



CONSOLIDATED ANNUAL REPORT

2018



AS MERKO EHITUS

GROUP

CONSOLIDATED ANNUAL REPORT

01.01.2018 – 31.12.2018

Business name:	AS Merko Ehitus
Main activities:	Holding companies General contracting of construction Real estate development
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Supervisory Board:	Toomas Annus, Teet Roopalu, Indrek Neivelt
Management Board:	Andres Trink, Tõnu Toomik
Auditor:	AS PricewaterhouseCoopers

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MAIN FACTS



The largest listed construction company in the Baltics

AS MERKO EHITUS CONSISTS OF:

- Estonia's leading construction company AS Merko Ehitus Eesti
- Latvian market oriented SIA Merks
- UAB Merko Statyba operating on the Lithuanian market
- Norwegian construction company Peritus Entreprenor AS

Merko Ehitus group focuses on general contracting of construction and on providing complete solutions in professional construction and real estate development. Long-term experience in various countries, a wide scope of construction services, flexibility, reliability and meeting the deadlines and primarily quality have helped group companies to achieve a strong position in the Baltics.

Merko Ehitus group is also the leading apartment developer in the Baltics, having developed and built more than 4,000 apartments in Estonia, Latvia and Lithuania.



**2018 new contracts signed
EUR 246.4 mln**



**2018 revenue
EUR 418.0 mln**

COMPETITIVE ADVANTAGES:

- Broad range of construction services and products, comprehensive solutions offered to clients
- Strong quality management system
- Experienced project managers and engineers
- Longstanding experience on the subcontractors and suppliers market
- Innovative technological approaches and construction solutions
- Strong financial capability
- Inventory of residential development projects and a strong brand



**2018 EBITDA
EUR 21.9 mln**



**2018 net profit
EUR 19.3 mln**



**31 December 2018
764 employees**

VALUE OFFERING

AS A GENERAL CONTRACTOR, WE OVERSEE THE ENTIRE CONSTRUCTION PROCESS AND ARE RESPONSIBLE FOR THE COMPLETION OF THE CONSTRUCTION PROJECT AS A WHOLE:

- Integrated project management and construction service, provision of strategic consultation to the contracting entity throughout the process
- As needed, combined use of subcontractors and Merko workforce (concrete works, road construction, electrical constructions both indoor and outdoor)
- Real estate investments and development, managing the entire apartment development process: design, construction, sales, warranty-period service
- Co-investing, risk distribution and participation in PPP (public-private partnership) projects
- International quality, environmental protection and occupational safety certificates ISO 9001, ISO 14001 and OHSAS 18001



Estonia's leading builder of substations

STATEMENT OF THE CHAIRMAN OF THE MANAGEMENT BOARD

Dear shareholders,

The Baltic states' construction sector continued on the rising path in 2018 and was one of the main engines driving economic growth. We were among the beneficiaries of the growth in the construction market – the group's revenue increased over 30 per cent and crossed the EUR 400 million mark for the first time. The foundation for the extraordinarily high construction volumes and rapid growth was laid in the form of large-scale construction contracts concluded several years ago. We have never had so many large projects – shopping centres, offices, hotels and public buildings – under construction at the same time in all three Baltic states than we did last year.

We are glad that besides the rapid growth in revenue, we also preserved profitability – the group's net profit also grew more than 30 per cent and net return on equity was in excess of 15 per cent, which is the best result in the last decade. The solid results can be attributed to the contributions and professionalism of our employees. We are also grateful to customers and partners who have put their trust in us.



ANDRES TRINK
AS MERKO EHITUS
CHAIRMAN OF THE
MANAGEMENT BOARD

Construction is a project-based business where we depend directly on the volume of orders on the market. Looking at the future, we must acknowledge that the rapid growth period is over on the construction market and a period of stabilization and maybe even decline is about to start. In recent years, commercial buildings have been built in the Baltics in great numbers and it will take time for the market to absorb the accrued volumes of commercial space. Construction has also become much more expensive, among other things because of rapidly growing wages and salaries. This has made real estate developers cautious when it comes to launching new projects. We perceived a clear decline in the volume of construction orders already in the first half of 2018 and the group's secured order book decreased by close to one-third during the year. We are prepared to adapt to the construction market and our primary focus is on operating profitably. The state remains an important player on the public building and infrastructure field and we shall see what will happen on the construction market in two or three years' time, if construction of Rail Baltica should go ahead.

