now, it is available with its new image and the name **Active Life.** Carefully selected products of the Active Life line follow the recommendations and modern findings in healthy nutrition as they are picked in cooperation with the Kranj Institute of Public Health. In addition to complying with the guidelines on wholesome food, Active Life products remain as tasty as ever.

Our offer was further enriched by the new product line called **Pro Magic** available exclusively at Mercator stores. The line offers products for home and household.

In communicating the **Lumpi** line, we teamed up with Slovenia's best ski jumper, world champion, and winner of the small crystal globe in ski flying **Robert Kranjec**. Advantages of Lumpi products were related to the success of Robert Kranjec in an amusing way that is tailored to the target group of children and parents.

In late March, products of the **Grosuplje bakery** won **nine gold medals of quality** by the Slovenian Chamber of Commerce and Industry. Nine products made without any additives (Krjavelj, Malnar, Sosed, whole-grain bread, Dolenc, Home-made bread, Home-made buckwheat bread, Home-made corn bread, and Korošec) impressed the expert jury at the 12th contest of bread, pastry and pasta held by the Bakers Section of the Chamber of Agricultural and Food Companies.

3. Shopping offered by Mercator is transparent, simple, and well-priced.

In 2012, Mercator launched its intensive process of modernization of retail network in Slovenia and in Croatia. This year, we shall comprehensively refurbish a large number of supermarket format stores both in terms of comprehensive offer and transparent tagging, and in terms of offer (e.g. adding the service of baking pizzas, extending the fresh produce departments, extending the offer of ready-made products).

Our customer loyalty card **Mercator Pika** has been offered to our customers for thirteen years. We appreciate and reward the loyalty of our customers by awarding double and triple Pika bonus points, offering discounts on selected products (special Pika discounts), offering deferred payment without charging any interest, and by offering 3-6% discount on the entire offer subject to the amount of collected Pika points.

At Mercator, we are constantly expanding and improving our offer of quality services; thus, we are adding **new tourist service arrangements** (we issued a new catalogue Spring-Summer), and we are offering the **Photo Finish** photo services.

In January 2012, we opened the first **Maxen** petrol station located next to the Mercator center Kranj Primskovo. On the day of the opening, we treated the customers to live music and catering, as well as an opening-day discount on the fuel prices.

4. Mercator is committed to sustainability for the benefit of the consumer and the environment.

At Mercator, corporate social responsibility is manifest in focus on humanitarian, cultural, educational, healthcare, and sports projects of national importance in every country of Mercator's operations. Our bond with the local communities is strengthened through sponsorships and donations that go a long way in improving the quality of life in particular local environments.

Mercator's responsibility towards the natural environment is also manifest in the reduction of the use of natural resources and generation of waste. We have laid down our goals in terms of energy efficiency to be attained by the year 2016. These goals comply with the adopted National Action Plan for energy efficiency. Currently, we are in the stage of analyzing the energy status and planning of the use of alternative energy sources. Furthermore, processes are under way to calculate our corporate carbon footprint and the footprint of our sustainable store and Mercator private label products.

Digital Communication

Proliferation of new media and next generation communication tools has caused profound changes in the way we communicate. Simple messaging of extensive contents has been made possible for all web contents managers, which offers the users an opportunity to share their thoughts, ideas, and creative achievements virtually without limitations with the global audience.

Websites and web stores

In March, we refurbished and upgraded the website www.mholidays.si. The site's design was refreshed and user experience was improved in order to actually see more visitors make a booking and payment for the travel arrangement online.

We have set up new presentation websites for the visitors of Mercator centers MC Maribor Tabor II, MC Ljubljana, MC Kranj Primskovo, MC Koper, and MC Celje, at our central website at www.mercator.si. The purpose of the extension to the website is to present the offer at these centers in an **even more transparent way and with more information.**

Activities at social networking sites

Mercator continued to communicate its activities through its profiles on social networks, both in Slovenia and in the markets of Southeastern Europe. Thus, our **circle of friends is ever expanding and it now includes over 120,000 users**. We are looking to include more new approaches to our customers in our regular communication activities. Thus, our customers in Croatia were able to participate in the **5 per day** prize contest on our Facebook profile in January.

Mercator Facebook profile was also updated with Facebook's new application called timeline which will be used for all brands appearing online.

Monitoring Mercator presence in digital media

In the first quarter of 2012, our digital communication activities included intensive efforts to improve the monitoring and response to issues related to Mercator which appear in the digital media. To avoid any disputable situations, we **adopted the Rules and Regulations for Communication of Mercator Employees on the Web and in Social Networks** which includes rules and recommendations on the conduct in social network for all employees.

Store Formats

Currently, Mercator Group's retail units are present in seven markets of different economic maturity. This requires adjusting our operations to the needs of the customers in each market. To this end, Mercator has put in place a **multi-level strategy of store brands** and a **multi-format strategy** with a broad range of store formats. These are intended to cater to major, previously planned shopping sessions, as well as minor, daily or occasional shopping for fast-moving consumer goods, technical consumer goods, cosmetics, apparel and sportswear.

Fast-moving consumer goods

Mercator Group has developed a dense and extensive retail network throughout Slovenia and other countries, providing high-quality offer to meet every customer's desires, tastes, and needs. We are working to bring our shopping centers, hypermarkets, supermarkets, neighbourhood stores, convenience stores, Hura! discount stores, and the web store as close as possible to the customers, and to provide a pleasant shopping experience.

Home products

Mercator Group is offering home products in stores called M Tehnika (technical consumer goods), M Gradnja (construction), and M Pohištvo (furniture); the offer of products is complemented by favourable terms of payment. The offer includes high-quality and reliable construction materials, modern furniture and equipment for every room in the home and office, modern home appliances and major appliances, and consumer electronics by globally renowned manufacturers. In order to accommodate the consumers' rapid pace of every day even better, we also offered technical consumer goods in our web store.

Other operating activities

In order to present a comprehensive offer to consumers, Mercator Group has been developing additional business activities that include the offer of sportswear at the Intersport stores, apparel at Modiana stores, Maxen self-service petrol stations, and M holidays tourist services. Mercator Group also includes the manufacturing company Mercator-Emba, d.d.

Composition of retail units as at March 31, 2012

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	21	15	13	8	2	1	3	63	296,716	194,459
Supermarkets	128	45	29	31	10	-	1	244	265,155	171,282
Neighbourhood stores	331	51	39	48	68	2	1	540	192,783	111,698
Convenience stores	2	-	1	1	-	-	-	4	6,373	3,752
Getro market	-	-	23	-	-	-	-	23	11,938	7,557
Cash & Carry	13	5	16	-	-	-	-	34	143,285	101,580
Hard discount stores	9	-	-	-	-	-	-	9	6,452	4,820
Restaurants	22	7	-	2	1	-	-	32	9,888	5,879
M holidays	13	-	-	-	-	-	-	13	229	229
TOTAL FMCG program	**539**	**123**	**121**	**90**	**81**	**3**	**5**	**962**	**932,818**	**601,256**
Home program	64	13	12	-	3	-	-	92	121,236	72,730
Furniture program	30	1	-	-	1	-	-	32	32,270	24,227
TOTAL home program	**94**	**14**	**12**	**-**	**4**	**-**	**-**	**124**	**153,507**	**96,957**
Clothing program and drugstores	**91**	**17**	**34**	**12**	**1**	-	-	**155**	**70,875**	**59,572**
Clothing program	74	9	34	8	1	-	-	126	67,594	56,772
Drugstores and perfumeries	17	8	-	4	-	-	-	29	3,281	2,800
Intersport	**32**	**9**	**29**	**9**	**2**	**2**	-	**83**	**51,683**	**39,824**
TOTAL specialised programs	**123**	**26**	**63**	**21**	**3**	**2**	**-**	**238**	**122,558**	**99,395**
TOTAL retail units under management	**756**	**163**	**196**	**111**	**88**	**5**	**5**	**1,324**	**1,208,883**	**797,608**
Franchise stores	**225**	**10**	**53**	**-**	**-**	**-**	**-**	**288**	**52,450**	**34,509**
TOTAL with franchise stores	**981**	**173**	**249**	**111**	**88**	**5**	**5**	**1,612**	**1,261,333**	**832,117**

Composition of retail units is not comparable between the periods due to the changes in the classification of retail units.

Development of New Technological Solutions

In order to be perceived as a modern and innovative retailer, Mercator is looking to keep up with the latest technological solutions that reduce energy consumption and waste, provide pleasant and stimulating shopping experience for the customers and a pleasant and healthier working environment for the employees.

Development of New Store Concepts

Neighbourhood stores

Modern trends and changes in the market conditions again favour smaller stores. At Mercator, we are aware that neighbourhood stores are our major competitive advantage (number of stores, regional coverage, locations) which has not been fully taken advantage of (some stores are outdated, lack innovation and are not adjusted to the local environment).
Accordingly, Mercator launched a campaign to reposition this store format in order to maintain and consolidate the position of the best neighbour in every neighbourhood, one that is "always there, caring, friendly, and involved in the local community". We wish to contribute to the benefit of the neighbourhood and our customers by offering excellent fresh program and innovative ideas for the mix of products and services that will make our customers' lives easier.

Convenience stores

As an innovative retailer that keeps up to date with the modern market trends, we actively approached the development of the store format of convenience stores. The offer at this format is adjusted to each particular micro location and its main mission is to allow quick shopping and varied choice of ready-made products for a customer in a hurry.

COUNTER-CRISIS MEASURES AND STRATEGIC PROJECTS

Counter-crisis measures

In order to efficiently manage and hedge the risks in the current harsh economic conditions, Mercator Group is conducting the adopted counter-crises measures that are targeted at creation of value for the consumer and rationalization of operations. The measures are devised to constructively tackle the challenging macroeconomic conditions in the markets of our operations, which include high unemployment rates, lower purchasing power, and sensitivity to prices on the part of the consumers.

1. Let us work with the suppliers to find internal untapped improvement potential and invest the savings into better prices for the consumers!	**LET US GENERATE VALUE FOR OUR CUSTOMERS – LET US BE DETERMINED AND INNOVATIVE!**
2. Let us increase the share of private label sales and adjust the product assortment to the changed consumer behaviour!	
3. Let us communicate more efficiently with the consumers, and find new sales channels to reach new consumers!	
4. Let us revise the Mercator Pika customer loyalty system and bring it closer to a wider range of consumers!	
5. Let us revise the offer of the home products and become the leading technical consumer goods retailer in the entire region!	
6. Let us boost the appeal of other offer for the consumers: Modiana, Intersport, hospitality services, M-Mobil, M Holidays, Maxen!	
7. Let us improve our inventory and receivables management, and obtain additional sources to finance more investment!	**LET US FIND THE INTERNAL IMPROVEMENT POTENTIAL – LET US BE EFFICIENT!**
8. Let us improve the efficiency of the processes in sales and invest the savings into favourable pricing!	
9. Let us improve the efficiency of the processes in logistics and invest the savings into favourable pricing!	
10. Let us improve the efficiency of the processes in administration and invest the savings into favourable pricing!	
11. Let us invest within the limits of our own sources and let us improve the usage efficiency of our real property!	
12. Let us partly monetize our real property and reduce our debt to further consolidate our financial stability and development potential!	

