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BRIEF OVERVIEW OF THE GROUP

AS Merko Ehitus, a company founded in 1990, currently operates as a holding company. Group companies in Estonia, Latvia and Lithuania offer complete solutions in the field of construction and real estate development. In the construction sector, the group's largest companies are AS Merko Ehitus Eesti (100%), SIA Merks (100%), UAB Merko Statyba (100%) and the companies belonging to the AS Merko Ehitus Eesti group: Tallinna Teede AS (100%) and AS Merko Infra (100%).

The main activity of the holding company is development and implementation of the strategies of Merko Ehitus group's separate business areas primarily through long-term planning of resources.

Merko Ehitus Eesti group is the market leader of the Estonian construction sector with about 7% of the total volume of the Estonian construction market.

In Latvia and Lithuania, Merko Ehitus operates through its subsidiaries SIA Merks and UAB Merko Statyba, focusing selectively on projects where the competitive advantage is perceivable as compared to other market players.

Merko Ehitus has the highest owners' equity in the Estonian construction sector and is able to finance projects by itself. Our objective is to maintain liquidity. We have been conservative in involving debt capital. We observe that we would have sufficient necessary resources to continuously invest in attractive projects.

The shares of Merko are listed on Tallinn Stock Exchange since 1997. As at the year-end 2012, the Group employed more than 900 people.

Long-term experience in different markets, a wide scope of construction services, flexibility, reliability and meeting of deadlines and primarily quality have helped Merko Ehitus to achieve and maintain the position of the market leader in the Baltics. Depending on the expectations of contracting entities, the group companies perform both small-scale construction works as well as large scale, complicated and innovative projects, with a focus on general contracting and project management.

International quality, environmental protection and occupational safety certificates ISO 9001, ISO 14001 and OHSAS 18001 have been assigned to the group's larger construction companies.

VISION

Our vision is the reliable solutions and quality performance for your ideas.

VALUES

RESPONSIBILITY

We decide based on business thinking/awareness and ethical beliefs. We offer continuous and environment-friendly solutions.

KEEPING PROMISES

We give realistic promises to the shareholders, contracting entities cooperation partners, employees and we keep our promises. Good solutions are born in cooperation, the keeping of one's promises is mutual.

COMPETENCE

We value quality and professionalism. We constantly develop our professional knowledge and skills.

INITIATIVE

We manage processes and we are result-oriented. We accept the challenges which presume more.

CREATIVITY

We are open, innovative and creative in working out and implementing the solutions. We are willing to carry out our thoughts.

STRATEGY

The business strategy of AS Merko Ehitus subsidiaries focuses on improving profitability and enhancing the efficiency of the cost base, offering general contracting services in the field of construction of buildings and infrastructure facilities and developing residential real estate in its home markets Estonia, Latvia and Lithuania. The group's objective is to remain the leader in the Baltic construction market. Considering weak growth prospects of the construction market, finding new growth opportunities is part of the business strategy.

LONG-TERM FINANCIAL OBJECTIVES UNTIL 2018

At the meeting held on 8 April 2013, the Management Board and the Supervisory Board of AS Merko Ehitus reviewed the company's strategic development directions and approved long-term financial objectives until 2018.

Considering the weak growth perspective of the Baltic construction and real estate market in the coming few years, the overall low interest environment and the company's high equity base, the strategy and the financial objectives are focussed on improving the return on invested capital and increasing the efficiency of the balance structure.

The objectives are based on the following assumptions concerning the external environment:

- The Baltic construction market will not experience considerable growth in the coming two years;
- The share of public procurements in construction contracts will remain high, but their volume will temporarily decrease as of the second half of 2013 due to the end of the current EU funding period. On the whole, the financial resources allocated to economy will remain at the same level in the new EU funding period (2014-2020), but the structure thereof will change. The activity of private clients in developing and launching larger construction projects will recover slowly.
- The number of service providers in the construction sector exceeds the demand and there is still a surplus capacity of property, plant and equipment. The tightening competition in the construction market puts increasing pressure on the profit margins of construction companies.
- The Baltic apartment market will continue to see a moderate growth in transaction activity and prices, particularly in capital cities.

The long-term financial objectives of AS Merko Ehitus cover the period until 2018 and will be reviewed annually based on the market situation, the company's financial standing and strategy:

- The minimum period average return on equity (ROE): 10%
- Dividend pay-out ratio: 50-70% of the annual profit
- Equity ratio: at least 40%

STATEMENT OF THE CHAIRMAN OF THE MANAGEMENT BOARD

Dear shareholders

The previous financial year of Merko Ehitus can be considered successful. After three consecutive years of declining profits and a loss incurred in 2011, we completed the previous year with the largest net profit in the last four years. Revenue of group companies increased by 13.6% and we also significantly improved the company's financial position.

Generally, 2012 can be considered the post-crisis year of recovery in the Baltic construction and real estate market. Volumes of construction works in the sector grew significantly and in the real estate market saw an increase both in the transaction activity and the overall price level. The situation in the construction sector is still dominated by public sector orders that will remain a significant development engine of the construction market also in the next few years. In terms of the development of the construction sector, the key will be the volume of construction works in the framework of the next EU budgeting period (2014-2020) that are hopefully clarified within 2013. The activity of private contracting entities and developers was also positive news last year although the number of real estate projects that were launched in reality still remained modest.

The construction sector was last year characterised by extremely tough competition, in particular in the segment of buildings where price offers are becoming ever more aggressive. It is extremely important that the focus of customers on cheaper prices at the end of the year will not lead to a decline in the building quality, weakening of occupational safety and tax evasion. I hope that professionalism and cooperation aimed at a better end-result at all levels of the construction sector will lead to an improvement.

At the start of 2012 we adopted a new holding structure and during the year carried out several changes in the group's management with the aim of enhancing efficiency,

improving the quality of management information and focusing on the most important aspects with regard to the group's operating result. The results have improved largely thanks to the constant efforts of dedicated managers and employees of our subsidiaries and in-depth knowledge of their work and business segment. I am proud to say that the planners, engineers, project managers and site teams of our construction companies continue to be among the best in the construction market.

Last year we successfully delivered to customers a number of structures in the field of building construction, water management, electrical construction and road construction. We remain among the leading apartment developers in the Baltic States. Our objective is to maintain the leading position in the construction market also in the future.

Assessing the prospects of the next few years in the Baltic construction and real estate market, we are fully aware that the company's development cannot only rely on general economic growth. It is our responsibility to tirelessly seek opportunities for improving operating results and to find sources for new growth. This is how we can create value for our customers, offering development opportunities to our employees and preserving the attractiveness for shareholders. We are working at achieving these targets every day.



Sincerely
Andres Trink
Chairman of the Management Board
AS Merko Ehitus



AS MERKO EHITUS GROUP

CONSOLIDATED ANNUAL REPORT

Translation of the Estonian original
Beginning of financial year: 01.01.2012
End of financial year: 31.12.2012

Business name:	AS Merko Ehitus
Main activity:	general contracting of construction
Commercial Register no.:	11520257
Address:	Järvevana tee 9G, 11314 Tallinn
Postal address:	Pärnu mnt. 141, 11314 Tallinn
Phone:	+372 650 1250
Fax:	+372 650 1251
E-mail:	merko@merko.ee
Web site:	www.merko.ee
Auditor:	AS PricewaterhouseCoopers

Supervisory Board:	Toomas Annus, Tõnu Toomik, Teet Roopalu, Indrek Neivelt, Olari Taal
Management Board:	Andres Trink, Viktor Mõisja

MANAGEMENT REPORT

Brief overview of 2012

Profitability has improved: net profit in 2012 was EUR 7.63 million (2011: net loss was EUR 14.08 million).

Revenue is up: group revenue increased mainly on account of growth in engineering projects in Estonia and revenue of apartment developments in all three Baltic States.

Strong cash position: by the end of the reporting period, the group had EUR 35.32 million in cash and cash equivalents.

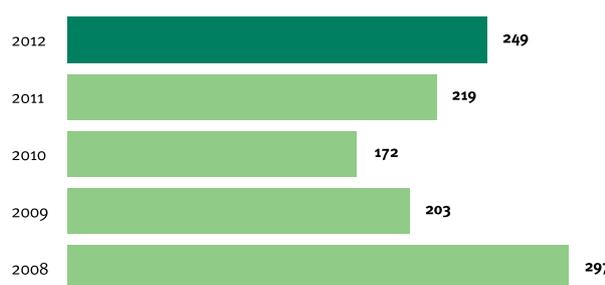
Secured order book is stable: as at 31 December 2012 totalled EUR 190 million (31 December 2011: EUR 166 million).

Changes in business activities: liquidation of operations in Ukraine, creating a legal platform in Finland and Russia. Sale of shares of AS TMB and, in connection with the review of the Lithuanian business strategy, to end implementation of water management projects in Lithuania.

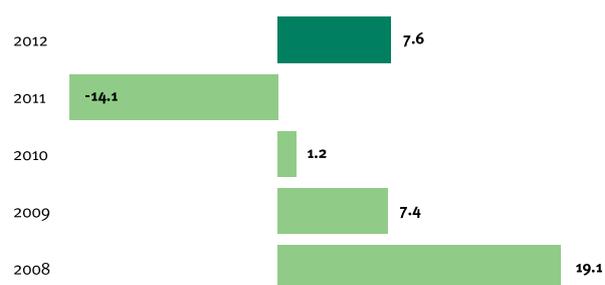
		2012	2011
Revenue	million EUR	249.1	219.3
Gross profit	million EUR	17.9	-3.6
Gross profit margin	%	7.2	-1.6
Net profit (equity holders of the parent)	million EUR	7.6	-14.1
Net profit margin	%	3.1	-6.4
EPS	EUR	0.43	-0.80
Dividends per share	EUR	0.30*	0.00
As of year-end:			
ROE	%	6.8	-12.2
Equity ratio	%	52.0	49.6
Secured order book	million EUR	190	166
Total assets	million EUR	225	220
Number of employees	people	915	917

* according to proposal of the Management Board

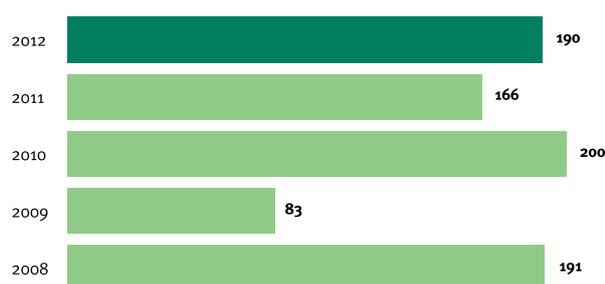
Revenue
in million euros



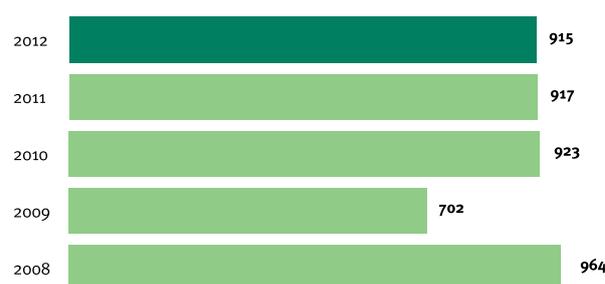
Net profit
in million euros



Secured order book
in million euros



Number of employees, at year-end



The main factors influenced the construction market in 2012

The most important indicators influencing the construction market

	Estonia	Latvia	Lithuania
GDP change, y-o-y, in current prices	+3.2%	+5.6%	+3.6%
Construction price index change, y-o-y, in current prices	+4.6%	+6.8%	+3.7%
Labour force	+6.3%	+15.8%	+4.2%
Building machines	+7.2%	+12.2%	+2.9%
Building materials	+3.7%	+0.7%	+3.6%

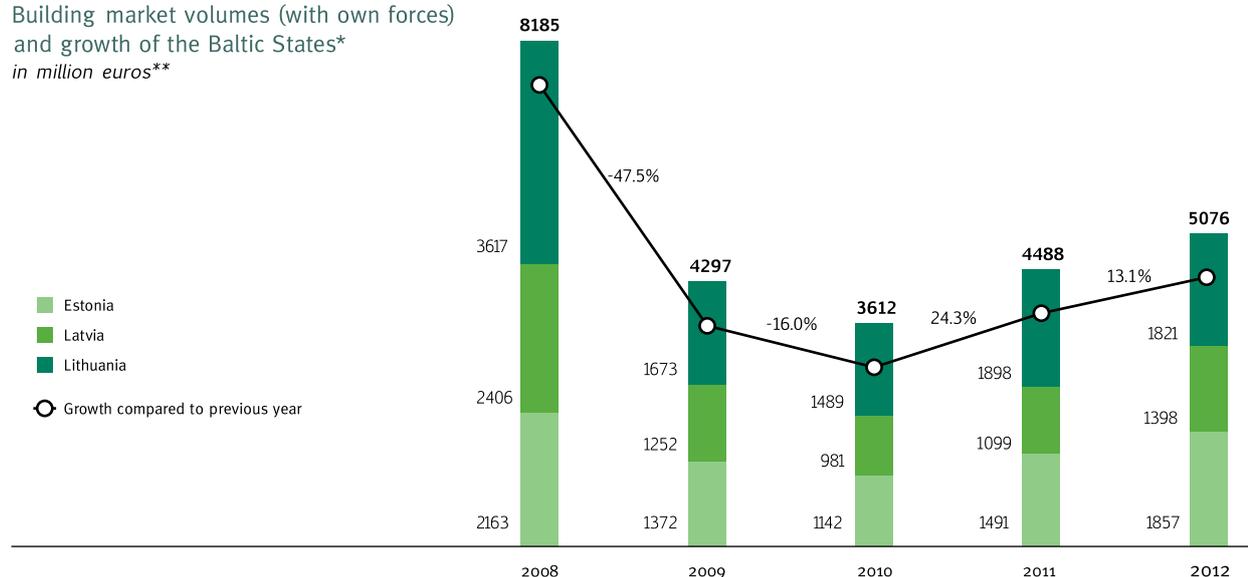
The stabilisation of the economic environment in the Baltic States over the last couple of years has given a positive impetus for the growth in the construction sector as compared to the pre-crisis years.

The volumes of construction works increased in all three Baltic States, but are still considerably lower as compared to the boom years of 2007 and 2008. In 2012, construction works with own resources were performed in the Baltic region for EUR 5,076 million which is EUR 588 million higher than in 2011. Due to the low reference base following the economic recession in 2010, the Baltic construction market increased by 24.3% in current prices in 2011 and by 13.1% in 2012. The reason for the slightly more modest growth as compared to 2011 was attributable to the 4% contraction of the Lithuanian construction market in current prices while the Estonian construction market increased by 24.5% and the Latvian construction market increased by 27.2%. While construction works in current prices were performed for EUR 1,398 million in Latvia, they were performed for EUR 1,821 million in Lithuania and EUR 1,857 million in Estonia. The Estonian construction market makes up the largest share of the Baltic construction market with 36.6%, followed by Lithuania with 35.9% and despite more than a 25% increase in the Latvian construction market, the Latvian market still makes up the smallest share of the Baltic construction market, i.e. 27.5%.

In a year, the volume of works completed by Estonian companies in foreign countries increased by 18.5%, Lithuanian exports increased by 34.6% and Latvian exports decreased by 7.3%. While year-over-year, the construction market has been growing, quarterly comparison within a year shows that construction volumes have been declining in all Baltic States, a trend deteriorated by the end of the current European Union financing framework and overall decline in number of public procurements.

In 2012, construction works per capita were performed for EUR 1,414 in Estonia, EUR 684 in Latvia and EUR 608 in Lithuania.

Building market volumes (with own forces) and growth of the Baltic States* in million euros**



* Based on the data of local statistical offices.

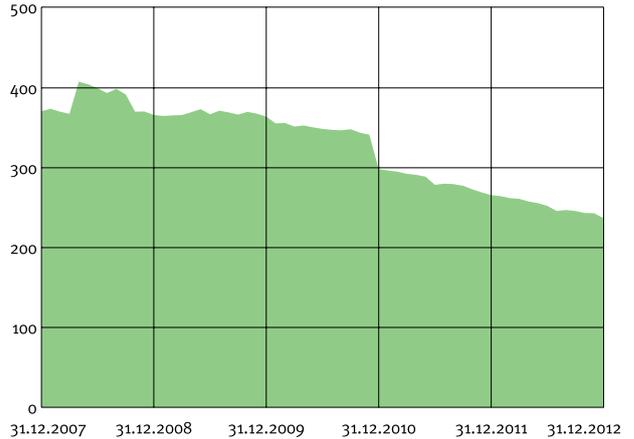
** According to the exchange rates of European Central Bank and Eesti Pank.

Activity in the real estate market continues to grow moderately, mainly due to low base interest rates and limited supply in the apartment market over the last three years. There are now more transactions as compared to the recession in the real estate market in 2009. However, in comparison with the peak in 2006, the volume of transactions is still approximately 40% lower. The banks are still not ready to finance residential development projects of smaller developers which gives a competitive advantage for group in launching the new apartments to the market.

Moderately positive developments in the Baltic real estate market assure that Merko Ehitus made the right decisions in initiating new apartment developments in Tallinn, Riga and Vilnius.

Stock of loans granted to housing development projects in Estonia

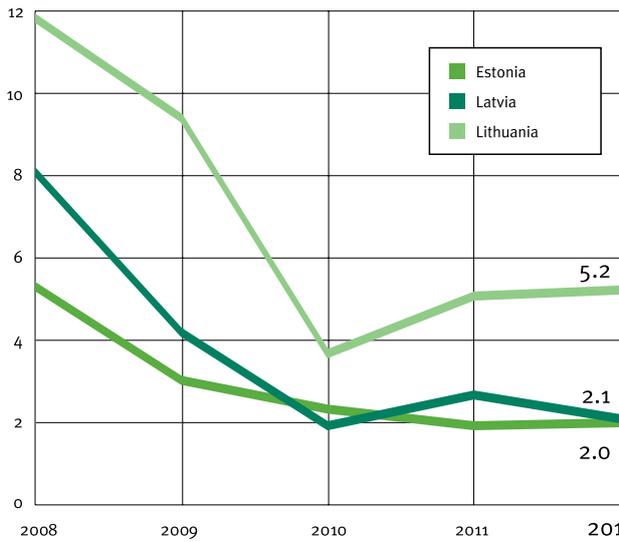
in million euros



Source: Eesti Pank

The number of authorisations for use issued for new residential premises

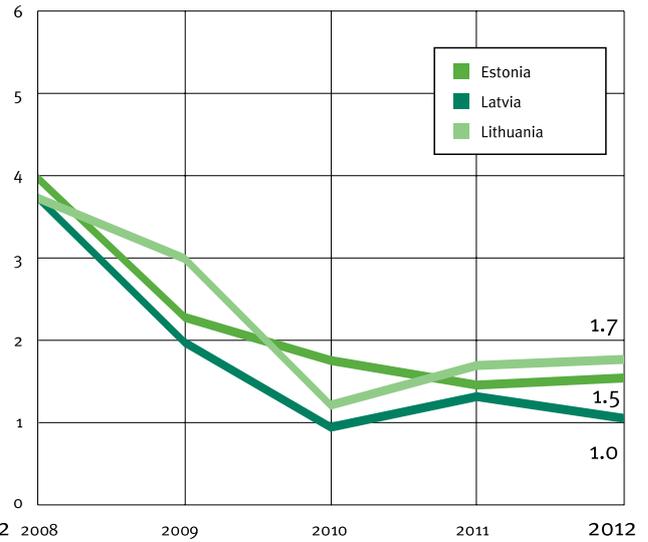
thousand pcs



Source: Statistic Departments

The number of authorisations for use issued for new residential premises

per thousand person, pcs



Despite of consumers remaining price-sensitive, demand for quality residential premises in good locations remains high in all three Baltic countries.

Outlook for 2013

In 2013, the economies of the three Baltic countries are forecast to grow 3-4%. The worsening economic confidence indices in Sweden and Finland are reflecting weaker economic growth prospects, and the Scandinavian construction market is expected to post no growth next year. Euro base rates remain low, although we continue to believe that there are still inflationary risks in the longer term. The outlook of the Russian economic is mainly related to the oil price. Russia's economic growth is expected to exceed that of the Eurozone, but at a higher inflation rate. The real estate market in Russia's larger cities is supported by relatively strong domestic demand and the growing middle class. The Latvian economy and investments are likely to get a boost from the country's planned transition to the euro in 2014. Also Lithuania's prospects in joining the Eurozone have become more realistic.

We expect construction volumes in the Baltic States to decline by 5-10%, which is primarily related to the expected decrease in the volume of public procurement tenders resulting from the expiry of EU's current budgeting period. The activity of private customers in launching new projects in the segment of trade, logistics and other commercial premises that started in 2012 will continue, although the total number of projects is likely to remain modest.

We believe that in 2013 competition on the Baltic construction market will remain tough and bidding for construction tenders will be aggressive. Because customers remain focused on the lowest construction cost, it is still difficult to stand out in the competition with other general contractors. No new significant competitors are expected to arrive in the construction market. On the contrary, one expects the market to consolidate further, mainly through phased downsizing or liquidation of business by several construction companies.

The improvement in the profitability of larger construction companies that started in 2012 is likely to slow down in 2013. The average profitability of construction companies is expected to remain at last year's level or, as a result of price competition, decline. This will provide a competitive edge in the market to construction companies that are efficient and have flexible cost base.

A large share of public procurement tenders in construction orders means that the working capital of construction companies remain under pressure, although the situation has somewhat improved in a year. Taking into consideration the weak growth outlook of the construction sector, the wage pressure is likely to remain modest. Moreover, we are not expecting input prices in construction to change significantly in the upcoming year.

Because the road construction sector suffers from excess capacity of fixed assets, profitability requires reduction of machinery and the efficiency of the cost basis. In road maintenance, several long-term maintenance tenders will be carried out in 2013, which may result in certain re-distribution of market shares. As for the investments into the road segment, we expect to see fewer large-scale rebuilding projects of traffic junctions and road sections because limited financial resources mean that contracting authorities will focus on smaller road building and road repair tenders.

In the field of electrical construction, investments and orders for modernisation and development of main and distribution grids are ongoing in all three Baltic countries and the market is very competitive as there is a limited number of companies.

In the market of residential premises, the supply of new apartments will increase due to the growth in the number of development projects that were either launched in 2012 or will be launched this year. In 2013, the apartment market will remain moderately active, with the number of transactions and average price per square meter are both expected to grow, supported by low base interest rates. In the market of residential premises, development projects that offer better energy efficiency, sound insulation and higher quality of living environment will have an advantage. In the Latvian apartment market, the share of foreign investors who invest with the objective of acquiring a residence permit for the European Union remains prominent in the market of new apartments. On the Lithuanian apartment market, the sale of apartments as a so-called "grey box" remains a dominant feature.

As the largest general contractor, Merko Ehitus Eesti, subsidiary of Merko Ehitus, is well positioned in the Estonian construction market and is capable of competing in all activity segments. In Latvia, SIA Merks, a subsidiary of Merko Ehitus, belongs to among 5-6 leading general contractors and we believe that we can maintain our position. In Lithuania, the construction activity of the subsidiary of Merko Ehitus is focused primarily on the general construction segment (buildings, structures) where competition remains very tough in the field of public procurements. In the Lithuanian market, the position of general contractors is continuously dominated by the activities of advisers that represent contracting authorities and reduce the possibilities of general contractors to win construction orders. In both Latvia and Lithuania, foreign companies still face major challenges in successfully participating in public procurement tenders.

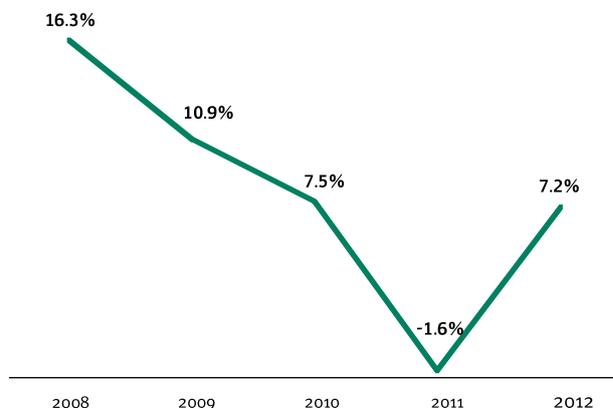
Operating results

Revenue

Group revenue
in million euros

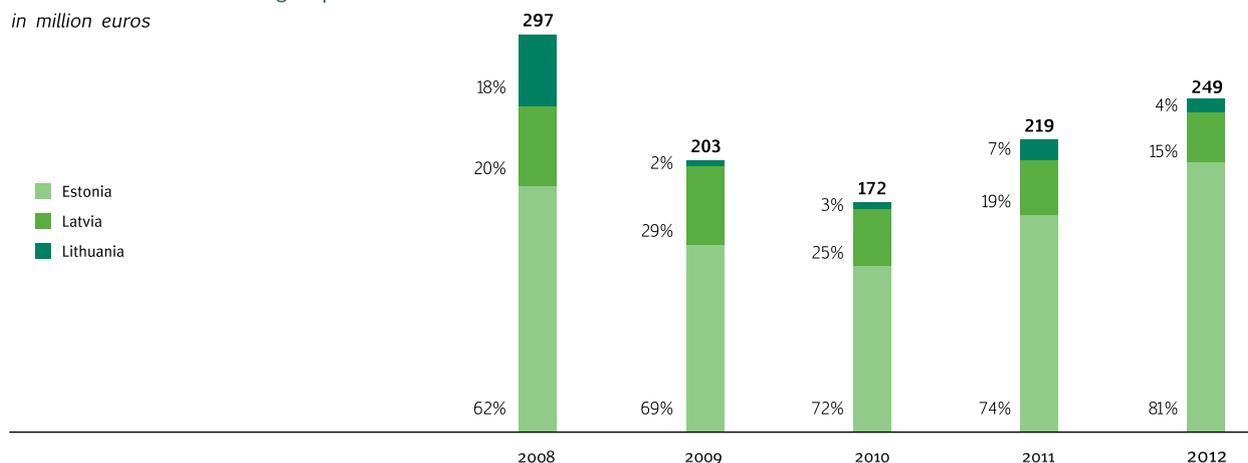


Group gross profit margin
percentages



In 2012, the revenue of Merko Ehitus was EUR 249.1 million. 81.1% of the revenue was generated in Estonia, 15.4% in Latvia and 3.5% in Lithuania. As compared to 2011, the group's revenue increased by 13.6%, including a 24.6% increase in Estonia and a 8.3% decline in Latvia and a 43.5% decline in Lithuania. The group's revenue growth can be mainly attributed to the increases in the revenue generated from engineering projects in Estonia (including the aircraft maintenance complex of Tallinn Airport, Ülemiste traffic junction) and the apartment projects in all three Baltic States. A bulk of the revenue generated from the construction sector can be attributed to projects co-financed by the EU Structural Funds. Considering the 13.1% growth of the Baltic construction market, it should be noted that the group's revenue increased in line with the market growth and since we ended the year with the net profit of EUR 7.63 million and improved the company's financial position, we can consider the results of the financial year generally positive.

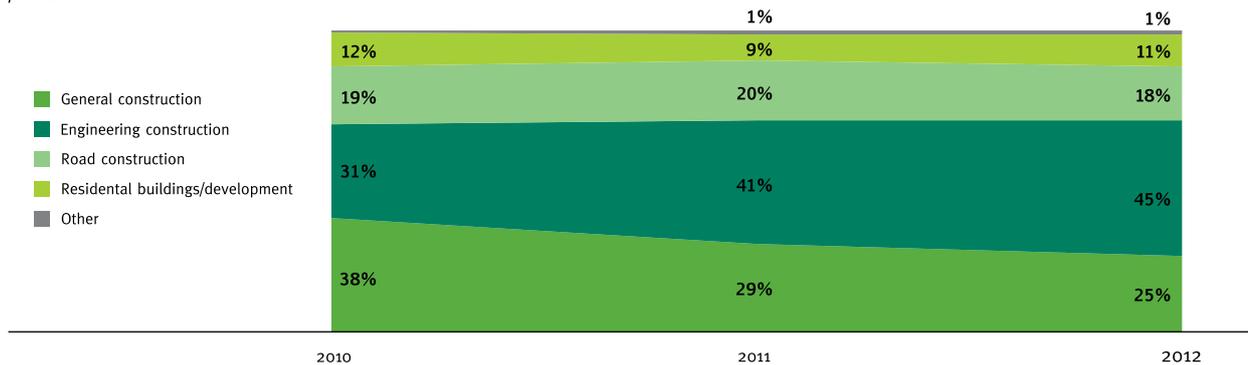
Revenue of Merko Ehitus group
in million euros



Engineering construction contributed 45%, general construction 25%, road construction 18%, development construction 11% and other revenue was 1% of the Group's revenue. 65% related to new construction and 35% renovation and reconstruction works of the construction activities.

Distribution of Group revenue according to segments

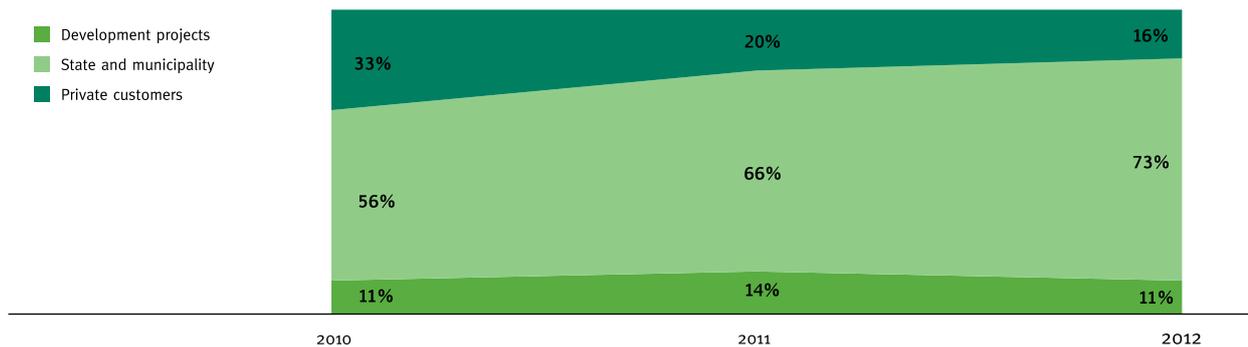
per cent



Confidence in the private sector slightly recovered during 2012, as did courage to invest in real estate and infrastructure development. A large share of public procurements continues to impact the development of the construction sector, and it will dominate the construction market also in the next few years. In terms of the development of the construction sector, the key will be the volume of construction works in the framework of the next EU budgeting period (2014-2020) that is still not finally determined.

Distribution of Group revenue according to customers

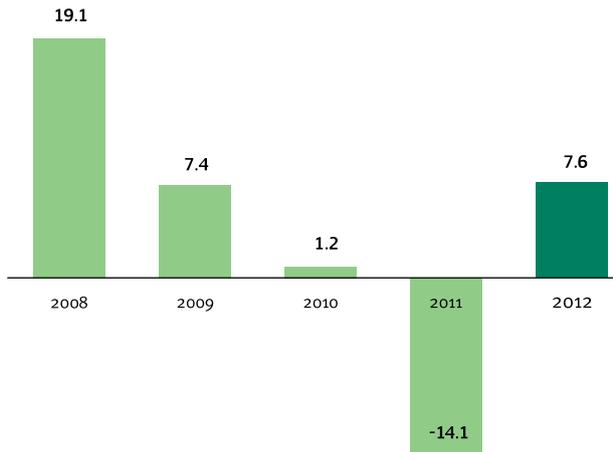
per cent



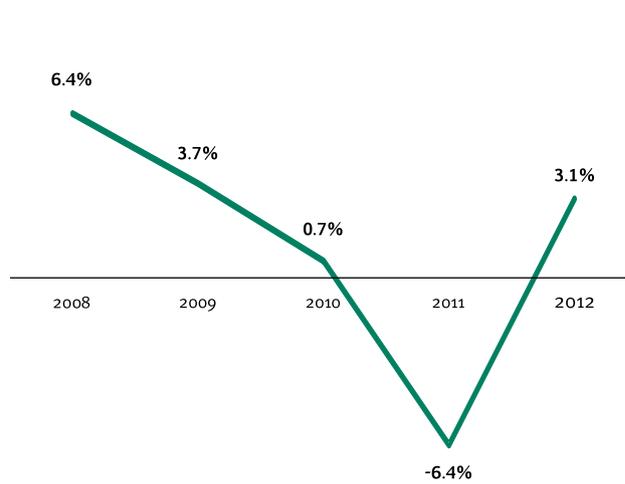
Profit

In 2012, the group's gross profit from development and construction activities totalled EUR 17.9 million (2011: gross loss of EUR 3.6 million). The impact of seasonal factors in construction on the 12-month results for 2012 was insignificant as compared to the same period last year. New and profitable projects and sales of apartment developments have led to a positive gross profit trend as compared same period a year earlier. In addition, recognition of the losses from problematic projects already in previous periods has a positive impact. For the same reasons, the gross profit margin has improved by 8.8% (2012: 7.2%) as compared to 2011 (-1.6%). In light of the ever more competitive construction sector, it is a major challenge for subsidiaries in the field of construction sector to maintain their gross margin at the same level.