Alongside general contracting of construction, we have shifted our focus even more to apartment development. Merko's brand as a home developer and builder continues to be strong in all of the Baltic states. Last year was noteworthy also in the sense that we launched construction of more than 1,000 new apartments in the Baltics combined. That is almost twice as many as in past years.

We are confident in our capability to create a quality, modern living environment for smaller and larger families, for younger people and those with longer life experience, for higher income segments and more economically minded home buyers alike. Our apartment development business has a long perspective arc – we are ready to invest and offer the apartments that buyers demand in both market boom periods and more stable phases.

Merko puts a premium on quality and trustworthiness. We want to build a better future through our main activity and also by giving back to society in general. We intend to continue working with partners who share our goals and values.



Andres Trink

MERKO GROUP

VISION

Our vision is reliable solutions and quality performance for customers' ideas.

VALUES

RESPONSIBILITY

We decide based on business thinking, awareness and ethical beliefs. We offer enduring and environmentally 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 are result-oriented. We accept challenges, which presume more.

CREATIVITY

We are open, innovative and creative in working out and implementing the solutions. We have the will to carry out forward-looking ideas.



T1 MALL OF TALLINN

STRATEGY

The business strategy of AS Merko Ehitus subsidiaries is focussed 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 main home markets Estonia, Latvia, Lithuania and Norway. Merko Ehitus aims to be a preferred partner to its clients for construction works.

FINANCIAL OBJECTIVES

The Management Board and Supervisory Board of AS Merko Ehitus have approved the group's strategic development directions and long-term financial objectives, which are:

average return on equity at least
10%

dividend rate
50-70%
of annual profit

equity ratio at least
40%

Considering the competitive situation of the Baltic construction and real estate market and the overall low interest rate environment, as well as the group's high equity base, the strategy and financial objectives are focused towards improving the return on invested capital and on increasing the efficiency of the balance sheet.

In 2018, the group fulfilled all set financial objectives:

return
on equity
15.3%

dividend rate
92%
of annual profit

equity ratio
49%

Considering the high equity level of the group and modest debt level, the group's management has made the proposal to pay dividends to shareholders above the current dividend policy rate. Due to that, the estimated dividend rate for 2018 is 92% (2017: 120%).

FULFILLMENT OF LONG-TERM FINANCIAL OBJECTIVES 2014-2018

	2018	2017	2016	2015	2014	AVERAGE
Return on equity, ROE (on yearly basis)	15.3%	11.9%	5.0%	8.0%	10.1%	10.1%
Dividend rate	92%*	120%	119%	90%	58%	96%
Equity ratio 31.12.	48.9%	47.0%	51.6%	59.5%	51.0%	51.6%