In addition to the counter-crisis measures already in place, the Management Board adopted a set of additional measures in the first quarter of 2012 to alleviate the negative effects of the economic crisis in the region on the Group performance and to keep the Group on track towards the planned annual results.

Refreshment of (Mercator's) FMCG Offer in Slovenia

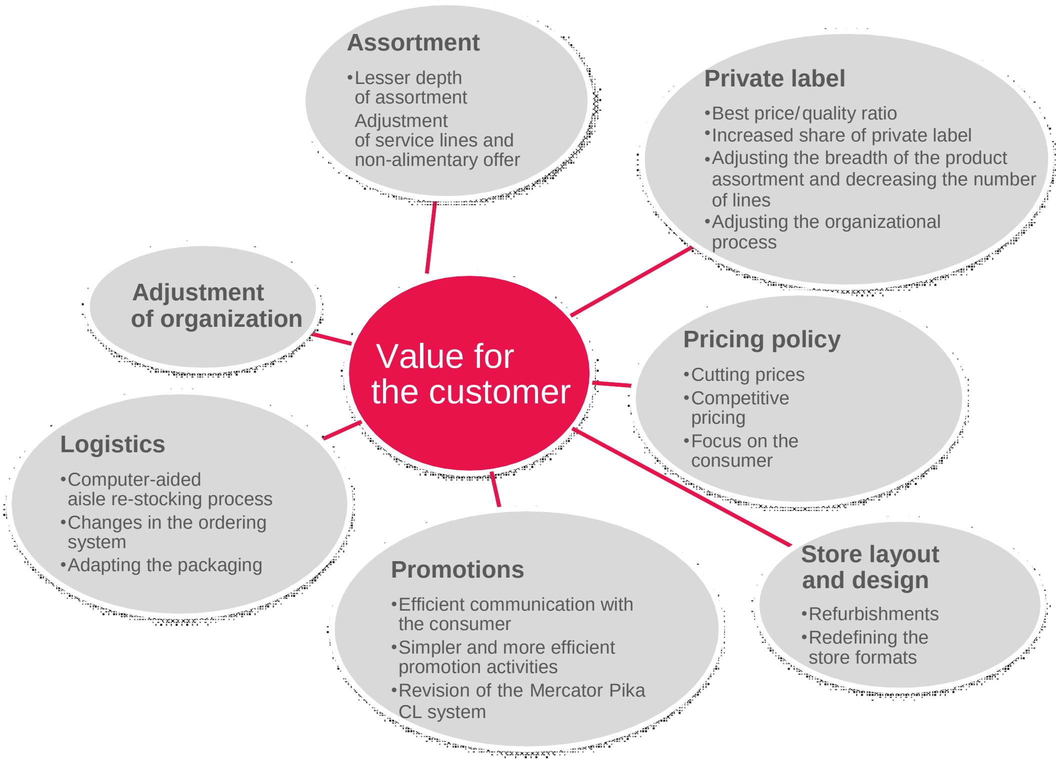
In the first quarter of 2012, Mercator stepped up the efforts to revise and refresh the retail network. Modernization and a new look of our stores pursues the goal of simple and fast shopping, as well as optimization of the retail area and the program mix. We are looking to convey a clear message to the customers at the very point of sale, or at the stores, that Mercator is a retailer whose mix of offer, products, and services provides the customers added value for their money, and that Mercator is the first and the right choice for the consumers.

Today, consumers look for well-priced products, as well as the best value in the market without making compromises in terms of requirements for product quality. Thus, the trend in fast-moving consumer goods is pointing towards a quest for solutions that will please the consumers despite the harsh environment by providing good value for money, while allowing the retailer to build trust and customer loyalty. Therefore, Mercator does not seek merely to provide choice; we wish to make shopping easier for the consumer, to maintain a high level of quality and services, to develop suitable store formats and activities targeted at satisfaction of consumer's needs, and to maintain the consumers' standard of living. It is important not to yield to the economic crisis and not to allow it to be translated into a crisis of quality and value, nor into a standstill in terms of development of services; competition should not be focused exclusively on cutting the prices.

At Mercator, the goals of the project of refreshment of FMCG offer will be attained by gradually:

- adjusting the offer to include the majority of products that are actually bought by our customers;
- increasing the share of private label products;
- updating the stores and allowing easier and faster shopping and a pleasant shopping experience;
- implementing new sales promotion activities and adjusted offer.

The project will take place in seven fields and the measures will be adjusted to the individual store formats.



Offer

The assortment or the entire offer of products is being adjusted to the shopping behaviour and needs of our customers, as well as individual store formats. The focus is on products that are most frequently purchased or which are purchased daily by the customers at a particular store. We are increasing the breadth, i.e. the variety of offer. Categories are laid out appropriately across the retail area. We shall also expand the share of fresh program, emphasizing self-service.
To improve cooperation with suppliers, Mercator migrated to the net-net pricing system early this year, which is the simplest and the most transparent system of cooperation between business partners and which is also recommended in the Code of Practice for stakeholders in the agricultural and food industry which Mercator fully complies with.

Private label

Customers seek the right value for a lower price. With some products, they may remain faithful to several brands, but in general, they are not willing to pay more for a similar product in different packaging; hence, demand for private label products is rising. We are therefore working with our suppliers to develop new innovative products, to adjust our offer within each line, and thus to pursue the sustainability trends. At Mercator, we are looking to increase the share of private label products as the shopping behaviour has changed profoundly. Suppliers are therefore given an excellent opportunity to make private label products that reach high sales figures, thus securing their own growth.

Promotions

It is Mercator's goal to offer the customers the best value and the best price for their basket of products. Hence, we are developing new marketing activities for our customers in order to come closer to them and convince them that we are offering more. In the future, Mercator's promotional activities will be even simpler, more transparent and more effective.

Pika customer loyalty program

Today, over half of Mercator's revenue in Slovenia is generated through the Mercator Pika system; however, it is our goal to further boost this share as this will also extend the scope of benefits for our loyal customers. We are constantly improving our offer and our services based on analyses of customer behaviour and customer needs. We also operate a free call center to take customer complaints and recommendations, and to provide information about out activities for them.

Modernization of store concept

Modernization of stores is always focused on a customer-friendly layout of departments in individual stores, which allows simple and fast shopping. Internal and external labelling and tagging are systematized and store formats are redefined. Above all, we are expanding the shares of fresh program, adjusting the service lines in favour of self-service, and increasing the share of partly pre-baked bread and offer of pre-packaged bread. We are including rotisseries, pizza ovens, and other solutions that will save our customers' time and allow them to adjust their shopping to their needs.

Pursuant to the new supermarket concept, twelve stores were refurbished in the first quarter of the year as a part of the refreshment project. The new supermarket concept has been developed to match the modern shopping trends and it allows our customers to save time, to choose the products more easily and more quickly, to enjoy a wider offer of fresh program, and to see special and low-priced offer clearly positioned at the store. We shall continue to refurbish our stores in the future.

We have also established, a clearer communication related to Mercator's core messages at the point of sale.

Logistics

We are implementing a computer-aided process of replenishing the aisles, the so-called CRP – Continuous Replenishment Process which has become well established with major retailers abroad. The update is not restricted merely to the shelf or aisle; it also includes other adjustments in all distribution channels.

The use of STECO packaging for fruits and vegetables throughout the logistics process:

providing high standards of hygiene,
33% lesser ozone layer depletion,
46% less summer smog,
49% less greenhouse emissions,
up to **95%** reduction in waste generation,
up to **39%** overall energy savings,
less damage to the goods, improved safety in transport and manipulation; the goods stay fresh longer.

Refreshment and Restructuring of (Mercator's) FMCG offer in Croatia

Main project objective

The main objective of the project Refreshment and Restructuring of FMCG Offer in Croatia is to adjust the offer to the changes in consumer behaviour. As in the project of Refreshment of FMCG Offer in Slovenia, the Croatian project, too, involves gradual changes in several areas in order to attain these goals. These areas include assortment and pricing policy, private label, organization, promotions, customer loyalty system, logistics, and store appearance. At the same time, restructuring to optimize the retail area and expand the offer with more attractive third-party providers is also under way in Croatia, particularly at Getro.

Specific goals in particular fields

Following are the specific project goals:

- expanding the breadth and reducing the depth of the assortment;
- further investment into competitive pricing and considerable increase in the sales of private label products in the overall composition of sales (improving the pricing perception among consumers);
- adjusting the customer loyalty system to a broader group of consumers;
- adjusting the service and more efficient communication with the consumers;
- optimization of the cost aspect of operations (cutting back on operating and administrative costs, logistics costs per unit of product, lease/rental expenses);
- Getro C&C is being restructured into Getro centers in order to optimize the retail area and to add attractive tenants (more comprehensive and more appealing offer for price-sensitive consumers); elsewhere, restructuring operations are under way (Getro Črnomerec is being restructured into a Mercator center).

Project status

2012 is the key year for changes with the first test units scheduled for opening in the second quarter of the year and implementation or roll-out in the third. This year, a total of 17 Mercator stores will be refreshed and/or restructured, in addition to all Getro stores, subject to agreement with the potential tenants. Restructuring of the first test store Getro Pula, which was opened on March 29, 2012, has shown positive effects as the key indicators have been attained (sales/square meter, productivity, share of private label etc.).

Establishing the chain of technical consumer goods stores

Consistently with the focus on the core activity, the company Poslovni sistem Mercator, d.d., transferred as of January 1, 2012 the technical consumer goods program to an independent business entity M - Tehnika, trgovina in storitve (trade and services), d.d. Through a network of subsidiaries, the company and the entire M - Tehnika Group shall also be present in other markets of Southeastern Europe where Mercator Group is already conducting operations.

The M - Tehnika Group is looking to offer its consumers quality technical consumer goods in different price segments, and the best in-store consulting service. Confidence and loyalty of the largest possible number of customers will be built by additional innovative combinations in terms of offer of complementary products or services, and by a permanent reasonably priced offer. When working with businesses (legal persons), establishing long-term business relationships with key strategic buyers shall be of paramount importance; with all other customers, maintaining a professional business relation will be the key. Orientation towards more demanding segments of customers with lower credit risk shall be essential. Target groups of customers include retailers and franchise stores, legal persons offering services of building completion and finishing, and public enterprises. The company's offer will also be present online where its revised sales policy will mostly address the segment of younger buyers.

Activities in the first quarter of 2012

Numerous activities have taken place with regard to product management in order to lay down the foundations of optimized operations. This is expected to yield results in the coming months.
We conducted negotiations with all suppliers and signed new contracts, which resulted in an improvement of procurement conditions.

We identified the categories, brands, and products with lesser turnover and defined the criteria for identifying obsolete inventory. We approached the clearance of obsolete inventory in a systematic manner, predominantly from our distribution centers and subsequently from our retail units. A part of the merchandise was returned to suppliers; for the majority of the goods, we cut the retail prices. Clearance is taking place at currently existing stores, at the Outlet store opened in January in Maribor, and via web store.