Group net profit
in million euros



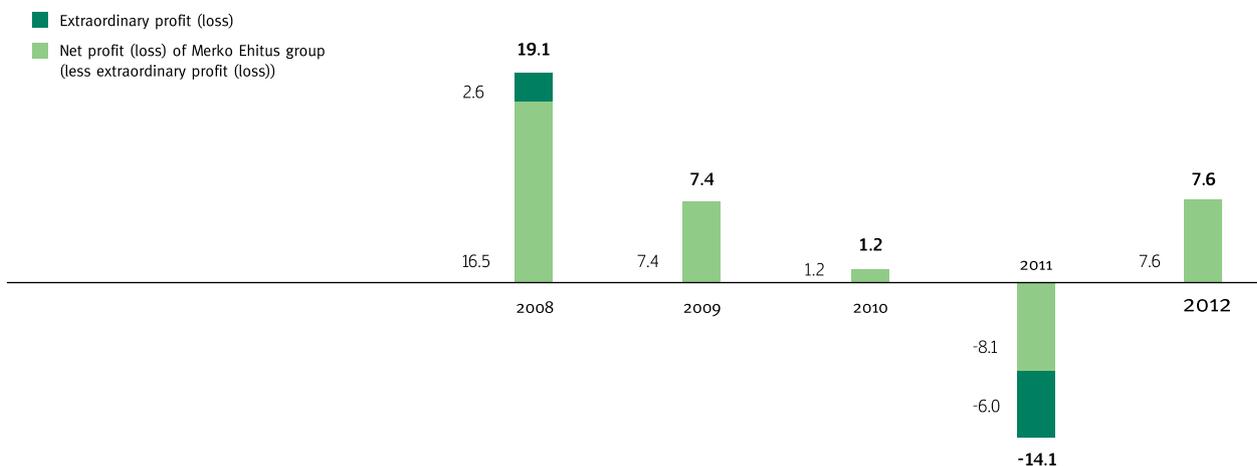
Group net profit margin
percentages



In 2012, the group's pre-tax profit totalled EUR 7.9 million and the net profit was EUR 7.6 million as compared to the pre-tax loss of EUR 14.0 million and net loss of EUR 14.1 million in 2011.

The biggest contribution to the profit came from the Estonian market, followed by Latvia. Operations in Lithuania ended the year with a small loss. Latvian and Lithuanian markets continue to pose major challenges, especially in the field of public procurement tenders. We are continuously focused on increasing the efficiency of the cost basis, improving profitability and, if necessary swift re-adjustment according to the market situation.

Net profit (loss) of Merko Ehitus group
in million euros



Business segments

The group manages business activities in the following areas at activity:

- General construction
- Engineering construction
- Road construction
- Real estate development

General construction

The general construction segment includes the construction of buildings for different purposes including offices, hotels, museums, culture and business centres, social, production and service buildings as well as buildings of various industrial structures. While only a few years ago the construction market was dominated by large-scale construction projects of private contracting entities, due to the economic situation, in recent years the main contracting authority has been the public sector. Last year was also characterised by various public projects, mainly aimed at reducing energy efficiency, that were financed from the proceeds of sale of emission credits.

General construction segment (million EUR)	2012	2011	Variance
Revenue	61.7	64.7	-4.7%
% of revenue	24.8%	29.5%	
Gross profit	5.0	4.6	+9.8%
Gross profit margin, %	8.1%	7.1%	

In 2012, the revenue of the general construction segment was EUR 61.7 million. While the revenue was 4.7% lower than in 2011, we managed to improve the gross profit of the general construction segment by 9.8%, despite tougher competition and the resulting pressure on margins. While the company was completing so-called transition projects that had been won in public procurements in recession years and that were somewhat unprofitable because of risky price bids, on the other hand, good annual results enabled us to start 2013 with several large-scale contracts (e.g. general construction works for the North Estonian Regional Hospital and for the 300 MW power unit of AS Eesti Energia Narva Elektriijaamad).

Throughout 2012 we were working on about ten different general construction projects. Among others, we completed the aircraft maintenance complex of Tallinn Airport and successfully finished the renovation of two large libraries – that of Tartu University and the National Library. Of the new contracts signed, one of the largest is the renovation of North Estonia Regional Hospital that will be completed in 2015. Our strength is the capability to simultaneously carry out several complex and long-term projects and to offer quality construction service to contracting entities that meet their specific requests.

The key to the success of Merko is the wide scale of its operations – if a certain business segment has more or less work, it is possible to re-assign staff and manage risks. Another competitive advantage is the professional team and a high level of process implementation.

Key data of the largest projects completed in 2012:

Project name		Location	Size	Country
Eesti Energia oil industry (condensation system; Enefit-280 pipe bridge)	new	Auvere village, Vaivara municipality		Estonia
Apartment building at 4 Hiiu-Suurtüki Street	new	Hiiu-Suurtüki 4, Tallinn	5,140 m ²	Estonia
Estonian National Library technical utility systems and facades	rec	Tõnismägi 2, Tallinn		Estonia
Tallinn Airport airplane maintenance complex	new	Väike-Sõjamäe 1A, Tallinn	11,901 m ²	Estonia
Elme Messer gas plant	new	Auvere village, Vaivara municipality		Estonia
Ice Age theme park	new	Kõrveküla, Tartu County	1,247 m ²	Estonia
Training and logistics centre of Tartu district unit of the Defence League	rec	Lehola 1, Tartu	2,734 m ²	Estonia
Lähte student home	new	Lähte, Tartu County	1,119 m ²	Estonia
Office and warehouse building	new	Kirsi 48C, Pärnu city	1,722 m ²	Estonia
Apartment building at 12 Kreutzwaldi Street	rec	Kreutzwaldi 12, Tallinn	1,300 m ²	Estonia
Laagri Maksimarket	rec	Pärnu mnt 558, Laagri	1,770 m ²	Estonia
Office and warehouse building	new	Katlakalna iela 9, Rīga	23,000 m ²	Latvia
Modernization of the Veterinary Faculty building infrastructure of the Latvian University of Agriculture	new	K.Helmaņa iela 8, Jelgava	5,891 m ²	Latvia
Saulaine school building	rec	Saulaine, Rundāles municipality	5,768 m ²	Latvia
Gas filtration plant in Liepāja	rec	Brīvības iela 92B, Liepāja	1,004 m ²	Latvia
Vilniaus Pergale industry and warehouse building	new	V. A. Graičiūno 26, Vilnius	13,730 m ²	Lithuania

Tallinn Airport airplane maintenance complex

Construction site: **Tallinn Airport airplane maintenance complex**

Contracting entity: AS Tallinna Lennujaam

Construction period: 2011-2012

Location: Tallinn, Estonia

Project cost: EUR 10.4 million (not including VAT)

Project manager: Marek Hergauk

The contract for design and construction of the aircraft maintenance complex was signed with Tallinn Airport in June 2011 and there was 12 months for designing and construction of the maintenance complex. The preliminary design was completed in early September 2011 and the building permit was received on 8 December 2011. In spite of the fact that it was a difficult project from the engineering standpoint and the deadline was short, we delivered the building to the contracting entity in August 2012. The maintenance complex was opened on 5 September.

From the outside, the aircraft maintenance complex is a simple building but it is quite complicated from an engineering and technological standpoint. The basic materials from which the design proceeded were the schematic design, explanatory memorandum and the technical specifications for the aircraft (the complex was built to serve Boeing 737 Classic/New Generation, Boeing 757-200/-300, Airbus A320 Family and Embraer CRJ type planes). The design development work, which culminated with the construction of the building, was dealt with by OÜ Innopolis Insenerid. This was a Yellow FIDIC Book contract. The FIDIC Engineer team had eight members who kept an eye on our work. In addition, the working group included representatives of the building owner and contracting entity (Tallinn Airport) and the building lessor, Air Maintenance Estonia.



Before the start of the design work, the lessor organized a trip to familiarize them with a similar hangar in Sofia, Bulgaria, as it was desired after construction of the Tallinn hangar to use many innovative solutions for which Estonia lacked the necessary know-how.

The building has a total gross area of 12,943 m², of which the principal part, 5,000 m², comprises the maintenance hangar in the middle of the building. Noteworthy elements in the hangar certainly include the 90 metre long and 11 metre high main girder that weighed 117 tons and was assembled in the air from five sections. Another key element is the aero-lift, the opening of which (less fixtures) was 90 metres and the height of its highest section, 15 metres. The maintenance hangar can service three planes at once. In building the maintenance hangar it was a major challenge to manufacture and install the airplanes' tail maintenance platforms, which were also in our contract and with regard to which we decided to design and built them ourselves with the help of contractor OÜ RED Technologies. The particularity of the tail maintenance platform is the fact that it had to move up and down over a range of 3.5 metres based on the type of plane and the lower platform part had to move horizontally over a range of 2 metres.

The maintenance hangar is surrounded by office wing, non-work building/canteen with personnel dressing rooms and a separate warehouse wing. In addition to the building our task was to design and establish a 8,800 m² aircraft platform, two aircraft parking spots and a 3,400 m² blacktop apron the building as well as fencing for a restricted-security area.

As for the design of the structural part of the building, the most complicated task was the airplane maintenance hangar part, which we decided to build using reinforced concrete posts and steel roofing supports. The solution for the building was made complicated by the fact that the basic wind speed to be used for calculations was 27 m/s instead of the usual 21 m/s. This significantly changed the building's weight-bearing and shell structures (such as fastenings for windows and doors, selection of exterior siding and fastening systems, and roofing fastening systems etc). Although nearly two-thirds of the hangar is covered with overhead cranes, the steel roofing structure had to be designed in order to be rigid enough to service planes by crane even in winter conditions when the roof is bearing a load of snow.

In addition, a problem in designing the hangar was the compressive and tensile force exerted on the foundations, as we had to take into account a situation where the hangar door is completely open; thus we made additional use of tension pile shafts to anchor the foundations.

We designed and built modern utility systems throughout the building, built a foam extinguishing system in the airplane maintenance hangar, the service channels in the floors for airplanes along with the necessary utilities, as well as the 400 Hz power supply system to feed power to airplanes along with distribution grid, and explosion-proof ventilation systems for airplane fuel tanks.

As the entire design and build process had fit into quite a short contract performance term, the process offered sufficient challenge to the entire team and auxiliary workforce. There were many difficult and non-standard situations, an example was that the terms of reference specified that it had to withstand an extraordinarily high wind load – it meant that the whole building had to be much stronger. The project proceeded at an extremely fast rate from beginning to end, and although no more similar projects will likely be built in Estonia, it gave Merko the experience to build buildings with extremely high security and safety requirements.



Engineering or infrastructure construction

The engineering construction segment of Merko builds port structures, landfilling areas at landfills, various road structures (tunnels, overpasses, bridges), water and sewerage pipelines, water treatment plants and other complex engineering and environmental projects.

Civil engineering segment (million EUR)	2012	2011	Variance
Revenue	113.3	90.8	24.8%
% of revenue	45.5%	41.4%	
Gross profit	9.0	1.9	+385.4%
Gross profit margin, %	7.9%	2.0%	

Revenue in 2012 was 24.8% higher than in 2011. In 2012 our largest construction projects were pipeline renovation projects in Maardu, Tapa, Tamsalu, Sillamäe and Kehra, water treatment stations in Ahtme and Püssi. The gross profit in the amount of EUR 9.0 million (2011: EUR 1.9 million) and gross profit margin of 7.9% (2011: 2.0%) have been moving in the positive direction, attributable mainly due to recognition of unprofitable projects in previous periods.

One of the keys to our success in the segment of engineering construction is the skills and knowhow in linking the skills of separate units in carrying out complex engineering projects through skilled project management.

In addition to enhancing our project management capacity, in recent years we have been improving our technical capacity in performance of works. Among others, we have at our disposal several different no-dig technologies for building water and sewerage pipelines in different soils. Examples of no-dig technology in recent years include the renovation project of water and sewerage mains in the town of Sillamäe where most of the renovated pipelines are under green parks and use of a traditional digging method would damage the whole greenery. The no-dig method enables to perform such works with a minimum additional impact on the existing environment.

Since a large number of public water system renovation projects that were co-financed by the EU Structural Funds and coordinated by the Environmental Investment Centre were due for completion in 2012 and 2013, the volume in this segment may decline several times in the following few years.

In the field of electrical construction, the company is mainly focused on providing complex solutions for high-voltage substations. The competitive advantage of Merko is that the company does not depend on one specific manufacturer and has an excellent team that covers the whole cycle, from designers to final tuning, plus a professional project management team.

The Aruküla substation that was completed in 2012, about a year earlier than the contractual deadline, is a clear example of our capability and professional and ambitious engineers who are interested and willing to prove themselves in this field.

The specifications of projects completed in 2012:

Project name		Location	Country
Kohtla-Järve district water intakes and water treatment plants	new	Kohtla-Järve, Ida-Viru County	Estonia
Aruküla 330/110 KV substation	new	Aruküla, Raasiku municipality	Estonia
Helme Energia 110 KV substation, buried cable and internal network	new	Patküla, Helme municipality	Estonia
Enefit Turbiinihall electricity supply	new	Auvere village, Vaivara municipality	Estonia
Ülemiste traffic interchange storm water drainage system	rec	Tallinn	Estonia
Valmiera public water supply and sewerage system	rec	Valmiera	Latvia
Mārupe water treatment plant	rec	Mārupe	Latvia

Aruküla 330/110KV substation

Construction site: **Aruküla 330/110KV substation**

Location: Aruküla, Raasiku municipality, Estonia

Contracting entity: Elering AS

Construction period: 2011-2012

Project cost: EUR 7.2 million (without VAT)

Project manager: Siim Õispalu

In 2012, we delivered to Elering AS the newly completed 330/110/20 kV substation in Aruküla, which provides power supply to a large part of Tallinn. The construction of this site, with its high level of responsibility, took place as a turnkey project – all of the equipment included in the project cost were delivered along with the necessary design development work, installed, configured, tested and handed over fully hooked up to the grid.

The old Aruküla substation was the last of three plants supplying Tallinn with power to be modernized. The construction was planned for 2011-2013, but the site was completed about a year before the term, and we are very proud of this fact. As specified in the design, new 330 kV, 110 kV and 20 kV switchyards were delivered and installed along with reconnection of the lines, a new control building was built and new relay fuse, automation and auxiliary voltage equipment were installed in the control building. In addition, a new well, sewerage system and fire fighting water source were developed.

For Merko, Aruküla was the first 330 kV substation that had to be designed from the equipment foundation and structures right up to installation. The technical requirements were provided by the contracting entity, and the rest had to be done by the builder, including the installation of equipment on the plot. It is likely that Estonia will not see so extensive new substation site but on the world scale such a reference is a major asset in a builder's portfolio. In addition, the site had a heightened hazard level, as the old substation was operating alongside it during the construction of the new one.

The construction of the 330/110 kV substation posed a number of challenges. The uniqueness and complexity of the site added its own nuances that had to be taken into account. As this was the first such project, we gained very good experience in this field with regard to equipment and technology as well as configurations. With regard to procurement, it was a major test for us to order equipment from suppliers in 23 different countries.

One part of the complexity of the project was due to mechanical equipment and assembly, but the other part was the final configuration. For the first time, we installed high-frequency communication equipment and technically demanding pantograph switches at such a high voltage. Thus it was very important to provide on-going training to the project staff and to keep abreast of the very voluminous project as-built documentation.

We installed about 80 km of secondary cables as part of the Aruküla substation procurement, tested over 3,500 remote-controlled signals reaching the Elering centre and fit the entire substation and the new control building onto a territory of two hectares. The first comment from the contracting entity was that the substation was pleasantly lacy and air-filled and that everything was optimized. That was good to hear.



Road construction

In this segment, Merko carries out road construction and builds the associated infrastructure. In addition, we carry out road maintenance works and maintenance repair.

Road construction segment (million EUR)	2012	2011	Variance
Revenue	45.2	43.3	+4.3%
% of revenue	18.1%	19.7%	
Gross profit	1.7	(5.7)	+129.9%
Gross profit margin, %	3.8%	-13.2%	

In 2012, the revenue in the road construction segment totalled EUR 45.2 million in 2012 and was 4.3% higher than in 2011. After several years of making losses, the gross profit earned in 2012 amounted to EUR 1.7 million, mainly because the loss expected from unprofitable projects has been reported already in earlier periods.

In 2012, we completed one of our largest road construction projects in recent years – 6.8 km long Loo-Maardu road section with the associated infrastructure that complies with Class A requirements. In addition, the construction of the Ülemiste traffic junction that will be completed at the end 2013 made up a significant share in 2012 revenue.

In road construction, the price of bitumen, one of the most important components of asphalt, has remained very volatile and had a negative effect on the public procurement projects that were won 2-3 years ago.

Key data of the most important projects completed in 2012:

Project name		Location	Size	Country
Loo-Maardu road	rec	Primary highway E20 (Tallinn-Narva), segment from Loo-Maardu (km 10.6-17.4)	6.8 km E20 category I road; 2 pedestrian and bicycle bridges; 2 overpasses; 4 tunnels	Estonia
Papiniidu extension	new	Pärnu city	84,273 m ² asphalt-concrete surface, tunnels for pedestrians and bicycles	Estonia
Pärnu-Jaagupi Kergu pavement construction	rec	Pärnu County, Vändra municipality	58,637 m ² asphalt-concrete surface, 60,585 m ² landscaping	Estonia

Loo-Maardu road segment

Construction site: **Loo-Maardu road segment**

Location: Loo-Maardu segment of primary road E20 (Tallinn-Narva) (km 10.6-17.4), Estonia

Contracting entity: Road Administration

Construction period: 2010-2012

Project cost: over EUR 22 million (without VAT)

Project manager: Ahto Aruväli

Merko builds Estonia's first three-grade crossing.

In 2012, Merko's most important road construction site was the transformation of the 6.8 km long Loo-Maardu segment of the Tallinn-Narva highway into a first class road. The outcome was greater traffic safety and smoother traffic on one of the most heavily used arteries in Estonia and the completion of the first three-grade crossing in Estonia.

Besides the nearly 7 km of first class road, Merko built two cycle/pedestrian bridges, two cycle/pedestrian tunnels, a railway tunnel and car tunnel. To ensure traffic safety, 36 km of guardrails were installed.

Already a few years back in the planning stage, it could be seen that this was not a simple project. Unforeseen problems took additional time: to approve conventional traffic schemes, many traffic and exit calculations and round-about capacity figures were needed, the permits from network possessors had expired and subgrade with a very specific smell reminiscent of an asphalt road built in the 1950s emerged from underneath the old concrete road, which had to be subjected to additional investigation due to a concerns about hazardous waste. In addition, an on-going land transfer process affected the collector road and access to three plots was made possible only in the autumn of each of the years, 2010 and 2011.

The Iru-Loo tunnel was the biggest worry, as some of the issues were said to have been not dealt with completely during the tunnel's design development process and the railway operator EVR Infra AS unexpectedly called for expert analysis of the railway overpass. As Estonia lacks experts with competence sufficient to carry out such analysis of a railway given what is at stake, we had to call in experts from St. Petersburg, who inspected the entire railway structure, possibilities of building and soil properties (all this should have already been carried out before the procurement was announced) and took part in monitoring the construction work until the tunnel was completed.

In spring 2011, we had two possibilities: to wait for May when we would start stage II of the tunnel or to divide the tunnel into three parts. As waiting would have ruled out all possibility of the site being completed on time, we opted for the second alternative. Looking back, this was the best decision.

The 2.5-year-long project was large and complex, as it was a challenge to constantly tackle new surprises, unforeseen circumstances and constant public scrutiny in conditions of everyday traffic. Besides the experience of working with Russian experts, we had to build, for the first time in Estonia, a car tunnel including lighting where we used, also for the first time in Estonia, a new bitumen with an SBS-in two uppermost layers of the pavement and recovered the excavated limestone to obtain the optimum mix of crushed stone. The experiences gained were very costly, but not available from any institution of learning.



Real estate development

Over the years, Merko's business area of real estate development including development of apartment projects, long-term financial investments and commercial real estate projects has become the flagship of Estonia's residential construction. Since 1992, we have built homes for more than 2,000 families. Every experience gained in Estonia, Latvia and Lithuania has been implemented in new residential construction projects; positive experience obtained from different countries shared within the group and learning from one another have given out project managers invaluable knowhow and expertise.

In comparison with the recession in 2008-2010, the real estate market became more active in 2012 both in terms of the number of transactions and prices. Also, our residential development business improved clearly in 2012. Managing such a large and valuable portfolio of properties requires careful and detailed planning of the whole process: the development of apartment buildings starts by organising details, detailed planning, designing and construction and ends with the sale of completed production and warranty service.

The underlying idea of our development activities is to value land through detailed planning and building development, to find customers for the property and sell the site either as real estate or to keep it as an opportunity for long-term financial income. In the framework of long-term projects, our portfolio includes, for instance, Jõgeva Police and Court building that was completed in 2012.

Merko's trademark of residential construction "A Home for Years" is a modern and convenient household solution that includes all development phases of new housing – planning, designing, building and sales. The keywords behind "A Home for Years" are integrated living environments, high energy efficiency, good sound insulation from indoor and outdoor noise as well as healthy interior climate.

With regard to private homes, detached houses and apartment buildings, our objective is to create homes that architecturally fit the specific region, have an attractive living environment, functional design solutions, quality interior design materials, optimal construction cost and energy efficiency. A home that is being offered for customers must also be reliable and valuable in years to come.

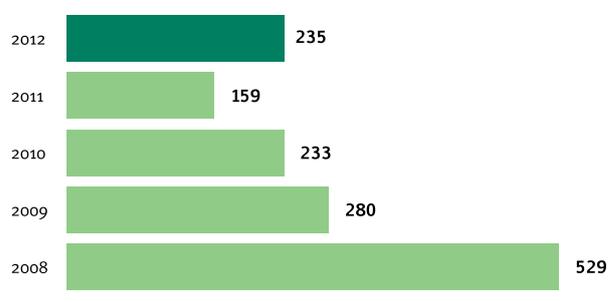
Real-estate development (million EUR)	2012	2011	Variance
Revenue	27.1	18.9	+43.4%
% of revenue	10.9%	8.6%	
Gross profit	2.4	(3.9)	+161.3%
Gross profit margin, %	8.9%	-20.7%	

In 2012, the revenue was EUR 27.1 million (2011: EUR 18.9 million) and the gross profit was EUR 2.4 million (2011 gross loss: EUR 3.9 million). The gross loss of 2011 was mostly influenced by impairment of assets in the amount of EUR 4.6 million.

A total of 235 apartments were sold in 12 months of 2012 at the total value of EUR 25.0 million (excl. VAT), (2011: 159 apartments and EUR 18.2 million, respectively). 147 were sold in Estonia, 73 in Latvia and 15 in Lithuania from the total of 235. At the end of the period, Merko Ehitus group's inventory comprised 155 completed but not yet sold apartments (55 in Estonia, 47 in Latvia and 53 in Lithuania). At the end of 2011, 33 completed apartments were unsold (28 in Estonia and 5 in Latvia).

Apartments sold

pcs



The following table lists the apartment projects in progress:

	Town/Country	Completion time	No of apartments
Räägu 9	Tallinn, Estonia	2013 summer	20
Eha 4 / Paldiski 17	Tallinn, Estonia	2013 summer	27
Vaarika 5	Tartu, Estonia	2013 summer	15
Pallasti 46, 48, 50	Tallinn, Estonia	2013 autumn	69
Grostonas 17	Riga, Latvia	2013 autumn	62
Tedre 55	Tallinn, Estonia	2014 spring	47
Total			240

In addition, the construction activity on 311 apartments from 2007 and 2008 has been frozen.

Key data of the most significant developments completed in 2012:

Project name		Location	Size	Country
Commercial and residential building at 50A Tartu Road	new	Tartu 50A, Tallinn	11,975 m ² , 93 apartments	Estonia
Apartment buildings at 6 and 8 Hane Street	new	Hane 6 and 8, Tallinn	3,722 m ² , 41 apartments	Estonia
Apartment buildings at 42, 44, 52 Pallasti Street	new	Pallasti 42,44,52 Tallinn	3,301 m ² , 39 apartments	Estonia
Jõgeva Police and Court building	new	Suur 1, Jõgeva	2,466 m ²	Estonia
Skanstes Virsošnes apartment buildings	new	Skanstes Street, Riga	ca 70,000 m ² , 496 apartments	Latvia
Apartment building in Moksliniku Street	new	Moksliniku Street, Vilnius	5,993 m ² , 68 apartments	Lithuania

One of our objectives is to keep a moderate portfolio of land plots to ensure stable implementation of property development projects considering the market conditions. At the same time the real estate market has become more selective – key aspects considered in the evaluation of risks prior to the launch of each project are the location, scale of development, design solutions and the target group. In view of the low mortgage interest rates and the limited supply on the market of new apartments over the last three years, demand and transaction activity in the apartment market has grown moderately.

Skanstes Virsotnes residential project, with close to 500 apartments

Construction site: **Skanstes Virsotnes residential project, with close to 500 apartments**

Construction period: 2006-2012

Builder: SIA Merks

Construction cost: approximately EUR 57 million

Project managers Ivo Brālēns and Maksims Momots

In 2012, SIA Merks completed the fourth tower in the project "Skanstes virsotnes" – "Peaks of Skanste" - in Riga. Over the years, 496 new flats were built, most of which have now been sold. The project was very special for SIA Merks as it is the first high-rise apartment project that has been come to completion since SIA Merks was founded.

The Skanstes Virsotnes residential complex has been called the most ambitious construction project of the new millennium in Riga. The buildings are in Riga's Vidzeme suburb, which has a close to four-hectare park area. The attractive buildings are connected with closed two-storey parking garages, whose roofs boast children's playgrounds. Each building has about 130 1-5-room apartments with floor space of 50 to 150 m².

The materials and technologies used are modern and the balconies built into the facade make the buildings distinct from other high-rises. The parking lot uses post-tensioned reinforced concrete technology to allow the concrete slabs to span greater distances.

What made the project complicated was that the work was done very high off the ground. It was especially difficult to transport materials like concrete and finishing materials to the upper stories. The concrete necessitated a special container while the other materials had a loading hoist fastened to the facade.

SIA Merks is not just a construction firm, but a real estate developer. The project is important for SIA Merks to remain one of the leading players on the apartment sale market.

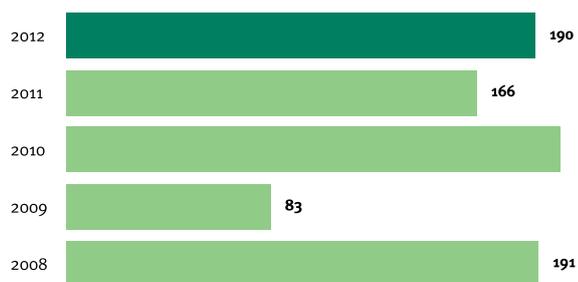


Portfolio of contracts

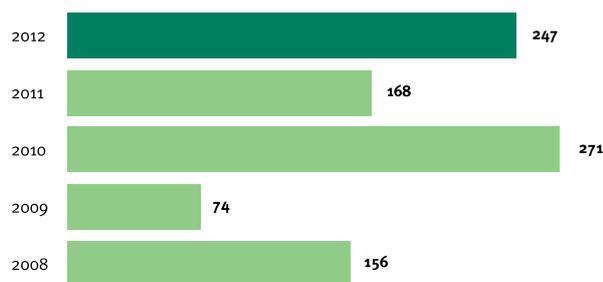
The group's portfolio of contracts contains the volume of actually signed construction contracts as at the reporting date. The portfolio of contracts does not include apartment buildings that the group itself is developing and building or other developments where the group is acting as the developer.

As at 31 December 2012, the group's portfolio of uncompleted construction contracts amounted to EUR 190 million as compared to EUR 166 million as at 31 December 2011.

Secured order book
in million euros



New contracts signed
in million euros



In the last 12 months, EUR 247 worth of new contracts were signed (without apartment developments) as compared to EUR 168 million in 2011. The table below shows the largest construction contracts that were signed in 2012:

Brief description of contract	Cost million EUR	Completion time
North-Estonia Medical Centre (PERH) Regional Hospital	23.9	2015 May
Narva city water treatment plant	21.1	2015 Spring
General construction, AS Eesti Energia Narva Elektriijaamad 300MW energy unit	17.3	2013 July
Vääna-Jõesuu water and sewerage pipe construction, Part 2 and 3	14.6	2015 August
Renovation and expansion of Narva-Jõesuu public water supply and sewerage, Part 1 and 2	8.8	Part 1 2015 March Part 2 2014 October
Vääna-Jõesuu and Viti village public water supply and sewerage and wastewater pumping stations	7.7	2015 Spring
Kiisa emergency backup power plant	7.2	2013 June
Riga University of Technology electronics and telecommunications department	6.6	2013 December
Tõrva city public water supply and sewerage system design and construction	5.6	2013 October

Although the share of public procurements was still predominant among construction contracts in 2012, the private customer segment has become more active in the construction markets of all three Baltic countries. With the current EU financial framework period ending, a certain drop in the volume of public procurements can be forecast starting in the latter half of 2013. As a result, it will be a challenge in its own right to keep the volume of new construction agreements at the 2012 level.

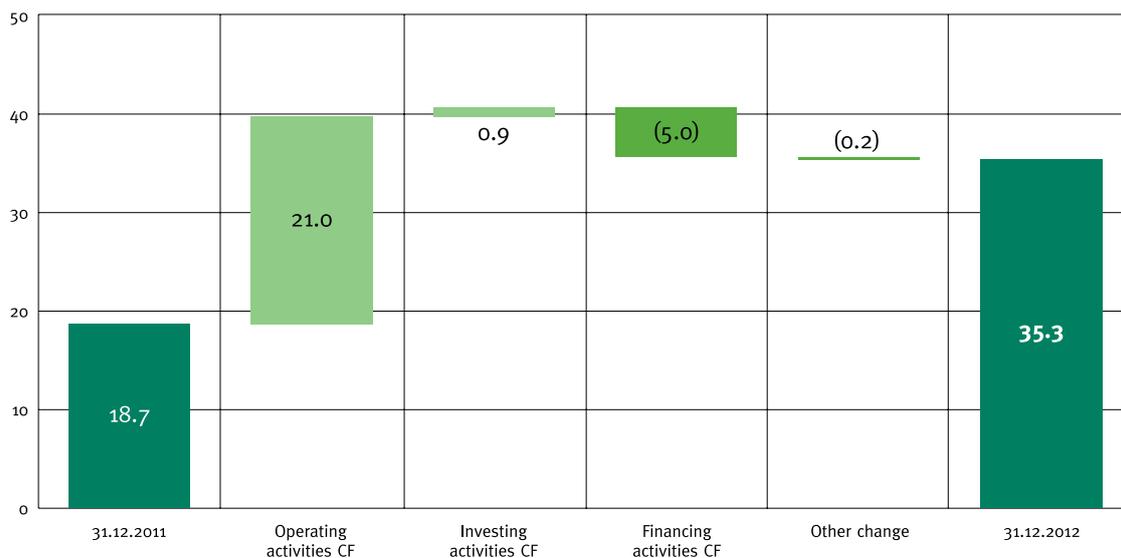
Cash flows

The change in short-term investments and cash equivalents of Merko Ehitus group was positive by EUR 16.9 million and as at 31 December 2012, the group had cash equivalents in the amount of EUR 35.3 million (2011: EUR 18.7 million) in its bank accounts and term deposits.

The operating cash flows of 2012 were positive by EUR 21.0 million (2011: negative by EUR 6.2 million), the cash flows from investment activities were positive by EUR 0.9 million (2011: EUR 2.6 million) and cash flows from financing activities were negative by EUR 5.0 million (2011: positive by EUR 12.1 million).

Change in cash and cash equivalents

in million euros



Cash flows from operating activity was most influenced by the operating profit of EUR 8.8 million, positive change in receivables and prepayments related to operating activities in the amount of EUR 7.3 million, positive change in inventories related to operating activities in the amount of EUR 5.4 million and negative change in trade and other receivables related to operating activities – EUR 3.0 million. Notably higher inflow of cash is related to the repayment of operating development loans in the amount of EUR 9.9 million. In its 2012 report the group changed the presentation method of these loans. More detailed explanations are provided in Clause 1.29 of Annex 1 of the annual report.