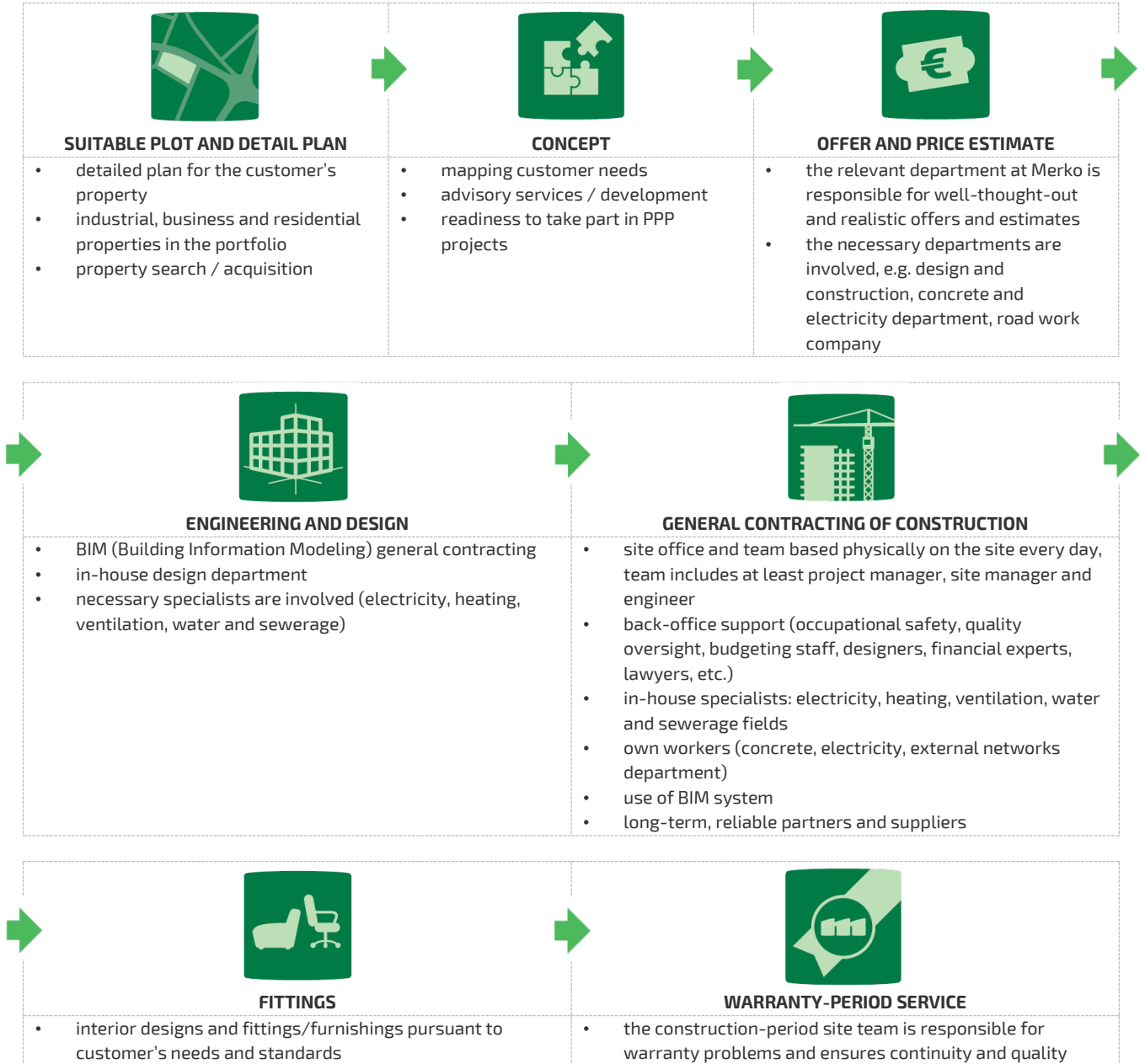
* Pursuant to the Management Board's proposal



APARTMENT BUILDING AT BOKSTO 14 IN VILNIUS, COMPLETED IN 2018.