Considering the adopted strategy of defining the target categories, we have analyzed our competitors and the sales results in order to unify our procurement sources and to manage them more efficiently. We created closed assortments for 25 major categories.

FINANCIAL MANAGEMENT

Stable Financial Operations

Mercator Group's net financial debt as at March 31, 2012 amounted to EUR 1,096,171 thousand, which is virtually the same as at the end of last year and as in the relevant period last year.

in EUR thousand	**March 31, 2012**	**March 31, 2011**	**Index March 31, 2012/ March 31, 2011**
Non-current financial liabilities	769,697	799,335	96.3
Current financial liabilities	409,872	372,047	110.2
Derivative financial instruments (liabilities)	5,073	1,531	331.4
Financial liabilities including derivative financial instruments	**1,184,642**	**1,172,912**	**101.0**
Cash and cash equivalents	21,517	12,920	166.5
Derivative financial instruments (assets)	69	58	119.0
Available-for-sale financial assets	2,621	3,959	66.2
Loans and deposits	64,264	70,661	90.9
Financial assets	**88,471**	**87,598**	**101.0**
NET FINANCIAL DEBT	**1,096,171**	**1,085,315**	**101.0**

Working capital management

Harsh economic conditions compel us to tap into the internal improvement potential within the Mercator Group as much as possible. One such possibility is the improvement of working capital management that would release additional funds tied up in working capital. Hence, Mercator Group laid down in this year the working capital management project which is to improve the days outstanding for working capital.

In the first quarter of 2012, Mercator Group decreased the value of inventory by EUR 21,339 thousand, especially by intensively conducting the following activities:

- optimizing the strategic stock;
- optimization of the ordering process;
- even more intensive adjustment of the product assortment to the needs of the customers, and adjusting the dynamics of ordering to the dynamics of sales,
- update and implementation of new application tools for aid in ordering and clearance of old inventory.

Management of trade receivables included the following activities conducted at the Mercator Group:

- intensive efforts to collect unpaid overdue receivables;
- updating the application support for receivables management;
- faster calling on the instruments used as payment insurance;
- looking for additional possibilities to offset the receivables;
- earlier stop of deliveries in case of payment defaults;
- restricting open sales without first-grade insurance;
- raising the bar for suitability of payment insurance.

Mercator Group shall continue to conduct the working capital optimization project in the future.

Diversifying the Sources of Financing

For Mercator, long-term operating lease of trade facilities has become a very important form of investment financing. These facilities were either taken on lease by Mercator form their respective owners or they were constructed for Mercator by local property development partners.

Ratio of variable to fixed or hedged financial liabilities

As at March 31, 2012 the ratio between variable and fixed or hedged financial liabilities at the Mercator Group amounted to 42.7 percent vs. 57.3 percent (as at March 31, 2011, the ratio was at 55.7 percent vs. 44.3 percent).

Finance expenses

In the first quarter of 2012, the variable interest rate 6-month EURIBOR fell from 1.606% to 1.078% while the average reference rate remained virtually the same as in the corresponding period last year. Aggravation of the financial crisis caused the pressure on the interest rate margins to mount. Given the slightly higher average level of Mercator Group's debt in the first quarter in comparison to the equivalent period last year, which is a result of refinancing risk management activities, this resulted in an increase of finance expenses.

Debt to equity and current to non-current financial liability ratio

As at March 31, 2012 Mercator Group attained a debt-to-equity ratio of 1:1.45. The ratio is a quotient between equity, which includes share capital as reported in financial statements and long-term provisions, and net financial debt.
In the first quarter of 2012, Mercator Group's composition of financial liabilities by maturity took a slight turn for the worse. The share of long-term financial liabilities as at March 31, 2012, amounted to 65.3 percent (68.2% as at March 31, 2011).

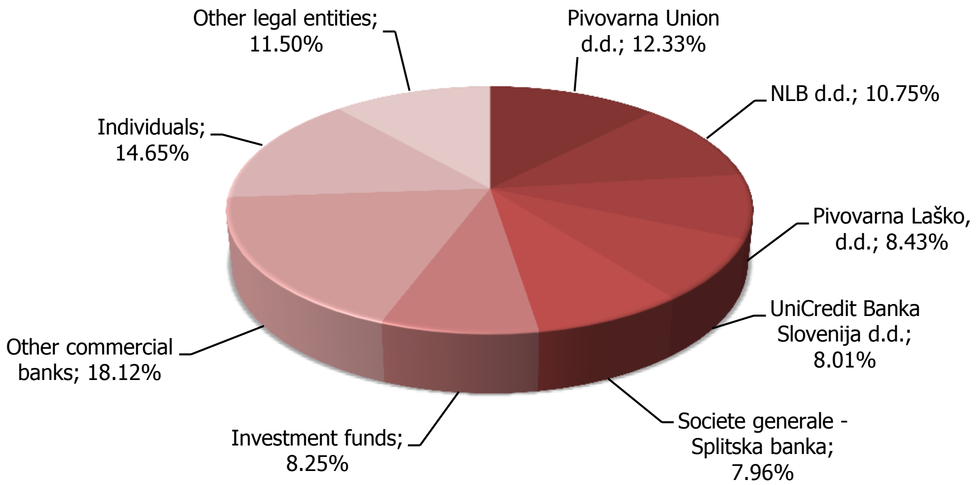
MERCATOR SHARE AND INVESTOR RELATIONS

Mercator share and ownership structure

Basic information on the share of the company Poslovni sistem Mercator, d.d., as at March 31, 2012

Code / Symbol	**MELR**
Type	Ordinary share
Listing	Prime market of Ljubljana Stock Exchange, d.d.
Share capital	EUR 157,128,514.53
Number of shares	3,765,361
Number of treasury shares	42,192
Number of shareholders	15,457

Ownership structure of the company Poslovni sistem Mercator, d.d., as at March 31, 2012



Major Shareholders

As at March 31, 2012, the following ten largest shareholders combined owned 65.18 percent of the company.

	Major Shareholders	Country	Number of shares	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	Societe Generale-Splitska banka, d.d.	Croatia	299,772	7.96%
6	Nova KBM, d.d.	Slovenia	197,274	5.24%
7	GB, d.d.	Slovenia	142,920	3.80%
8	Prvi faktor - faktoring, d.o.o.	Serbia	125,963	3.35%
9	Abanka Vipa, d.d.	Slovenia	103,400	2.75%
10	Radenska, d.d.	Slovenia	96,952	2.57%
		Total	**2,454,438**	**65.18%**

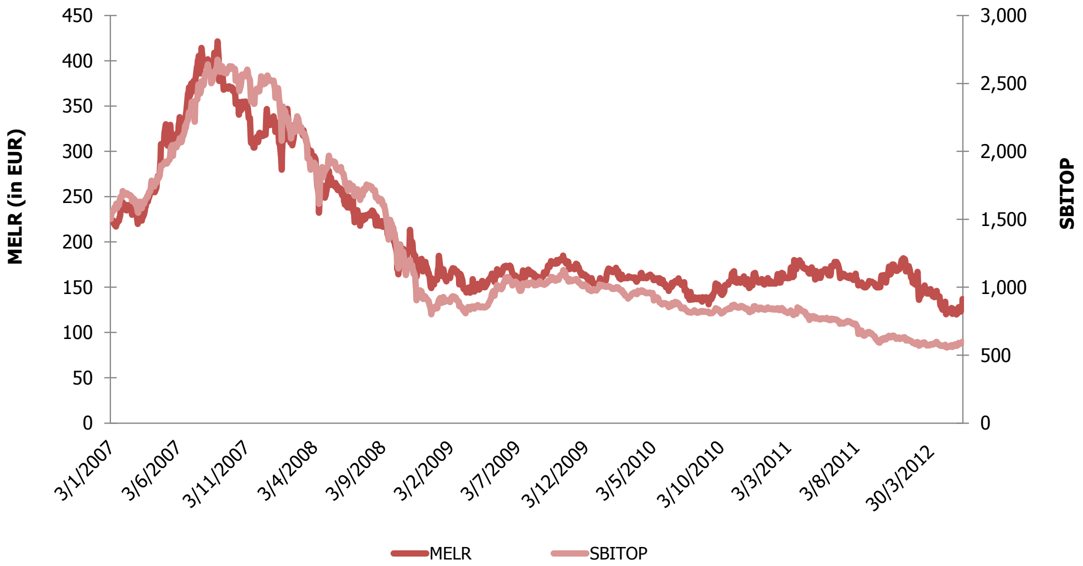
Foreign shareholders

As at March 31, 2012, the share in the company Poslovni sistem Mercator, d.d., held by foreign investors amounted to **18.45 percent**, which is 1.01 percentage point more than at the end of 2011.

Shares held by Management and Supervisory Board Members as at March 31, 2012

	First and last name	Position	Number of shares	Share
	Management Board			
1	Žiga Debeljak	Management Board President	1,100	0.0292%
2	Melita Kolbezen	Senior Vice President	0	0.0000%
3	Vera Aljančič Falež	Senior Vice President	30	0.0008%
4	Peter Zavrl	Senior Vice President	60	0.0016%
5	Stanka Čurović	Senior Vice President	0	0.0000%
		Total	**1,190**	**0.0316%**
	Supervisory Board			
1	Matej Lahovnik	Supervisory Board Chairman	0	0.0000%
2	Rok Rozman	Deputy Supervisory Board Chairman	0	0.0000%
3	Boris Galić	Supervisory Board member	0	0.0000%
4	Zdenko Podlesnik	Supervisory Board member	0	0.0000%
5	Marjeta Zevnik	Supervisory Board member	0	0.0000%
6	Mateja Širec	Supervisory Board member	36	0.0010%
7	Sandi Leban	Supervisory Board member	0	0.0000%
8	Ivan Valand	Supervisory Board member	0	0.0000%
		Total	**36**	**0.0010%**

Movement of closing price per MELR share in last five years, compared to the movement of the SBITOP index



Key information for the shareholders

	March 31, 2012	December 31, 2011	Index
Number of shares entered in the Court Register	3,765,361	3,765,361	100.0
Number of treasury shares	42,192	42,192	100.0
Market capitalization (in EUR)	515,854,457	553,508,067	93.2
Market price per share (in EUR)	137.00	147.00	93.2
Book value per share (in EUR)	214.39	221.81	96.7
Minimum close rate in the period (EUR)	120.00	136.00	88.2
Maximum close rate in the period (EUR)	151.95	182.00	83.5
Average close rate in the period (EUR)	132.77	162.85	81.5

Market capitalization is calculated by multiplying the number of shares entered into the court register as at the end of the period with market price per share as at the end of the period.
Share book value is calculated as the ratio between the value of the equity of the company Poslovni sistem Mercator, d.d., as at the end of the period, and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.

Dividend policy

Pursuant to the resolution adopted at the 18th regular Shareholders Assembly held on March 30, 2012, the company Poslovni sistem Mercator, d.d., paid out gross dividend of **EUR 6.00** per ordinary share in 2011.

Treasury shares

As at March 31, 2012, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares. In period 1-3 2012, the company neither acquired nor disposed of treasury shares.