It should still be emphasised in this connection that the share of public sector orders with a long payment term has increased as a proportion of the group's cash flows from operating activities (by contract, an average of 56 days after evaluation of the work) and there is an additional burden on working capital, including optimal management of cash flows. To support cash flows arising from operating activity, the group has been prudent in raising additional external capital, including factoring. At the same time, the debt ratio has remained at a moderate level (15.8% as at 12 months of 2012).

Cash flows from investing activities in the amount of EUR 0.9 million are made up of positive EUR 2.8 million generated from the disposal of the ownership interest in AS TMB. Negative cash flows consist of EUR 1.5 million spent on the acquisition of investment property (mainly the construction of the court and police department building in Jõgeva).

In the cash flow from financing activities, the balance of bank loans received and repaid resulted in negative cash flow in the net amount of EUR 5.6 million. Repayments of the principal of capital lease totalled EUR 0.9 million and factoring had a positive cash flow of EUR 1.5 million. Loans received and repaid were mainly related to the group's development activities, whereas in 2012, mainly due to the more active sale of apartments, the volume of loans repaid was higher than the volume of loans received.

Financial ratios (attributable to equity holders of the parent)

		2012	2011	2010
Income statement summary				
Revenue	million EUR	249	219	172
Gross profit	million EUR	17.9	(3.6)	12.8
Gross profit margin	%	7.2	-1.6	7.5
Operating profit	million EUR	8.8	(12.3)	2.4
Operating profit margin	%	3.5	-5.6	1.4
Profit before tax	million EUR	7.9	(14.0)	1.8
EBT margin	%	3.2	-6.4	1.0
Net profit	million EUR	7.6	(14.2)	1.1
attributable to equity holders of the parent	million EUR	7.6	(14.1)	1.2
attributable to non-controlling interest	million EUR	(0.0)	(0.1)	(0.1)
Net profit margin (attributable to equity holders of the parent)	%	3.1	-6.4	0.7
Other key figures				
ROE	%	6.8	-12.2	1.0
ROA	%	3.4	-6.6	0.6
ROIC	%	6.0	-9.0	1.6
Equity ratio	%	52.0	49.6	63.8
Debt ratio	%	15.8	18.3	13.2
Current ratio	times	2.1	2.0	2.7
Quick ratio	times	1.1	1.0	1.1
Accounts receivable turnover	days	58	56	46
Accounts payable turnover	days	47	45	40
EBITDA margin	%	4.6	-4.6	2.8
General expense ratio	%	4.5	4.6	6.4
Personnel expense ratio	%	8.3	7.6	9.3
Revenue per employee	thousand EUR	278	235	208
Average number of employees (group)	people	895	934	825
Secured Order Book	million EUR	190	166	200

*Calculations of ratios is provided on page 105 of the report.

Risk management

Risk management is part of strategic management and is inseparable from daily operations of the company. In managing risks, the main objective of the company is to determine larger and more significant risks and to optimally manage these risks so that the company achieves its strategic and financial objectives. The company considers it important to assess aggregate group's risks, instead of the impact factors of individual risks. Turning constant attention to risk management enables to exclude or minimise a possible financial loss. For the company, the most important risks are market risk, operating risk and financial risks. The latter including interest rate risk, foreign currency risk, credit risk, liquidity risk, equity risk and legal risks. Detailed description of financial risks is provided in Note 36.

Because of the group's balance sheet structure and the market position, none of these risks has a significant impact as at the date of this report.

Market risk. One of the peculiarities of construction activities is the fact that the execution of the contracts concluded is a long-term process, making the sector inert to changes in the economic environment. Due to this, both positive and negative changes in the economic environment reach the construction industry with a lag of approximately 12-18 months. This time lag enables the sector to arrange its activities to be prepared for potential setbacks as well as booms.

Significantly more attention is being paid to potentially major volatility of input prices in the construction sector that could complicate the budgeting process, completion of projects at planned costs, cause additional risks in carrying out fixed-price construction contracts and weaken projects' profitability. Therefore, the overall economic development is being closely monitored and taking excessive price risks already in the bidding phase is avoided.

The residential development area is one of the main sources of market risk arising from the value of real estate for Merko Ehitus group. The real estate market has become more selective and in pre-launch risk assessment, consideration is given to such important aspects as the project's location, development volume, planning solutions and the target group. Taking into account low interest rates on loans and limited supply on the market of new apartments, in the last three years the demand and transaction activity on the apartment market has grown moderately. Because of the selectiveness of the real estate market, setting the right sale price for new development projects in the given region have become very important. For hedging the area's price risk, price statistics collected by the group and available from other public sources is being constantly analysed.

Market risk that is part of financial risks includes **currency risk and interest risk**. The analysis of these risks is provided in Note 36 to the annual report.

Operating risk. The group concludes total risk insurance contracts with insurance companies in order to hedge the risk of unanticipated loss events occurring in the construction process. The general policy is entered into for one year and it compensates the customer, subcontractors and third parties for any losses caused by Merko Ehitus or its subcontractor for up to EUR 9.6 million. The risks of the projects which cost exceeds EUR 9.6 million or the annual policy does not cover (water construction, railroad construction, bridges, etc.) are additionally mapped out and an insurance contract is concluded separately for each object taking into consideration its peculiarities. In concluding contracts for services involving design work, an insurance contract for professional liability is required from subcontractors or an insurance contract at own expense is concluded, covering the damage arising from design, erroneous measurement, advice and instructions. The services of insurance brokers are used in mapping out risks, concluding insurance contracts and handling loss events. In 2012, indemnity applications submitted to insurance companies totalled EUR 0.98 million (2011: EUR 0.58 million), and insurance benefits were received in the amount of EUR 0.17 million (2011: EUR 0.02 million).

A warranty provision has been provided at the Company to cover for the construction errors which have become evident during the warranty period. In 2012, warranty provisions were set up at the group in the total amount of EUR 0.81 million (2011: EUR 1.06 million) and disbursements amounted to EUR 0.56 million (2011: EUR 0.82 million). As at the year-end, the Company's warranty provision amounted to EUR 1.62 million (31.12.2011: EUR 1.37 million). With regard to work performed by subcontractors, the subcontractor is responsible for elimination of defects that became evident during the warranty period. With regard to critically significant contracts, the performance of contractual obligations of the contractor arising from contracts of services is guaranteed with bank guarantees to be paid upon first demand.

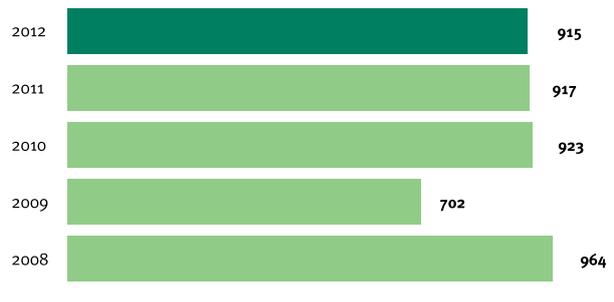
One important part of managing operating risks is the mapping out of the situation and anticipation of risks. ISO 9001/14001 management systems have been set up the largest group entities and the occupational health and safety system OHSAS 18001 has been set up at Merko Ehitus Eesti, Merko Infra, Merko Tartu as well as the Latvian and Lithuanian subsidiaries. Sixteen full-time quality control specialists work at the group whose work responsibilities include ensuring the development and functioning of quality, occupational safety and management systems.

The analysis on **credit, liquidity and legal risks** is provided in Note 36 to the financial statements.

Employees

The number of the group's employees decreased by 2 in the last 12 months (-0.2%) and as at 31 December 2012, the group had a total of 915 employees (including fixed-term and part-time employees). Within the framework of the efficiency program implemented at the beginning of 2012, changes were made in the management of Merks and Merko Statyba and the number of administrative employees in the Lithuanian and Latvian subsidiaries was cut, although by the year-end, the number of group's employees had reached the level of the beginning of the year.

Number of employees



Personnel policy

The group's personnel policy supports achievement of the company's goals, ensuring sustainability of the organisation and management, staying competitive, maintaining and increasing the value of the organisation and constant development of competence.

We choose and develop employees who considers the success of the company important, who have willpower and take on challenges that require more.

We develop responsible management throughout the organisation, guided by the strategy, management system, applicable law, ethical values and good organisation management practice. We treat employees as partners, involving everyone in the decision-making process and perceiving that the right to make decisions includes responsibility.

We value our employees, ensuring an adequate, fair and competitive salary that complies with the contribution of the employee and a motivation package. We keep in mind work relations and traditions that further cooperation.

We provide employees with conditions for professional development and career opportunities by supporting studies and acquisition of professional knowledge and experience. Each employee is responsible for his/her competence.

Safety and health

Creating a safe working environment for well trained, healthy and motivated employees, both in the office and on construction sites, has always been an important aspect in the operations of the group's construction companies. Pre-construction risk analysis remains constantly in focus, aimed at identifying common protection needs of site workers, measures and requirements for use of personal protection equipment. Basic and supplementary training in the field of occupational health and safety forms part of our personnel policy. Training provides knowhow and skills that enables to prevent risks, analyse them and find the most suitable technical and economic solutions. The management system for occupational health and safety that was certified in 2004 and complies with the OHSAS 18001 standard allows to effectively monitor working environment in construction sites and offices. Basic and supplementary training has always been available for inspectors to guarantee their competence.

Periodic health inspection provided by the occupational health partner to assess work-related risk factors helps to prevent employee health problems, plan safer working environments or, with the partial support of the company, to allow employees to use the necessary health rehabilitation measures. Promoting sports among the employees and direct support by the company also help to create a "healthier" working environment.

Personnel development and recognition

We value and support employees who wish to develop their skills and offer them various training opportunities. Employees can further their knowledge in different areas at specialisation in both as individual study or team training.

We have created conditions and opportunities for achieving professional results and making a career by encouraging existing employees to apply for vacant or new positions within the company.

We thoroughly support studies of our employees and are interested that everyone is able to graduate in due time. For recognition of graduates, they are invited to a spring reception hosted by the management where everyone is remembered with a present.

We continuously contribute to healthy and comfortable working environment so that it would be comfortable and safer for all of us to work on sites as well as in the office.

In order to support healthy way of living and to maintain working ability we pay our employees sports and health allowance. Additionally, we organise free vaccinations, periodic health checks and, naturally, provide the on-site personnel with comfortable work clothes and footwear.

In order to recognise the most prominent employees of the company and the best cooperation partners, we annually elect Merko's Achievers of the Year. The Achievers of the Year 2012 were:

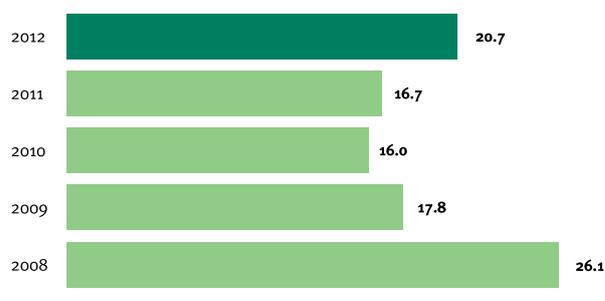
Site Operator of the Year or "The Bull"	Marek Hergauk	project manager
Site Team Member of the Year or "Little Bull"	Sander Põld	specialist, department of electrical works
Manager of the Year or "The Ram"	Boris Tehnikov	head of the department of electrical works
Office Employee of the Year or "The Rat"	Tiit Riisalu	quality specialist
Newcomer of the Year or "The Fox"	Holger Tilk	lawyer
Cooperation Partner of the Year or "The Horse"	AS Maleko	

Remuneration

The group's objective is to pay its employees competitive salary. The interests of employees and the company are balanced by performance-based remuneration.

Gross wages and salaries paid to employees in 2012 totalled EUR 20.7 million, of which base wages and salaries accounted for 74.8% and bonuses accounted for 25.2% (2011: EUR 16.7 million, of which base wages and salaries were 84.6% and bonuses were 15.4%). In a year, gross wages and salaries increased by 24.0%, including a 9.7% increase in base wages and salaries and a 102.4% increase in bonuses.

Gross remuneration
in million euros



Environment

The environmental management system that complies with ISO 14001 standard continues to focus on waste handling issues of construction sites, highlighting the need to sort waste in the most appropriate location and handing waste over only to such service providers that are licensed to handle such waste. In cooperating with such companies we have often discovered polluted soil and waste containing hazardous substances. For years, the company has been recording the quantities of waste created in construction sites and submitted respective annual reports to the Environmental Authority.

In environmentally sensitive tenders, we have always considered the requirements to the environmental impact assessment of projects, carried out preliminary research if necessary or conducted replacement planting, if it has been inevitable to fell trees when preparing the construction site.

Social responsibility

The group is responsible for its decisions and activities that have an impact on our employees, customers and partners and, more broadly, on local communities. In 2012, the group supported sports, culture and education and paid a total of EUR 0.27 million in charitable donations (2011: EUR 0.29 million).

In the area of sports, we support for several years project called the Eesti Terviserajad (*Estonian Hiking Tracks*) and the Estonian Ski Association. In culture, we continued cooperation with the Estonian Art Museum and in the education sector, we support foundation Noored Kooli (*Young to Schools*).

Recreational trails project supported by Merko Ehitus receives award from IOC

A foundation initiated by Merko Ehitus, Eesti Energia and Swedbank for year-round recreational sport – SA Eesti Terviserajad (Estonian recreational trails foundation) – won the 2012 award for sport and environment from the International Olympic Committee.

Director of SA Eesti Terviserajad Jaak Teppan said the award was a great honour for the foundation. He added that the activities of the foundation were very committed to the goal – today Estonia has nearly three times more recreational trails than when the organization started. “And most of all, the number of illuminated trails and kilometres has seen a nearly fivefold increase, we have systems for snow-making and also important development in trail quality. The award shows that people have taken notice of the jump in the development of trails and that the people approve of it, which certainly increases enthusiasm to set new goals.”

In addition, the International Olympic Committee award shows that Estonian companies can make large projects a reality when thinking about society’s needs.

For Merko Ehitus, Eesti Terviserajad is one of the group’s largest sponsorships, which besides well-maintained sports facilities also helps shape the habit of regular exercise among the population.

Today Estonia’s pro and amateur athletes have access to close to 90 trails, with 750 km of them maintained and mostly illuminated. The trails have been warmly welcomed by the people – they see more than 75,000 uses a week year-round which adds up to nearly 4 million visits a year. The most popular sport centres are Tallinn’s Nõmme sport centre, a similar one in the Pirita district and the Jõulumäe centre in Pärnu County. Fortunately Estonia’s natural diversity provides inexhaustible possibilities for new activities and new sites.

Estonia has provided EUR 23 million into free recreational trails

SA Eesti Terviserajad was founded a few years before the Turin Winter Olympics in realization of the sad fact that Estonia did not have a rising generation of athletes who would be internationally competitive. And since there were few free, pleasant and naturally scenic places to engage in sport, it is hard to find arguments in favour of getting people to be active out of doors. In this less than promising situation, a board member of the Ski Association, Toomas Annus (Chairman of the Supervisory Board of AS Merko Ehitus) decided to map out the current situation, possibilities and development scenarios of trails. As the investments to be made into Estonian recreational trails were very substantial, the foundation Eesti Terviserajad was launched at the initiative of Merko Ehitus, Hansabank and Eesti Energia in spring 2005. “Actually Merko’s investment into trails started before the foundation was established. It was Merko that really laid the groundwork for the entire initiative,” recalls Teppan.

The goal of the joint enterprise was to support the development of Estonian recreational trails to ensure that people had a free opportunity to exercise outside year round and that these would be available to all. Over seven years, over EUR 23 million has been invested into the trails, including by SA Eesti Terviserajad, local governments, Ministry of Culture and the European Union.

One of the goals of the foundation is to bring as many people as possible to the recreational trails and be a support and initiator for well-organized public sport events and series of such events. Taking part in public sport events as one way of spending free time could be embraced by many. Everyone should have a chance to exercise in natural environments in a manner that is available, free of charge and safe. As people are increasingly interested in exercising and staying in good physical shape, our living environment must be as high in calibre as possible around the year!

Read more: www.terviserajad.ee.



In 2012, the activities of AS Merko Ehitus were recognised additionally in the form of the following prizes:

The Entrepreneurship Award 2012

AS Merko Ehitus was granted the most competitive company's award in the field of construction at the Entrepreneurship Award competition organised by Enterprise Estonia, the Estonian Chamber of Commerce and the Estonian Employers' Confederation.

Euromoney – Real Estate Survey 2012

In its real estate market survey for 2012, Euromoney – the international financial journal with a history of more than 40 years – declared AS Merko Ehitus Estonia's best developer. The Real Estate Survey 2012 is the eighth survey conducted by Euromoney with the aim of ranking the best in real estate on the basis of the market data, as well as the assessments of developers, counsellors, business customers, investors and banks.

Share and shareholders

The shares of Merko Ehitus are listed in the Main List of NASDAQ OMX Tallinn. As at 31 December 2012, the company had 17,700,000 shares. The number of shares did not change during 2012.

In 2012, 1,662 transactions were conducted with the shares of Merko Ehitus (2011: 3,719 transactions), in the course of which 0.94 million shares were traded and the total monetary value of transactions was EUR 5.5 million. The lowest share price was EUR 5.37 and the highest share price was EUR 7.30. The closing price of the shares as at 31.12.2012 was EUR 5.90 (31 December 2011: 5.40). As at 31.12.2012, the market capitalisation of AS Merko Ehitus was EUR 104 million (31 December 2011: EUR 96 million).

The number of shares that belong to the members of Supervisory Board and Management Board as at 31 December 2012 was 11,067,968 shares (31 December 2011: 11,067,968 shares) that accounted for 62.5% of the number of shares. A more detailed presentation of the members of the Supervisory Board and Management Board and the number of shares they own are provided in the Good Governance Report.

Information on security

Issuer	AS Merko Ehitus
Name of security	Share of Merko Ehitus
Residency of issuer	Estonia
Stock Exchange List	Main List
ISIN	EE3100098328
Nominal value	without nominal value
Number of securities	17,700,000
Volume of issue	12,000,000
Currency	EUR
Registration at ECSD	08.07.2008

Earnings per share (EPS)

EUR

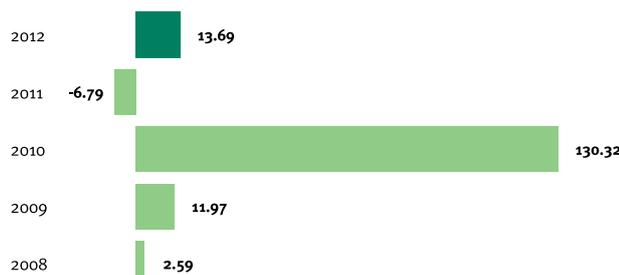


Equity per share

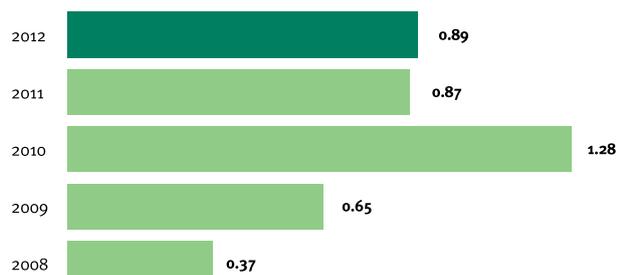
EUR



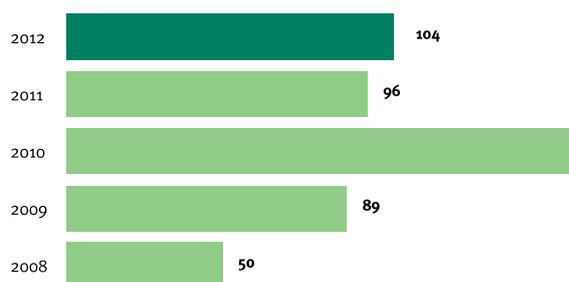
P/E (price / earnings ratio)



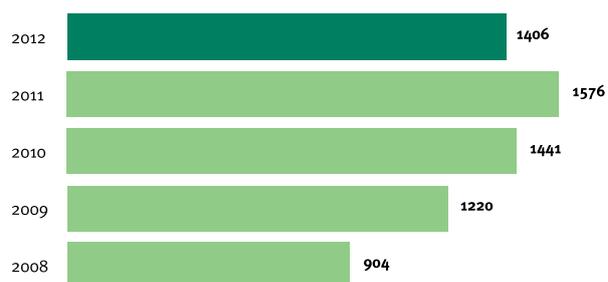
P/B (price to book ratio)



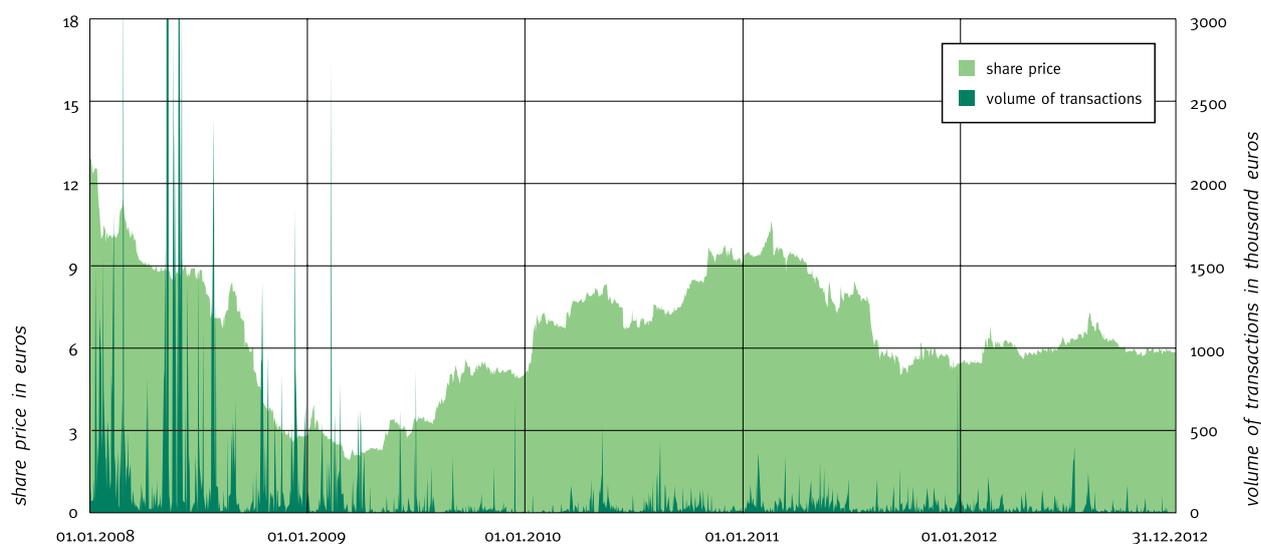
Market value
in million euros



Number of shareholders at the end of period



Performance of Merko Ehitus share at NASDAQ OMX Tallinn Stock Exchange



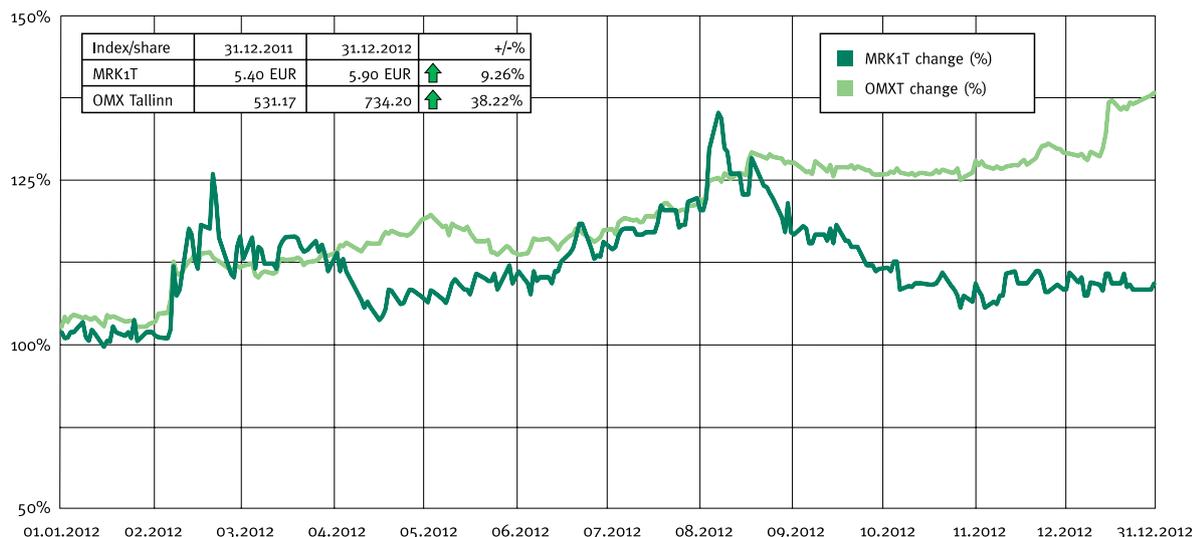
Trading history of securities, EUR

	2012	2011	2010
Highest	7.30	10.65	9.89
Lowest	5.37	4.90	5.05
Closing	5.90	5.40	9.05
Average	6.04	7.49	7.72
Change, %	+9.26	-40.33	+80.30
Traded shares	935,891	1,057,616	1,696,902
Turnover, million EUR	5.47	8.02	13.09
Market value, million EUR, as at the year-end	104.43	95.58	160.19

Structure of shareholders as of 31.12.2012

Number of shares	Number of shareholders	% of shareholders	Number of shares	% of shareholders
1 000 001 – ...	1	0.07%	12,742,686	71.99%
100 001 – 1 000 000	10	0.71%	3,079,937	17.40%
10 001 – 100 000	28	1.99%	845,449	4.77%
1001 – 10 000	236	16.79%	709,342	4.01%
101 – 1000	731	51.99%	300,686	1.70%
1 – 100	400	28.45%	21,900	0.13%
Total	1406	100%	17,700,000	100%

Performance of the share of Merko Ehitus and comparison index OMX Tallinn



Main shareholders of AS Merko Ehitus as of 31.12.2012 and change compared to the previous year:

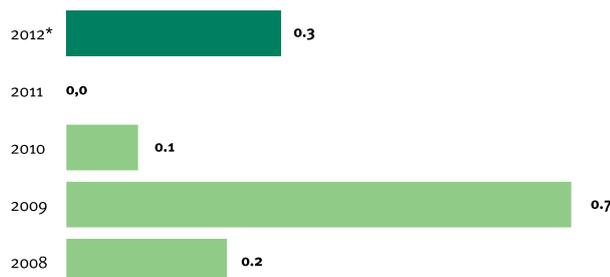
	Number of shares	% of total 31.12.2012	% of total 31.12.2011	Variance
AS Riverito	12,742,686	71.99	71.99	-
ING Luxembourg S.A., clients	974,126	5.50	5.50	-
Skandinaviska Enskilda Banken Ab, clients	896,864	5.07	4.39	+119,146
Firebird Republics Fund Ltd	302,395	1.71	0.79	+163,341
Gamma Holding OÜ	163,256	0.92	0.78	+25,299
State Street Bank and Trust Omnibus Account a Fund No OMO1	153,018	0.86	0.89	-3,700
SEB Elu- ja Pensionikindlustus AS	125,520	0.71	0.71	-
Skandinaviska Enskilda Banken Finnish clients	125,191	0.71	0.49	+37,800
Andersson Investeeringud OÜ	120,015	0.68	0.44	+41,442
AS Midas Invest	117,055	0.66	0.58	+14,250
Clearstream Banking Luxembourg S.A. clients	102,497	0.58	0.61	-4,833

Dividend policy

Distribution of dividends to the company's shareholders is recognised as a liability in the financial statements at the time when the payment of dividends is approved by the company's shareholders. Throughout the years, Merko Ehitus has attempted to distribute approximately 20% of the year's net profit as dividends to its shareholders. In some years, exceptions have been made in this policy. Over the last five years, the dividends have been paid to the shareholders for the respective periods as follows:

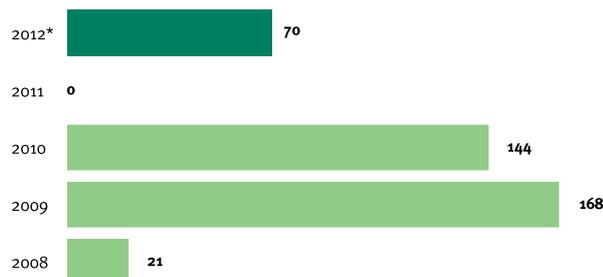
Dividend per share

EUR



Dividend rate

percentages



*according to proposal of the Management Board

*according to proposal of the Management Board

Information for shareholders

Annual General Meeting 2013

AS Merko Ehitus Annual General Meeting will be held on Wednesday, June 5th 2013 at 14.00 at the Arcturus conference hall of Nordic Hotel Forum (Viru square 3, Tallinn).

Agenda

1. Approval of the annual report of the year 2012 and overview of the economic results and the prospective of the on-going year
2. Proposal on distribution of profits
3. Recall of Supervisory Board member

Participation rights

The circle of shareholders, entitled for the participation in general meeting, will be determined as of May 29th 2013, at 23.59 o'clock.

Registration

Registration of participants of the meeting is about to be opened on June 5th 2013 at 13.30.

You're asked to submit the following for the registration of participants of the general meeting:

- Passport or ID document is required to identify natural persons-shareholders; a suitably prepared Proxy is also required of representatives;
- Representatives of a legal person-shareholders are required to provide an excerpt from an appropriate (business) register where the legal person is registered, which identifies the individual's right to represent the shareholder (legal representation) and passport or identification document of the representative; if the type of representation is other than legal representation, a suitably prepared Proxy must also be provided (authorities granted by transaction) and the representative's passport or identification document. You are kindly asked to legalise the registration documents of a legal person, registered in a foreign country (with the exception of unattested proxy) or have them apostilled, if not provided otherwise by an international treaty. AS Merko Ehitus may register shareholders, who are legal persons registered in a foreign country, as participants of general meeting, when all the required information on the legal person and representative concerned are given in a notarised proxy, issued to the representative in a foreign country, and the proxy is acceptable in Estonia.

A shareholder may notify AS Merko Ehitus of appointing a representative and having withdrawn a proxy before the general meeting, by supplying a digitally signed proxy and other required documents by e-mail to the following address: merko@merko.ee or delivering the written and signed documents on paper (proxy and other required documents) to the office of AS Merko Ehitus at Pärnu mnt 141 Delta Plaza 7th floor, Tallinn (on working days from 10.00 through 16.00) by June 4th 2013, 16.00, as latest, using the forms published by AS Merko Ehitus on its website at <http://www.merko.ee>. It is not possible to vote electronically or by mail at the general meeting.

Dividend

Supervisory Board proposes to pay the shareholders the total amount of EUR 5,310,000 as dividends from net profit brought forward, which totals to EUR 0.3 per share. Shareholders, entered into the share register of AS Merko Ehitus on June 26th 2013, at 23.59, will be entitled to dividends. Dividends will be paid to the shareholders on July 3rd 2013 by transferring the amount concerned to shareholder's bank account, linked to security account.

Documents

The annual report of AS Merko Ehitus for 2012 and the sworn auditor's report are available for inspection at the website of NASDAQ OMX Tallinn Stock Exchange at <http://www.nasdaqomxbaltic.com>.

Documents related to the regular meeting of shareholders of AS Merko Ehitus, including draft resolutions, annual report for the financial year 2012, sworn auditor's report and proposal for distribution of profits and written report, drawn up for the annual report by the Supervisory Board, are available for inspection as of May 13th 2013 at the website of AS Merko Ehitus at <http://www.merko.ee> or on working days at 10.00-16.00 at Pärnu mnt 141 Delta Plaza 7th floor, Tallinn. Questions concerning the agenda of the regular meeting can be asked by sending them to the e-mail address merko@merko.ee. Questions and answers will be disclosed at the website of AS Merko Ehitus on Internet.

Shareholders rights

Shareholders are entitled to be provided information concerning the business of AS Merko Ehitus from the Management Board at the regular meeting. The Management Board may refuse from giving the information, if there is a good reason to believe that this may cause material damage to the interests of the public limited company. Should the Management Board refuse from granting the information, the shareholder concerned may demand the regular meeting to adopt a decision, regarding the legitimacy of his/her demand, or file an application for proceedings on application to the court to demand the Management Board to supply the information.