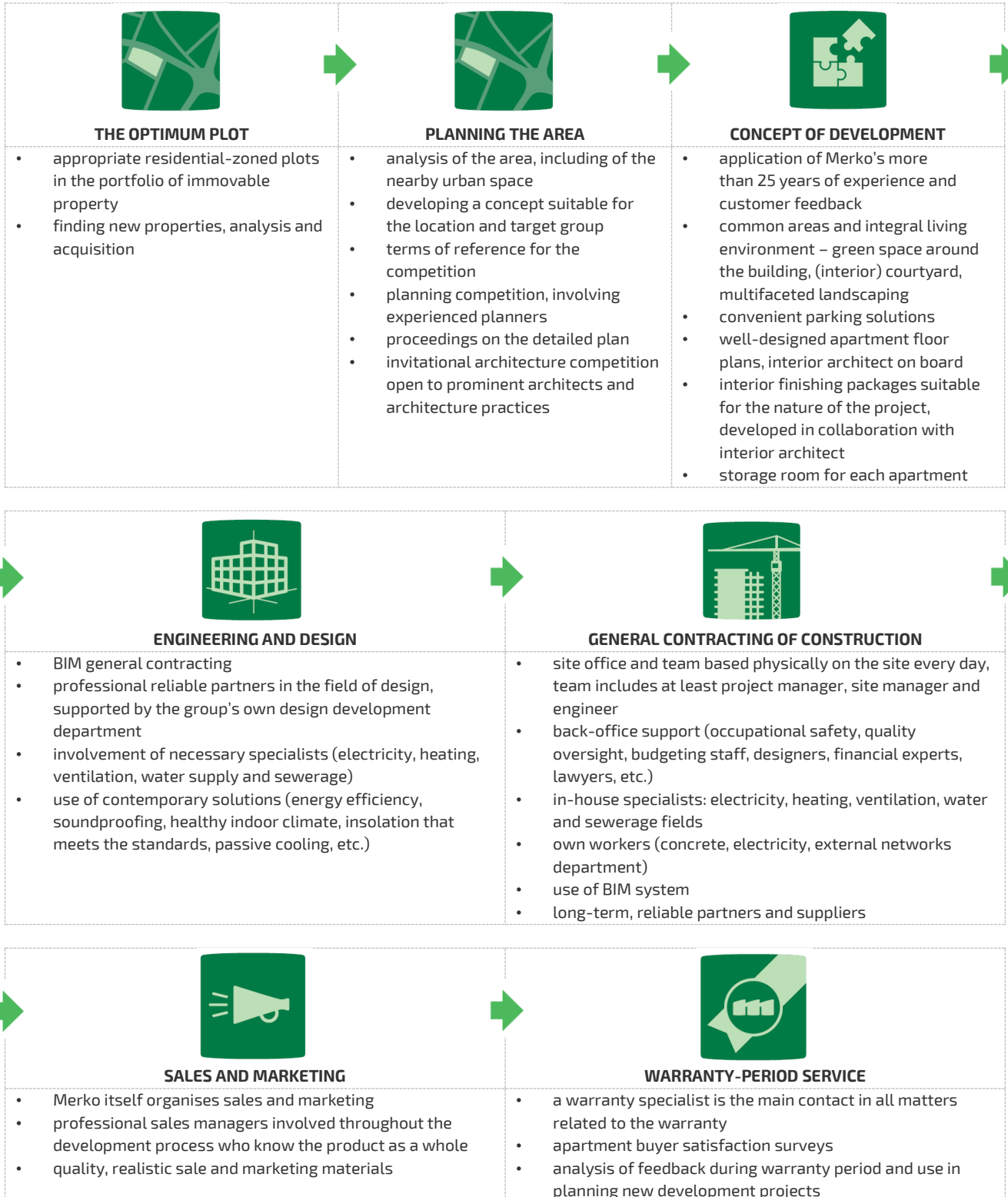
BUSINESS MODEL: CONSTRUCTION SERVICES TO CUSTOMERS

In the framework of general contracting of construction, Merko offers strategic advisory services and high-quality full-scale solutions throughout the whole process pursuant to the customer's needs: preparation, design, construction, fittings and warranty-period service. If the customer so chooses, we also offer commercial real estate development service, covering preparation for construction along with performance of the construction works. For the best outcome, Merko should be engaged already at the outset of the construction project planning period, and cooperation should take place in the framework of the design and construction agreement.



BUSINESS MODEL: PROPERTY DEVELOPMENTS

Merko has become the leading residential development company in the Baltics – we have developed and built more than 4,000 apartments in Estonia, Latvia and Lithuania, with more than 1,000 apartments in construction currently and thousands of new homes in long-term development. To ensure the best quality, we manage all phases of the development project: planning, design development, construction, sales, and service during the warranty period. As a developer of apartments, Merko focuses on developing an integral residential environment with apartment buildings planned for a specific potential customer target group and suitable for its surroundings, boasting distinguished architecture, functional floor plans, high-quality interior finishing materials and high energy efficiency.