RISK MANAGEMENT

Management of key risks in the period 1-3 2012

Risk is defined as any uncertainty regarding future business events, which can decrease the probability of attainment of the business goals laid down or the level of attainment of business goals, thus bearing a negative effect on the performance. Harsh and unpredictable economic circumstances that have been the background of our operations for a while, require systematic and deliberate management of risks the company is facing in its operations. Active risk management is geared towards the objective of timely recognition and response to potential threats by developing appropriate measures to hedge against identified risks or to reduce risk exposure.

In the first quarter of 2012, challenging economic conditions in global financial markets put a damper on the entire economic environment both globally and in the markets of Mercator's operations. This was reflected in notable drop in retail demand and a change in the composition of consumption, as well as in the persistence of the trend of uncertainty with regard to financial risks which were not common in the period before the crisis. For Mercator Group, systematic and deliberate risk management is of key importance in such difficult economic environment.

Business Risks

Business risks are related to company operations and our core activity.

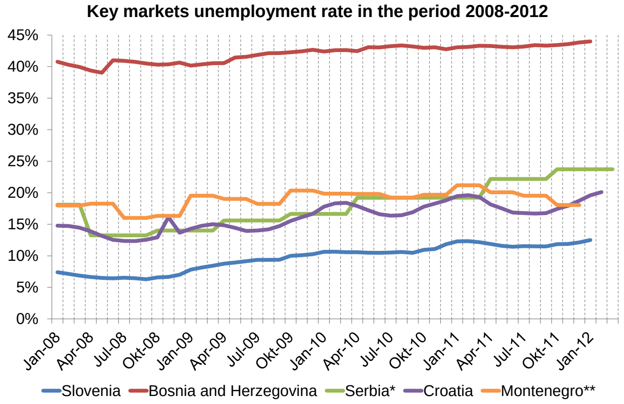
Risks in the operations of trade companies increase as a result of economic conditions due to changes in the shopping behaviour of the consumers, and particularly due to a drop in their purchasing power. The unemployment rate is the key indicator of purchasing power and the sense of security on the part of the consumers. In recent months, this category has reached the highest levels in recent years in the key markets of Mercator's operations.

Risk of a decline in purchasing power

Assessment of the risk of a decline in purchasing power (size of market) due to challenging economic conditions.

The risk of a decline in purchasing power is related to economic growth, unemployment rate, increase in personal income, and changes in the prices of essentials. In 2011, economic situation had a negative impact on the purchasing power of consumers; such effect persisted in the first quarter of 2012. **In Slovenia**, economic growth was negative in the third and fourth quarter of 2011 which means Slovenia slid back into recession. The outlook for 2012 is bleak as well: gross domestic product is estimated to decline by around 1%. In January 2012, the unemployment rate continued to rise. The unemployment rate hit 12.5% to set a record in more than a decade. In the first quarter of 2012, prices of essential consumer goods rose somewhat faster than in the last three years, which adds to the pressure on the consumers' purchasing power.

In key foreign markets of Mercator's operations, unemployment rate is even higher than in Slovenia; moreover, it – with the exception of Montenegro – continues to rise. In Mercator's foreign markets, average income is notably lower than in Slovenia. In the long run, we may expect these markets to converge and close in on the gap in development; however, in a time of economic slowdown, considerable increase in purchasing power cannot be expected for these markets even in the medium run. Growth of personal income is slow in all



** Survey measurement; semi-annual data are extrapolated to the monthly level.*
*** Survey measurement; quarterly data are extrapolated to the monthly level.*

markets except Serbia; however, the effect of increase in net personal income is offset by the inflation rate which, although it is slowing down, is still the highest in Serbia.

Risks of suboptimal marketing mix and effects of the competitive environment

Assessment of risk based on market conditions and Mercator's position in the Group's target markets.

At Mercator Group, we are regularly monitoring the perception of key elements of the marketing mix. In the first quarter of 2012, we further pursued the implementation of the measures adopted to mitigate the risk of suboptimal marketing mix and effects of the competition. The strategic projects of refreshment (and restructuring) of FMCG offer in Slovenia and Croatia and the establishment of a technical consumer goods chain are consistent with our goal of adjusting the marketing mix to the needs of our customers. We are also implementing a new assortment policy according to which the best-selling products should be available at all stores at any moment. 2012 is also a key year for the project of refreshment and restructuring of Mercator's FMCG offer in Croatia where three stores have already been refurbished to accommodate the new, adjusted offer which is better suited to the changes in consumer behaviour. In the period at hand, a lot was done to improve the procurement sources for non-alimentary products and technical consumer goods. In order to preserve the purchasing power of consumers, Mercator Group managed its retail prices on daily basis in the first quarter of 2012. The purpose of such price management is to improve the competitiveness of our pricing and to approach more effectively the consumers who have cut back on their spending since the onset of the crisis.

Risks of failure to attain the planned profit margin

Assessment of the risk of failure to attain the planned profit margin.

Due to the increasingly harsh economic situation and impaired competitiveness, additional investments in terms of pricing are and will be required at the Mercator Group in 2012; this will affect the profit margin attained. This year's transition to net-net pricing will allow even more efficient daily management of regular and special offer retail prices. Positive effects of the transition to the net-net pricing are expected in the second half of the year when the effects of daily price negotiations and more active management of retail prices to improve the competitiveness of Mercator's pricing as perceived by the consumers are evident.

Risks in the supply process

Assessment of global and local impact on Mercator's supply processes.

In the first quarter of 2012, we worked with proven suppliers with whom operations are clear and transparent. This allows timely identification of problems that suppliers are facing in the aggravated economic conditions, and prompt adjustment to reduce the possibility of delivery failures. Regular monitoring and checking of supplier solvency allows timely redirection to new supply sources.
Fuel and energy prices rose in the first quarter of 2012. Therefore, we expect an increase in the prices of products the pricing of which depends heavily on energy prices. Carefully thought out procurement policy and choice of different suppliers for each category will reduce or disperse the risk.

Financial risks

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.

Circumstances in the global financial markets in 2012 are aggravating and the economic conditions are growing more challenging and severe. As a result, the majority of European countries entered a new cycle of recession as early as last year. Corporate and consumer confidence is still relatively low as a result of the economic crisis. In the first quarter, consumer confidence suffered an additional blow.

Credit risk in wholesale

Assessment of the risk that receivables from business partners resulting from deferred payment will only be settled partly or not at all.

In the period 1-3 2012, we saw the payment defaults and delinquency grow even more rampant in all markets of our operations. Due to increased credit risk in wholesale, Mercator Group adopted additional risk hedging measures (earlier stop of delivery, reducing the limits etc.) and restricted deferred payment sales without first-grade insurance. These measures additionally mitigate and hedge the risk of bad receivables.

Mercator Pika card credit risk

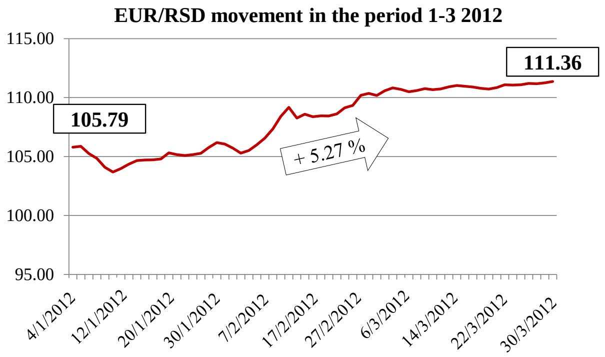
Assessment of the Mercator Pika card credit risks (possibility that receivables from customers, resulting from deferred payment, shall only be settled partly or not at all).

In the period 1-3 2012, we monitored daily the changes in receivables and credit risk pertaining to the Mercator Pika card, and continued to implement the measures to hedge this risk.

Currency risk

Assessment of the loss of economic benefit due to changes in exchange rate.

In the period 1-3 2012, we saw strong volatility of exchange rates of Serbian dinar and Croatian kuna which had a negative impact on Mercator Group's performance in the first quarter of the year. The exchange rate EUR/RSD alone rose from 105.79 to 111.36 in the first three months of 2012, which represents a 5.27% depreciation of the Serbian dinar relative to euro. Average exchange rate for the Serbian dinar in the first quarter of 2012 was at RSD 108.11 per 1 EUR; average rate of the Serbian dinar in the equivalent period of 2011 was at RSD 103.95 per 1 EUR.



Interest rate risk

EURIBOR interest rate is subject to market fluctuations and it is changing on a daily basis, which can lead to increased financing costs.

In the first quarter of 2012, the variable interest rate 6-month EURIBOR fell from 1.606% to 1.078% while the average reference rate remained virtually the same as in the corresponding period last year. Aggravation of the financial crisis caused the pressure on the interest rate margins to mount. Furthermore, interest rate for Mercator Group financing is somewhat higher due to the implementation of measures to hedge the refinancing risk, as the level of current financial liabilities rose at the end of 2011; by the end of the first quarter of 2012, it was balanced out.

Liquidity risk

Assessment of the risk that at a certain moment, the company will not have enough liquid assets to settle its current liabilities.

The ratio between non-current and current financial liabilities worsened from 68.2%:31.8% (March 31, 2011) to 65.3%:34.7% (March 31, 2012).

Operational risks

Operational risks affect the ability to conduct business processes and to attain the goals laid down, and the cost efficiency of Mercator Group operations.

Category management operational risks

Increase of tradable commodity prices, seasonal effect.

Our category management involves close monitoring of the prices of raw materials, on which the prices of our products are heavily dependent. Since commodity market changes affect the prices for all products in a category, loss of sales and profit margin cannot be recovered by the use of substitutes. We are actively monitoring the surges in energy prices and their impact on manufacturer prices. According to the European Commission estimate, the prices of agricultural products will remain approximately the same in the medium run. Circumstances in the market for grain will depend on low inventories and prices that will exceed the most recent average. In the dairy sector, the European Commission is anticipating positive developments due to competition from the emerging countries; for meat sector, conditions are expected to improve gradually, especially for pork and poultry.
High inventory of goods or low profit margin due to extreme cuts in retail prices are a result of changes in shopping behaviour and the drop in purchasing power of the consumers, which was reflected on the demand for seasonal products. We take special care to monitor the inventory of seasonal products and we adopt measures to clear such inventory as necessary.

IT risks

Mercator Group IT risks appear in management of business data, business IT systems, and internal business processes. In the first quarter of 2012, there were no major changes in IT risks.

Environmental risks

Inefficient use of electric energy.

In order to mitigate the effects of critical environmental risks pertaining to the use of electric energy, we developed a **Monthly environmental report for the users** which includes information on the amount and value of the electric energy consumed, data on specific use of electric energy, and plans and indices of the use of electric energy. The persons in charge of retail analyze the environmental report on monthly basis. We have also compiled a list of 15 problematic units in which the reasons for deviations in the use of electric energy from the planned figures will be examined.

SUSTAINABILITY REPORT

Sustainable development policy

Mercator operations are sustainable and responsible, creating a healthy and safe future for the people and the environment.

Sustainable Development Council

Responding to the effect of economic conditions, Mercator Group's Sustainable Development Council examined and revised the commitments in the medium run sustainable development strategy and the action plan for 2012.