Shareholders, holding shares, which represent at least 1/20 of the share capital of AS Merko Ehitus, may submit a draft resolution of each item on the agenda to the public limited company no later than 3 days prior to the general meeting, that is, until June 2nd 2013, submitting it in writing to the following address: AS Merko Ehitus, Pärnu mnt 141 Delta Plaza 7th floor, 11314 Tallinn.

Shareholders, holding shares, which represent at least 1/20 of the share capital of AS Merko Ehitus, may demand that additional items are added to the agenda of the general meeting, provided that such a request has been submitted in writing at least 15 days prior to the general meeting, that is, until May 21st 2013, to the following address: AS Merko Ehitus, Pärnu mnt 141 Delta Plaza 7th floor, 11314 Tallinn.

Important dates related to the Annual General Meeting

Shareholders, entitled for the participation in general meeting, will be determined as of: May 29th 2013, at 23.59

Registration of participants of the meeting is about to be opened on: June 5th 2013 at 13.30

Annual General Meeting: June 5th 2013 at 14.00

Dividend ex-date: June 21st 2013

Dividend record date: June 26th 2013 at 23.59

Dividend payment: July 3rd 2013

REPORT ON GOOD CORPORATE GOVERNANCE

CORPORATE GOVERNANCE AND STRUCTURE

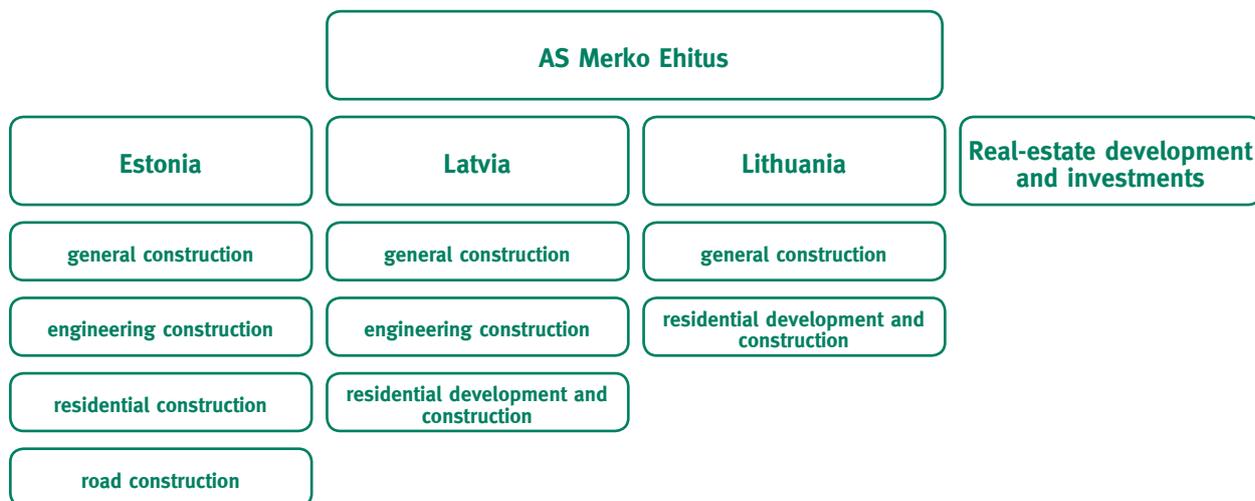
Adherence to the principles of Good Corporate Governance is part of the management of AS Merko Ehitus. Generally, this system is regulated by relevant legislation, the company's articles of association and the company's internal policies. Starting from 1 January 2006, issuers of shares listed on the NASDAX OMX Tallinn Stock Exchange are recommended to adhere to the principles of Good Corporate Governance approved by the Financial Supervisory Authority that covers good practices of enterprise management and treatment of shareholders. AS Merko Ehitus has followed these principles throughout 2012.

AS Merko Ehitus is dedicated to following high standards of corporate governance, for the implementation of which the Management Board and the Supervisory Board are responsible for shareholders. Our objective is to be transparent in our economic activity, in disclosing information and in relations with shareholders.

AS Merko Ehitus operates as a holding company whose companies in Estonia, Latvia and Lithuania offer complete solutions in the field of construction and real estate development. In the construction sector, the group's largest companies are AS Merko Ehitus Eesti (100%), SIA Merks (100%), UAB Merko Statyba (100%) and the companies belonging to the AS Merko Ehitus Eesti group: Tallinna Teede AS (100%) and AS Merko Infra (100%). The main activity of the holding company is the development and implementation of the strategies of Merko Ehitus group's separate business areas primarily through long-term planning of resources.

In connection with the review of the Lithuanian business strategy in the autumn 2012, the Supervisory Board of UAB Merko Statyba decided to end the implementation of water management projects on the Lithuanian market and focus on the field of general construction and apartment development.

Management structure of group's business areas as at 31 December 2012:



CHANGES IN THE LEGAL STRUCTURE OF THE GROUP

In the first quarter of 2012, a 100% subsidiary Merko Finland OY was registered in Finland with the aim of establishing technical preconditions for starting potential construction projects in Russia over the long term and as a result of an intra-group transaction Lithuanian subsidiaries UAB Balsiu Mokyklos SPV and UAB Merko Bustas were transferred to OÜ Merko Property and AS Merko Ehitus, respectively.

At 6 July 2012, AS Merko Ehitus transferred, in connection with review of its investment strategy, its 25% stake in the reinforced concrete element manufacturer AS TMB to the company management.

In connection with the revising of the Ukrainian market prospects, the Supervisory Board of AS Merko Ehitus approved, at 4 September 2012, the management's proposal for the initiation of the liquidation of the 100% subsidiary Merko Ukraine LLC. The company has no work-in-progress, contracts that needed to be served, or employees in Ukraine.

In October 2012, the shareholders of OÜ Unigate signed a notarized plan for a division under which registered immovable properties with natural conservation restrictions were separated from OÜ Unigate and distributed equally among the owners. AS Merko Ehitus founded two 100% subsidiaries in order to receive five immovables arising from the transaction: Väike-Paekalda OÜ and Suur-Paekalda OÜ.

In December 2012, a 100% subsidiary in Russia was founded and registered, OOO Lenko Stroi (registry code 1129847028288). The subsidiary was founded through the 100% Finnish subsidiary Merko Finland OY. The share capital of the new subsidiary is EUR 4,986. This was a technicality aimed at establishing a legal platform for operations in Russia. No actual business activity is currently taking place in Russia.

At 25 July 2012, SIA Merks acquired a 99.96% ownership interest in SIA Polystar, an entity that was part of the group of E.L.L. Kinnisvara AS. For acquisition of the registered immovable included within inventories, the share capital of SIA Polystar was increased by the prepayment in the amount of EUR 6.46 million made by SIA Merks to SIA Polystar in previous years. In the consolidated statement of financial position, the acquired registered immovable is carried in the amount of EUR 3.81 million after recognition of impairment losses in the amount of EUR 2.65 million for the prepayment made by SIA Merks in previous years. It is planned that SIA Polystar will be divided by separation in 2013 so that a 0.04% share that belongs to AS E.L.L. Kinnisvara will be transferred into a new entity and SIA Merks will wholly-own its subsidiary SIA Polystar. The planned restructuring will have no impact on the assets of the Merko Ehitus group.

CHANGES IN THE MANAGEMENT STRUCTURE OF AS MERKO EHITUS

As a result of the changes introduced in the company's management structure at the beginning of 2012, the Supervisory Board of AS Merko Ehitus resolved, at its meeting of 3 September 2012, to recall the Management Board member Alar Lagus from the Management Board of AS Merko Ehitus. Mr Lagus will continue serving as a member of the Management Board of AS Merko Ehitus Eesti, a 100% subsidiary of AS Merko Ehitus. The Management Board of the holding company will continue with two members: Andres Trink and Viktor Mõisja. The members of the Supervisory Board of the company are Toomas Annus as Chairman of the Supervisory Board and Tõnu Toomik, Teet Roopalu, Indrek Neivelt and Olari Taal as members.

GENERAL MEETING OF SHAREHOLDERS

The Company's highest governing body is the General Meeting of Shareholders, the authorities of which are regulated by legislation and the articles of association of the Company.

The annual general meeting of shareholders of AS Merko Ehitus held at 7 June 2012 approved the consolidated annual report for the financial year 2011, adopted a resolution on covering the loss and increase of mandatory reserve capital, amendment of the Articles of Association and approval of the auditor for the financial years 2012-2013. The Management Board made a presentation about the operating results of the company and outlooks.

In accordance with the Commercial Code, its Articles of Association and Good Governance Code, AS Merko Ehitus calls the annual and extraordinary general meeting of shareholders by notifying the shareholders through the Tallinn Stock Exchange and by publishing a meeting call in one national daily newspaper at least 3 weeks in advance. The general meeting shall be held at the place shown in the notice, on a working day and between 9 a.m. and 6 p.m., enabling most of the shareholders to participate in the General Meeting of Shareholders.

Before their publication, agendas at annual and extraordinary general meetings of the company's shareholders are approved by the Supervisory Board that shall also present to the general meeting subjects for discussion and voting. Agenda items of the general meeting, recommendations of the Supervisory Board with relevant explanations, procedural guidance for participation in the general meeting and how and when new agenda items can be proposed are published together with the notice on calling the general meeting.

General meetings can be attended by any shareholder or his or her authorised representative. AS Merko Ehitus does not allow participation in general meetings by means of communication equipment electronic since the deployment of reliable solutions for the identification of shareholders some of whom live abroad would be too complicated and costly. No picture taking or filming is allowed at the general meeting, because it may disturb the privacy of shareholders. Participation in the general meeting cannot be accomplished through the means of communication because there are no reliable ways to identify shareholders and to ensure the privacy of participating shareholders.

Annual and extraordinary general meeting of shareholders shall be chaired by an independent person. In 2012, the general meeting was chaired by attorney-at-law Vesse Võhma who introduced the procedure for conducting the general meeting and the procedure of asking questions from the Management Board and Supervisory Board about the company's activities.

On behalf of the company, usually the Chairman of the Management Board and the Chairman of the Supervisory Board shall participate in the General Meeting of AS Merko Ehitus, and if necessary, other members of the Management and Supervisory Boards shall be involved. If necessary, the company's auditor shall participate.

The annual general meeting of shareholders of AS Merko Ehitus held in 2012 was attended by Andres Trink (Chairman of the Management Board), Alar Lagus (member of the Management Board) and Toomas Annus (Chairman of the Supervisory Board).

SUPERVISORY BOARD

The Supervisory Board shall plan the activities of the company, organise the management of the company and supervise the activities of the Management Board. The Supervisory Board shall notify the general meeting of shareholders of the results of a review. According to the Articles of Association of Merko Ehitus, the Supervisory Board has 3 to 5 members who shall be elected for the term of three years.

At the annual general meeting of shareholders held at 28 June 2011, it was decided to extend the term of office of Supervisory Board members Tõnu Toomik, Teet Roopalu, Indrek Neivelt and Olari Taal until 28 June 2014, i.e. for three years and, in addition, to elect Toomas Annus as the additional member of the Supervisory Board of AS Merko Ehitus with a term of office until 28 June 2014. The Supervisory Board of AS Merko Ehitus has 5 members of whom, in accordance with the requirements of the Good Governance Code, two - Indrek Neivelt and Olari Taal - are independent members:

Toomas Annus (52)	Tõnu Toomik (52)	Teet Roopalu (63)
Chairman of the Supervisory Board	Member of the Supervisory Board	Member of the Supervisory Board
		
<p>Positions held:</p> <p>2011-... Merko Ehitus AS, Chairman of the SB. 2009-... E.L.L.Kinnisvara AS, Member of the MB. 2008-... Järvevana AS, Chairman of the MB. 1999-2009 E.L.L.Kinnisvara, Chairman of the SB. 1997-2008 Merko Ehitus AS, Chairman of the SB. 1996-... Riverito AS, Chairman of the MB. 1991-1996 EKE MRK, Chairman of the MB. 1989-1991 EKE MRK, director of the company.</p> <p>Education:</p> <p>Tallinn University of Technology, industrial and civil engineering. Tallinn Technical School of Building and Mechanics (TEMT; presently known as the University of Applied Sciences), industrial and civil engineering.</p> <p>Number of shares: 8,322,914</p>	<p>Positions held:</p> <p>2011-... Merko Ehitus AS, Member of the SB. 2008-2011 Merko Ehitus AS, Chairman of the SB. 1997-2008 Merko Ehitus AS, Chairman of the MB. 1993-1997 Merko Ehitus AS, Project Manager. Member of Supervisory Boards of the group's subsidiaries and associated companies.</p> <p>Education:</p> <p>Tallinn University of Technology industrial and civil engineering.</p> <p>Number of shares: 1,607,185</p>	<p>Positions held:</p> <p>2004-... Merko Ehitus AS, Member of the SB. 2010-... Riverito AS, Member of the MB. 2002-2004 Merko Ehitus AS, Adviser to the MB. Has worked for different construction companies, including as a director of finance. Has been in charge of economic activities in the EKE (Estonian Collective Farm Construction) as a chief economist; worked as a bank director; and has also worked in building design. Member of Supervisory Boards of subsidiaries and associated companies.</p> <p>Education:</p> <p>Tallinn University of Technology construction economics and organisation.</p> <p>Number of shares: –</p>
Indrek Neivelt (46)	Olari Taal (59)	
Member of the Supervisory Board	Member of the Supervisory Board	
		
<p>Positions held:</p> <p>2008-... Merko Ehitus AS, Member of the SB. 2005-... Bank Saint Petersburg, Chairman of the SB. 1999-2005 Hansabank, Director General of the Group, Chairman of the MB. 1991-1999 Hansabank, various positions. Belongs to Supervisory Boards of various companies.</p> <p>Education:</p> <p>Tallinn University of Technology civil engineering economics and management. Stockholm University, banking and finance, MBA.</p> <p>Number of shares: 31,635</p>	<p>Positions held:</p> <p>2008-... Merko Ehitus AS, Member of the SB. Has been the head of the Tartu Elamuehituskombinaat (Tartu Housing Plant; Tartu Maja) and Eesti Hoiupank (Estonian Savings Bank). Has served the Republic of Estonia as Minister of Construction, Minister of Economic Affairs, Minister of the Interior and as a Member of the 10th Riigikogu (Parliament of Estonia).</p> <p>Education:</p> <p>Tallinn University of Technology, civil engineering.</p> <p>Number of shares: 2,500</p>	

SB – Supervisory Board.
MB – Management Board.

The meetings of the Supervisory Board generally take place once a month, except in summer months. In 2012, the Supervisory Board held 15 regular meetings. No extraordinary Supervisory Board meetings were held. Participation of members of the Supervisory Board at meetings:

Name	Participation in meetings	Participation %
Toomas Annus	14	93%
Teet Roopalu	13	87%
Tõnu Toomik	13	87%
Indrek Neivelt	14	93%
Olari Taal	14	93%

The Supervisory Board fulfilled all its obligations laid down in legal acts. The Supervisory Board has set up an audit committee as its work body. The Supervisory Board has not considered it necessary to set up a remuneration committee or appointment committee. Remuneration of the members of the Supervisory Board is approved by the general meeting of shareholders. The valid procedure for remuneration of Supervisory Board members was approved by the general meeting of shareholders held at 31 October 2008.

No termination benefits are paid to the members of the Supervisory Board upon the termination or non-extension of the contract. In 2012 and 2011 financial years, the members of the Supervisory Board were remunerated as follows (in euros):

Name	2012	2011
Toomas Annus*	42,182	21,091
Tõnu Toomik*	38,347	40,264
Teet Roopalu	38,347	38,347
Indrek Neivelt	38,347	38,347
Olari Taal	38,347	38,347
Total	195,570	176,396

*Toomas Annus has been the Chairman of the Supervisory Board since 28 June 2011. Until that date, the responsibilities of the Chairman of the Supervisory Board were fulfilled by Tõnu Toomik.

Remuneration, less the statutory taxes, to the members of the Supervisory Board is paid on a monthly basis.

MANAGEMENT BOARD

The Management Board is a governing body which represents and manages AS Merko Ehitus in its daily activities in accordance with the law and the Articles of Association. The Management Board has to act in the most economically purposeful manner, taking into consideration the best interests of all shareholders and ensures the company's sustainable development in accordance with set objectives and strategy.

To ensure that the company's interests are met in the best way possible, the Management and Supervisory Boards shall extensively collaborate. At least once a month, a joint meeting of the members of the Supervisory and Management Boards shall take place, in which the Management Board shall inform the Supervisory Board of significant issues regarding the company's business operations, the fulfilment of the company's short and long-term goals and the risks impacting them. For every meeting of the Supervisory Board, the Management Board shall prepare a management report and submit it well in advance of the meeting so that the Supervisory Board can study it. The Management Board prepares reports for the Supervisory Board also in between the meetings, if it is considered necessary by the Supervisory Board or its Chairman.

Pursuant to the Articles of Association approved at the general meeting of shareholders in 2012, the Management Board may have up to three members. From 01.01.2012, the Management Board of AS Merko Ehitus had 3 members: the Chairman of the Management Board is Andres Trink, the members of the Management Board are Viktor Mõisja and Alar Lagus (until 31 December 2011: 6 members). After the structural change which became effective at 1 January 2012, five members of the Management Board of AS Merko Ehitus started to work as members of the Management Board of AS Merko Ehitus Eesti and no compensation was paid to them.

Starting from 3 September 2012, the Management Board of AS Merko Ehitus has 2 members: Andres Trink (Chairman of the Management Board) and Viktor Mõisja (member of the Management Board).

Andres Trink (46)	Viktor Mõisja (62)
Chairman of the Management Board Appointed: 1 January 2012. Term ends: 31 December 2014.	Member of the Management Board Appointed: 21 December 2010. Term ends: 20 December 2013.
	
<p>Positions held: 2012-... Merko Ehitus AS, Chairman of the Management Board. Chairman of the Supervisory Board of Merko Ehitus Eesti AS and SIA Merks and Member of the Supervisory Board of UAB Merko Statyba. Has held various executive positions in the private and public sector. Before being hired at Merko Ehitus, worked for 15 years in the financial sector, including as a member of the Management Board of Baltic banking at Hansabank (now Swedbank).</p> <p>Education: Tallinn University of Technology, automated management systems engineering (summa cum laude) Estonian Business School, international business administration Graduate of the INSEAD University (France), executive management programme.</p> <p>Number of shares: –</p>	<p>Positions held: 2010-... Merko Ehitus AS, Member of the Management Board. Works for Merko Ehitus since 1991 as a foreman, site manager and, since 2001, head of concrete work department.</p> <p>Education: Tallinn University of Technology, heating and gas supply and ventilation.</p> <p>Number of shares: 1,103,734</p>

The responsibilities of Andres Trink, Chairman of the Management Board, include, among others, fulfilling daily obligations of the CEO of AS Merko Ehitus, managing and representing for the company, ensuring compliance with the Articles of Association, legal acts, organising the work of the Management Board and supervisory boards of the more important subsidiaries, coordinating the development of strategies and providing for their implementation.

The area of responsibility of Viktor Mõisja is quality management and supervision.

Members of the Management Board have entered three-year contracts of service with the company. The procedure and principles of remuneration of Management Board members are approved by the Supervisory Board. The members of the Management Board are paid a fee for fulfilling their official duties. Bonuses payable to the Management Board depend on the fulfilment of the targets of the given financial year by the group and the Management Board. The members of the Management Board are paid bonuses once a year based on the fulfilment of the targets of the previous financial year.

Fees paid to the members of the Management Board in the financial year 2012 totalled EUR 186 thousand (financial year 2011: EUR 318 thousand). The two Management Board members of AS Merko Ehitus have different rates of severance compensation for up to 12 months of service fee.

SUPERVISORY AND MANAGEMENT BOARDS OF SUBSIDIARIES

Authorisation and responsibility of supervisory boards of subsidiaries of AS Merko Ehitus are based on their Articles of Association and intergroup rules. Generally, Supervisory Boards of subsidiaries consist of members of the Management Board or Supervisory Board of the company that is the main shareholder of the specific subsidiary. Supervisory Board meetings of the most significant subsidiaries are held usually once a month, otherwise according to the group's needs, Articles of Association of subsidiaries and legal provisions. Generally, no separate fee is paid to members of the Supervisory Board of subsidiaries. Members of the Supervisory Board will also receive no termination benefit in case their contract of service is terminated before due date or not extended.

The chairman or member of the Management Board of the subsidiary shall be named by the subsidiary's Supervisory Board. Below are the supervisory boards and management boards of the most significant subsidiaries that are wholly-owned by AS Merko Ehitus:

Company	Supervisory Board	Management Board
AS Merko Ehitus Eesti	Andres Trink (Chairman), Teet Roopalu, Tõnu Toomik, Taavi Ojala	Tiit Roben (Chairman), Andres Agukas, Jaan Mäe, Alar Lagus, Veljo Viitmann
AS Merko Infra	-	Tarmo Pohlak, Arno Elias
Tallinna Teede AS	Tiit Roben (Chairman), Andres Agukas, Alar Lagus	Jüri Läll (Chairman), Richard Viies, Jüri Helila
SIA Merks	Andres Trink (Chairman), Tõnu Toomik, Jaan Mäe, Ivars Geidāns	Oskars Ozoliņš (Chairman), Jānis Šperbergs
UAB Merko Statyba	Gediminas Tursa (Chairman), Andres Trink, Tõnu Toomik, Jaan Mäe	Saulius Putrimas (Chairman), Jaanus Rāstas

At its meeting held at 29 March 2012, the Supervisory Board of UAB Merko Statyba, wholly-owned subsidiary of AS Merko Ehitus, decided to approve changes in the company's management, by which General Manager Gediminas Tursa was named the chairman of the company's Supervisory Board. Andres Trink, Jaan Mäe and Tõnu Toomik continue as members of the company's supervisory board. Financial Manager Saulius Putrimas was named the company's new General Manager. The changes were made in the framework of the group's efficiency program and in connection with the need to adjust the company's management model in a better way to the strategic objectives on the Lithuanian market.

The changes introduced in the management of SIA Merks, the Latvian-based subsidiary of AS Merko Ehitus, took effect in September 2012, with the former Chairman of the Management Board Ivars Geidāns being appointed a member of the Supervisory Board of SIA Merks, and the former CFO Oskars Ozoliņš the Chairman of the Management Board of SIA Merks. The Management Board of SIA Merks will continue with two members: Oskars Ozoliņš as the chairman and construction director Jānis Šperbergs as member of the Management Board. The company's Supervisory Board will continue with Andres Trink serving as the chairman, and Tõnu Toomik, Jaan Mäe and Ivars Geidāns as members.

AUDIT COMMITTEE

The responsibility of the audit committee is advising the Supervisory Board in supervision related issues. The Committee executes supervision in the areas at: a) arrangement of accounting, b) preparation and approval of the financial budget and reports, c) management of financial risks, d) performance of external audit, e) functioning of an internal control system and f) legality of the activities.

As at 10 January 2011, the company's Supervisory Board set up a 3-member audit committee and appointed Indrek Neivelt and Olari Taal as its members and Teet Roopalu as its Chairman. A member of the committee is elected for a term of three years, but at the decision of the Supervisory Board, a member of the committee may be recalled before the expiration of their term of office.

Members of the auditing committee are not separately remunerated.

CONFLICT OF INTERESTS AND HANDLING OF INSIDER INFORMATION

It is important to appropriately handle insider information in order to protect shareholders' interest and ensure honest and fair trading of shares. Significant information about AS Merko Ehitus and its subsidiaries must be available in a timely, consistent and equal manner for all shareholders and potential new shareholders. It is inevitable that persons related to AS Merko Ehitus and its subsidiaries have, because of their job, at certain times and in certain cases more information about the group than investors and the public. To prevent the misuse of such information, we have adopted internal rules in the group's companies on maintaining and publication of insider information and on making transactions on the basis of insider information (hereinafter: insider information rules). Insider information rules include a reporting system under which employees who may develop a conflict of interest when fulfilling their job duties are required to disclose their economic interests and confirm their independence by self-assessment.

The members of the Management and Supervisory Board of AS Merko Ehitus are users of insider information (so-called insiders). They have signed a relevant statement, are aware of insider information rules of AS Merko Ehitus and together with people connected with them are registered in the list of the company's insiders. Moreover, the list of insiders includes the financial employees of the parent company who have access to the group's consolidated operating results as well as members of the Management and Supervisory Boards of the more important subsidiaries together with the employees who are responsible for preparing and presenting accounting information.

To the best of our knowledge, in the financial year 2012 there were no cases of any misuse of insider information or conflicts of interest. No transactions with related parties were made at other than market terms. No members of the company's supervisory or management board hold shares in an entity that operates in the code business area of AS Merko Ehitus – construction sector.

DISCLOSURE OF INFORMATION

In disclosing information, AS Merko Ehitus shall follow the rules and regulations of NASDAQ OMX Tallinn Stock Exchange and immediately disclose important information regarding the company's activities to the shareholders after obtaining reasonable assurance as to its correctness and that the disclosure of such information shall not harm the interests of the company and its business partners. In respect of construction contracts entered into, contracts with the volume of EUR 5 million and higher shall be disclosed separately in stock exchange releases provided they do not include contractual restrictions on publication of confidential information. Important information shall be disclosed through the stock exchange system and on the company's Web site. In 2012, we published 26 stock exchange releases through the stock exchange system.

Number of releases	Content of release
7	New construction contracts
6	Economic results
5	Changes in structure and management
2	General meeting
2	Extraordinary notices regarding discount of registered immovable properties and court decision in criminal case 1-09-20251
1	Legal requirement regarding information publicly disclosed by AS Merko Ehitus
3	Preliminary notices regarding time of publication of economic results

In 2013, we will publish consolidated interim reports as follows:

Week	Dated	Event
19 (2013)	06.05 – 10.05	2013 3 months and I quarter unaudited interim report
32 (2013)	05.08 – 09.08	2013 6 months and II quarter unaudited interim report
45 (2013)	04.11 – 08.11	2013 9 months and III quarter unaudited interim report
7 (2014)	10.02 – 14.02	2013 12 months and IV quarter unaudited interim report

Merko Ehitus generally informs the stock exchange about publishing interim financial statements and the annual report at least two days prior to their disclosure. Reports are published after the end of the trading day. Operating results of subsidiaries are not generally published, but they can be obtained, if necessary, from AS Merko Ehitus or the Commercial Registry (<https://ariregister.rik.ee>).

Our objective is to support fair pricing of Merko shares through constant and continued distribution of information to all market operators. Moreover, our objective is to maintain the loyalty of existing shareholders towards the company and to create interest in new shareholders and analysts.

It is our responsibility to prepare quarterly and annual reports, stock exchange releases and presentation and to plan and organise investor meetings with shareholders and analysts. We also collect and analyse feedback from investors and analysts in order to increase the value of information to be disclosed.

The company shall not hold meetings with analysts or presentations for investors immediately before the dates of disclosure of financial reporting (interim reports, annual report). AS Merko Ehitus communicates regularly with its larger shareholders and potential investors and, if requested, holds meetings. The information presented in these meetings is public, i.e. available from the company's reports, website or other public sources. We carefully monitor insider information rules during these meetings.

For informing the company's shareholders an annual general meeting of shareholders is called at least once a year where all shareholders can ask questions from members of the company's Management Board and Supervisory Board.

The main analysts who cover AS Merko Ehitus are:

Swedbank AS

Liivalaia 8 Tallinn, 15040 Estonia
Phone: +372 631 0310
e-mail: info@swedbank.ee
www.swedbank.ee

SEB Enskilda

Tornimäe 2, Tallinn, 15010 Estonia
Phone: +372 665 5100
e-mail: info@seb.ee
www.seb.ee

AS LHV Pank

Tartu mnt 2 Tallinn, 10145 Estonia
Phone: +372 680 0457
e-mail: research@lhv.ee
www.lhv.ee

Information on investor relations of AS Merko Ehitus is available from:

Andres Trink

Chairman of the Management Board
Phone: +372 650 1250
Fax: +372 650 1251
andres.trink@merko.ee

Signe Kukin

Group CFO
Phone: +372 650 1250
Fax: +372 650 1251
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AS Merko Ehitus

Delta Plaza, 7th floor
Pärnu mnt 141 11314 Tallinn
Phone: +372 650 1250
www.merko.ee

REPORTING AND FINANCIAL AUDIT

Availability of adequate and timely information is the basis for obtaining quality management decisions. It is important to ensure that reporting is factual, but also forward-looking. This will enable to manage, to the best of one's knowledge, risks and, in competition with other market operators, turn them into opportunities. The company's reporting can be roughly divided into: a) financial reporting and b) management reporting.

Financial reporting consists of interim reports of consolidated economic indicators and annual reports of companies that belong to the AS Merko Ehitus group, that are made public through the stock exchange system of NASDAQ OMX Tallinn and that are available to all shareholders, potential investors and analysts covering the company.

On the other hand, management reporting is meant for the company's internal use. It is appropriate to separate reporting on various operating indicators that focuses on the performance of business segments and different group companies as well as return on equity. Management reporting includes budgets and forecasts that AS Merko Ehitus does not disclose.

Financial audits are conducted on the basis of International Standards on Auditing. The auditor of AS Merko Ehitus is approved by the general meeting of shareholders. The selection process is managed by the Supervisory Board and its findings are presented to the general meeting for approval. As a result of the tender and with the resolution made by the general meeting in 2012, the financial auditor for annual reports 2012-2013 is AS PricewaterhouseCoopers (PwC). Auditors authorised to sign the report differ, depending on the country of residence. Chartered auditor Ago Vilu is responsible for the consolidated audit report.

AS Merko Ehitus considers it important to ensure independence of the financial auditor and to avoid of conflicts of interest. In 2012, PwC did not perform to AS Merko Ehitus services that could have affected the independence of the auditor. We find that the financial audit was conducted in 2012 in compliance with regulative acts, international standards and expectations.

DECLARATION OF CONFORMITY TO RECOMMENDATIONS OF GOOD GOVERNANCE CODE

The CGC principles are recommended to the publicly traded companies and the entities are free to decide whether to follow the main CGC principles or not. The Corporate Governance Code is based on the principle of follow or explain according to which an entity shall explain its standpoints and activities with regard to those CGC provisions which it does not follow.

We have assessed the structure and functions of the management of AS Merko Ehitus on the basis of Good Governance Code. Above we have described significant components of corporate governance. Having assessed the compliance of the structure and functioning of the company's management system, we find that our organisation and activities are in significant part in compliance with the Good Governance Code. Also, our activities comply with the Estonian legislation that regulates several principles provided in the code in more detail. AS Merko Ehitus has not followed some recommendations that are provided below with the explanation why the company is not following them at the present:

Corporate Governance Recommendations	Explanations by Management Board and Supervisory Board
<p>2.2.7 Basic wages, performance pay, severance packages, other payable benefits and bonus schemes of a Management Board member as well as their essential features (incl. features based on comparison, incentives and risk) shall be published in clear and unambiguous form on website of the Issuer and in the Corporate Governance Recommendations Report. Information published shall be deemed clear and unambiguous if it directly expresses the amount of expense to the Issuer or the amount of foreseeable expense as of the day of disclosure.</p>	<p>The company publishes in its annual report the total amount of remuneration and bonuses paid to members of the Management Board, as it believes that public disclosure of personal income does not create value added for shareholders, but does violate the privacy of members of the Management Board.</p>
<p>5.6 The Issuer shall disclose the dates and places of meetings with analysts and presentations and press conferences organized for analysts, investors or institutional investors on its website. The Issuer shall allow the shareholders to take part in the said events and make presentations available on its website.</p>	<p>The company has published contact details on its website and in its reports, allowing all shareholders to request a meeting with company representatives. The information presented at the meetings is public, i.e. available from the company's reports, website or other public channels. At these meetings, the company shall not dispense additional information that it has not previously sent to all shareholders.</p> <p>In our opinion, the public disclosure of the schedule of meetings does not give shareholders material additional information and thus the information shall not be disclosed.</p>
<p>6.2.1 The Supervisory Board shall describe in its evaluation report regarding the auditor's activity, inter alia, the services (including advisory services) that the auditor has provided to the Issuer during the preceding year or shall provide during the next year. Also the remuneration the Issuer has paid or shall pay to the auditor shall be published.</p>	<p>AS Merko Ehitus does not publicly disclose the fee for performing financial audits, as we believe it could impair results of tenders in future periods and thereby result in economic harm for the company.</p>

MANAGEMENT DECLARATION

The Management Board declares and confirms that according to their best knowledge, the year 2012 annual accounts, prepared in accordance with International Financial Reporting Standards as adopted by European Union, present a correct and fair view of the assets, liabilities, financial situation and loss or profit of AS Merko Ehitus and the undertakings involved in the consolidation as a whole, and the management report gives a true and fair view of the development and results of the business activities and financial status of AS Merko Ehitus and the undertakings involved in the consolidation as a whole and contains a description of the main risks and doubts.

Andres Trink

Chairman of the
Management Board



28.03.2013

Viktor Mõisja

Member of the
Management Board



28.03.2013

FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

in thousands of euros

	Note	2012	2011
Revenue	3	249,131	219,322
Cost of goods sold	4	(231,220)	(222,928)
Gross profit (-loss)		17,911	(3,606)
Marketing expenses	5	(2,107)	(2,104)
General and administrative expenses	6	(9,173)	(7,910)
Other operating income	7	2,961	2,580
Other operating expenses	8	(834)	(1,308)
Operating profit (-loss)		8,758	(12,348)
Finance income	9	184	594
Finance costs	10	(1,203)	(1,161)
Profit (-loss) from associates and joint ventures	20	163	(1,120)
Profit (-loss) before tax		7,902	(14,035)
Corporate income tax expense	11	(289)	(121)
Net profit (-loss) for financial year		7,613	(14,156)
incl. net profit (-loss) attributable to equity holders of the parent		7,627	(14,084)
net profit (-loss) attributable to non-controlling interest		(14)	(72)
Other comprehensive income			
Currency translation differences of foreign entities		58	354
Comprehensive income (-loss) for the period		7,671	(13,802)
incl. net profit (-loss) attributable to equity holders of the parent		7,685	(13,730)
net profit (-loss) attributable to non-controlling interest		(14)	(72)
Earnings per share for profit (-loss) attributable to equity holders of the parent (basic and diluted, in EUR)	12	0.43	(0.80)

The notes set out on pages 53-98 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	Note	31.12.2012	31.12.2011
ASSETS			
Current assets			
Cash and cash equivalents	14	35,316	18,510
Short-term deposits	15	-	140
Trade and other receivables	16	60,343	64,449
Prepaid corporate income tax		478	686
Inventories	18	82,830	87,834
Total current assets		178,967	171,619
Non-current assets			
Investments in associates and joint ventures	20	7,190	9,986
Other long-term loans and receivables	21	17,188	17,065
Deferred income tax assets	22	1,919	1,870
Investment property	23	3,566	2,313
Property, plant and equipment	24	14,853	16,057
Intangible assets	25	1,365	1,427
Total non-current assets		46,081	48,718
TOTAL ASSETS		225,048	220,337
LIABILITIES			
Current liabilities			
Borrowings	27	16,299	16,574
Payables and prepayments	28	63,209	61,635
Short-term provisions	29	6,165	6,781
Total current liabilities		85,673	84,990
Non-current liabilities			
Long-term borrowings	27	19,205	23,764
Deferred income tax liability	22	327	131
Other long-term payables	30	1,576	856
Total non-current liabilities		21,108	24,751
TOTAL LIABILITIES		106,781	109,741
EQUITY			
Non-controlling interests		1,342	1,356
Equity attributable to equity holders of the parent			
Share capital	32	12,000	12,000
Statutory reserve capital		1,200	1,131
Currency translation differences		(512)	(570)
Retained earnings		104,237	96,679
Total equity attributable to equity holders of the parent		116,925	109,240
TOTAL EQUITY		118,267	110,596
TOTAL LIABILITIES AND EQUITY		225,048	220,337

The notes set out on pages 53-98 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

in thousands of euros

	Equity attributable to equity holders of the parent					Non-controlling interest	Total
	Share capital	Statutory reserve capital	Currency translation differences	Retained earnings/accumulated losses	Total		
Balance as at 31.12.2010	11,312	1,131	(924)	113,221	124,740	1,428	126,168
Profit (loss) for the financial year	-	-	-	(14,084)	(14,084)	(72)	(14,156)
Other comprehensive income	-	-	354	-	354	-	354
Total comprehensive income (loss) for the financial year	-	-	354	(14,084)	(13,730)	(72)	(13,802)
Bonus issue	688	-	-	(688)	-	-	-
Dividends	-	-	-	(1,770)	(1,770)	-	(1,770)
Total transactions with owners	688	-	-	(2,458)	(1,770)	-	(1,770)
Balance as at 31.12.2011	12,000	1,131	(570)	96,679	109,240	1,356	110,596
Balance as at 31.12.2011	12,000	1,131	(570)	96,679	109,240	1,356	110,596
Profit (loss) for the financial year	-	-	-	7,627	7,627	(14)	7,613
Other comprehensive income	-	-	58	-	58	-	58
Total comprehensive income (loss) for the financial year	-	-	58	7,627	7,685	(14)	7,671
Transfer to statutory reserve capital	-	69	-	(69)	-	-	-
Balance as at 31.12.2012	12,000	1,200	(512)	104,237	116,925	1,342	118,267

The notes set out on pages 53-98 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

in thousands of euros

	Note	2012	2011
Cash flows from (used in) operating activities			
Operating profit		8,758	(12,348)
Adjustments:			
Depreciation	23-25	2,608	2,242
(Profit)/loss from sale of non-current assets	7	(123)	(722)
Change in receivables and liabilities related to construction contracts recognised under the stage of completion method	33	(729)	3,979
Interest income from business activities	7	(2,173)	(1,419)
Change in provisions	29, 30	1,974	2,931
Change in trade and other receivables related to operating activities		7,334	(24,993)
Change in inventories	18	5,420	8,146
Change in trade and other payables related to operating activities		(3,039)	15,755
Interest received	9, 16	1,953	758
Interest paid	10, 28	(1,281)	(1,208)
Other finance income and costs	9, 10	90	(18)
Corporate income tax (paid)/reclaimed		209	688
Total cash flows from (used in) operating activities		21,001	(6,209)
Cash flows from investing activities			
Proceeds from sale of associates	20	2,750	-
Purchase/proceeds from deposits with maturities greater than 3 months	15	140	2,511
Purchase and receipt of long-term deposits	21	131	-
Purchase of investment property	23	(1,463)	(3,648)
Proceeds from sale of investment property	7, 23	-	3,334
Purchase of property, plant and equipment	24, 28	(890)	(1,008)
Proceeds from sale of property, plant and equipment	7, 24	186	1,426
Purchase of intangible assets	25	(23)	(64)
Proceeds from sale of intangible assets	7, 25	-	3
Interest received	9, 16	14	22
Dividends received	20	88	59
Total cash flows from investing activities		933	2,635
Cash flows from (used in) financing activities			
Proceeds from borrowings	27	12,974	20,995
Repayments of borrowings	27	(18,640)	(5,484)
Factoring	27	1,544	-
Sale-leaseback under finance lease terms		-	65
Finance lease principal payments	27	(902)	(1,747)
Dividends paid	13	-	(1,770)
Total cash flows from (used in) financing activities		(5,024)	12,059
Net increase/decrease in cash and cash equivalents		16,910	8,485
Change in deposits with maturities greater than 3 months	15	(140)	(2,511)
Total change		16,770	5,974
Cash and cash equivalents at the beginning of the period	14	18,510	9,856
Deposits with maturities greater than 3 months at the beginning of the period	15	140	2,651
Total at the beginning of the period		18,650	12,507
Effect of exchange rate changes		(104)	169
Cash and cash equivalents at the end of the period	14	35,316	18,510
Deposits with maturities greater than 3 months at the end of period	15	-	140
Total at the end of the period		35,316	18,650

The notes set out on pages 53-98 are an integral part of these consolidated financial statements.

NOTES

Note 1 Summary of significant accounting policies

1.1. General information

The consolidated financial statements of AS Merko Ehitus (hereinafter the parent) and its subsidiaries (hereinafter the group) for the financial year ended 31 December 2012 were signed by the Management Board at 28 March 2013.

Pursuant to the Commercial Code of the Republic of Estonia, the annual report prepared by the Management Board and approved by the Supervisory Board and which also includes the consolidated financial statements shall be approved at the General Meeting of Shareholders. Shareholders have the right not to approve the annual report prepared and presented by the Management Board and require preparation of a new annual report.

AS Merko Ehitus is a corporation registered in the Republic of Estonia (Commercial Register no.: 11520257, address: Järvevana tee 9G, Tallinn) and it operates mainly in Estonia, Latvia and Lithuania. Its main activities are construction and real estate development.

From 22 July 1997, the shares of AS Merko Ehitus are listed on NASDAQ OMX Tallinn Stock Exchange. As at 31 December 2012, the majority shareholder AS Riverito owned 71.99% of the Company's shares through which the ultimate controlling person is Toomas Annus.

AS Merko Ehitus was established in the demerger of the former AS Merko Ehitus, currently AS Järvevana, as a result of which all operating areas, i.e. all assets and liabilities other than the liabilities related to the criminal proceeding, were transferred to the new entity.

From 1 January 2012, the group's construction operations in Estonia were transferred to AS Merko Ehitus Eesti. Thereafter, AS Merko Ehitus operates as a holding entity with no independent production activities. It has 100% ownership interests in construction entities in Estonia, Latvia and Lithuania and a real estate development unit consisting of entities holding real estate properties.

1.2. Bases for preparation of the consolidated financial statements

The consolidated financial statements of Merko Ehitus group have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

The consolidated financial statements have been prepared under the historical cost convention.

Several financial figures are based on management's estimates, including for example, assessment of profitability of construction contracts using the stage of completion method, assessment of the useful lives of items of property, plant and equipment, estimation of allowances for receivables and inventories, recognition of provisions for warranty obligations. Management's estimates have been made to the best of its knowledge, but they may not be accurate. The effect of changes in accounting estimates is reported in the financial statements of the period in which the change occurred.

Assets and liabilities are classified as current and non-current in statement of financial position. Current assets include assets that are expected to be used within the next financial year. Current liabilities include liabilities the due date of which is within 12 months after the balance sheet date. The remaining assets and liabilities are classified as non-current.

Expenses are classified according to their function in the income statement.

Items included in the financial statements of Merko Ehitus group entities are measured using the currency of their primary economic environment (the functional currency): the euro, Latvian lats and the Lithuanian litas. The consolidated financial statements are presented in euros. The primary financial statements and notes are presented in thousands of euros.

1.3. New International Financial Reporting Standards, amendments to published standards and interpretations of the International Financial Reporting Interpretations Committee (IFRIC)

a. Adoption of New or Revised Standards and Interpretations

New or revised standards or interpretations that are effective for the first time for the group for the financial year beginning on or after 1 January 2012 are not expected to have a material impact to the group.

b. New Accounting Pronouncements

The issued new or revised standards and interpretations that are mandatory for the group's annual periods beginning on or after 1 January 2013, and which the group has not adopted early.

IFRS 12, Disclosure of Interest in Other Entities, effective for annual periods beginning on or after 1 January 2013; not yet adopted by the EU. The standard applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. It replaces the disclosure requirements currently found in IAS 28 "Investments in associates". IFRS 12 requires entities to disclose information that helps financial statement readers to evaluate the nature, risks and financial effects associated with the entity's interests in subsidiaries, associates, joint arrangements and unconsolidated structured entities. To meet these objectives, the new standard requires disclosures in a number of areas, including (i) significant judgements and assumptions made in determining whether an entity controls, jointly controls, or significantly influences its interests in other entities, (ii) extended disclosures on the share of non-controlling interests in group activities and cash flows, (iii) summarised financial information of subsidiaries with material non-controlling interests, and (iv) detailed disclosures of interests in unconsolidated structured entities. The group is currently assessing the impact of the standard on its financial statements.

The other new or amended standards or interpretations, which are not yet effective, are not expected to have a material impact on the group.

1.4. Consolidation

Subsidiaries, i.e. entities that are either directly or indirectly controlled by the parent AS Merko Ehitus through fellow subsidiaries, have been consolidated on a line-by-line basis in the consolidated financial statements. Control exists when the parent owns more than one half of the voting power of the subsidiary or otherwise has power to govern the operating and financial policies of the other entity. Subsidiaries are fully consolidated in the financial statements of the group from the date of acquiring control until the date at which control ceases.

Upon consolidation, intra-group receivables and liabilities, income and expenses as well as unrealised profits and losses arising from intra-group transactions have been eliminated unless a loss is caused by impairment.

Group entities use uniform accounting policies.

1.5. Business combinations

The group uses the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are initially measured at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the group makes an election whether to recognise any non-controlling interest in the acquiree at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. From the date of acquisition, the revenue and expenses of the acquired entity are reported in the income statement of the group and goodwill is reported in the statement of financial position of the group.

The excess of the consideration transferred, the amount of any non-controlling interests in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the group's share of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the statement of comprehensive income.

Goodwill is subsequently measured at its cost less any impairment losses. Goodwill arising in a business combination is not amortised. Instead, an impairment test is carried out once a year. Goodwill is written down to its recoverable amount if the carrying amount is not recoverable (Note 1.11).

If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Transactions with non-controlling interests

The group treats transactions with non-controlling interests as transactions with equity owners of the group starting from 1 January 2010. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share

acquired of the carrying amount of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

1.6. Associates

Associates are all entities in which the group has significant influence but not control over their operating and financial policies. Significant influence is presumed to exist when the parent owns between 20% and 50% of the voting rights. Investments in associates are initially recognised at cost and subsequently measured using the equity method of accounting. Investments in associates include goodwill identified on acquisition.

The group's share of its associates' post-acquisition profits or losses is recognised in the group's income statement, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the group's share of losses in an associate equals or exceeds its interest in the associate, the group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the group and its associates are eliminated to the extent of the group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. The accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the group.

1.7. Joint ventures

A joint venture is a contractual arrangement whereby two or more parties undertake an economic activity that is subject to common control. Joint ventures are accounted for under the equity method. A holding in a jointly controlled entity is initially recognised at cost and subsequently adjusted for the post-acquisition changes that have occurred in the group's share of the net assets under common control. The income statement of the group includes the group's share in the profits or losses of the entity under common control. Unrealised gains and losses from transactions between the group and its joint ventures are eliminated similarly to transactions with associates (Note 1.6).

1.8. Jointly controlled operations

Under IAS 31 *Interests in Joint Ventures*, jointly controlled operations are joint operations with third parties, whereby the assets and other resources of venturers are used without the establishment of a new entity or another unit or creation of a separate financial structure. Each venturer uses its own property, plant and equipment and carries its own inventories in the statement of financial position. The venturer also incurs its own expenses and liabilities and raises its own funds which represent its own obligations. In respect of its interest in jointly controlled operations, a venturer recognises in its financial statements:

- the assets that it controls and the liabilities that it incurs;
- the expenses that it incurs and its share of revenue that it earns from the sale of goods or services of the jointly controlled operation.

1.9. Foreign currency

Foreign currency transactions are recorded based on the foreign currency exchange rates of the European Central Bank prevailing at the dates of the transactions. Monetary financial assets and liabilities denominated in foreign currencies at the balance sheet date are translated into euros based on the foreign currency exchange rates of the European Central Bank prevailing at the balance sheet date. Exchange rate differences from translation are reported in the income statement of the reporting period.

The functional currency of subsidiaries located abroad is the currency of their business environment; therefore the financial statements of such subsidiaries are translated into euros for consolidation purposes; the asset and liability items are translated using the foreign exchange rates of the European Central Bank prevailing at the balance sheet date, income and expenses using the weighted average foreign exchange rates for the year and other changes in equity using the foreign exchange rates at the date at which they arose. Exchange rate differences arising from translation are reported in the equity item *Currency translation differences* and in the consolidated comprehensive income item *Currency translation differences of foreign entities*.

1.10. Financial assets

The purchases and sales of financial assets are recognised at the trade date.

Depending on the purpose for which financial assets were acquired, financial assets are classified into the following categories at the group:

- financial assets at fair value through profit or loss;
- loans and receivables;
- held-to-maturity investments;
- available-for-sale financial assets.

Management determines the classification of its financial assets at initial recognition.

The Company does not have any held-to-maturity investments, financial assets at fair value through profit or loss and available-for-sale financial assets. The group does not have any derivatives either.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are included within current assets except for maturities greater than 12 months after the balance sheet date. Such assets are classified as non-current assets. Loans and receivables are initially recognised at their fair value less transaction costs. After initial recognition, the group carries loans and receivables at amortised cost (less any impairment losses), calculating interest income on the receivable in the following periods using the effective interest rate method.

Receivables are assessed based on the collectible amounts. Each receivable is assessed separately considering all known information about the solvency of the party to the transaction. Receivables whose collection is improbable are written down during the reporting period (see also 1.11)

1.11. Impairment of assets

Financial assets at amortised cost

The group assesses at each balance sheet date whether there is any indication that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (loss events) has an impact on the estimated future cash flows of the financial asset or a group of financial assets that can be reliably estimated. Objective evidence that a financial asset or a group of financial assets is impaired includes observable data that is available to the group regarding the following events:

- significant financial difficulties of the debtor;
- a breach of contract, such as a default or delinquency in payments;
- probability that the debtor will enter bankruptcy;
- disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a financial asset or a group of financial assets, although the decrease cannot yet be measured reliably.

If there is objective evidence that an impairment loss has incurred for loans and receivables or held-to-maturity investments carried at amortised cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have already been recognised), discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can objectively be related to an event occurring after impairment was recognised (such as improved credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

Non-financial assets

Assets that have indefinite useful lives are not subject to amortisation but they are tested annually for impairment, by comparing their carrying amounts with their recoverable amounts. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. In the event of such circumstances, the recoverable amount of the asset is assessed and compared with the carrying amount. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating unit). Non-financial assets that suffered an impairment loss are reviewed at each reporting date and if necessary, the impairment loss is reversed except for impairment of goodwill.

1.12. Inventories

Inventories are recorded in the statement of financial position at cost, which consists of the purchase costs, production costs, transportation and other costs incurred in bringing the inventories to their present location and condition.

In case of separately identifiable inventory items, their cost is determined based on expenditure incurred specifically for the acquisition of each asset. If inventory items are not clearly distinguishable from each other, then the weighted average cost method is used.

Inventories are recognised in the statement of financial position at the lower of cost and net realisable value. The net realisable value is the sales price less estimated costs to sell.

Expenditure incurred for real estate development is reported either as work-in-progress or finished goods, depending on the stage of completion in the line *Inventories* in the statement of financial position. When the development of property is financed with a loan, the borrowing costs incurred during development are included in the cost of the property. Borrowing costs incurred during the period of construction are capitalised until a permit for use is obtained for the project. Expenses associated with maintenance or usage of the property are not capitalised.

A completed real estate property is sold either in parts (by houses, apartments, office spaces, etc.) or as a whole. Revenue is recognised as income from the sale of goods (Note 1.21). Upon the sale of real estate properties, the group and the acquirer enter into a notarially authenticated agreement for transferring the property, and a respective entry is made in the land register.

1.13. Investment property

Investment property is a real estate property which is primarily held for the purpose of earning rental income or for capital appreciation or for both, but not for the production of goods or services, administrative purposes or sale in the ordinary course of business. Investment property is measured using the cost method, i.e. at cost less any accumulated depreciation and any accumulated impairment losses.

Buildings included in investment properties are depreciated on a straight-line basis over the period of 12.5 to 33.3 years. Land is not depreciated.

1.14. Property, plant and equipment

An item of property, plant and equipment is an asset used for production, provision of services or administrative purposes over a period longer than one year.

An item of property, plant and equipment is carried in the statement of financial position at its cost less any accumulated depreciation. The cost consists of the purchase price and other costs directly related to the acquisition that are necessary for bringing the asset to its operating condition and location. Subsequent expenditure incurred for items of property, plant and equipment is recognised as non-current assets when it is probable that future economic benefits associated with the asset will flow to the Company and the cost of the asset can be measured reliably. Other repair and maintenance costs are recognised as expenses at the time they are incurred. Items of property, plant and equipment leased under the finance lease terms are accounted for similarly to purchased property, plant and equipment.

Depreciation is calculated on a straight-line basis over the following useful lives:

- buildings 10-33.3 years;
- machinery and equipment 2-20 years;
- other items of property, plant and equipment 2.5-5 years;
- right of superficies 50 years.

Land is not depreciated.

At each balance sheet date, the validity of applied depreciation rates, the depreciation method and the residual values applicable to assets is assessed.

If an item of property, plant and equipment consists of separately identifiable components with different useful lives, these components are accounted for as separate assets and accordingly, separate depreciation rates are set for them depending on their useful lives.

Items of property, plant and equipment are derecognised on disposal or when no future economic benefits are expected from their use or disposal. Gains or losses arising from derecognition of items of property, plant and equipment are included either within other operating income or other operating expenses in the income statement.

Non-current assets are written down to their recoverable amount if the latter is lower than their carrying amount. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

1.15. Intangible assets

Intangible assets are recognised in the statement of financial position when the asset can be controlled by the Company, the expected future benefits attributable to the asset will flow to the Company and the cost of the asset can be measured reliably. The cost of an intangible asset consists of its purchase price and other expenditure directly related to the purchase. Intangible assets are carried in the statement of financial position at cost less any accumulated amortisation and any accumulated impairment losses. Goodwill is not amortised.

Software and information systems

The costs related to the development of information systems and software which are reported as intangible assets, are depreciated under a straight-line method over their estimated useful lives (2-10 years).

1.16. Finance and operating leases

Leases of property, plant and equipment which transfer all significant risks and rewards of ownership to the lessee are classified as finance leases. All other leases are recognised as operating leases.

Assets and liabilities leased under the finance lease terms are reported in the statement of financial position at the lower of fair value of the leased asset and the present value of minimum rental payments. Items of property, plant and equipment leased under the finance lease terms are depreciated over the shorter of the lease term and the useful life.

Finance lease liabilities are reduced by principal payments; interest expenses on lease payments are included within finance costs in the income statement. Finance costs are allocated to the rental period so as to achieve a constant periodic rate of interest on the remaining balance of the liability.

Operating lease payments are reported in the income statement as expenses on a straight-line basis over the lease term.

1.17. Financial liabilities

All financial liabilities of the group belong to the category "other financial liabilities at amortised cost".

All financial liabilities (trade payables, borrowings, and other short and long-term borrowings) are initially recorded at their fair value and are subsequently stated at amortised cost, using the effective interest rate method. The amortised cost of current financial liabilities normally equals their nominal value; therefore current financial liabilities are stated in the statement of financial position at their redemption value. To calculate the amortised cost of non-current financial liabilities, they are initially recognised at fair value of the proceeds received (net of transaction costs incurred) and an interest cost is calculated on the liability in subsequent periods using the effective interest rate method.

Financial liabilities are classified as current when they are due to be settled within twelve months after the balance sheet date; or the group does not have an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date. Borrowings that are due within 12 months after the balance sheet date, but which are refinanced after the balance sheet date as non-current, are recognised as current ones. Also, borrowings are classified as current if the lender had a contractual right at the balance sheet date to demand immediate repayment of the borrowing due to the breach of conditions set forth in the agreement.

Borrowing costs directly related to the construction of a real estate property until the property is ready for use or sale, are capitalised. In other cases, borrowing costs are recognised as an expense in the period in which they are incurred.

Factoring

Recognition of the amounts received for resale of receivables that arose in the ordinary course of business (factoring) depends on whether in case it is not collected, the buyer of the receivable (factor) has the right to transfer it back to the buyer (factoring with recourse) or not (factoring without recourse). For factoring without recourse, the amounts collected are recognised as a reduction

of the receivable. The difference between the book value of the receivable and the amount collected is recognised within period expenses. Factoring with recourse is accounted for as a financial liability assumed using receivables as collateral. Until collection of the receivable by the factor, the amounts collected from the sale of receivables are recognised as interest-bearing liabilities. The difference between the book value of the receivable and the proceeds received is recognised within period finance costs.

1.18. Corporate income tax

According to the Income Tax Act of the Republic of Estonia, legal entities are not subject to income tax on profits earned. Corporate income tax is paid on fringe benefits, gifts, donations, costs of entertaining guests, dividends and payments not related to business operations. Thus, in Estonia there are no differences between the tax bases and the carrying amounts of assets which would give rise to a deferred income tax asset or liability. In 2013, the tax rate on dividends payable is 21/79 (in 2012 and 2011 also 21/79) of the amount paid out as net dividends. The corporate income tax arising from the payment of dividends is accounted for as an expense in the period when dividends are declared.

Corporate income tax on profits and deferred income tax expense or income of the subsidiaries located in Latvia and Lithuania as well as corporate income tax on dividends of Estonian entities are reported in the consolidated income statement.

Deferred income tax is calculated on all significant temporary differences between the tax bases of assets and liabilities and their carrying amounts. Deferred tax assets are recognised in the group's statement of financial position if their future realisation is probable.

Legal entities in Latvia, Lithuania and Ukraine that are part of the group calculate taxable income and corporate income tax in accordance with the legislation of the Republic of Latvia, the Republic of Lithuania and the Republic of Ukraine. The profits of entities located in the Republic of Latvia are taxed at the rate of 15% (2011: 15%), in the Republic of Lithuania at the rate of 15% (2011: 15%), in the Republic of Ukraine at the rate of 21% (2011: 23%) and in the Republic of Finland at the rate of 24.5% (2011: 26%).

1.19. Employee benefits

Termination benefits

Termination benefits are payable when employment is terminated by the group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without a possibility of withdrawal; or providing termination benefits as a result of another offer made to encourage voluntary redundancy. Termination benefits are discounted to their present value.

Profit-sharing and bonus plans

The Company recognises a liability and an expense for bonuses and profit-sharing plans, based on a formula that takes into consideration the profit attributable to the parent's owners after certain adjustments. The group recognises a provision where contractually obliged or when there is past practice that has created a constructive obligation.

1.20. Provisions

Provisions are constructive or legal obligations which arise as a result of events occurring before the balance sheet date. Setting up of provisions or increasing existing provisions is recognised as an expense in the income statement of the reporting period.

Provisions are recognised in the statement of financial position based on the best estimate of the management board at the present value of the expenditure expected to be sufficient to settle the obligation. A pre-tax rate of discount is used, which reflects current market valuations of the time value of money and the risks associated with liabilities that are not already included in the best estimate of the related expenses.

Pursuant to respective building acts, the construction companies of the group provide 2-year warranties on their buildings. The calculation of warranty provisions is based on management estimates and previous periods' experience with regard to actual warranty expenses.

The expected loss arising from construction contracts is immediately recognised as an expense. A provision is recognised for onerous construction contracts which have not yet been completed (Note 1.22).

1.21. Revenue

Revenue is recognised at the fair value of the consideration received or receivable.

Revenue from the provision of construction services is recognised as revenue by reference to the stage of completion of the contract (see Note 1.22) in accordance with IAS 11 *Construction Contracts*. Proceeds from the sale of own real estate development projects (private houses, apartments, office premises, etc. that have been built on the registered immovables owned by entities of Merko Ehitus group) is recognised as revenue in accordance with IAS 18 *Revenue* when significant risks and rewards of ownership of the goods are transferred to the buyer, the receipt of payment is probable and the costs incurred in respect of the transaction can be measured reliably.

When goods are sold or swapped in exchange for dissimilar goods or services, the exchange is regarded as a transaction which generates revenue. Revenue is measured at the fair value of the goods or services received, adjusted by the amount of any cash or cash equivalents received or paid. When the fair value of the goods or services received cannot be measured reliably, revenue is measured at the fair value of the goods or services given up, adjusted by the amount of any cash or cash equivalents received or paid.

Revenue from the provision of services is recognised based on the stage of completion of the service at the balance sheet date.

Revenue arising from interest and dividends is recognised when it is probable that future economic benefits associated with the transaction will flow to the entity and the amount of revenue can be measured reliably.

1.22. Construction contracts in progress

Income and expenses of construction contracts in progress have been matched under the stage of completion method. The stage of completion is determined on the basis of the relationship between the actual costs incurred by the balance sheet date and the estimated costs of the contract. The actual costs of the contract consist of direct and overhead costs of the construction contract.

If invoices submitted to the customer by the balance sheet date are either higher or lower than the income calculated under the stage of completion method, then the difference is recognised as a liability or as a receivable in the statement of financial position.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately and in full.

1.23. Cash and cash equivalents

In the statement of financial position and the cash flow statement, cash and cash equivalents comprise highly liquid funds with low variation in value, such as cash on hand, cash in bank accounts and term deposits with maturities of three months or less. Management regards deposits with maturities greater than 3 months as investments and hence does not include them in cash and cash equivalents. In addition to changes in cash and its equivalents, the consolidated cash flow statement also includes changes in short-term bank deposits with maturities greater than 3 months due to the possibility of using these deposits immediately as the need arises without a significant effect on the group's financial position.

The indirect method has been used for the preparation of the cash flow statement.

1.24. Contingent liabilities

Contingent liabilities are those liabilities the realisation of which is less probable than non-realisation and the amount of which cannot be determined reliably. Contingent liabilities are not recognised in the statement of financial position, but they are disclosed in the notes to the financial statements.

1.25. Statutory reserve capital

Reserve capital is formed to comply with the requirements of the Commercial Code. During each financial year, at least one-twentieth of the net profit shall be entered in reserve capital, until reserve capital reaches one-tenth of share capital. Reserve capital may be used to cover a loss, or to increase share capital. Payments shall not be made to shareholders from reserve capital.

1.26. Events after the balance sheet date

The financial statements of the reporting period include material circumstances affecting the assessment of assets and liabilities which became evident between the balance sheet date and the date of preparing the financial statements but that are related to transactions in the reporting period or previous periods. Material events after the balance sheet date not related to transactions in the reporting period or previous periods are not reported in the statement of financial position but they are disclosed in the notes to the financial statements.

1.27. Dividends

The distribution of dividends to the Company's shareholders is recognised as a liability in the financial statements in the period in which the dividends are approved by the Company's shareholders.

1.28. Segment reporting

According to IFRS 8 *Operating Segments*, segment reporting is applicable to operating segments whose results are regularly reviewed by the entity's chief operating decision maker to make business-related decisions. Operating segments are components of the entity for which it is possible to obtain discrete financial information to make decisions about resources to be allocated to the segment and assess its performance.

1.29. Changes in presentation of information

- a. In previous reporting periods, issued loans were recognised as investing activities in the cash flow statement of Merko Ehitus group. However, loans have been granted to real estate developers under the assumption that Merko Ehitus group will get an opportunity to provide a construction service in development projects. Due to the direct connection between the loans granted and the group's business, these loans and the related interest charges are recognised in the cash flows from operating activities in the cash flow statement.
- b. In 2011, finance income recognised in the income statement included interest income earned on a receivable not paid off by the buyer of Balsiu school-house. Considering the fact that the construction of Balsiu schoolhouse was essentially the group's business, the respective interest income was reclassified from finance income to operating income in the income statement. Interest received on the receivable from the buyer of Balsiu schoolhouse is also included within cash flows from operating activities.

The comparative information of the previous financial year that is presented in the consolidated financial statements for 2012 has been changed to correspond to the new presentation. Thus, the following items have been adjusted in the financial statements:

- issued loans that are related to operating activities are included in the item *Change in payments and receivables related to operating activities* under cash flows from operating activities in the consolidated cash flow statement, last year they were included in the items *Loans granted* (2011: EUR -310 thousand) and *Repayments of loans granted* (2011: EUR 5,613 thousand) under cash flows from investing activities;
- interest income from operating activities is included in the item *Interest received* under cash flows from operating activities in the consolidated cash flow statement, last year it was included in the item *Interest received* (2011: EUR 758 thousand) under the cash flows from investing activities;
- interest income on accounts receivable is included in the item *Other income* in the consolidated statement of comprehensive income; last year it was included in the item *Finance income* (2011: EUR 969 thousand);
Due to the change in the income statement, the items *Operating profit* and *Interest income from operating activities*, the items *Other finance income* and *incl. interest income* in Note 3 *Operating Segments*, the item *Interest income* under *Other income* in Note 7 and the item *Interest income* under *Finance income* in Note 9 has been changed by the same amount in the cash flow statement;
- in Note 37 *Additional disclosures about the parent*, the loans are recognised in the cash flow statement item *Change in payments and receivables related to operating activities*, last year they were included in the items *Loans granted* (2011: EUR -13,309 thousand) and *Repayments of loans granted* (2011: EUR 19,533 thousand) under cash flows from investing activities. Interest income from operating activities was included in the item *Interest received* under the cash flows from operating activities of the parent; last year they were included in the item *Interest received* (2011: EUR 3,109 thousand) under cash flows from investing activities.

The comparative information for 2011 has been changed in the financial statements as follows: in the consolidated statement of comprehensive income, other income and operating profit have increased by EUR 969 thousand; finance income has decreased by the same amount. In the consolidated cash flow statement, cash flows from operating activities increased by EUR 6,061 thousand, cash flows from investing activities decreased by the same amount. In the cash flow statement of the parent, cash flows from operating activities increased by EUR 9,333 thousand, cash flows from investing activities decreased by the same amount.