Mercator is a member of several Slovenian and international associations within which the company has an opportunity for dialogue with the stakeholders and for exchange of sound practice:

- Regarding Environment Protection, we are members of the Environment Committee with the Slovenian Chamber of Commerce, and the Committee of Environment and Logistics with the Eurocommerce Association.
- In the field of marketing, we work with the Slovenian Marketing Association, Slovenian Advertising Chamber, and the Consumer Goods Forum which is a global association of retailers and producers.
- We play an active role in the United Nations Global Compact Slovenia sustainable development initiative, part of the UN Global Compact (UNCG) network.
- We successfully complied with our commitments laid down in the Retail Environmental Sustainability Code, which was proven by the review of the international organization Retailers' Environmental Action Programme (REAP).
- We are taking part in the European project titled PLASTiCE – Innovative value chain development for sustainable plastics in Central Europe.

RESPONSIBILITY TO CUSTOMERS

Care for the customers is Mercator's core and fundamental principle. Therefore, our marketing activities will be planned and conducted, in compliance with the marketing strategy laid down, with consideration of the trends and needs of our customers. These activities will reflect Mercator's commitment to offering environmentally friendly products and services, and to promote environmental awareness and environmentally friendly activity. We shall continue to pay particular attention to all processes and procedures of providing food safety for products in our aisles, and to bring the information on our offer closer to the customers through innovative approaches.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1-3 2012)
Care for food safety.	• **128 regular and 9 extraordinary controls** were carried out. • We recorded 253 inspection reviews. • We analyzed **373 samples of private label products**. • We **monitored 336 samples** in open departments (mostly meat departments). We recorded **11 samples** from national monitoring.

Introduction of environmentally friendly formats, standards, and technologies at our stores.	• We founded a workgroup for managing the category of organic ("eco") products, and prepared instructions for standardized and conspicuous positioning of eco products at particular store formats. • We have temporarily halted the project of installing electronic price tags. • We reduced power consumption at stores with closed refrigerators and freezers **by 10%.** • Pursuant to EU Commission Regulation No. 1062/2010 on requirements for energy labelling of TV sets, M-Tehnika, d.d., launched the preparations for such advertising in catalogues and in our web store in March. When shopping for any TV set, the customer will receive the information on the energy efficiency class of the model; power consumption in operation mode; and annual power consumption.
Marketing activities related to the offer of environmentally friendly and well-priced products and services, and informing and educating the consumers about the environmentally friendly activities.	• In March, we installed **"Grown in Slovenia"** tags in fruit and vegetable departments to inform the customers of the origin of the product. • We provided communication support to the **tender and invitation to bid for Slovenian growers and farmers.** Working with the winners of our contest "Draft solutions for packaging made of environmentally friendly packaging materials for organic and other products of Slovenian origin", we are **developing packaging** and designing a solution that will make the packaging appear as a uniform line, as well as make the packaging cost effective.   • From February 15, 2012 to May 31, 2012 we are conducting a sales promotion activity based on the humanitarian donation called "Following the Kekec's footsteps to knowledge!", which will involve working with the company Henkel (selected based on a contest by the Eko School) to enable a free natural science camp at the Kekec Eco House in Srednji Vrh for 100 children. • Major appliances are paid special attention as the key and target category both in terms of placement in the sales assortment and preparation of sales promotion activities.

RESPONSIBILITY TO EMPLOYEES

Number of employees

MARKET	Number of employees as at March 31, 2012	Number of employees as at December 31, 2011	Index Number of employees March 31, 2012/ December 31, 2011	Number of employees based on hours worked in the period 1-3 2012
Slovenia	12,020	12,034	99.9	11,198
Serbia	4,662	4,806	97.0	4,634
Croatia	3,771	3,873	97.4	3,432
Bosnia and Herzegovina	2,003	1,722	116.3	1,929
Montenegro	1,442	1,429	100.9	1,434
Bulgaria	251	268	93.7	241
Albania	130	134	97.0	115
TOTAL	**24,279**	**24,266**	**100.1**	**22,983**

In the period 1-3 2012, we wish to emphasize the **shop manager training** at the company Poslovni sistem Mercator, d.d., and in the territory of Southeastern Europe, which was attended by 533 retail managers. We defined new competencies for leaders and prepared everything required to start the **assessment of competencies** for 2,341 leaders at the Mercator Group. A new HR priority has been introduced to our HR strategy: **management of 55+ employees**.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1-3 2012)
Leadership development **Employee education and training** **Employee motivation and compensation** **Staffing**	• Great attention was paid to revision and assessment of leader competencies which include: focus on objectives (management by objectives), organization of work, ethical conduct, positive outlook, openness to change, and care for co-workers. Employing the 360° method, competencies will be assessed by a questionnaire with 38 typical patterns of behaviour pertaining to particular competencies. • We organized shop manager training in Slovenia and Mercator's Southeastern European markets for a total of 533 attendants. In Slovenia, the schools are organized as three-day workshops for smaller groups which involved a total of 105 participants; in Southeastern Europe, an event for 428 leaders was held. • Pursuant to the corporate standard of induction of new employees, we organized at our parent company for the first time a ten-day rotation for 18 new employees with level VII education. Newly recruited employees learned up and close about the work in category management, marketing, logistics, retail, and wholesale. • We also developed a new HR priority within our HR strategy: management of 55+ employees. This shifts the focus on a considerable part of employees with different needs, traits, and characteristics due to their age. • We devised a corporate system of internal instructors, which motivates training of new ones, i.e. new lecturers,

	trainers, mentors, and instructors. • At the company Poslovni sistem Mercator, d.d., we organized the "prep school of management"; in Southeastern Europe, the "school for future leaders" was organized. At the company Mercator-BH, d.o.o., we held a number of introductory seminars for workers that joined Mercator as a result of the Drvopromet, d.o.o., merger. • In Slovenia, we developed an e-library titled Mercator's Growing Book. It includes elements of an e-library and it allows e-applications to third-party training and education. This saved the cost of paper documentation. • President of the Management Board met the alumni of the Mercator Academy of Business at a round table on the challengers laying ahead for Mercator. • In Southeastern Europe, awards for the best stores in 2011 were presented.
Dialogue with employees and social partners Occupational health and safety	• 74 news announcements were made on the Intranet in Slovenia. • In Southeastern Europe, we introduced informative brochures that are handed out with the salary reports at all companies. • 64 parents of newborn babies were presented with Lumpi packages. • Mercator Humanitarian Foundation provided a total of EUR 21 thousand of aid to 39 employees that were ill or in social distress. • We held the Week of "Safe Moving of Heavy Loads" was held at the companies Poslovni sistem Mercator, d.d., Mercator IP, d.o.o., and Modiana, d.o.o. • Mercator sports and culture society now has 719 members.

RESPONSIBILITY TO NATURAL ENVIRONMENT

We are systematically establishing a relation to our natural environment through energy-efficient construction or refurbishment of stores and office buildings, efficient use of energy, and careful waste management, as well as by considering other relevant aspects. We provide sustainable logistics and we proactively convey the right information and present our environmentally friendly offer to our customers.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1–3 2012)
Reducing consumption of power and fuels for heating by implementing savings measures, current maintenance, and minor investments.	• Installation of three combined heat and power (co-generation) units at the facilities MC Maribor, MC Ptuj ERA, and MC Ptuj Ormoška. • Development of regular monthly reports for monitoring the use of energy at retail units. • Start of the pilot project of establishing control of the operation of the Retail-care refrigeration equipment.
Implementation of the Eco House project (environmentally friendly store).	• Obtaining the building permit.
Cutting the use of natural resources and waste generation.	• We prepared an Analysis of Environmental Risks for 2012 complete with relevant measures to reduce critical environmental risks. • We implemented a system for recording and analysis of extraordinary events in environmental protection, and prepared a set of response and preventive measures for such events. • We issued a preliminary draft of the calculation of the corporate carbon footprint for the entire company, a particular store, and products of Mercator private label line.
Expanding the use of environmentally friendly freight vehicles.	• In compliance with available resources we are increasing the number of environmentally friendly freight vehicles.
Relocation of logistics services to energy-efficient and people- and environmentally friendlier, suitably located facilities outside urban areas.	• The project has been slowed down due to a cutback in investment funding.

RESPONSIBILITY TO SOCIAL ENVIRONMENT

Mercator's vision of sustainable development and corporate social responsibility dictates specific activities that contribute to the development of both local and regional environment and which improve the quality of people's lives. Sponsorships and donations and inclusion in the socially beneficial campaigns are an important part of Mercator Group's strategy of comprehensive corporate responsibility. We support and make possible humanitarian, sports, cultural, scientific, educational, and other projects.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1–3 2012)
Corporate social responsibility	• We supported the organization of the following major projects in Slovenia: - international Slovenian open table tennis championships; - "kurentovanje" carnival in Ptuj; - international Alpine ski race for the Loka Trophy 2012; - finals of the ski jumping World Cup in Planica 2012; - Slovenian drama week in Kranj; - celebration of the 500th anniversary of the birth of the famous cartographer and geographer Gerardus Mercator; - 6th days of Slovenian municipalities and meeting of mayors.

RESPONSIBILITY TO SUPPLIERS

Partnership with suppliers is a key element of sustainable responsibility in business. We work with the suppliers to build solid partnerships based on transparent and straightforward transactions, while making every effort to establish an environmentally friendly supply chain.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1–3 2012)
Working with proven suppliers	• In order to see the food grown and produced at Slovenian farms reach the customers earlier and in appropriate package, we invited Slovenian farmers and small growers to work with us. We offer them standardized modern packaging made of environmentally friendly raw materials at a reasonable price. The invitation, complete with terms and conditions, will be announced on our website at **www.mercator.si** • The project Lokalnost ("Locality") involved further activities to include products of Slovenian origin, by local suppliers, in our offer. The project **"Locality"** includes products that represent: - local offer of farms and small (minor) growers; - offer by growers and producers of a certain region, - pan-Slovenian local offer – e.g. Slovenian apples; • Our aisles include **410 products by 80 small, local producers and growers.** • Statements on safety, quality, and compliance of food and materials supplied to Mercator, d.d., were signed by the contractual suppliers for 2012.

	• Statement of compliance with human rights and relation to the broad environment is consistent with the ETI (Ethical Trading Initiative) Code.

RESPONSIBILITY OF PROVIDING SECURITY

Consistently with the GRI guidelines, we included in 2012 the activities pertaining to provision of security in our sustainability reports.

At Mercator Group, we are aware that security and safety of our customers, employees, and our property is an important aspect for successful operations, which in turn is the responsibility of all employees. **The basic guideline for the provision of security and implementation of relevant activities is defined in the document Mercator Group Security Policy.** Responsible persons authorized for security both at the level of Mercator Group and the operational business areas of Mercator Operations Slovenia and Mercator Operations Southeastern Europe work with security experts to make sure all security activities are being conducted in compliance with the security principle. In order to provide a uniform approach and operations, persons in charge of security in particular companies of the Mercator Group coordinated their efforts. We prepared a document "Organizational Rule on Management and Implementation of Security Standards and Services at Mercator Group" in order to provide comprehensive and uniform operations. The organizational rule is intended for the users of security services and responsible persons in this regard. It lays down the foundations for systematic and coordinated management and implementation, or execution, of security standards at the Mercator Group. We worked closely with third-party security providers (security service providers), especially to provide the quality of such services. Consistently with the security assessment and perceived risks, we were focused on conducting preventive, training and educational activities in respective organizational units. The purpose of these activities was to reduce the risks and improve security of both employees and customers. Persons in charge of security actively took part in planning and implementation of the technical security systems in case of investments and refurbishments of retail facilities.