Note 2 Management estimates

The preparation of the financial statements in conformity with International Financial Reporting Standards requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the group's accounting policies. Although these estimates are based on management's best knowledge of current events and actions, actual results may ultimately differ from those estimates. However, it can be stated that seasonality and cyclicity do not have a significant effect on the group's activities within a year. The areas involving a higher degree of judgement or complexity, or the areas where assumptions and estimates are relevant to the consolidated financial statements of Merko Ehitus group, are disclosed below. Changes in management's estimates are reported in the income statement of the period of the change.

Valuation of receivables

For valuation of receivables, each receivable is analysed separately. For determining the need for a complete or partial write-down of receivables, the debtor's financial position, the guarantees provided, the solutions offered to pay off the loan and the previous payment behaviour of the debtor are considered.

Provision for warranty obligations

For determining the provision for warranty obligations, the statistical cost of the Company's warranty works is considered.

Inventory write-down

Inventories are valued separately by individual properties (registered immovable or building). A business plan is prepared for each property based on its nature (intended use and building rights currently effective or being effected) and the project's costs are compared with expected income. If the property's costs exceed the expected revenue to be generated from the realisation of the project (net realisable value), the group shall write down assets in the amount by which the costs exceed income. Due to the volatility of the construction market and low liquidity of the real estate market, determination of the net realisable value of the assets depends largely on management estimates. The sensitivity analysis of inventories showed that had the net realisable value been overestimated by 10% (i.e. income would be 10% lower upon the disposal of assets), the company's write-down of inventories (construction in progress, finished buildings, acquisition of real estate properties for sale) would have been EUR 3,344 thousand higher in 2012 (2011: EUR 5,987 thousand higher), incl. real estate properties for sale in the amount of EUR 2,573 thousand (2011: EUR 1,776 thousand), construction in progress in the amount of EUR 673 thousand (2011: EUR 3,224 thousand) and finished buildings in the amount of EUR 97 thousand (2011: EUR 987 thousand). Had the value been underestimated by 10% (income would be 10% higher upon the disposal of assets), the write-down of inventories for the year 2011 would have been EUR 2,012 thousand lower, incl. real estate properties for sale in the amount of EUR 453 thousand, construction in progress in the amount of EUR 831 thousand, finished buildings in the amount of EUR 728 thousand. This sensitivity test is of no importance in 2012, because no inventories were written down and thus, impairment losses of inventories would have no impact on inventories.

Revenue under the stage of completion method

Revenue from construction in progress is recognised under the stage of completion method (Note 1.22), which also assumes that the stage of completion of construction contracts can be determined reliably. A precise, systematic calculation and estimation of costs, forecasting and reporting of income and expenses has been introduced for determining the stage of completion. The estimated final result to be derived from each construction project is being constantly monitored, deviations from the budget are analysed and if necessary, the profit estimate is adjusted. As at 31.12.2012, the amount of the provision for onerous contracts was EUR 2,067 thousand (2011: EUR 3,526 thousand), which was determined after the evaluation of the stage of completion of construction contracts (Note 29). The risk analysis showed that a change in the estimated costs of construction projects in the range of +/-5% would result in a change in the net profit between EUR -30,702/+13,430 thousand (2010: EUR -22,419/+11,287 thousand).

Determination of the useful lives of items of property, plant and equipment

Management has estimated the useful lives of items of property, plant and equipment, taking into consideration conditions and volumes of business activities, historical experience in this area and future outlook. Management estimates that the useful lives of buildings and facilities are between 10 and 33.3 years depending on their structure and the purpose of use. The average useful lives of machinery and equipment are on average between 3 and 5 years and those of other fixtures between 2.5 to 5 years depending on the purpose of use of the asset.

Valuation of property, plant and equipment and intangibles

At each balance sheet date, an impairment test is performed for the intangible assets with indefinite useful lives including goodwill, and the carrying amount is written down to its recoverable amount if it is lower than the carrying amount. An impairment test is also carried out for property, plant and equipment and intangibles when an event or change in circumstances indicates that impairment may have occurred.

The recoverable amount is the higher of the fair value of an asset less costs to sell and its value in use. Evaluation of fair value is based on reliable information regarding the proceeds from a sale to an informed, interested and independent party, less costs of disposal. The test is used both for single assets and for a cash-generating unit. Assets, intangible assets included, which have

no autonomous (independent from other assets) capacity to earn revenue, are treated as cash-generating units and valuation of their recoverable amount is based on their value in use.

For the purpose of the test, in order to assess the value in use, management prepares a realistic forecast for the cash flows to be earned in subsequent periods by the business unit and calculates the present value of these cash flows. For determining the present value, the discount rate is used which according to management objectively reflects the risk level of the respective business unit and its expected rate of return. If the recoverable amount determined in such a way exceeds the carrying amount of non-current assets and goodwill of the business unit subject to testing, goodwill is not written down.

Valuation of investment property

Investment properties are recognised at cost, less any accumulated depreciation and any impairment losses. Management estimates that the carrying amount of investment properties as at 31.12.2012 does not significantly differ from their fair value. Management's estimate regarding the fair value of investment properties is based on the existing market value of the assets. The estimated amount for which the asset can be exchanged in a transaction between independent parties at the date of estimation is considered to be its market value. External experts were not involved in the estimation of the fair value of investment properties. Market value estimates are mostly based on market transactions.

Borrowing costs

Borrowing costs that are related to a qualifying asset (one that necessarily takes a substantial period of time to get ready for its intended use or sale) are recognised in the cost of inventory. Interest expenses related to holding and later use of assets are recorded under finance costs as period costs. Most of the interest expense incurred at the group is related to the acquisition of immovables and construction of residential properties. The decision regarding capitalisation or expensing of borrowing costs is made by the management. The management uses the following considerations for decision-making purposes:

- Upon acquisition of immovables which are ready for intended use or sale, the borrowing costs related to holding such assets are not capitalised;
- Borrowing costs related to a specific development project are capitalised during the construction period until obtaining the permit for use. If, depending on the market situation, the management temporarily suspends the construction of an object, the capitalisation of borrowing costs is ceased at the same time and the borrowing costs incurred during the period of suspended development are expensed.

In 2012, a total of EUR 180 thousand (2011: EUR 94 thousand) of the borrowing costs was capitalised (Note 27).

Note 3 Operating segments

in thousands of euros

The chief operating decision-maker, i.e. the Management Board of parent AS Merko Ehitus, monitors the business of the group by operating segments. The performance of the segments is assessed by the chief operating decision-maker based on segment revenue derived from outside the group and pre-tax profit. Pre-tax profit of segments is made up of income and expenses directly related to them. Other income and expenses not directly related to segments cannot be allocated and they are monitored together at the group level.

Based on internal management information, the group's Management Board monitors activities by the following segments:

- general construction (Buildings in the financial statements for 2011),
- engineering construction (Facilities in the financial statements for 2011),
- road construction,
- real estate development,
- other.

The first three segments are engaged in provision of construction services. The real estate segment is primarily engaged in the group's own real estate development – construction and sale, to a lesser degree, it also includes real estate maintenance and leasing. Other operating areas (management services, supervision service, etc.) are insignificant to the group and they are not monitored as separate segments. The amount of each cost item in segment reporting is a figure presented to management for making decision about allocation of resources to segments and valuation of segment operating results. The costs that come after the profit of reporting segments are recognised in segment reporting using the same principles as in the financial statements and they are not used for evaluation of the results of operating segments by the company's management.

In segment reporting, all intra-group transactions with income, expenses and assets and unrealised gains and losses between reportable segments have been eliminated unless the loss is due to impairment.

	General construc- tion	Enginee- ring const- ruction	Road construc- tion	Real estate develop- ment	Other	Total segments
2012						
Segment revenue	61,953	113,586	45,152	37,493	2,527	260,711
Inter-segment revenue	(263)	(293)	-	(10,386)	(638)	(11,580)
Revenue from external clients	61,690	113,293	45,152	27,107	1,889	249,131
Gross profit (-loss)	5,017	8,995	1,714	2,401	(216)	17,911
Segment pre-tax profit (loss)	5,040	8,569	1,671	3,404	21	18,705
incl. interest income from operating activities (Note 7)	4	-	-	1,357	-	1,361
depreciation (Note 4)	(76)	(502)	(1,035)	(131)	(491)	(2,235)
recognition of a provision (Notes 4, 29)	(422)	(926)	(148)	(374)	(1)	(1,871)
gain (loss) on associates and joint ventures (Note 20)	-	-	-	(71)	234	163
other finance income (costs) (Notes 9, 10)	(38)	(27)	(87)	(263)	(2)	(417)
incl. interest income	-	-	-	51	-	51
interest expenses	(38)	(27)	(87)	(314)	(2)	(468)
Segment assets 31.12.2012	13,092	27,091	24,651	120,248	1,572	186,654
incl. associates and joint ventures (Note 20)	-	18	-	7,172	-	7,190

	General construc- tion	Enginee- ring const- ruction	Road construc- tion	Real estate develop- ment	Other	Total segments
2011						
Segment revenue	68,837	109,928	52,019	24,014	2,588	257,386
Inter-segment revenue	(4,089)	(19,177)	(8,718)	(5,107)	(973)	(38,064)
Revenue from external clients	64,748	90,751	43,301	18,907	1,615	219,322
Gross profit (-loss)	4,569	1,853	(5,736)	(3,917)	(375)	(3,606)
Segment pre-tax profit (loss)	5,010	1,922	(5,736)	(4,906)	(72)	(3,782)
incl. interest income from operating activities (Note 7)	969	-	-	-	-	969
depreciation (Note 4)	(72)	(212)	(1,161)	(90)	(302)	(1,837)
impairment of inventories (Notes 4, 18)	-	-	-	(4,562)	-	(4,562)
reversal of impairment of inventories (Notes 4, 18)	-	-	-	252	-	252
recognition of provision (Notes 4, 29)	(860)	(536)	(2,878)	(338)	(278)	(4,890)
gain (loss) on associates and joint ventures (Note 20)	-	17	-	(1,457)	320	(1,120)
other finance income (costs) (Notes 9, 10)	(539)	(12)	-	(190)	(30)	(771)
incl. interest income	2	-	-	-	-	2
interest expenses	(541)	(12)	-	(179)	(29)	(761)
Segment assets 31.12.2011	21,704	31,448	25,171	108,002	5,843	192,168
incl. associates and joint ventures (Note 20)	-	18	-	7,367	2,601	9,986

In addition to the segment assets, the group holds assets in the amount of EUR 38,394 thousand (2011: EUR 28,169 thousand) that cannot be associated with a specific segment or the allocation of which to segments would be impracticable. The unallocated assets of the group comprise cash and cash equivalents, deposits, loans receivable excluding loans to associates and joint ventures, tax prepayments, other receivables and an unallocated portion of property, plant and equipment.

Reconciliation of the pre-tax profit of segments and the group

	2012	2011
Profit (loss) from reporting segments	18,705	(3,782)
Unallocated expense (income)		
marketing expenses (Note 5)	(2,107)	(2,104)
general and administrative expenses (Note 6)	(9,173)	(7,910)
incl. setting up of provisions (Note 29)	(32)	(20)
other operating income (expense)	1,079	(443)
incl. interest income from operating activities (Note 7)	812	450
setting up of provisions (Note 8,29)	-	(1,013)
finance income (costs) (Note 9,10)	(602)	204
incl. interest income	39	91
interest expense	(688)	(388)
Profit before tax	7,902	(14,035)

Unallocated finance costs and income include income from bank deposits, foreign exchange gains (losses), uncapitalised loan interest expenses and other finance income and costs.

Revenue by client location

	2012		2011	
Estonia	202,149	81%	162,217	74%
Latvia	38,305	15%	41,754	19%
Lithuania	8,677	4%	15,351	7%
Total	249,131	100%	219,322	100%

Non-current assets (except for financial assets and deferred income tax assets) by location of assets:

	31.12.2012	31.12.2011
Estonia	19,168	19,154
Latvia	523	532
Lithuania	93	111
Total	19,784	19,797

Note 4 Cost of goods sold

in thousands of euros

	2012	2011
Construction services	130,456	109,207
Materials	38,266	45,956
Staff costs	20,770	16,448
Properties purchased for resale	14,392	17,941
Construction mechanisms and transport	11,871	11,244
Depreciation	2,235	1,837
Design	1,273	1,964
Provisions (Note 29)	1,871	4,890
Allowance for inventories (Note 18)	-	4,562
Reversal of the allowance for write-down of inventories (Note 18)	-	(252)
Real estate management costs	193	313
Other expenses	9,893	8,818
Total cost of goods sold	231,220	222,928

Note 5 Marketing expenses

in thousands of euros

	2012	2011
Staff costs	1,355	1,186
Advertising, sponsorship	340	293
Transport	136	155
Construction tenders	88	109
Depreciation	17	16
Other expenses	171	345
Total marketing costs	2,107	2,104

Note 6 General and administrative expenses

in thousands of euros

	2012	2011
Staff costs	5,763	4,838
Office expenses, communication services	649	508
Consulting, legal, auditing	690	686
Transport	493	506
Computer equipment and software	401	309
Depreciation	347	389
Provisions (Note 29)	32	20
Other expenses	798	654
Total general and administrative expenses	9,173	7,910

Note 7 Other operating income

in thousands of euros

	2012	2011
Interest income from operating activities	2,173	1,419
Profit from sale of non-current assets	123	722
Fines and penalties for delay received	98	57
Collection of doubtful receivables	7	66
Other income	560	316
Total other operating income	2,961	2,580

Note 8 Other operating expenses

in thousands of euros

	2012	2011
Fines, penalties	95	29
Setting up of provision for fines (Note 36)	-	1,013
Gifts, donations	243	146
Doubtful receivables expense (Note 36)	439	83
Other expenses	57	37
Total other operating expenses	834	1,308

Note 9 Finance income

in thousands of euros

	2012	2011
Interest income	90	93
Foreign exchange gains	-	501
Other finance income	94	0
Total finance income	184	594

Note 10 Finance costs

in thousands of euros

	2012	2011
Interest expense	1,156	1,149
Other finance costs	47	12
Total finance costs	1,203	1,161

Note 11 Corporate income tax

in thousands of euros

The income tax on the group's profit before tax differs from the theoretical amount that would arise using the statutory tax rates applicable to profits of the consolidated entities for the following reasons:

2012	Latvia	Lithuania	Ukraine	Estonia	Total
Profit (loss) before tax	1,667	3,918	(21)	2,338	7,902
Tax rate applicable to profits	15%	15%	21%	0%	
Tax calculated at domestic tax rates applicable to profits in the respective countries	(249)	(588)	4	-	(833)
Tax calculated on expenses not deductible for tax purposes	(136)	(1,440)	-	-	(1,576)
Tax calculated on income not subject to tax	26	1,629	-	-	1,655
Tax losses of previous periods recognised in the reporting period	389	250	-	-	639
Tax losses not recognised in the reporting period	-	(33)	(4)	-	(37)
Deferred income tax on dividends	-	-	-	(137)	(137)
Total income tax expense	30	(182)	-	(137)	(289)
incl. income tax expense	-	(449)	-	-	(449)
deferred income tax expense (Note 22)	30	267	-	-	297
income tax withheld on intra-group transactions	-	-	-	(137)	(137)

2011	Latvia	Lithuania	Ukraine	Estonia	Total
Profit (loss) before tax	(5,422)	(1,456)	(29)	(7,128)	(14,035)
Tax rate applicable to profits	15%	15%	23%	0%	
Tax calculated at domestic tax rates applicable to profits in the respective countries	813	218	7	-	1,038
Tax calculated on expenses not deductible for tax purposes	28	68	-	-	96
Tax calculated on income not subject to tax	(24)	(85)	-	-	(109)
Tax losses of previous periods recognised in the reporting period	-	(4)	-	-	(4)
Tax losses not recognised in the reporting period	(533)	(328)	(7)	-	(868)
Deferred income tax on dividends	-	-	-	(274)	(274)
Total income tax expense	284	(131)	-	(274)	(121)
incl. deferred income tax expense (Note 22)	284	(131)	-	-	153
income tax withheld on intra-group transactions	-	-	-	(274)	(274)

As at 31.12.2012, it is possible to pay out dividends to shareholders from retained earnings in the amount of EUR 81,943 thousand and the corresponding income tax would amount to EUR 21,782 thousand. As at 31.12.2011, it would have been possible to pay out EUR 75,872 thousand as dividends, and the corresponding income tax would have amounted to EUR 20,168 thousand.

Note 12 Earnings per share

Basic earnings per share for profit attributable to equity holders of the parent have been derived by dividing the net profit attributable to shareholders by the weighted average number of shares.

	2012	2011
Net profit(-loss) attributable to shareholders (<i>in thousand EUR</i>)	7,627	(14,084)
Weighted average number of ordinary shares (<i>thousand pcs</i>)	17,700	17,700
Earnings (loss) per share (<i>in euros</i>)	0.43	(0.80)

In 2011 and 2012, the group did not have any potential ordinary shares to be issued; therefore the diluted earnings per share equal the basic earnings per share.

Note 13 Dividends per share

Dividends payable are recognised after the approval of profit allocation at the General Meeting of Shareholders. In accordance with the profit allocation proposal, dividends payable in 2013 will total EUR 5,310 thousand, incl. EUR 0.30 per share, and the accompanying maximum income tax liability would amount to 21/79 on the amount paid out, i.e. EUR 1,411.5 thousand.

No dividends were paid in 2012. In 2011 the parent company AS Merko Ehitus distributed dividends in the amount of EUR 1,770 thousand, i.e. EUR 0.10 per share. AS Merko Ehitus did not have to pay corporate income tax due to the dividends received from subsidiaries and taxed in prior periods.

Note 14 Cash and cash equivalents

in thousands of euros

	31.12.2012	31.12.2011
Cash on hand	16	10
Bank accounts	5,808	9,173
Overnight deposits	17,492	9,327
Term deposits with maturities of 3 months or less	12,000	-
Total cash and cash equivalents (Note 36)	35,316	18,510

As at 31.12.2012, the weighted average interest on overnight deposits was 0.06% (31.12.2011: 0.12%). The weighted average interest on bank deposits with maturities of 3 months or less was 0.26% and the average duration as at 31.12.2012 was 49 days.

Note 15 Short-term deposits

in thousands of euros

	31.12.2012	31.12.2011
Bank deposits with maturities greater than 3 months (Note 36)	-	140

As at 31.12.2011, the bank deposit with maturity greater than 3 months was collected at 25.06.2012. The interest on the bank deposit was 1.3%.

Note 16 Trade and other receivables

in thousands of euros

	31.12.2012	31.12.2011
Trade receivables (Note 36)		
Accounts receivable	34,967	36,151
Allowance for doubtful receivables	(864)	(544)
Total trade receivables	34,103	35,607
Tax prepayments excluding corporate income tax		
Value added tax	791	618
Other taxes	10	5
Total tax prepayments excluding corporate income tax	801	623
Amounts due from customers of contract works (Notes 33, 36)	18,981	16,016
Other short-term receivables		
Short-term loans (Notes 17, 36)	1,887	7,673
Interest receivables (Note 36)	948	881
Other short-term receivables (Note 36)	1,256	1,444
Short-term receivable from the buyer of subsidiary (Note 36)*	96	-
Total other short-term receivables	4,187	9,998
Prepayments for services (Note 36)		
Prepayments for construction services	1,388	1,499
Prepaid insurance	416	296
Other prepaid expenses	467	410
Total prepayments for services	2,271	2,205
Total trade and other receivables	60,343	64,449
incl. short-term loan receivables from related parties (Note 17)	1,382	1,343
other short-term receivables and prepayments to related parties (Note 34)	943	1,027

* In 2006, AS Merko Ehitus sold 25% of the shares of its subsidiary AS Gustaf. The receivable is discounted at a 5% interest rate and its final due date is 16 January 2013.

In 2012, the payment discipline of customers did not significantly change as compared to last year. The share of overdue receivables increased from 16.6% to 22.1% in total receivables, and as at the balance sheet date, the amount of overdue receivables was EUR 7,547 thousand. By 15 March 2013, overdue receivables had been collected in the amount of EUR 6,641 thousand. In 2012, the average age of trade receivables was 58 days (2011: 56 days). In 2012, the group's balance sheet included doubtful receivables in the amount of EUR 864 thousand (2011: EUR 544 thousand) and wrote off uncollectible receivables in the amount of EUR 439 thousand (2011: 82 thousand), incl. irrecoverable receivables in the amount of EUR 98 thousand (2011: EUR 53 thousand). Of the amount of uncollectible receivables written off, EUR 350 thousand is related to the receivables from Latvian and Lithuanian branches with pending court cases but the probability of winning them is considered to be low. The management estimates that there are sufficient reasons to conclude that the trade receivables reported in the financial statements will be paid off by buyers.

A more detailed overview of the Company's credit risk is provided in Note 36.

Note 17 Loans granted

in thousands of euros

	Loans granted to				total
	associates and joint ventures (Note 34)	entities under common control (Note 34)	unrelated legal entities	unrelated individuals	
2012					
Loan balance at beginning of the year	4,930	-	7,732	107	12,769
Granted	54	-	2,658	-	2,712
Collected	-	-	(9,912)	(21)	(9,933)
Exchange rate difference	8	-	(3)	-	5
Loan balance at end of the year	4,992	-	475	86	5,553
incl. current portion (Notes 16, 36)	1,382	-	475	30	1,887
non-current portion 1...5 years (Notes 21, 36)	3,610	-	-	56	3,666
Average effective interest rate	4.9%	-	7.3%	4.9%	
2011					
Loan balance at beginning of the year	4,755	1,557	6,400	111	12,823
Granted	122	-	5,371	-	5,493
Collected	-	(1,557)	(4,052)	(4)	(5,613)
Write-down (Note 36)	-	-	(1)	-	(1)
Exchange rate difference	53	-	14	-	67
Loan balance at end of the year	4,930	-	7,732	107	12,769
incl. current portion (Notes 16, 36)	1,343	-	6,223	107	7,673
non-current portion 1...5 years (Notes 21, 36)	3,587	-	1,509	-	5,096
Average effective interest rate	6.0%	6.3%	7.7%	4.8%	

All issued loans reported as at the balance sheet date had not yet fallen due.

Note 18 Inventories

in thousands of euros

	31.12.2012	31.12.2011
Materials	563	807
Work-in-progress	18,528	33,056
Finished goods	21,499	10,549
Goods for resale		
Registered immovables purchased for resale	39,548	36,570
<i>incl. registered immovables located on nature preserve areas*</i>	3,272	3,163
Other goods purchased for resale	1,000	1,062
Total goods for resale	40,548	37,632
Prepayments for inventories		
Prepayments for real estate properties	1,097	5,560
Prepayments for other inventories	595	230
Total prepayments for inventories	1,692	5,790
Total inventories	82,830	87,834
incl. prepayments for inventories to related parties (Note 34)	-	3,810

* There are strict building restrictions on immovables located on nature preserve areas and their use for development purposes, either directly or indirectly, is not permitted. According to the Nature Conservation Act of the Republic of Estonia, an immovable which is located within the territory of a protected area, special conservation area or species protection site and the use of which for intended purposes is significantly hindered by the protection procedure, may be transferred to the state by an agreement between the state and the owner of land for a consideration equivalent to the usual value of the immovable (§20 of Nature Conservation Act). Until the entry into force of the new version of the Act, an older version was in force until 01.08.2008 which laid down the exchange of nature preserve areas with the state.

The value of an immovable, other than a forest immovable, is determined using the transaction comparison method. In determining the value of an immovable, the real rights which due to their nature cannot be deleted from the land register are considered (e.g. servitudes, neighbourhood rights) as well as those arising from laws other than the restrictions on an immovable property arising from the protection procedure which forms a basis for the acquisition of an immovable.

Due to the overall economic environment and a tense state budget situation, the transfer of the registered immovables is unlikely in the near term. At 31 January 2013, the Government of the Republic of Estonia approved the amendment to the Nature Conservation Act, terminating land swapping of nature conservation plots and replacing them by their purchase by the state. The amendment to the act has been presented for approval to Riigikogu (Parliament of Estonia). Upon entry into force of the Act, the state is obligated to apply only the acquisition of registered immovables for cash as a compensatory mechanism. The Management Board has accounted for nature conservation land as land without restrictions.

The inventory pledged as collateral as at 31.12.2012 for loans total EUR 38,942 thousand (2011: EUR 38,286 thousand) (Note 31).

In 2012, no impairment losses were recognised for inventories and previous impairment losses have not been reversed. Impairment losses and their reversals in 2011 (Notes 2, 4, 36):

31.12.2011	Carrying amount before write-down	Write-down	Reversal of write-down	Carrying amount after write-down
Finished goods	10,402	-	147	10,549
Work-in-progress	35,356	(2,300)	-	33,056
Land purchased for resale	37,586	(1,121)	105	36,570
Prepayments for real estate	6,701	(1,141)	-	5,560
Total	90,045	(4,562)	252	85,735

Note 19 Shares in subsidiaries

in thousands of euros

	Ownership and voting rights %		Location	Area of operation
	31.12.2012	31.12.2011		
AS Merko Ehitus Eesti	100	100	Tallinn	Construction
Tallinna Teede AS	100	100	Tallinn	Road construction
OÜ Tevener	100	100	Tallinn	Mining
AS Vooremaa Teed	100	100	Jõgeva	Road construction
AS Merko Infra	100	100	Tallinn	Construction
AS Gustaf	85	85	Pärnu	Construction
OÜ Gustaf Tallinn	80	80	Tallinn	Construction
AS Merko Tartu	66	66	Tartu	Construction
OÜ Raadi Kortermaja	100	100	Tartu	Real estate
OÜ Fort Ehitus	75	75	Harju County, Viimsi	Construction
OÜ Mineraal	100	100	Tallinn	Mining
SIA Merks	100	100	Republic of Latvia, Riga	Construction
SIA SK Viesturdarzs	100	100	Republic of Latvia, Riga	Real estate
SIA Merks Investicijas	100	100	Republic of Latvia, Riga	Real estate
SIA Industrias Parks	100	100	Republic of Latvia, Riga	Real estate
SIA Elniko	100	100	Republic of Latvia, Riga	Real estate
SIA Ropažu Priedes	100	100	Republic of Latvia, Riga	Real estate
SIA Skanstes Virsotnes	100	100	Republic of Latvia, Riga	Real estate
SIA Polystar	99,96	-	Republic of Latvia, Riga	Real estate
PS Merko-Merks	100	100	Republic of Latvia, Riga	Construction
UAB Merko Statyba	100	100	Republic of Lithuania, Vilnius	Construction
UAB Merko Inžinerija	100	100	Republic of Lithuania, Vilnius	Construction
OÜ Merko Property	100	100	Tallinn	Real estate
UAB Balsiu mokyklos SPV	100	100	Republic of Lithuania, Vilnius	Real estate
UAB Merko Bustas	100	100	Republic of Lithuania, Vilnius	Real estate
UAB MN Projektas	100	100	Republic of Lithuania, Vilnius	Real estate
UAB Jurininku aikštele	100	100	Republic of Lithuania, Vilnius	Real estate
Ringtee Tehnopark OÜ	100	100	Tallinn	Construction
OÜ Jõgeva Haldus	100	100	Tallinn	Real estate
OÜ Woody	100	100	Tallinn	Real estate
OÜ Maryplus	100	100	Tallinn	Real estate
OÜ Metsailu	100	100	Tallinn	Real estate
OÜ Constančia	100	100	Tallinn	Real estate
OÜ Käibevara	100	100	Tallinn	Real estate
OÜ Baltic Electricity Engineering	100	100	Tallinn	Electricity systems
OÜ Tähelinna Kinnisvara	100	100	Tallinn	Real estate
Merko Ukraine LLC	100	100	Republic of Ukraine, Kharkiv	Construction
Merko Finland OY	100	-	Republic of Finland, Helsinki	Construction
Lenko Stroi LLC	100	-	Russia, St. Petersburg	Construction
Väike-Paekalda OÜ	100	-	Tallinn	Real estate
Suur-Paekalda OÜ	100	-	Tallinn	Real estate

As at 1 January 2012, the entire construction activity in Estonia was transferred from AS Merko Ehitus to the subsidiary AS Merko Ehitus Eesti that was established during the internal restructuring in November 2011. According to the restructuring plan, the ownership interests of another seven Estonian subsidiaries were also transferred as a non-monetary equity contribution as at 1 January 2012. These entities were: AS Merko Infra, AS Gustaf, AS Merko Tartu, Tallinna Teede AS, OÜ Gustaf Tallinn, OÜ Fort Ehitus and OÜ Mineraal. In addition, contributions were made to the equity reserve of AS Merko Ehitus Eesti in the amount of up to EUR 56,000 thousand during 2012.

At 13 March 2012, AS Merko Ehitus established a wholly-owned subsidiary Merko Finland OY registered in Finland with the share capital of EUR 2,500 for the purpose of creating technical capabilities for launching possible construction projects in Russia. At 11 October 2012, Merko Finland OY established a subsidiary Lenko Stroi LLC in St. Petersburg, Russia, with the share capital of EUR 5 thousand.

In intra-group transactions at 30 March 2012, AS Merko Ehitus acquired a 100% ownership interest of its subsidiary UAB Merko Statyba in the latter's subsidiary UAB Merko Bustas that is engaged in real estate development and the subsidiary of AS Merko Ehitus, OÜ Merko Property, acquired a 100% ownership interest of UAB Merko Statyba in the latter's subsidiary UAB Balsiu Mokyklos SPV that is engaged in real estate management.

At 25 July 2012, SIA Merks acquired a 99.96% ownership interest in SIA Polystar, an entity that was part of the group of E.L.L. Kinnisvara AS under common control with AS Merko Ehitus. The transaction was not accounted for as a business combination but as acquisition of a one-asset entity. For acquisition of the registered immovable included within inventories, the share capital of SIA Polystar was increased by the prepayment in the amount of EUR 6,455 thousand made by SIA Merks to SIA Polystar in previous years. In the consolidated statement of financial position, the acquired registered immovable is carried in the amount of EUR 3,810 thousand after recognition of impairment losses in the amount of EUR 2,645 thousand for the prepayment made by SIA Merks in previous years.

According to the decision of the Supervisory Board of AS Merko Ehitus made at 4 September 2012, liquidation proceedings were launched for the subsidiary Merko Ukraine LLC which will continue in 2013. Due to this, the share capital of the subsidiary was increased by EUR 56 thousand.

At 19 November 2012, AS Merko Ehitus established two wholly-owned subsidiaries Väike-Paekalda OÜ and Suur-Paekalda OÜ, where a non-monetary contribution was made in the form of registered immovables received through the division of the joint venture OÜ Unigate in the amount of EUR 36 and 104 thousand, respectively.

At 19 December 2012, a contribution was made to the equity reserve of OÜ Jõgeva Haldus in the amount of EUR 750 thousand.

Acquisition of subsidiaries in 2011

Additional contributions were made into the share capital of AS Merko Infra in the amount of EUR 6,395 thousand in September 2011, and into the share capital of Tallinna Teede AS in the amount of EUR 1,500 thousand in December.

At 28 November 2011, AS Merko Ehitus established a subsidiary AS Merko Ehitus Eesti with share capital EUR 100 thousand.

At 6 December 2011, AS Merko Ehitus established a subsidiary OÜ Merko Property for the purpose of real estate development which had not yet launched its operations by the date of preparation of the financial statements.

At 15 August 2011, a subsidiary OÜ Pallasti Kinnisvara was established which acquired an office building as an investment property from the group. At 20 December 2011, OÜ Pallasti Kinnisvara was disposed off. As it represented a single-asset entity, its acquisition and disposal was not treated as a business combination.

Note 20 Investment in associates and joint ventures

	Ownership and voting rights %		Location	Area of operation
	31.12.2012	31.12.2011		
Associate				
AS TMB	-	25	Tartu	concrete elements
Joint ventures				
OÜ Unigate	50	50	Tallinn	real estate
Poolkoksimeä Sulgemise OÜ	50	50	Tallinn	construction
SIA Zakusala Estates	50	50	Republic of Latvia, Riga	real estate
OÜ Kortermaja	50	50	Tartu	real estate

At 29 June 2012, AS Merko Ehitus sold its ownership interest in its associate AS TMB at the sale price of EUR 2,750 thousand. As at 31.12.2012, the receivable had been collected in full.

At 5 October 2012, the shareholders of OÜ Unigate concluded a notarial division plan, under which registered immovables with nature conservation restrictions were split off from OÜ Unigate and were redistributed equally among the shareholders. In November 2012, AS Merko Ehitus established subsidiaries Väike-Paekalda OÜ and Suur-Paekalda OÜ to receive the five split off registered immovables with the carrying amount of EUR 140 thousand.

<i>in thousands of euros</i>	Investment at 31.12.2011	Changes in 2012					Investment at 31.12.2012
		acquisition (sale)	net assets- split off in division	gain (loss) on entities	dividends	exchange rate differences	
Associate							
AS TMB	2,601	(2,750)	-	234	(85)	-	-
Joint ventures							
OÜ Unigate	60	-	(140)	(1)	-	-	(81)
Poolkoksīmāe Sulgemise OÜ	18	-	-	0	-	-	18
SIA Zakusala Estates	7,280	-	-	(47)	-	19	7,252
OÜ Korteremaja	27	-	-	(23)	(3)	-	1
Total joint ventures	7,385	-	(140)	(71)	(3)	19	7,190
Total associates and joint ventures	9,986	(2,750)	(140)	163	(88)	19	7,190

<i>in thousands of euros</i>	Investment at 31.12.2010	Changes in 2011			Investment at 31.12.2011
		gain (loss) on entities	dividends	exchange rate differences	
Associate					
AS TMB	2,281	320	-	-	2,601
Joint ventures					
OÜ Unigate	61	(1)	-	-	60
Poolkoksīmāe Sulgemise OÜ	2	16	-	-	18
SIA Zakusala Estates	8,616	(1,448)	-	112	7,280
OÜ Korteremaja	93	(7)	(59)	-	27
Total joint ventures	8,772	(1,440)	(59)	112	7,385
Total associates and joint ventures	11,053	(1,120)	(59)	112	9,986

As at 31.12.2012, the difference between the value of the investment in SIA Zakusala Estates and the equity of the investee in the amount of EUR 7,395 thousand is attributable to the difference between the cost and market value of the 126 thousand square meter registered immovable located on Zakusala island in the centre of Riga that was privatised in December 2010 by the joint venture. SIA Zakusala Estates had previously held a lease agreement with the City of Riga regarding the this registered immovable until 2 June 2051, pursuant to which SIA Zakusala Estates had the right to use the land and which was not included in the statement of financial position of the joint venture.

Associate	Assets 31.12.	Liabilities 31.12.	Revenue	Net profit/(loss)
<i>in thousands of euros</i>				
2011				
AS TMB	14,477	4,073	21,897	1,297

Joint ventures <i>in thousands of euros</i>	Assets 31.12.		Liabilities 31.12.		Equity 31.12.	Income	Expenses	Net profit/ (loss)
	Current assets	Non- current assets	Current liabilities	Non- current liabilities				
2012								
OÜ Unigate	3,615	-	3,777	-	(162)	-	2	(2)
Poolkoksimäe Sulgemise OÜ	416	75	455	-	36	6,146	6,146	0
SIA Zakusala Estates	45	4,064	4,395	-	(286)	-	94	(94)
OÜ Kortermaja	6	-	3	-	3	51	97	(46)
Total	4,082	4,139	8,630	-	(409)	6,197	6,339	(142)
2011								
OÜ Unigate	3,637	-	3,517	-	120	-	1	(1)
Poolkoksimäe Sulgemise OÜ	596	161	721	-	36	4,103	4,070	33
SIA Zakusala Estates	70	4,054	462	3,854	(192)	-	67	(67)
OÜ Kortermaja	68	-	14	-	54	140	188	(48)
Total	4,371	4,215	4,714	3,854	18	4,243	4,326	(83)

Note 21 Other long-term loans and receivables

in thousands of euros

	31.12.2012	31.12.2011
Long-term loans (Notes 17, 36)	3,666	5,096
Long-term interest receivables (Note 36)	-	17
Long-term bank deposit (Note 36)*	49	180
Long-term receivable from buyer of subsidiary (Note 36)	-	96
Long-term receivables from customers of construction services (Note 36)**	13,473	11,676
Total other long-term loans and receivables	17,188	17,065

* As at 31.12.2012, long-term receivables included a deposit in the amount of EUR 35 thousand with the due date of 27 June 2018 and interest rate of 5.35%, a deposit in the amount of EUR 2 thousand with the due date 23 July 2017 and interest rate of 0.66 % and a deposit in the amount of EUR 12 thousand with the due date of 12 January 2016 and interest rate of 2.0%.

** incl. long-term receivables to buyer of Balsiu School in amount of EUR 10,459 thousand (31.12.2011: EUR 10,639 thousand).

Note 22 Deferred income tax assets and liabilities

in thousands of euros

Break-down of deferred income tax assets and liabilities in Latvian and Lithuanian subsidiaries:

31.12.2012	Latvia	Lithuania	Total
Deferred income tax liability			
effect of other payables	-	(327)	(327)
Deferred income tax assets			
tax loss carryforwards	-	704	704
effect of carrying amount of property, plant and equipment	(12)	-	(12)
effect of stage of completion method	43	47	90
effect of write-down of receivables	32	17	49
effect of write-down of inventories	806	-	806
effect of provisions	-	17	17
other effects	265	-	265
Deferred income tax assets	1,134	785	1,919
Deferred income tax charge of the financial year (Note 11)	(30)	(267)	(297)
31.12.2011	Latvia	Lithuania	Total
Deferred income tax liability			
effect of other payables	-	(1,764)	(1,764)
other effects	-	(15)	(15)
offsetting of deferred income tax assets and liabilities	-	1,648	1,648
Deferred income tax liability	-	(131)	(131)
Deferred income tax assets			
tax loss carryforwards	-	629	629
effect of carrying amount of property, plant and equipment	(12)	-	(12)
effect of stage of completion method	47	46	93
effect of write-down of receivables	32	17	49
effect of write-down of inventories	804	198	1,002
effect of provisions	-	17	17
effect of other payables	-	1,509	1,509
other effects	231	-	231
offsetting of deferred income tax assets and liabilities	-	(1,648)	(1,648)
Deferred income tax assets	1,102	768	1,870
Deferred income tax expense(-charge) of the financial year (Note 11)	(284)	131	(153)

Note 23 Investment property

in thousands of euros

	Land	Right of superficies	Buildings	Construction in progress	Total
Cost at 31.12.2010	134	-	1,152	2,418	3,704
Accumulated depreciation 31.12.2010	-	-	(119)	-	(119)
Carrying amount at 31.12.2010	134	-	1,033	2,418	3,585
Exchange rate difference	2	-	3	-	5
Acquisition	-	-	2,536	1,112	3,648
Disposals	-	-	(2,460)	-	(2,460)
Reclassification	-	21	14	(2,418)	(2,383)
Depreciation	-	-	(82)	-	(82)
Carrying amount at 31.12.2011	136	21	1,044	1,112	2,313
Cost at 31.12.2011	136	29	1,215	1,112	2,492
Accumulated depreciation at 31.12.2011	-	(8)	(171)	-	(179)
Carrying amount at 31.12.2011	136	21	1,044	1,112	2,313
Acquisition	-	-	-	1,463	1,463
Reclassification	-	-	2,491	(2,575)	(84)
Depreciation	-	(1)	(125)	-	(126)
Carrying amount at 31.12.2012	136	20	3,410	-	3,566
Cost at 31.12.2012	136	29	3,662	-	3,827
Accumulated depreciation at 31.12.2012	-	(9)	(252)	-	(261)
Carrying amount at 31.12.2012	136	20	3,410	-	3,566

As at 31.12.2012, the carrying amounts of investment properties do not significantly differ from their fair values (31.12.2011: the carrying amounts of investment properties did not significantly differ from their fair values). Fair values have mainly been estimated based on market transactions.

Investment properties have been acquired for the purpose of earning rental income as well as for capital appreciation or development in the future. Buildings located on the plot of land have temporarily been leased out under the operating lease terms. Information about leased investment properties is disclosed in Note 26. Rental income receivable, maintenance costs incurred and improvement expenses are immaterial.

Investment properties pledged as collateral as at 31.12.2012 for the loan total EUR 607 thousand (2011: EUR 642 thousand) (Note 31).

Note 24 Property, plant and equipment

in thousands of euros

	Land	Buildings	Right of superficies	Machinery and equipment	Other fixtures	Construction in progress and pre-payments	Total
Cost at 31.12.2010	825	5,692	29	17,608	4,986	-	29,140
Accumulated depreciation at 31.12.2010	-	(895)	(8)	(7,828)	(2,662)	-	(11,393)
Carrying amount at 31.12.2010	825	4,797	21	9,780	2,324	-	17,747
Currency translation differences	-	-	-	2	-	-	2
Acquisition	-	34	-	1,220	421	14	1,689
Disposals	-	-	-	(1,288)	(18)	-	(1,306)
Reclassification	-	-	(21)	9	4	(14)	(22)
Write-offs	-	-	-	(2)	(6)	-	(8)
Depreciation	-	(185)	-	(1,507)	(353)	-	(2,045)
Carrying amount at 31.12.2011	825	4,646	-	8,214	2,372	-	16,057
Cost at 31.12.2011	825	5,726	-	16,947	5,169	-	28,667
Accumulated depreciation at 31.12.2011	-	(1,080)	-	(8,733)	(2,797)	-	(12,610)
Carrying amount at 31.12.2011	825	4,646	-	8,214	2,372	-	16,057
Currency translation differences	-	-	-	(1)	-	-	(1)
Acquisition	-	62	-	793	450	11	1,316
Disposals	-	-	-	(109)	(4)	-	(113)
Reclassification	-	-	-	(7)	(2)	-	(9)
Write-offs	-	-	-	-	(6)	-	(6)
Depreciation	-	(188)	-	(1,551)	(652)	-	(2,391)
Carrying amount at 31.12.2012	825	4,520	-	7,339	2,158	11	14,853
Cost at 31.12.2012	825	5,788	-	16,963	5,518	11	29,105
Accumulated depreciation at 31.12.2012	-	(1,268)	-	(9,624)	(3,360)	-	(14,252)
Carrying amount at 31.12.2012	825	4,520	-	7,339	2,158	11	14,853

Information on leased assets is provided in Note 26 and on lease payments in Note 27.

Property, plant and equipment pledged as collateral as at 31.12.2012 for the loan total EUR 1,868 thousand (2011: EUR 1,762 thousand) (Note 31).

Note 25 Intangible assets

in thousands of euros

	Goodwill*	Software	Prepayments	Total
Cost at 31.12.2010	891	1,160	87	2,138
Accumulated amortisation at 31.12.2010	-	(630)	-	(630)
Carrying amount at 31.12.2010	891	530	87	1,508
Acquisitions	-	64	-	64
Disposals	-	(3)	-	(3)
Reclassification	-	-	(35)	(35)
Amortisation	-	(107)	-	(107)
Carrying amount at 31.12.2011	891	484	52	1,427
Cost at 31.12.2011	891	1,209	52	2,152
Accumulated amortisation at 31.12.2011	-	(725)	-	(725)
Carrying amount at 31.12.2011	891	484	52	1,427
Acquisitions	-	23	-	23
Amortisation	-	(85)	-	(85)
Carrying amount at 31.12.2012	891	422	52	1,365
Cost at 31.12.2012	891	1,231	52	2,174
Accumulated amortisation at 31.12.2012	-	(809)	-	(809)
Carrying amount at 31.12.2012	891	422	52	1,365

Prepayments for intangible assets relate to prospective replacement of the group's accounting software.

* As at the balance sheet date, an impairment test was performed for reasons of conservatism for the cash-generating unit AS Vooremaa Teed which goodwill is attributable to. In the reporting period, goodwill was not written down because the recoverable amount of the cash-generating unit exceeded the carrying amount of the non-current assets and goodwill of the cash-generating unit. The recoverable amount of the assets is determined as its value in use, using management-approved cash flow projections for the next 5 years. Post-projection period cash flows are extrapolated using reasonable growth rates. The management has re-evaluated the near-term outlook for road construction and therefore, it has used 0.0% (2011: 2.5%) as the long-term growth rate of income and expenses, 3% (2011: 21% growth) as the average sales decline and 12% (2011: 12%) as the average EBITDA margin. The average weighted cost of capital of 9% is used as the discount rate, which takes account of the company's area of activity and risk level. For determining the budgeted gross margin, the management used previous periods' business experience and competitive situation.

Note 26 Leased assets

in thousands of euros

Assets acquired under finance lease terms	31.12.2012	31.12.2011
Machinery and equipment		
Cost	6,378	9,004
Accumulated depreciation	(2,489)	(2,854)
Carrying amount	3,889	6,150

Assets leased under non-cancellable operating lease terms	2012	2011
Land lease agreements		
Payments in the reporting period	2	2
Payments in subsequent periods:	18	21
Payable next year	2	2
Payable in 1...5 years	7	8
Payables after 5 years	9	11

On the basis of cancellable lease agreements, operating lease payments totalling EUR 867 thousand were paid for passenger cars in 2012 (2011: EUR 879 thousand). The Company does not intend to use a bargain purchase option for the assets leased under the operating lease terms in the reporting period.

Lease agreements does not set any limits to groups' dividend or financing policies. Rented assets are not re-rented.

Investment property leased out under non-cancellable operating lease terms	31.12.2012	31.12.2011
Cost	3,798	1,351
Accumulated depreciation	(252)	(171)
Carrying amount	3,546	1,180

	2012	2011
Operating lease income received for investment properties	212	71
Future operating lease income:	2,303	237
next year	312	70
In 1...5 years	1,112	167
later than 5 years	879	-

Note 27 Borrowings

in thousands of euros

	Finance lease liabilities at present value	Loans from					Total borrowings (Note 36)	
		banks	entities under common control (Note 34)	management members (Note 34)	other entities	factoring		total
2012								
Balance at beginning of the year	2,974	29,909	6,945	-	510	-	37,364	40,338
Received	412	11,668	1,200	102	4	1,544	14,518	14,930
Paid	(902)	(18,638)	-	-	(2)	-	(18,640)	(19,542)
VAT paid on principal	(43)	-	-	-	-	-	-	(43)
Reclassification of loan to other payables	-	-	-	-	(197)	-	(197)	(197)
Exchange rate difference	-	18	-	-	-	-	18	18
Loan balance at end of the year	2,441	22,957	8,145	102	315	1,544	33,063	35,504
incl. current portion	782	5,513	8,145	-	315	1,544	15,517	16,299
non-current portion 1...5 years	1,659	17,444	-	102	-	-	17,546	19,205
Interest cost of reporting period	114	807	188	3	18	47	1,063	1,177
incl. capitalised interest cost	-	180	-	-	-	-	180	180
Average effective interest rate	3.7%	2.5%	1.9%	5.0%	5.5%	1.9%		
Base currencies	EUR	EUR, LTL	EUR	EUR	EUR	EUR		
2011								
Balance at beginning of the year	3,948	14,489	6,989	-	313	-	21,791	25,739
Received	773	20,798	-	-	197	-	20,995	21,768
Paid	(1,747)	(5,484)	-	-	-	-	(5,484)	(7,231)
Offset with a receivable	-	-	(44)	-	-	-	(44)	(44)
Exchange rate difference	-	106	-	-	-	-	106	106
Loan balance at end of the year	2,974	29,909	6,945	-	510	-	37,364	40,338
incl. current portion	825	8,294	6,945	-	510	-	15,749	16,574
non-current portion 1...5 years	2,149	21,615	-	-	-	-	21,615	23,764
Interest cost of reporting period	159	771	193	-	18	-	982	1,141
incl. capitalised interest cost	-	94	-	-	-	-	94	94
Average effective interest rate	3.1%	3.2%	3.2%	-	5.5%	-		
Base currencies	EUR, LVL	EUR, LTL, LVL	EUR	-	EUR	-		

	2012	2011
Minimum future payments under finance lease	2,580	3,254
incl. current portion	851	941
non-current portion with the term of 1...4 years	1,729	2,313

Borrowings with floating interest rates related to Euribor, Rigibor (Riga Interbank Offered Rate - the index of Latvian interbank credit interest rates) or Vilibor (Vilnius Interbank Offered Rate - the index of Lithuanian interbank credit interest rates) are divided by the interest rate changes and the contractual repricing dates as follows:

	2012	2011
Finance lease liabilities		
6-12 months	1,910	2,320
Bank loans		
1-5 months	1,719	8,825
6-12 months	21,238	21,084
Loans from entities under common control		
6-12 months	8,145	6,945
Loans from management members		
6-12 months	102	-
Factorings		
6-12 months	1,544	-
Total	34,658	39,174

Borrowings with the contractual fixed interest rate are divided as follows:

	2012	2011
Finance lease liabilities	531	654
Loans from other entities	315	510
Total	846	1,164

Although different risk factors prevailed in global financial markets throughout the year, it was generally relatively stable. The risk margins on loans did not significantly change as compared to last year, but falling EURIBOR had a more pronounced effect on loan interest. Therefore, we can state that the fair value of bank loans generally equals their carrying amount. Among the loans from entities under common control, there is a loan from AS Järvevana originating from the demerger, the interest of which after the first 12 months is 12 month Euribor + 1%.

Loan collaterals and pledged assets are presented in Note 31.

Note 28 Payables and prepayments

in thousands of euros

	31.12.2012	31.12.2011
Trade payables (Note 36)	21,602	34,206
Payables to employees	5,541	2,835
Tax liabilities, except for corporate income tax		
value added tax	2,186	837
personal income tax	533	458
social security tax	989	871
land tax	-	118
unemployment insurance tax	88	86
contributions to mandatory funded pension	40	28
other taxes	240	106
Total tax liabilities, except for corporate income tax	4,076	2,504
Amounts due to customers for contract works (Notes 33, 36)	12,550	10,314
Other liabilities (Note 36)		
interest liabilities	113	111
payable for registered immovables from demerger	5,380	6,391
other liabilities	2,639	402
Total other liabilities	8,132	6,904
Prepayments received	11,308	4,872
Total payables and prepayments	63,209	61,635
incl. payables to related parties (Note 34)	5,412	7,093

Note 29 Provisions

in thousands of euros

	Provision for warranty obligation for construction	Provision for onerous const- ruction contracts	Provision for legal costs and claims filed	Other provisions	Total provisions
2012					
Residual value at beginning of the year	1,367	3,526	1,326	628	6,847
Set up (Notes 4, 6)	814	173	15	901	1,903
Used during the year	(563)	(1,632)	-	(372)	(2,567)
Exchange rate difference	1	-	1	-	2
Balance at end of the year	1,619	2,067	1,342	1,157	6,185
incl. current portion	1,619	2,067	1,342	1,137	6,165
non-current portion (Note 30)	-	-	-	20	20
2011					
Residual value at beginning of the year	1,112	2,226	262	74	3,674
Set up (Notes 4, 6 ,8)	1,063	2,914	1,063	883	5,923
Used during the year	(815)	(1,616)	-	(330)	(2,761)
Exchange rate difference	7	2	1	1	11
Balance at end of the year	1,367	3,526	1,326	628	6,847
incl. current portion	1,367	3,526	1,326	562	6,781
non-current portion (Note 30)	-	-	-	66	66

Note 30 Other long-term payables

in thousands of euros

	31.12.2012	31.12.2011
Trade payables (Note 36)	1,553	790
Long-term interest payables	3	-
Long-term provision (Note 29)	20	66
Total other long-term payables	1,576	856

Note 31 Loan collaterals and pledged assets

in thousands of euros

The group has entered into commercial pledge contracts to secure loans and other liabilities, set mortgages on assets and pledged the shares of its subsidiaries:

Commercial pledges	31.12.2012	31.12.2011
Movable property	53,897	34,320
Term deposit (Note 21)	1	145
Financial assets*	13,179	11,759
Total	67,077	46,224

* The financial assets of UAB Balsiu mokyklos SPV which OÜ Merko Property has pledged to secure the investment loan in the amount of EUR 7,081 thousand for the benefit of Nordea Bank Finland Plc.

Mortgages	31.12.2012	31.12.2011
Inventories (Note 18)	38,942	38,286
Land and buildings (Note 24)	613	3,704
Other non-current assets (Note 24)	1,255	1,624
Investment properties (Note 23)	607	642
Total	41,417	44,256

Pledges of shares

In addition to the commercial pledge for financial assets, OÜ Merko Property has pledged the shares of its wholly-owned subsidiary UAB Balsiu mokyklos SPV for the benefit of Nordea Bank Finland Plc. An investment loan in the amount of EUR 7,081 is secured by the pledge.

UAB Merko Bustas has pledged the shares of its wholly-owned subsidiary UAB MN Projektas for the benefit of Swedbank AB. An investment loan in the amount of EUR 2,141 thousand is secured by the pledge.

Note 32 Share capital

In 2012, no changes were made to the share capital.

In conjunction with the accession of the Republic of Estonia to the eurozone at 1 January 2011 and pursuant to the amendments to the Commercial Code entered into force at 1 July 2010, the share capital of AS Merko Ehitus was translated from EEK 177,000 thousand into EUR 11,312 thousand and shares without nominal value were taken into use in 2011. The share capital of AS Merko Ehitus consists of 17,700 thousand shares without nominal value. In addition, the share capital was increased by means of a bonus issue from retained earnings in the amount of EUR 688 thousand through increasing the book value of shares so that the new size of the share capital is EUR 12,000 thousand. The new book value of the share is EUR 0.67797.

The Commercial Code of the Republic of Estonia specifies the following requirements for the share capital of the entities registered in Estonia:

- the minimum share capital of a public limited company shall be at least EUR 25 thousand;
- the net assets of a public limited company shall be at least one half of the Company's share capital but not less than EUR 25 thousand.

The size of share capital or its minimum and maximum limits are set out in the articles of association of a public limited company whereas the minimum share capital shall equal at least $\frac{1}{4}$ of maximum share capital.

According to the current articles of association of AS Merko Ehitus, the Company's share capital consists of 17,700 thousand registered ordinary shares without nominal value which have been fully paid for and without amending the articles of association of the public limited company, changes can be made to the Company's share capital within the range of EUR 6,000 – 24,000 thousand. As at 31.12.2012, the share capital of AS Merko Ehitus was EUR 12,000 thousand and the net assets were EUR 116,925 thousand, therefore the Company's equity and share capital were in compliance with the requirements established in the Republic of Estonia.

Note 33 Construction contracts in progress

in thousands of euros

	31.12.2012	31.12.2011
Costs incurred for construction contracts in progress and corresponding profit*	583,046	395,877
Progress billings submitted	(576,615)	(390,175)
Revenue recorded from construction services during the period	220,135	198,294
Amounts due from customers for contract works (Notes 16, 36)	18,981	16,016
Amounts due to customers for contract works (Notes 28, 36)	(12,550)	(10,314)
Advance payments received for contract works	11,188	3,522

Amounts due from customers for contract works are included in the statement of financial position line *Trade and other receivables*. Amounts due to customers for contract work are included in the statement of financial position line *Trade and other payables*.

* Costs incurred for construction contracts in progress and corresponding profit have been presented for contracts in effect, including those entered into in 2011 and 2010.

Note 34 Related party transactions

in thousands of euros

In compiling the Annual Report, the following entities have been considered as related parties:

- parent company AS Riverito;
- shareholders of AS Riverito with significant influence over AS Merko Ehitus through AS Riverito;
- other shareholders with significant influence;
- other subsidiaries of AS Riverito, so-called 'entities controlled by the parent';
- associates and joint ventures;
- key members of the management (supervisory and management board), their close relatives and entities under their control or significant influence.

Significant influence is presumed to exist when the person has more than 20% of the voting power.

The parent of AS Merko Ehitus is AS Riverito. As at 31.12.2012 and 31.12.2011, AS Riverito owned 71,99% of the shares of AS Merko Ehitus. The ultimate controlling party of the group is Mr Toomas Annus.

Goods and services

in thousands of euros

	2012	2011
Provided services		
Parent company	6	-
Associates and joint ventures	251	159
Entities under common control	29	1,462
Members of the management	2	6
Other related parties	668	23
Total services provided	956	1,650
Interest income		
Associates and joint ventures	111	108
Entities under common control	-	44
Total interest income	111	152
Purchased services and materials		
Parent company	115	115
Associates and joint ventures	-	74
Entities under common control	153	137
Other related parties	126	204
Total purchased services and materials	394	530
Interest expense		
Parent company	79	122
Entities under common control	188	193
Members of the management	3	-
Total interest expense	270	315

Balances with related parties

in thousands of euros

	31.12.2012	31.12.2011
Receivables from related parties		
Loans granted (Note 17)		
Associates and joint ventures	4,992	4,930
Receivables and prepayments (Note 16)		
Parent company	9	3
Associates and joint ventures	920	807
Entities under common control	13	191
Other related parties	1	26
Total receivables and prepayments	943	1,027
Prepayments for inventories (Note 18)		
Entities under common control	-	3,810
Total receivables from related parties	5,935	9,767
Payables to related parties		
Loans received (Note 27)		
Entities under common control	8,145	6,945
Members of the management	102	-
Total loans received	8,247	6,945
Payables and prepayments (Note 28)		
Parent company	12	27
Entities under common control	5,397	6,963
Associates and joint ventures	-	51
Members of the management	3	-
Other related parties	-	52
Total payables and prepayments	5,412	7,093
Total payables to related parties	13,659	14,038

In 2012, no impairment losses were recognised for receivables from entities under common control (2011: EUR 991 thousand).

Remuneration of the members of the Supervisory and Management Boards

In 2012, the members of the Supervisory and Management Boards of AS Merko Ehitus and Management Boards of its significant subsidiaries were paid remuneration totalling EUR 1,821 thousand (2011: EUR 1,269 thousand).

Termination benefits of members of the Supervisory and Management Boards

Authorisation agreements have been entered into with the members of the Supervisory Board according to which no termination benefits are paid to them upon the termination of the contract. Upon premature removal or termination of authority of the members of the Supervisory and Management Boards, the group has the obligation to pay compensation totalling EUR 731 thousand (2011: EUR 674 thousand). In 2012, benefits were paid to the management members in the amount of EUR 157 thousand (2011: no benefits were paid).

Note 35 Contingent liabilities

in thousands of euros

The group has purchased the following guarantees from financial institutions to guarantee the group's obligations to third parties. These amounts represent the maximum right of claim by third persons against the group in case the group is unable to meet its contractual obligations. Management estimates that additional expenses related to these guarantees are unlikely.

	31.12.2012	31.12.2011
Performance period's warranty to the customer	26,731	22,276
Tender warranty	1,929	3,309
Guarantee warranty period	11,627	9,347
Prepayment guarantee	10,020	12,270
Contracts of surety	1,507	1,248
Payment guarantee	-	1,255
Total contingent liabilities	51,814	49,705

Performance period's warranty to the customer – warranty provider guarantees to the customer that the contractor's obligations arising from construction contract will be adequately completed.

Tender warranty – warranty provider guarantees to the customer arranging the tender process that the tenderer will sign a contract as per tender conditions.

Guarantee for warranty period – warranty provider guarantees to the customer that the construction defects discovered during the warranty period will be repaired.

Prepayment guarantee – warranty provider guarantees to the customer that advances will be reimbursed, if contractor fails to deliver goods or services agreed.

Payment guarantee – warranty provider guarantees to the customer payment for goods or services.

Tax authorities have the right to review the group's tax records within 6 years after submitting the tax declaration and upon detecting errors, impose additional taxes, interest and fines. The group's management estimates that there are not any circumstances which might lead the tax authorities to impose additional significant taxes on the group.

For legal risks, please refer to the respective paragraph of Note 36.

Note 36 Risk management

Financial risks management

In its daily activities, the group needs to consider various financial risks. The key risks include: market risk (incl. interest rate risk and foreign currency risk), credit risk, liquidity risk and equity risk. Based on the group's balance sheet structure and position in the market, none of these risks has a significant impact as at the date of preparation of the financial statements. The group's risk management is based on laws, regulations, requirements and regulations arising from International Financial Reporting Standards, as well as the group's internal regulations and good business practices. The group's finance department is responsible for management of financial risks.

1. Credit risk

Credit risk relates to a potential damage which would occur if the parties to the contract are unable to fulfil their contractual obligations. For mitigating credit risk, the payment behaviour of clients is constantly monitored, their financial position is analysed and if necessary, third persons are engaged as a guarantor in transactions. Construction activities are partially financed by customer prepayments. As a rule, a precondition for receiving a prepayment is a bank guarantee for the prepayment submitted to the customer. Free cash is mostly held in overnight deposits or term deposits at Swedbank, SEB and Nordea bank groups. Swedbank AS and SEB Pank AS do not have separate ratings by Moody's. The parent company of Swedbank AS - Swedbank AB and the parent company of SEB Pank AS - Skandinaviska Enskilda Banken AB have respectively ratings A2 and A1 by Moody. Nordea Bank Finland has rating Aa3. The management estimates that the group is not exposed to significant credit risk.

Financial assets exposed to credit risk

in thousands of euros

	Allocation by due dates		Carrying amount	Collateral
	1-12 months	2-5 years		
31.12.2012				
Cash and cash equivalents (Note 14)	35,316	-	35,316	-
Term deposits (Notes 15, 21)	-	49	49	-
Trade receivables (Notes 16, 21)	34,103	13,473	47,576	-
Amounts due from customers for contract works (Notes 16, 33)	18,981	-	18,981	-
Loans granted (Notes 16, 17, 21)	1,887	3,666	5,553	5,452
Interest receivables (Notes 16, 21)	948	-	948	-
Other short-term receivables (Note 16)	1,352	-	1,352	-
Total	92,587	17,188	109,775	5,452

31.12.2011				
Cash and cash equivalents (Note 14)	18,510	-	18,510	-
Term deposits (Notes 15, 21)	140	180	320	-
Trade receivables (Notes 16, 21)	35,607	11,772	47,379	-
Amounts due from customers for contract works (Notes 16, 33)	16,016	-	16,016	-
Loans granted (Notes 16, 17, 21)	7,673	5,096	12,769	11,152
Interest receivables (Notes 16, 21)	881	17	898	-
Other short-term receivables (Note 16)	1,444	-	1,444	-
Total	80,271	17,065	97,336	11,152

The group's customers are primarily large local entities or public sector entities (as at 31.12.2012, the public sector proportion in accounts receivable amounted to 37.4% (as at 31.12.2011: 58.3%)) with well-known and sufficient creditworthiness.

Trade receivables by due date (excluding long-term receivables):

	31.12.2012		31.12.2011	
Not overdue	26,556	77.9%	29,714	83.4%
1-30 days overdue	4,988	14.6%	4,686	13.2%
31-60 days overdue	1,008	3.0%	120	0.3%
61-90 days overdue	245	0.7%	232	0.7%
91-120 days overdue	876	2.6%	376	1.0%
121-180 days overdue	321	0.9%	380	1.1%
More than 180 days overdue	109	0.3%	99	0.3%
Total trade receivables (Note 36)	34,103	100%	35,607	100%

As at the balance sheet date, the amount of overdue receivables was EUR 7,547 thousand (31.12.2011: EUR 5,893 thousand), of which EUR 6,641 thousand has been collected by 15 March 2013. In a year, the share of overdue receivables in total receivables increased from 16.6% to 22.1%. The management estimates that there are sufficient reasons to conclude that the receivables reported in the financial statement will be paid off by the buyers. Trade receivables and receivables from customers of construction works under the stage of completion method have not been guaranteed with additional collateral as is customary in the industry.

As at balance sheet date, the loans granted to associates and joint ventures, the economic activities of which the group has a good overview of totalled EUR 4,992 thousand (31.12.2011: 4,930 thousand) and therefore, no additional collateral is required. As at 31.12.2012, the outstanding balance granted to unrelated legal entities was EUR 475 thousand (31.12.2011: EUR 7,732 thousand) and the outstanding loan balance granted to unrelated individuals was EUR 86 thousand (31.12.2011: 107 thousand), which in management's opinion is not exposed to material credit risk. As at the year-end, the management expects to collect these loans on time.

2. Market risk

Interest risk

Interest risk arises from interest rate changes in the financial markets as a result of which it may be necessary to revalue the group's financial assets and take into consideration higher financing costs in the future. Most of the group's bank loans have floating interest rates based on either Euribor or the interbank rates of the countries of incorporation of the entities. In 2012, the share of interest-bearing liabilities in the group's capital structure decreased and management considers this share to be moderate (as at 31.12.2012, 15.8% and as at 31.12.2011, 18.3% of the balance sheet total) and effect of changes in the interest rate environment to be insignificant for the group's results over the next 12-month.

Effect of changes in interest rate risk on finance costs

As at 31.12.2012, the group's interest-bearing liabilities totalled EUR 35,504 thousand, of which short-term loans and repayments of long-term liabilities totalled EUR 16,299 thousand and long-term loans and finance lease liabilities totalled EUR 19,205 thousand. Loan interest depended on interbank 1-12 month loan base interest in the entity's domicile and Euribor/Viliber. As at 31.12.2012, the break-down of interest-bearing borrowings was as follows:

	31.12.2012	31.12.2011
Fixed rate liabilities	846	1,164
Variable rate liabilities 1-5 months	1,719	8,825
Variable rate liabilities 6-12 months	32,939	30,349
Total interest-bearing borrowings	35,504	40,338

The management does not expect many changes in base interest rates, the market is stable and base interest rates remain low. Assuming that average EURIBOR is 10 bp and Viliber 20 bp higher over the next 12 months as compared to the beginning of the year and there is no change in the position of liabilities, interest expenses would increase by EUR 37 thousand.