RESPONSIBILITY TO QUALITY

In order to provide all-around quality, our activities include implementation of international management systems, preventive action of internal controls, efficient documentation and non-compliance management, implementation of corrective/preventive measures, and monitoring key quality indicators.

STRATEGIC FIELDS	ATTAINMENT OF GOALS (1–3 2012)
Maintenance, implementation, and certification of international quality management systems at Mercator Group companies by independent certified bodies.	• As at March 31, 2012, Mercator Group holds **13 active certificates**. • We coordinated the certification audit for the sustainability report within the Mercator Group Annual Report according to the GRI guidelines, and we were awarded the relevant certificate. • We conducted activities of preparation for external/independent audits.
Management of documentation, records, non-compliance, and corrective and preventive measures at the Mercator Group.	• As at March 31, 2012, Mercator Standards Collection included **2,437** valid documents. **507** new or updated documents were published in the period 1–3.
Systemic monitoring of quality management processes at the Mercator Group.	• We carried out activities to harmonize and unify the process of monitoring environmental indicators for particular environmental aspects at all companies of the Mercator Group.

	• Information on electric energy consumption and specific carbon dioxide emissions in the period 1-3 2012 for **Mercator Group** are as follows: - Electric energy consumption amounted to **146 GWh**; specific power consumption stood at **85.77 kWh/m^2**. - Specific carbon dioxide emissions of fuels amounted to **52 kg CO_2**/m^2; carbon dioxide emissions of fuels reached **88,077 tons of CO_2**.
Establishing IT support for managing the quality management system requirements at the Mercator Group (applications: AMS, eNPP, eIK, eKolegiji, SAP-BI-OK etc.).	• We are in the closing stage of extensions and improvements to the Mercator Standard Management Application. • Application for management of continuous improvements (eNPP) will be extended in such way that we are able to use it for monitoring of corrective measures following internal controls, inspection reviews, and monitoring. • At the company Mercator - S, d.o.o., the project of monitoring the environmental indicators using the SAP-BI-OK application is currently in progress.

FINANCIAL REPORT

All financial statements of the Mercator Group for the period 1–3 2012 have been prepared in compliance with International Financial Reporting Standards and they are unaudited.

ACCOUNTING POLICIES

Pursuant to the provisions of Article 7 of the **Code of Practice for the stakeholders in the agrifood chain**, adopted in 2011, Mercator Group changed on January 1, 2012 the way it manages its relations with majority of suppliers of fast-moving consumer goods in Slovenia, by implementing pricing according to **net-net price system**. Before, Mercator mostly managed its supplier relations according to the principle of manufacturer or wholesale prices. Since this is a notable change that also affects the valuation of inventories and cost of goods sold, Mercator made some changes pursuant to the provisions of IAS 8 as of January 1, 2012 to the relevant accounting policies at the level of the entire Group. In addition, appropriate restatements of previous period accounting categories provided comparability of financial statements between periods. Changes to accounting policies do not have any material effects on the past fiscal year from the aspect of performance or the value of Group assets.

In transition to the valuation of inventories according to the net-net pricing system, all rebates and other discounts that were previously reported for the entire period are now reported in current purchasing transactions, which results in a lower value of inventory. At the same time, the value of rebates and other discounts is reported as a decrease in the cost of goods sold rather than being reported in revenue. Furthermore, Mercator Group companies in Slovenia changed, due to gradual implementation of standardized IT systems in retail and warehouse units, which started during 2011 and which will presumably be completed by the end of 2012, the way of calculating and reporting the cost of goods sold from calculation method to the actual method. This has a one-off effect on the same accounting categories as the implementation of the net-net pricing system. Therefore, both changes were made at the same time; because of these changes, restatements were made in the previous financial statements pursuant to IAS 8.22. Detailed explanations regarding the restatements can be found in explanations to non-audited financial statements, pertaining to particular accounting categories. The plan for 2012 was also restated to reflect the changes in the accounting policies.

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS OF THE MERCATOR GROUP

Poslovni sistem Mercator, d.d. (hereinafter referred to as Mercator, d.d.), is a company headquartered in Slovenia. The address of its registered head office is Ljubljana, Dunajska cesta 107. Condensed consolidated financial statements for the period 1-3 2012 comprise the company Mercator, d.d., and its subsidiaries, as follows:

- **in Slovenia:** Intersport ISI, d.o.o., Modiana, d.o.o., M - Tehnika, d.d., Mercator - Emba, d.d., Mercator - Optima, d.o.o., Mercator IP, d.o.o., M.COM, d.o.o., M - nepremičnine, d.o.o., M - Energija, d.o.o., Argentum - A, d.o.o., Argentum - B, d.o.o., Argentum - C, d.o.o., Argentum - D, d.o.o., Argentum - E, d.o.o., Argentum - F, d.o.o., Argentum - G, d.o.o., Argentum - H, d.o.o., and Argentum - I, d.o.o.;

- **abroad:** Mercator - H, d.o.o., Croatia, Intersport - H, d.o.o., Croatia, Modiana, d.o.o., Croatia, Mercator centar tehnike, d.o.o., za trgovinu i usluge, Croatia, Mercator - S, d.o.o., Serbia, Intersport S - ISI, d.o.o., Serbia, Modiana, d.o.o., Serbia, Mercator - BH, d.o.o., Bosnia and Herzegovina, M - BL, d.o.o., Bosnia and Herzegovina, Intersport - BH, d.o.o., Bosnia and Herzegovina, Modiana, d.o.o., Bosnia and Herzegovina, Mercator - CG, d.o.o., Montenegro, Mercator - K, l.l.c., Republic of Kosovo, Mercator Makedonija, d.o.o.e.l., Macedonia, Investment Internacional, d.o.o.e.l., Macedonia, Mercator - B, e.o.o.d., Bulgaria and Mercator - A, sh.p.k., Albania;

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

Condensed consolidated statement of financial position

EUR thousand	31/3/2012	31/12/2011 restated	31/3/2011 restated	1/1/2011 restated
ASSETS				
Non-current assets				
Property, plant and equipment	1,883,854	1,906,018	1,907,733	1,870,428
Investment property	3,551	3,450	3,835	3,894
Intangible assets	44,906	47,623	51,411	52,626
Deferred tax assets	9,838	9,837	8,804	8,700
Loans and deposits	62,676	65,823	68,292	77,113
Available-for-sale financial assets	2,621	2,628	3,959	3,959
	2,007,446	**2,035,379**	**2,044,034**	**2,016,720**
Current assets				
Inventories	288,246	309,585	298,208	297,194
Trade and other receivables	262,758	243,402	269,812	231,871
Current tax assets	6,762	3,934	0	0
Loans and deposits	1,588	2,001	2,369	17,346
Derivative financial instruments	69	158	58	70
Cash and cash equivalents	21,517	27,540	12,920	20,766
	580,940	**586,620**	**583,367**	**567,247**
Total assets	**2,588,386**	**2,621,999**	**2,627,401**	**2,583,967**
EQUITY				
Share capital	157,129	157,129	157,129	157,129
Share premium	198,872	198,872	198,872	198,872
Treasury shares	(3,235)	(3,235)	(3,235)	(3,235)
Revenue reserves	260,104	260,104	245,307	245,307
Fair value reserve	191,431	192,209	201,123	200,187
Retained earnings	(3,867)	10,294	37,067	6,671
Profit for the period	723	7,983	10,183	30,396
Currency translation reserve	(74,188)	(60,275)	(54,338)	(62,295)
Total equity attributable to owners of the parent company	**726,969**	**763,081**	**792,108**	**773,032**
Non-controlling interest	**218**	**224**	**241**	**246**
Total equity	**727,187**	**763,305**	**792,349**	**773,278**
LIABILITIES				
Non-current liabilities				
Trade and other payables	3,900	2,369	2,512	2,447
Financial liabilities	769,697	822,145	799,335	674,375
Deferred tax liabilities	50,061	49,830	51,373	51,269
Provisions	30,123	32,711	36,041	35,709
	853,781	**907,055**	**889,261**	**763,800**
Current liabilities				
Trade and other payables	590,231	583,982	568,670	642,666
Current tax liabilities	2,242	507	3,543	5,892
Financial liabilities	409,872	362,588	372,047	395,853
Derivative financial instruments	5,073	4,562	1,531	2,478
	1,007,418	**951,639**	**945,791**	**1,046,889**
Total liabilities	**1,861,199**	**1,858,694**	**1,835,052**	**1,810,689**
Total equity and liabilities	**2,588,386**	**2,621,999**	**2,627,401**	**2,583,967**

Condensed consolidated income statement

EUR thousand	1-3 2012	1-3 2011 restated
Revenue	676,101	652,341
Cost of sales	(638,710)	(609,021)
Gross profit	**37,391**	**43,320**
Administrative expenses	(24,378)	(24,561)
Other income	6,490	6,446
Results from operating activities	**19,503**	**25,205**
Finance income	1,571	1,343
Finance expenses	(17,919)	(13,224)
Net finance expenses	**(16,348)**	**(11,881)**
Profit before income tax	**3,155**	**13,324**
Tax	(2,439)	(3,145)
Profit for the period	**716**	**10,179**
Profit for the period, attributable to:		
Owners of the parent company	723	10,183
Non-controlling interest	(7)	(4)

Condensed consolidated statement of comprehensive income

EUR thousand	1-3 2012	1-3 2011
Profit for the period	**716**	**10,179**
Other comprehensive income		
Foreign currency translation differences – foreign operations	(13,912)	7,956
Changes in fair value of cash flow hedges	(600)	936
Deferred tax	17	-
Other comprehensive income for the period	**(14,495)**	**8,892**
Total comprehensive income for the period	**(13,779)**	**19,071**
Total comprehensive income for the period, attributable to:		
Owners of the parent company	(13,773)	19,076
Non-controlling interest	(6)	(5)

Condensed consolidated statement of changes in equity

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interest	Total equity
Balance at January 1, 2011,	**157,129**	**198,872**	**(3,235)**	**270,194**	**200,187**	**6,671**	**30,396**	**(62,295)**	**797,919**	**246**	**798,165**
Effects due to changes in accounting policy	-	-	-	(24,887)	-	-	-	-	**(24,887)**	-	**(24,887)**
Balance at January 1, 2011 (restated)	**157,129**	**198,872**	**(3,235)**	**245,307**	**200,187**	**6,671**	**30,396**	**(62,295)**	**773,032**	**246**	**773,278**
Total comprehensive income for the period											
Profit for the period	-	-	-	-	-	-	10,183	-	10,183	(4)	10,179
Other comprehensive income	-	-	-	-	936	-	-	7,957	8,893	(1)	8,892
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**936**	**-**	**10,183**	**7,957**	**19,076**	**(5)**	**19,071**
Transfer of profit for the period to retained earnings	-	-	-	-	-	30,396	(30,396)	-	-	-	-
Balance at March 31, 2011 (restated)	**157,129**	**198,872**	**(3,235)**	**245,307**	**201,123**	**37,067**	**10,183**	**(54,338)**	**792,108**	**241**	**792,349**

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interest	Total equity
Balance at January 1, 2012 (restated)	**157,129**	**198,872**	**(3,235)**	**260,104**	**192,209**	**10,294**	**7,983**	**(60,275)**	**763,081**	**224**	**763,305**
Total comprehensive income for the period											
Profit for the period	-	-	-	-	-	-	723	-	723	(7)	716
Other comprehensive income	-	-	-	-	(778)	195	-	(13,913)	(14,496)	1	(14,495)
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**(778)**	**195**	**723**	**(13,913)**	**(13,773)**	**(6)**	**(13,779)**
Transactions with owners of the parent company directly recognised in equity											
Dividends to equity holders	-	-	-	-	-	(22,339)	-	-	(22,339)	-	(22,339)
Transfer of profit for the period to retained earnings	-	-	-	-	-	7,983	(7,983)	-	-	-	-
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**-**	**(14,356)**	**(7,983)**	**-**	**(22,339)**	**-**	**(22,339)**
Balance at March 31, 2012	**157,129**	**198,872**	**(3,235)**	**260,104**	**191,431**	**(3,867)**	**723**	**(74,188)**	**726,969**	**218**	**727,187**

Condensed consolidated statement of cash flows

EUR thousand	1-3 2012	1-3 2011
Cash flows from operating activities		
Gross cash flow from operating activities	**33,960**	**44,329**
Change in inventories	21,579	(1,014)
Change in trade and other receivables	(22,000)	(37,916)
Change in trade and other payables	(8,448)	(81,480)
	25,091	**(76,082)**
Interest paid	(13,705)	(12,114)
Income tax paid	(2,434)	(3,145)
Net cash from (used in) operating activities	**8,952**	**(91,342)**
Cash flows from investing activities		
Acquisition of subsidiary and business operations, net of cash acquired	(481)	-
Acquisition of property, plant and equipment and investment property	(12,579)	(46,943)
Acquisition of intangible assets	(436)	(483)
Proceeds from sale of property, plant and equipment and investment property	1,161	4,912
Proceeds from sale of intangible assets	3	-
Interest received	983	684
Loans and deposits repayments received	3,565	23,773
Net cash used in investing activities	**(7,784)**	**(18,057)**
Cash flows from financing activities		
Proceeds from (repayment of) borrowings	(6,148)	101,154
Dividends paid	(265)	-
Net cash from (used in) financing activities	**(6,413)**	**101,154**
Net (decrease) increase in cash and cash equivalents	**(5,245)**	**(8,244)**
Cash and cash equivalents as at the beginning of the period	27,540	20,766
Effect of exchange rate fluctuations on cash and cash equivalents	(778)	397
Cash and cash equivalents as at the end of the period	**21,517**	**12,920**

Notes to condensed consolidated interim financial statements

Notes to condensed consolidated income statement

Revenue
In the period 1-3 2012, Mercator Group generated EUR 676,101 thousand of revenue, which is 3.6% more relative to the period 1-3 2011 and 22.8% of planed revenue for year 2012. Majority of Group's revenue is generated by sales of goods, material and products, mostly retail and wholesale of trade goods. Revenue in Slovenia are in the same level as previous year (index 99.7); in foreign markets, the growth amounted to 9.5%.
In compliance with IAS 8, accounting policies were changed and consequently revenue were reclassified in total amount of EUR -23,174 thousand. This also reduced costs of goods sold in the period 1-3 2011.

Cost of sales
Mercator Group cost of sales which include the cost of goods sold, production costs, selling and marketing costs, and other expenses, amounted to EUR 638,710 thousand in the period 1-3 2012. This amount presents 22.8% of planned cost of sales for year 2012.
In compliance with IAS 8, accounting policies were changed and consequently cost of sales were reclassified in total amount of EUR -23,174 thousand. In the same amount revenue in the period 1-3 2011 were also reduced.

Gross profit
Gross profit for the period 1-3 2012 amounted to EUR 37,391 thousand. The share of gross profit in revenue is 5.5%. In order to maintain the purchasing power of the consumers, Mercator Group allocated significant amounts for investments in prices in the period at hand. Given the cost of sales that remained on par with the last year's figures, this resulted in a relative decrease of gross profit in the period 1-3 2012 compared to the equivalent period of the year before.

Administrative expenses
Mercator Group's administrative expenses in the period 1-3 2012 amounted to EUR 24,378 thousand, which is 23.1% of planned administrative expenses for financial year 2012.

Results from operating activities
In the period 1-3 2012, Mercator Group's results from operating activities reached EUR 19,503 thousand. The amount presents 25.5% of yearly planned item value.

Finance income and expenses

Finance income amounts to EUR 1,571 thousand. It mostly pertains to income from regular interest on financing, default interest and income from financial investments.

Finance expenses amount to EUR 17,919 thousand in the period at hand. They mostly pertain to expenses for regular interest on borrowings from commercial banks, negative foreign currency translation differences and expenses on impairment of trade and other receivables.

Profit before income tax
In the period 1-3 2012, Mercator Group's profit before income tax stood at EUR 3,155 thousand, which represents 13.1% of planned item for year 2012.

Profit for the financial period
In the period 1-3 2012, Mercator Group's profit for the financial period amounted to EUR 716 thousand.

Gross cash flow from operating activities

Mercator Group's gross cash flow from operating activities in the period 1-3 2012 amounted to EUR 33,960 thousand, which is 22.6% of planned item for year 2012.

Gross cash flow from operating activities before rental expenses

The relevant indicator of the ability to generate operating cash flow, which also accounts for the expansion of Mercator Group's retail network through operating lease, is the gross cash flow from operating activities before rental expenses which amounted to EUR 47,030 thousand in the period 1-3 2012, or 21.9% of yearly plan.

Notes to condensed consolidated statement of financial position

Assets

Mercator Group assets as at March 31, 2012 amounted to EUR 2,588,386 thousand, which is EUR 33,613 thousand less than as at the end of 2011.

As at March 31, 2012, the value of Mercator Group's non-current assets amounted to EUR 2,007,446 thousand, which is EUR 27,933 thousand less than as at December 31, 2011. The biggest share of non-current assets is represented by property, plant and equipment, accounting for 96.3% (EUR 1,932,311 thousand) of the total figure. Their value fell by EUR 24,780 thousand relative to the end of 2011. The change in value in the period 1-3 2012 is related to investments, depreciation and amortization, currency translation differences and disposal of unnecessary (non-core) and non-viable property, plant, and equipment.

As at March 31, 2012, the value of Mercator Group's current assets amounts to EUR 580,940 thousand, which is EUR 5,680 thousand less as at the end of 2011. The largest share thereof includes inventories (49.6%) and trade and other receivables (45.2%).

In compliance with changed accounting policies the Group as at January 1, 2012 lowered the value of inventory for EUR 24,887 thousand. The change in amount of EUR 18,836 thousand refers to the amount of rebates in inventory, and change in amount of EUR 6,051 thousand refers to evaluated difference due to changed calculation method of cost of goods sold. The value of rebates in inventory increased by EUR 777 thousand by the end of year 2011. Therefore, total restated value of inventories as at December 31, 2011 is EUR -25,664 thousand.

Equity and liabilities

Mercator Group's equity as at March 31, 2012 amounts to EUR 727,187 thousand, which is EUR 36,118 thousand or 4.7% less than as at the end of 2011. The decrease mostly pertains to payment of dividends and exchange differences at consolidating financial statement of foreign companies.

As at March 31, 2012, total financial liabilities amount to EUR 1,179,569 thousand, which is EUR 5,164 thousand less than as at the end of 2011. Net financial debt of the Mercator Group, calculated as the difference between financial liabilities and financial assets, amounted to EUR 1,096,171 thousand as at March 31, 2012 (March 31, 2011: EUR 1.085,315 thousand).

As at March 31, 2012, provisions amounted to EUR 30,123 thousand. Compared to the end of 2011, provisions have decreased by EUR 2,588 thousand.

Trade and other payables as at March 31, 2012 amounted to EUR 594,131 thousand, which is EUR 7,780 thousand more than at the end of 2011. The increase in trade payables is a result of year-on-year dynamics in the trade industry.

As at March 31, 2012, long-term coverage of non-current assets with non-current liabilities at the Mercator Group amounts to 78.8%, which is 3.3 percentage points less than as at the end of 2011.

The value of equity is restated, as a counterpart item of restated inventories on January 1, 2011 and at the end of 2011 in compliance with change in accounting policies and IAS 8. Revenue reserves were lowered for EUR 24,887 thousand. Net profit in 2011 was affected in amount of EUR -777 thousand due to the increase of rebates in inventory. The effect is immaterial on total profit for the year 2011 and is therefore recognized in revenue reserves. Therefore, the total restated equity value in year 2011 is EUR -25,664 thousand.

FINANCIAL REPORT OF THE COMPANY POSLOVNI SISTEM MERCATOR, D.D.

Poslovni sistem Mercator, d.d., (hereinafter referred to as Mercator, d.d.), is a company headquartered in Slovenia. The address of its registered head office is Ljubljana, Dunajska cesta 107. The company Mercator, d.d., is the parent/controlling company of a group of related companies headquartered in Slovenia, Serbia, Croatia, Bosnia and Herzegovina, Montenegro, Bulgaria, Albania, Republic of Kosovo, and Macedonia.

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

Due to the transfer of a part of operating activities to the company M-Tehnika, d.d., financial statements of the company Poslovni sistem Mercator, d.d., are not fully comparable between particular periods in terms of substance.