In addition to risk arising from changes in Euribor, Viliber and Rigibor, there is risk due to changes in the risk margin attributable to the changes in the economic environment related refinancing of liabilities. This is most directly manifested in a possible need to extend overdraft credit contracts. As at the year-end, group entities had entered in overdraft contracts with banks in the total amount of EUR 6,489 thousand, of which the withdrawn limit was EUR 196 thousand. In 2013, contracts in the total amount of EUR 3,895 thousand will expire, the extension of which is currently under consideration.

Foreign exchange risk

The group's economic activities are conducted mainly in the currencies of the countries of location of the companies: euros in Estonia, Latvian lats in Latvia and Lithuanian litas in Lithuania. From 1 January 2011, Estonia adopted the euro as its national currency. Latvian lats and Lithuanian litas are pegged to the euro. The exchange rate of the Latvian lats is 1 EUR= LVL 0.702804 +/-1% and Latvia is expected to adopt the euro at 1 January 2014. In order to eliminate foreign exchange risk, the proportions of assets and liabilities denominated in different currencies are monitored and key foreign contracts and the preferred currency for conclusion of long-term loan contracts is the euro. The break-down of assets and liabilities in local currencies as at the balance sheet date is as follows:

	In EUR	In LVL	In LTL	In USD
31.12.2012				
Assets	63.5%	25.8%	10.7%	0.0%
Liabilities	79.8%	14.5%	5.7%	0.0%
31.12.2011				
Assets	72.0%	24.2%	3.7%	0.1%
Liabilities	86.6%	12.9%	0.5%	0.0%

If as at the year-end, the national currencies of Latvia and Lithuania had been devalued by 25%, the Group would have incurred additional finance costs in the amount of EUR 9,120 thousand, incl. EUR 6,317 thousand on Latvian and EUR 2,803 thousand on Lithuanian position. As Estonia uses the euro and Latvia plans to adopt the euro at 1 January 2014, the need and probability for devaluation of the Lithuanian national currency is low and the situation as a whole is stable in the Baltic States.

3. Liquidity risk

The Company's liquidity or solvency represents its ability to settle its liabilities to creditors on time. As at 31.12.2012, the group's current ratio was 2.1 (31.12.2011: 2.0) and the quick ratio 1.1 (31.12.2011: 1.0). To complement available current assets, and to ensure liquidity and better management of cash flows, the group has concluded overdraft agreements with banks. As at end of the year, the group entities had concluded overdraft contracts with banks in the total amount of EUR 6,489 thousand (31.12.2011: EUR 7,495 thousand). In addition to the overdraft facility, the Company has a current loan facility with the limit of EUR 3,500 thousand (31.12.2011: EUR 3,500 thousand) from AS Riverito, which had not been withdrawn in full as at the end of current and previous financial years.

The management estimates that the group's capital structure – a solid proportion of equity at 52.0% of the balance sheet total and a moderate proportion of interest bearing liabilities at 15.8% of the balance sheet total – ensures the Company's trustworthiness for creditors in the changing economic climate and significantly improves the feasibility of the extension of existing financial liabilities and raising of additional debt.

Financial assets/liabilities

in thousands of euros

	Allocation by due date			Total	Carrying amount
	1-3 months	4-12 months	2-5 years		
31.12.2012					
Assets					
Cash and overnight deposits (Note 14)	35,316	-	-	35,316	35,316
Term deposits (Notes 15, 21)	-	-	49	49	49
Trade receivables (Notes 16, 21)	29,055	5,048	13,473	47,576	45,576
Due from customers of construction works (Notes 16, 33)	18,981	-	-	18,981	18,981
Loans and interest (Notes 16, 17, 21)	1,915	920	3,666	6,501	6,501
Other short-term receivables (Note 16)	1,320	32	-	1,352	1,352
Total	86,587	6,000	17,188	109,775	109,775
Liabilities					
Trade payables (Notes 28, 30)	15,937	5,665	1,553	23,155	23,155
Due to customers of construction works (Notes 28, 33)	12,550	-	-	12,550	12,550
Loan and finance lease liabilities (Note 27)*	8,916	7,383	19,205	35,504	35,504
Other liabilities (Note 28)	5,431	2,701	3	8,135	8,135
Total	42,834	15,749	20,761	79,344	79,344
Net assets / liabilities	43,753	(9,749)	(3,573)	30,431	30,431

	Allocation by due date			Total	Carrying amount
	1-3 months	4-12 months	2-5 years		
31.12.2011					
Assets					
Cash and overnight deposits (Note 14)	18,510	-	-	18,510	18,510
Term deposits (Notes 15, 21)	-	140	180	320	320
Trade receivables (Notes 16, 21)	31,261	4,346	11,772	47,379	47,379
Receivables recorded based on the stage of completion of construction contracts (Notes 16, 33)	16,016	-	-	16,016	16,016
Loans and interest (Notes 16, 17, 21)	6,297	2,257	5,113	13,667	13,667
Other short-term receivables (Note 16)	202	1,242	-	1,444	1,444
Total	72,286	7,985	17,065	97,336	97,336
Liabilities					
Trade payables (Notes 28, 30)	32,978	1,228	790	34,996	34,996
Due to customers of construction works (Notes 28, 33)	10,314	-	-	10,314	10,314
Loan and finance lease liabilities (Note 27)*	356	16,218	23,764	40,338	40,338
Other liabilities (Note 28)	6,724	180	-	6,904	6,904
Total	50,372	17,626	24,554	92,552	92,552
Net assets / liabilities	21,914	(9,641)	(7,489)	4,784	4,784

* The schedule of expected interest payments cannot be determined with reasonable accuracy. In line with the best practice of property development, the loan obligations to acquire land plots have been assumed with open-end maturities. The repayment of these loan obligations depends on the progress of related development projects and on the timing of cash flows generated from those projects after their completion. Consequently, the management is of opinion that even its best estimate of the timing of expected interest payments would not be sufficiently accurate for the users of these financial statements and this information has not been disclosed.

Capital management

The group considers debt and total equity as capital. As at 31.12.2012, the total equity attributable to equity owners of the parent was EUR 116,925 thousand (31.12.2011: EUR 109,240 thousand). The group's principle is to maintain a strong equity base for the purpose retaining its trustworthiness among its shareholders, creditors and the market, and to ensure the group's sustainable development. Over the long term, the group's goal is to generate income for its shareholders and ensure its ability to pay dividends.

The group's equity is currently greatly related to the land plots portfolio invested for the purpose of real estate development, which the group has either increased or decreased according to the changes in the market primarily through its own developments. The group can additionally regulate the equity structure through dividends payable to shareholders or repayments of paid in share capital.

The group considers it important to ensure an optimal capital structure. Therefore, it monitors that the group's equity to assets ratio should be at least 40% (31.12.2012: 52.0%, 31.12.2011: 49.6%) and interest-bearing debt to assets ratio would not exceed 25% (31.12.2012: 15.8%, 31.12.2011: 18.3%). The requirement laid down in the overdraft contract entered into with Nordea Bank Finland Plc Estonia branch specifies that the share of the company's consolidation equity in total assets would not fall below 35% and the group has complied with this requirement.

According to the good market practice, the group uses the ratio of net debt to total capital to monitor its capital:

	31.12.2012	31.12.2011
Borrowings	35,504	40,338
Less: cash and cash equivalents and short-term deposits	(35,316)	(18,650)
Net debt	188	21,688
Total equity attributable to owners of the parent	116,925	109,240
Total net debt and equity attributable to equity owners of the parent	117,113	130,928
Share of net borrowings	0.2%	16.6%

Other risks management

Legal risk

Due to different interpretations of contracts, regulations and laws related to group's principal activities, there is a risk that some buyers, contractors or supervisory authorities evaluate the Company's activities from the perspective of laws or contracts from a different position and dispute the legitimacy of the Company's activities.

As at 31 December 2012, a provision has been set up at the group in the amount of EUR 1,342 thousand for covering potential claims and legal costs (31 December 2011: EUR 1,326 thousand), (Note 29).

An overview of the key legal disputes of group entities as at 31 December 2012 is presented below.

Estonia

On 9 January 2011, a court case opened at Harju County Court which among other issues dealt with the claim filed against AS Merko Ehitus and its subsidiaries OÜ Metsailu, OÜ Woody, OÜ Constancia in relation to the giving of the bribe to the former Tallinn city official Ivo Parbus. The Prosecutor's Offices has charged Merko Ehitus and its subsidiaries with the giving of the bribe by the then member of management board Tõnu Korts – Estravel's gift coupon of EUR 1,597.80 and the book with the list price of EUR 26.20 titled "Eesti Talurahva Arhitektuur" (*Estonian Vernacular Architecture*) - in order to accelerate real estate business related proceedings in Tallinn City authorities.

On 30 March 2012 Harju County Court proclaimed the judgment, according to which AS Merko Ehitus, OÜ Metsailu, OÜ Woody, OÜ Constancia were convicted based on Penal Code section 297 subsection 3 (granting or promising a gratuity by a legal person) imposing a pecuniary punishment to AS Merko Ehitus in the amount of EUR 300,000, to OÜ Woody and OÜ Constancia each in the amount of EUR 200,000 and to OÜ Metsailu in the amount of EUR 100,000. According to the Income Tax Act, a pecuniary punishment is subject to income tax and upon the enforcement of the pecuniary punishment the group companies will have to pay EUR 213 thousand of income tax in addition to the amount of the pecuniary punishment. To reflect the judgment of Harju County Court after the balance sheet date, an additional provision in the amount of EUR 1,013 thousand was set up to cover the possible pecuniary punishment and associated tax liability.

At 21 January 2013, Tallinna District Court upheld the judgement of Harju County Court and dismissed the appeals of AS Merko Ehitus, OÜ Metsailu, OÜ Woody and OÜ Constancia. The judgment has not been entered into force, AS Merko Ehitus and its subsidiaries have appealed it to the Supreme Court.

Pursuant to § 38 subsection 1 clause 1, a contracting authority shall not award a public contract to a person and shall exclude from a procurement procedure a tenderer or candidate who or whose legal representative has been convicted of committing offences relating to professional misconduct in a criminal procedure, and whose data concerning punishment have not been deleted from the penal register in accordance with the Penal Register Act. Accordingly, AS Merko Ehitus, OÜ Metsailu, OÜ Woody, OÜ Constancia cannot participate in the public procurement in case of criminal conviction. The respective limitation does not concern other companies of the group.

The management of the group is of opinion that the company has not granted a gratuity and has conducted its activities in conformity with the laws of the Republic of Estonia.

At 5 December 2012, Sanoma Trade OY filed a claim in Helsinki Arbitration Court against AS Merko Ehitus Eesti in the amount of EUR 173 thousand. The claim is related to construction works performed by AS Merko Ehitus (10068022) in 1999-2001. The group's management is of opinion that Helsinki Arbitration Court lacks jurisdiction to review this claim; the claim has also expired and is manifestly unfounded.

Lithuania

At 25 May 2012, RUAB Vakarų inžineriniai tinklai (hereinafter „Vakarų“) filed a claim against the Lithuanian branch of AS Merko Ehitus in the amount of LTL 680 thousand (EUR 197 thousand), related to the repeal of the joint venture contract concerning the sewerage and wastewater pipeline project (project „Construction of Sewerage and Wastewater Pipelines in Seda, Plinkšiai and Bugeniai“). AS Merko Ehitus does not believe that the joint venture contract was terminated illegally, but rather that it was related to the breach of the contract by the partner.

As a legal restructuring has been launched for Vakarų, AS Merko Ehitus has filed a creditor's claim in the amount of LTL 490 thousand (EUR 142 thousand) in respect of the failure to fulfil the project's obligations. At 25 February 2013, AS Merko Ehitus filed an additional claim against Vakarų regarding a partial repeal of the invoice in the amount of LTL 242 thousand (EUR 70 thousand)

that had been included in the claim by Vakarų at 25 May 2012 in the amount of LVL 680 thousand (EUR 197 thousand). As at 31 December 2012, allowances have been set up in full by the group in respect of these claims.

At 10 October 2012, UAB Šiaulių Vandenys filed a claim against UAB Merko Statyba, because according to UAB Šiaulių Vandenys, UAB Merko Statyba failed to meet the deadline for works. The claim included a fine for delay, 7.75% interest and state property taxes in the amount of LTL 237 thousand (EUR 69 thousand). At 11 January 2013, UAB Merko Statyba filed a counterclaim in the amount of LTL 537 thousand (EUR 155 thousand) and extension of the deadline for works by 154 days, primarily due to the refusal by the counterparty to pay for the additional works contracted by UAB Šiaulių Vandenys and to extend the deadline for works. The pre-court institution – the Dispute Settlement Council – decided to satisfy the claim of UAB Merko Statyba regarding payment for additional works and extension of the deadline for works. The dispute will continue in the court. The hearing of the Court of First Instance has not been set by the time of preparation of the financial statements.

Value of assets

Although the economic environment has attained certain stability, the effect of the real estate market risk was material for assessing the company's activities. In 2011, faster than forecast appreciation of construction prices in respect of the contracts entered into in 2009/2010 and a slow recovery of the Baltic real estate market made it necessary to write down the group's development projects, due to which a loss in the amount of EUR 5,978 thousand was incurred in 2011. No write-downs were performed in 2012. However, a loss of EUR 448 thousand was recognised, primarily related to the write-down of irrecoverable receivables of Latvian and Lithuanian entities in the amount of EUR 448 thousand (2011: 83 thousand).

Note 37 Supplementary disclosures on the parent

The financial information of the parent comprises separate primary statements of the parent (income statement, statement of financial position, cash flow statement and statement of changes in equity), the disclosure of which is required by the Estonian Accounting Act. The primary financial statements of the parent have been prepared using the same accounting methods and measurement bases as those used for the preparation of the consolidated financial statements, except for subsidiaries, associates and joint ventures which are reported at cost in the separate primary financial statements of the parent.

INCOME STATEMENT

<i>in thousands of euros</i>	2012	2011
Revenue	13,815	111,489
Cost of goods sold	(14,357)	(111,969)
Gross profit	(542)	(480)
Marketing expenses	(102)	(1,229)
General and administrative expenses	(1,393)	(3,313)
Other operating income	46,540	8,451
Other operating expenses	(512)	(519)
Operating profit	43,991	2,910
Finance income/costs	(440)	(519)
Finance income/costs from investments in subsidiaries	2,771	-
Profit (loss) before tax	46,322	2,391
Deferred income tax expense	(137)	(275)
Net profit for the year	46,185	2,116

STATEMENT OF FINANCIAL POSITION

<i>in thousands of euros</i>	31.12.2012	31.12.2011
ASSETS		
Current assets		
Cash and cash equivalents	8,313	5,665
Receivables and prepayments	14,194	100,836
Prepaid corporate income tax	406	406
Inventories	15,940	21,265
Total current assets	38,853	128,172
Non-current assets		
Investments in subsidiaries	104,195	41,867
Investments in associates and joint ventures	54	258
Other long-term financial assets	33,284	3,147
Investment property	20	21
Property, plant and equipment	145	1,098
Intangible assets	-	390
Total non-current assets	137,698	46,781
TOTAL ASSETS	176,551	174,953
LIABILITIES		
Current liabilities		
Borrowings	12,519	15,810
Trade and other payables	9,432	39,017
Short-term provisions	946	2,752
Total current liabilities	22,897	57,579
Non-current liabilities		
Other long-term trade payables	104	10,009
TOTAL LIABILITIES	23,001	67,588
EQUITY		
Share capital	12,000	12,000
Statutory reserve capital	1,200	1,131
Retained earnings	140,350	94,234
TOTAL EQUITY	153,550	107,365
TOTAL LIABILITIES AND EQUITY	176,551	174,953

STATEMENT OF CHANGES IN EQUITY

Parent <i>in thousands of euros</i>	Share capital	Statutory reserve capital	Retained earnings	Total
Balance as at 31.12.2010	11,312	1,131	94,576	107,019
Net profit for financial year	-	-	2,116	2,116
Bonus issue	688	-	(688)	-
Dividends	-	-	(1,770)	(1,770)
Balance as at 31.12.2011	12,000	1,131	94,234	107,365
Carrying amount of holdings under dominant or significant influence				(42,126)
Value of holdings under dominant or significant influence under the equity method				44,001
Adjusted unconsolidated equity 31.12.2011				109,240
Net profit for financial year	-	-	46,185	46,185
Increase of statutory reserve capital	-	69	(69)	-
Balance as at 31.12.2012	12,000	1,200	140,350	153,550
Carrying amount of holdings under dominant or significant influence				(104,249)
Value of holdings under dominant or significant influence under the equity method				67,624
Adjusted unconsolidated equity 31.12.2012				116,925

Adjusted unconsolidated retained earnings represent the amount that is available for distribution to the shareholders according to the Estonian Accounting Act.

CASH FLOW STATEMENT

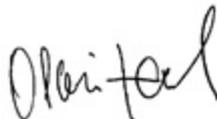
<i>in thousands of euros</i>	2012	2011
Cash flows from operating activities		
Operating profit	43,991	2,910
Adjustments:		
depreciation and impairment charge	14	283
(profit) loss from sale of a business unit	(43,111)	(4,591)
adjustment of revenue from construction contracts under stage of completion method	3,772	(279)
interest income from business activities	(3,424)	(3,921)
change in provisions	(2,332)	936
Change in trade and other receivables related to operating activities	43,523	(9,686)
Change in inventories	5,409	(8,092)
Change in trade and other payables related to operating activities	(21,227)	10,943
Interest received	658	3,109
Interest paid	(416)	(519)
Total cash flows from operating activities	26,857	(8,907)
Cash flows from investing activities		
Investments in subsidiaries	(57,696)	(8,000)
Sale of subsidiaries	-	14
Acquisition of associates	2,750	-
Purchase of/ proceeds from short-term deposits with maturities greater than 3 months	-	1,500
Sale of other financial investments	144	-
Purchase of property, plant and equipment	(134)	(183)
Proceeds from sale of property, plant and equipment	52	51
Purchase of intangible assets	-	(35)
Proceeds from sale of intangible assets	-	3
Sale of a business unit	43,111	4,515
Interest received	12	22
Dividends received	85	-
Total cash flows from investing activities	(11,676)	(2,113)
Cash flows from financing activities		
Proceeds from borrowings	3,996	16,037
Loan repayments received	(16,523)	(22)
Finance lease principal payments	(4)	(46)
Dividends paid	-	(1,770)
Total cash flows from financing activities	(12,531)	14,199
Net increase/decrease in cash and cash equivalents	2,650	3,179
Change in deposits with maturities greater than 3 months	-	(1,500)
Total change	2,650	1,679
Cash and cash equivalents in the beginning of period	5,665	2,477
Deposits with maturities greater than 3 months at the beginning of period	-	1,500
Total in the beginning of period	5,665	3,977
Effects of changes in foreign exchange rates	(2)	9
Cash and cash equivalents at end of the period	8,313	5,665

SIGNATURES OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD TO THE 2012 ANNUAL REPORT

The Management Board of AS Merko Ehitus has prepared the management report, the consolidated financial statements and the profit allocation proposal for 2012.

Andres Trink	Chairman of the Management Board		28.03.2013
Viktor Mõisja	Member of the Management Board		28.03.2013

The Supervisory Board has reviewed the Annual Report which consists of the management report and the financial statements prepared by the Management Board, and which also includes the auditor's report and the profit allocation proposal, and approved it for presentation at the General Meeting of Shareholders.

Toomas Annus	Chairman of the Supervisory Board		08.04.2013
Tõnu Toomik	Member of the Supervisory Board		08.04.2013
Teet Roopalu	Member of the Supervisory Board		08.04.2013
Indrek Neivelt	Member of the Supervisory Board		08.04.2013
Olari Taal	Member of the Supervisory Board		08.04.2013



INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholders of AS Merko Ehitus

We have audited the accompanying consolidated financial statements of AS Merko Ehitus and its subsidiaries, which comprise the consolidated statement of financial position as of 31 December 2012 and the consolidated statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

Management Board's Responsibility for the Consolidated Financial Statements

Management Board is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union, and for such internal control as the Management Board determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of AS Merko Ehitus and its subsidiaries as of 31 December 2012, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

AS PricewaterhouseCoopers

Ago Vilu
Auditor's Certificate No.325

Märten Padu
Auditor's Certificate No.513

1. April 2013

** This version of our report is a translation from the original, which was prepared in Estonian. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.*

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T: +372 614 1800, F: +372 614 1900, www.pwc.ee

PROFIT ALLOCATION PROPOSAL

in euros

Retained earnings	96,610,030
Net profit (loss) for 2012	7,627,029
Total retained earnings as at 31.12.2012	104,237,059

The Management Board proposes profit allocation as follows:

Dividends (EUR 0.30 per share)	5,310,000
Retained earnings after profit allocation	98,927,059

Andres Trink

Chairman of the
Management Board



28.03.2013

Viktor Mõisja

Member of the
Management Board



28.03.2013

KEY FINANCIAL INDICATORS IN 2007-2012

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	31.12.2012	31.12.2011	31.12.2010	31.12.2009	31.12.2008	31.12.2007
ASSETS						
Current assets						
Cash and cash equivalents	35,316	18,510	9,856	22,991	32,927	13,138
Short-term deposits	-	140	2,651	25,623	16,793	-
Trade and other receivables	60,343	64,449	44,938	42,306	49,894	76,666
Prepaid corporate income tax	478	686	1,366	248	247	152
Inventories	82,830	87,834	93,048	98,199	116,158	129,448
Assets held for sale	-	-	-	-	11	-
Total current assets	178,967	171,619	151,859	189,367	216,030	219,404
Non-current assets						
Investments in associates and joint ventures	7,190	9,986	11,053	11,467	13,214	17,446
Other long-term loans and receivables	17,188	17,065	8,258	2,075	1,857	926
Deferred income tax assets	1,919	1,870	1,571	2,050	1,548	217
Investment property	3,566	2,313	3,585	1,058	767	470
Property, plant and equipment	14,853	16,057	17,747	17,018	12,597	11,051
Intangible assets	1,365	1,427	1,508	1,549	755	804
Total non-current assets	46,081	48,718	43,722	35,217	30,738	30,914
TOTAL ASSETS	225,048	220,337	195,581	224,584	246,768	250,318
LIABILITIES						
Current liabilities						
Borrowings	16,299	16,574	12,554	28,605	13,208	19,485
Payables and prepayments	63,209	61,635	39,154	50,009	61,588	64,902
Corporate income tax liability	-	-	-	335	556	1,068
Government grant	-	-	-	-	-	96
Short-term provisions	6,165	6,781	3,674	2,410	2,065	4,680
Total current assets	85,673	84,990	55,382	81,359	77,417	90,231
Non-current liabilities						
Long-term borrowings	19,205	23,764	13,185	4,878	33,962	25,418
Deferred income tax liability	327	131	-	-	-	-
Other long-term payables	1,576	856	846	681	564	3,670
Total non-current liabilities	21,108	24,751	14,031	5,559	34,526	29,088
TOTAL LIABILITIES	106,781	109,741	69,413	86,918	111,943	119,319
EQUITY						
Non-controlling interests	1,342	1,356	1,428	1,734	2,213	2,169
Equity attributable to equity holders of the parent						
Share capital	12,000	12,000	11,312	11,312	11,312	11,312
Statutory reserve capital	1,200	1,131	1,131	1,131	1,131	1,131
Currency translation differences	(512)	(570)	(924)	(947)	(802)	(325)
Retained earnings	104,237	96,679	113,221	124,436	120,971	116,712
Total equity attributable to equity holders of the parent	116,925	109,240	124,740	135,932	132,612	128,830
TOTAL EQUITY	118,267	110,596	126,168	137,666	134,825	130,999
TOTAL LIABILITIES AND EQUITY	225,048	220,337	195,581	224,584	246,768	250,318

CONSOLIDATED INCOME STATEMENT

in thousands of euros

	2012	2011	2010	2009	2008	2007
Revenue	249,131	219,322	171,919	203,316	297,441	352,202
Cost of goods sold	(231,220)	(222,928)	(159,105)	(181,200)	(258,542)	(302,415)
Gross profit (-loss)	17,911	(3,606)	12,814	22,116	38,899	49,787
<i>% of revenue</i>	7%	-2%	7%	11%	13%	14%
Marketing expenses	(2,107)	(2,104)	(2,193)	(3,009)	(2,807)	(2,075)
General and administrative expenses	(9,173)	(7,910)	(8,724)	(9,842)	(12,963)	(13,665)
Other operating income	2,961	2,580	961	921	609	411
Other operating expenses	(834)	(1,308)	(478)	(1,746)	(2,769)	(1,157)
Operating profit (-loss)	8,758	(12,348)	2,380	8,440	20,969	33,301
<i>% of revenue</i>	4%	-6%	1%	4%	7%	9%
Finance income	184	594	696	2,525	2,199	704
Finance costs	(1,203)	(1,161)	(908)	(1,573)	(1,702)	(1,135)
Profit from sale of subsidiary	-	-	-	-	91	-
Profit (loss) from associates and joint ventures	163	(1,120)	(398)	(1,731)	(292)	4,885
Profit (loss) before tax	7,902	(14,035)	1,770	7,661	21,265	37,755
<i>% of revenue</i>	3%	-6%	1%	4%	7%	11%
Corporate income tax expense	(289)	(121)	(710)	(543)	(1,684)	(1,970)
Net profit (loss) for the financial year	7,613	(14,156)	1,060	7,118	19,581	35,785
incl. attributable to equity holders of the parent	7,627	(14,084)	1,229	7,424	19,120	34,835
attributable to non-controlling interest	(14)	(72)	(169)	(306)	461	950

OTHER KEY FIGURES

attributable to equity holders of the parent

		2012	2011	2010	2009	2008	2007
ROE	%	6.8	-12.2	1.0	5.5	13.8	30.2
ROA	%	3.4	-6.6	0.6	3.2	7.4	14.8
ROIC	%	6.0	-9.0	1.6	5.3	12.6	25.3
Equity ratio	%	52.0	49.6	63.8	60.5	53.7	51.5
Debt ratio	%	15.8	18.3	13.2	14.9	19.1	17.9
Current ratio	times	2.1	2.0	2.7	2.3	2.8	1.4
Quick ratio	times	1.1	1.0	1.1	1.1	1.3	1.0
Accounts receivable turnover	days	58	56	46	58	54	59
Accounts payable turnover	days	47	45	40	35	38	42
EBITDA margin	%	4.6	-5.0	2.8	5.3	7.8	10.0
General expense ratio	%	4.5	4.6	6.4	6.3	5.8	4.5
Staff costs ratio	%	11.2	10.2	12.4	11.4	10.4	9.3
Revenue per employee	thousand EUR	278	235	208	253	285	337
Number of employees	people	915	917	923	702	964	1115
Average number of employees	people	895	934	825	805	1042	1045
Secured Order Book	million EUR	190	166	200	83	191	264

SHARE-RELATED KEY FIGURES

attributable to equity holders of the parent

		2012	2011	2010	2009	2008	2007
Earnings per share (EPS)	EUR	0.43	-0.80	0.07	0.42	1.08	1.97
Equity per share	EUR	6.61	6.17	7.05	7.68	7.49	7.28
Dividend per share	EUR	0.3000*	0.0000	0.1000	0.7030	0.2237	0.0000
Dividend rate	%	70*	0	144	168	21	0
P/E	times	13.69	-6.79	130.32	11.97	2.59	6.61
P/B	times	0.89	0.87	1.28	0.65	0.37	1.79
Share price trend							
Average	EUR	6.04	7.49	7.72	3.71	7.59	21.01
Highest	EUR	7.30	10.65	9.89	5.78	12.95	25.70
Lowest	EUR	5.37	4.90	5.05	1.85	2.58	12.25
Share price 31.12	EUR	5.90	5.40	9.05	5.02	2.80	13.00
Market value 31.12	million EUR	104.43	95.58	160.19	88.85	49.56	230.10
Share turnover trend							
Share turnover	million EUR	5.47	8.02	13.09	9.38	18.22	117.00
Share turnover of shares outstanding	%	30.9	45.3	74.0	53.0	102.9	661.0
Number of shares	million EUR	17.70	17.70	17.70	17.70	17.70	17.70
Number of shareholders	pcs	1406	1576	1441	1220	904	720

*according to proposal of the Management Board

DEFINITIONS OF KEY FINANCIAL FIGURES

Gross profit margin (%) =	$\frac{\text{Gross profit}}{\text{Revenue}}$
Operating profit margin (%) =	$\frac{\text{Operating profit}}{\text{Revenue}}$
EBT margin (%) =	$\frac{\text{Profit before tax}}{\text{Revenue}}$
Net profit margin (%) =	$\frac{\text{Net profit (attributable to equity holders of the parent)}}{\text{Revenue}}$
Return on equity (%) =	$\frac{\text{Net profit (attributable to equity holders of the parent)}}{\text{Shareholders equity (average)}}$
Return on assets (%) =	$\frac{\text{Net profit (attributable to equity holders of the parent)}}{\text{Total assets (average)}}$
Return on invested capital (%) =	$\frac{\text{Profit before tax + interest income - foreign exchange gain (losses) + other financial income}}{\text{Shareholders equity (average) + interest-bearing liabilities (average)}}$
Equity ratio (%) =	$\frac{\text{Shareholders equity}}{\text{Total assets}}$
Debt ratio (%) =	$\frac{\text{Interest-bearing liabilities}}{\text{Total assets}}$
Current ratio =	$\frac{\text{Current assets}}{\text{Current liabilities}}$
Quick ratio =	$\frac{\text{Current assets - inventories}}{\text{Current liabilities}}$
Accounts receivable turnover (days) =	$\frac{\text{Trade receivables (average)} \times 365}{\text{Revenue}}$
Accounts payable turnover (days) =	$\frac{\text{Payables to suppliers (average)} \times 365}{\text{Cost of goods sold}}$
EBITDA margin (%) =	$\frac{\text{Operating profit} + \text{depreciation}}{\text{Revenue}}$
General expense ratio (%) =	$\frac{\text{General expenses}}{\text{Revenue}}$
Personnel expense ratio (%) =	$\frac{\text{Personnel expenses}}{\text{Revenue}}$
Staff costs ratio (%) =	$\frac{\text{Staff costs}}{\text{Revenue}}$
Revenue per employee (EUR) =	$\frac{\text{Revenue}}{\text{Number of employees (average)}}$
Earnings per share, EPS (EUR) =	$\frac{\text{Net profit (attributable to equity holders of the parent)}}{\text{Number of shares}}$
Equity / share (EUR) =	$\frac{\text{Shareholders equity}}{\text{Number of shares}}$
Dividend per share (EUR) =	$\frac{\text{Payable dividends}}{\text{Number of shares}}$
Dividend rate (%) =	$\frac{\text{Payable dividends} \times 100}{\text{Net profit (attributable to equity holders of the parent)}}$
Price per earnings ratio, P/E =	$\frac{\text{Share price 31.12}}{\text{Earnings per share}}$
Price to book ratio, P/B =	$\frac{\text{Share price 31.12}}{\text{Equity per share}}$
Share turnover (%) =	$\frac{\text{Number of shares traded} \times 100}{\text{Number of shares}}$
Market capitalisation =	Share price 31.12 x Number of shares

REVENUE BREAK-DOWN OF THE PARENT PRESENTED ACCORDING TO THE ESTONIAN CLASSIFICATIONS OF ECONOMIC ACTIVITIES

Revenue break-down of the parent of AS Merko Ehitus for the year 2011 is presented according to Estonian Classifications of Economic Activities (EMTAK 2008), as required under the Commercial Code § 4 p.6:

EMTAK code		<i>in thousands of euros</i>	
		2012	2011
	Rendering of construction services		
4120	construction of residential and non-residential buildings	-	18,918
4110	development of building projects	1,610	5,632
4211	construction of roads and railways	-	21,182
4221	construction of utility projects for fluids	241	43,136
4222	construction of utility projects for electricity and telecommunications	-	434
4291	construction of water projects	-	133
4213	construction of bridges and tunnels	-	792
4299	construction of other civil engineering projects n.e.c.	11	20,841
	Total rendering of construction services	1,862	111,068
	Real estate activities		
6810	sales of own real estate	11,918	335
6820	renting and operating of own or leased real estate	35	86
	Total real estate activities	11,953	421
	Total revenue	13,815	111,489