Condensed statement of financial position

EUR thousand	31/3/2012	31/12/2011 restated	31/3/2011 restated	1/1/2011 restated
ASSETS				
Non-current assets				
Property, plant and equipment	999,645	1,003,846	1,010,053	1,014,704
Investment property	3,415	3,450	3,835	3,894
Intangible assets	9,912	10,513	9,161	9,652
Deferred tax assets	8,657	8,657	8,217	8,216
Loans and deposits	865	870	276	286
Investment into equity of subsidiaries	633,617	636,319	620,812	618,813
Available-for-sale financial assets	2,399	2,399	3,547	3,547
	1,658,510	**1,666,054**	**1,655,903**	**1,659,112**
Current assets				
Inventories	92,087	136,003	139,155	136,429
Trade and other receivables	218,717	163,118	175,238	158,907
Current tax assets	4,847	2,167	-	5
Loans and deposits	35,663	34,575	44,243	48,848
Derivative financial instruments	69	158	58	70
Cash and cash equivalents	7,491	10,068	-	3,829
	358,874	**346,089**	**358,694**	**348,088**
Total assets	**2,017,384**	**2,012,143**	**2,014,597**	**2,007,200**
EQUITY				
Share capital	157,129	157,129	157,129	157,129
Share premium	198,872	198,872	198,872	198,872
Treasury shares	(3,235)	(3,235)	(3,235)	(3,235)
Revenue reserves	236,312	236,312	220,518	220,518
Fair value reserve	193,297	190,651	195,371	194,435
Retained earnings	6,481	13,246	40,418	3,612
Profit for the period	9,343	15,574	12,046	36,806
	798,199	**808,549**	**821,119**	**808,137**
LIABILITIES				
Non-current liabilities				
Trade and other payables	2,023	2,022	2,447	2,447
Financial liabilities	595,898	628,686	558,550	456,547
Deferred tax liabilities	39,805	39,805	40,814	40,814
Provisions	24,485	26,926	29,796	29,459
	662,211	**697,439**	**631,607**	**529,267**
Current liabilities				
Trade and other payables	292,149	306,686	300,229	341,239
Current tax liabilities	2,336	-	2,092	5,759
Financial liabilities	257,416	194,908	258,019	320,320
Derivative financial instruments	5,073	4,562	1,531	2,478
	556,974	**506,156**	**561,871**	**669,796**
Total liabilities	**1,219,185**	**1,203,595**	**1,193,478**	**1,199,063**
Total equity and liabilities	**2,017,384**	**2,012,143**	**2,014,597**	**2,007,200**

Condensed income statement

EUR thousand	1-3 2012	1-3 2011 restated
Revenue	369,306	371,769
Cost of sales	(337,345)	(339,027)
Gross profit	**31,961**	**32,742**
Administrative expenses	(14,144)	(13,262)
Other income	4,258	3,750
Results from operating activities	**22,075**	**23,230**
Finance income	1,341	1,708
Finance expenses	(11,737)	(9,881)
Net finance expenses	**(10,396)**	**(8,173)**
Profit before income tax	**11,679**	**15,057**
Tax	(2,336)	(3,011)
Profit for the period	**9,343**	**12,046**

Condensed statement of comprehensive income

EUR thousand	1-3 2012	1-3 2011
Profit for the period	**9,343**	12,046
Other comprehensive income		
Changes in fair value of cash flow hedges	(600)	936
Disposal of an investment in a subsidiary	3,246	-
Other comprehensive income for the period	**2,646**	**936**
Total comprehensive income for the period	**11,989**	**12,982**

Condensed statement of changes in equity

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Total equity
Balance at January 1, 2011	**157,129**	**198,872**	**(3,235)**	**238,015**	**194,435**	**3,612**	**36,806**	**825,634**
Effect due to change in accounting policies				(17,497)				**(17,497)**
Balance at January 1, 2011 (restated)	**157,129**	**198,872**	**(3,235)**	**220,518**	**194,435**	**3,612**	**36,806**	**808,137**
Total comprehensive income for the period								
Profit for the period	-	-	-	-	-	-	12,046	12,046
Other comprehensive income	-	-	-	-	936	-	-	936
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**936**	**-**	**12,046**	**12,982**
Transfer of profit for the period to retained earnings	-	-	-	-	-	36,806	(36,806)	-
Balance at March 31, 2011 (restated)	**157,129**	**198,872**	**(3,235)**	**220,518**	**195,371**	**40,418**	**12,046**	**821,119**

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit for the period	Total equity
Balance at January 1, 2012 (restated)	**157,129**	**198,872**	**(3,235)**	**236,312**	**190,650**	**13,246**	**15,574**	**808,548**
Total comprehensive income for the period								
Profit for the period	-	-	-	-	-	-	9,343	9,343
Other comprehensive income	-	-	-	-	2,646	-	-	2,646
Total comprehensive income for the period	**-**	**-**	**-**	**-**	**2,646**	**-**	**9,343**	**11,989**
Transactions with owners directly recognised in equity								
Dividends to equity holders	-	-	-	-	-	(22,339)	-	(22,339)
Transfer of profit for the period to retained earnings	-	-	-	-	-	15,574	(15,574)	-
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**-**	**(6,765)**	**(15,574)**	**(22,339)**
Balance at March 31, 2012	**157,129**	**198,872**	**(3,235)**	**236,312**	**193,296**	**6,481**	**9,343**	**798,199**

Condensed statement of cash flows

EUR thousand	1-3 2012	1-3 2011
Cash flows from operating activities		
Gross cash flow from operating activities	**28,220**	**33,662**
Change in inventories	43,916	(2,726)
Change in trade and other receivables	(44,384)	(16,332)
Change in trade and other payables	(39,762)	(39,833)
Interest paid	(9,738)	(9,820)
Income tax paid	(2,336)	(3,011)
Net cash from operating activities	**(24,084)**	**(38,060)**
Cash flows from investing activities		
Acquisition of subsidiaries (capital increase)	(14,481)	(7,000)
Acquisition of property, plant and equipment and investment property	(6,519)	(7,091)
Acquisition of intangible assets	(336)	(406)
Loans and deposits made	(1,082)	-
Proceeds from sale of subsidiary	11,282	-
Proceeds from sale of property, plant and equipment and investment property	2,156	3,205
Proceeds from sale of intangible assets	4	-
Interest received	1,027	1,214
Dividends received	-	-
Deposits repayments received	-	4,616
Net cash used in investing activities	**(7,949)**	**(5,462)**
Cash flows from financing activities		
Proceeds from (repayment of) borrowings	29,721	39,702
Dividends paid	(265)	(9)
Net cash from financing activities	29,457	**39,693**
Net increase (decrease) in cash and cash equivalents	**(2,576)**	**(3,829)**
Cash and cash equivalents as at the beginning of the period	10,068	3,829
Cash and cash equivalents as at the end of the period	**7,491**	**-**

Notes to condensed interim financial statements

Notes to condensed income statement

Revenue
In the period 1-3 2012, company Poslovni sistem Mercator, d.d., generated EUR 369.306 thousand of revenue. Majority of company revenue is generated by sales of goods, material and products, mostly retail and wholesale of trade goods.

In compliance with IAS 8, accounting policies were changed and consequently revenue were reclassified in total amount of EUR -8.335 thousand. This reduced cost of goods sold in the period 1-3 2011.

Cost of sales
Cost of sales at the company, which include the cost of goods sold, production costs, selling and marketing costs, and other expenses, amounted to EUR 337,345 thousand in the period 1-3 2012.

In compliance with IAS 8, accounting policies were changed and consequently cost of sales were reclassified in total amount of EUR -8.335 thousand. In the same amount revenue in the period 1-3 2011 were also reduced.

Gross profit

Gross profit for the period 1-3 2012 amounted to EUR 31,961 thousand. The share of gross profit in revenue is 8.7%.

Administrative expenses
Administrative expenses at the company in the period 1-3 2012 amounted to EUR 14,144 thousand.

Results from operating activities
In the period 1-3 2012, company result from operating activities amounted to EUR 22,075 thousand.

Finance income and expenses

Finance income amounts to EUR 1,341 thousand. It mostly pertains to income from regular interest on financing, default payment and income from financial investments.

Finance expenses for the relevant period amount to EUR 11,737 thousand, of which a major portion relates to expenses for regular interest on borrowings from commercial banks and expenses on impairment of trade and other receivables.

Profit before income tax and profit for the financial period

In the period 1-3 2012, profit before income tax of the company amounted to EUR 11,679 thousand, while profit for the financial period amounted to EUR 9,343 thousand.

Notes to condensed statement of financial position

Assets
Company’s assets as at March 31, 2012 amounted to EUR 2,017,384 thousand, which is EUR 5,241 thousand more than at the end of 2011.

As at March 31, 2012, the value of company's non-current assets amounted to EUR 1,658,510 thousand, which is EUR 7,544 thousand less than as at December 31, 2011. The biggest share of non-current assets is represented by property, plant and equipment, accounting for 61.1% (EUR 1,012,972 thousand) of the total figure. Their value dropped by EUR 4,837 thousand relative to the end of 2011. The change in value in the period 1-3 2012 is related to investments, depreciation and amortization, and disposal of unnecessary and non-viable property, plant, and equipment.

As at March 31, 2012, the value of company's current assets amounted to EUR 358,874 thousand, which is EUR 12,785 thousand more than as at the end of 2011. The largest share thereof includes inventories (25.7%) and trade and other receivables (60.9%).

In compliance with changed accounting policies the company Mercator, d.d., as at January 1, 2012 lowered the value of inventory for EUR 17,497 thousand. The change in amount of EUR 11,446 thousand refers to the amount of rebates in inventory, and change in amount of EUR 6,051 thousand refers to evaluated difference due to changed calculation method of costs of goods sold. The value of rebates in inventory decreased by EUR 220 thousand by the end of year 2011. Therefore, total restated value of inventories as at December 31, 2011 is EUR -17,277 thousand.

Equity and liabilities
As at March 31, 2012, company's equity amounted to EUR 798,199 thousand.
As at March 31, 2012, total financial liabilities amounted to EUR 853,314 thousand, which is EUR 29,720 thousand more than as at the end of 2011.
As at March 31, 2012, provisions amounted to EUR 24,485 thousand. Compared to the end of 2011, provisions have decreased by EUR 2,441 thousand.
Trade and other payables as at March 31, 2012 amounted to EUR 294,172 thousand, which is EUR 14,536 thousand less than at the end of 2011. The decrease in trade payables is a result of year-on-year dynamics in the trade industry.

The value of equity is restated, as a counterpart item of restated inventories on January 1, 2011 and at the end of 2011 in compliance with change in accounting policies and IAS 8. Revenue reserves were lowered for EUR 17,497 thousands. Net profit in 2011 was affected in amount of EUR 220 thousand due to the increase of rebates in inventory. The effect is immaterial on total profit for the year 2011 and is therefore recognized in revenue reserves. Therefore, the total restated equity value in year 2011 is EUR -17,277 thousand.

Related party transactions

There are two groups of related parties at the company Poslovni sistem Mercator, d.d.: managerial personnel and subsidiaries. Managerial personnel includes members of Management Boards, Supervisory Boards, and employees with individual employment contracts working at Mercator Group companies.

Transactions between the company Poslovni sistem Mercator, d.d., and its subsidiaries within the Mercator Group, taking place as a part of various forms of business and financial activity, are always effected according to the arm's length principle. Managerial personnel receives compensation and reward in compliance with their respective employment contracts or consistently with the Shareholder Assembly resolutions (Supervisory Board members).

MANAGEMENT BOARD STATEMENT PURSUANT TO ARTICLE 113 OF THE MARKET IN FINANCIAL INSTRUMENTS ACT

The Management Board hereby confirms that to their best knowledge, the summary of the financial report of the company Poslovni sistem Mercator, d.d., and the Mercator Group is compiled in compliance with the appropriate framework of financial reporting and that it presents a true and fair account of assets and liabilities, financial position, and the income of the company Poslovni sistem Mercator, d.d., and other companies included in the consolidated statements. The business report includes a fair account of information on relevant transactions with related parties, and it is compiled in compliance with the relevant accounting standards.

Poslovni sistem Mercator, d.d.
Management Board

Ljubljana, May 15, 2012