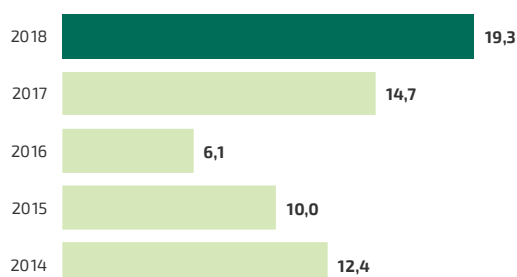
MANAGEMENT REPORT

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BRIEF OVERVIEW OF 2018

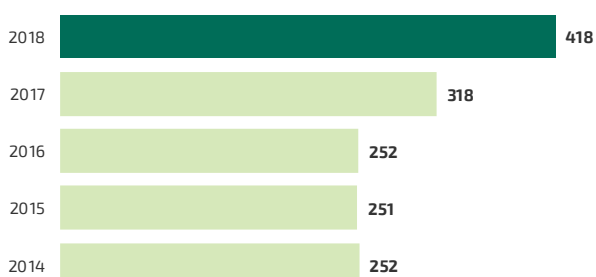
NET PROFIT

in million euros



REVENUE

in million euros



PROFITABILITY

Net profit in 2018 was EUR 19.3 million (2017: EUR 14.7 million), having increased by 31.6% compared to last year. Net profit margin attributable to equity holders of the parent remained at 4.6% (2017: 4.6%). Profit before tax in 2018 was EUR 19.8 million (2017: EUR 18.8 million), which is equivalent to a profit before tax margin of 4.7% (2017: 5.9%).

REVENUE

Revenue in 2018 was EUR 418.0 million (2017: EUR 317.6 million), which has increased by 31.6% compared to last year. The share of revenue earned outside of Estonia was 51.5% (2017: 39.9%) and the share of revenue earned in Estonia was 48.5% (2017: 60.1%).

REAL ESTATE DEVELOPMENT

The number of apartments sold in 2018 (482 units, incl. 131 in joint venture) increased by 23.0% (2017: 392 units, incl. 17 in joint venture). This was due to an increase in the number of apartments sold in the joint project. At the same time, the revenue of own developed apartments has decreased (EUR 41.3 million) compared to last year (2017: EUR 47.1 million). The decrease in revenue was in addition caused by lower average apartment price compared to 2017.

SECURED ORDER BOOK

In 2018, group companies signed new contracts in the amount of EUR 246.4 million (2017: EUR 334.9 million). As at 31 December 2018, the group's secured order book stood at EUR 229.0 million (31 December 2017: EUR 344.4 million).

CASH POSITION

At the end of the reporting period, the group had EUR 40.0 million in cash and cash equivalents and equity EUR 131.8 million (48.9% of total assets). Comparable figures as at 31 December 2017 were EUR 39.2 million and EUR 130.2 million (47.0% of total assets) respectively. As at 31 December 2018, the group had net debt of EUR 4.2 million (31 December 2017: EUR 20.1 million).

PROPOSAL FOR DISTRIBUTION OF PROFITS

The Management Board proposes to distribute to shareholders EUR 17.7 million (EUR 1 per share) in dividends from retained earnings in 2019. This is equivalent to a 92% dividend rate for 2018.

		2018	2017	CHANGE
Revenue	million EUR	418.0	317.6	+31.6%
Operating profit	million EUR	19.9	19.5	+1.7%
Operating profit margin	%	4.8	6.2	
Net profit attributable to equity holders of the parent	million EUR	19.3	14.7	+31.6%
Net margin	%	4.6	4.6	
		31.12.2018	31.12.2017	CHANGE
Equity ratio	%	48.9	47.0	
Number of employees	people	764	757	+0.9%

Calculation of ratios is provided on page 122 of the report.

THE MAIN FACTORS INFLUENCING THE CONSTRUCTION MARKET IN 2018

CONSTRUCTION SERVICES

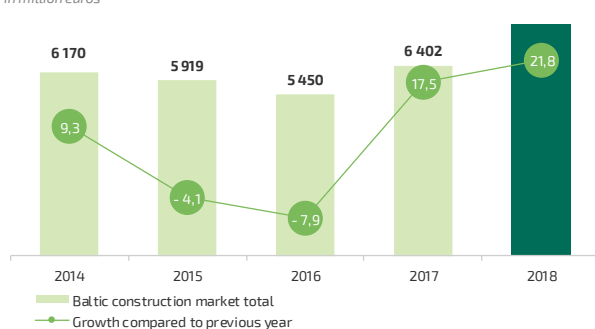
	2018			2017		
	Estonia	Latvia	Lithuania	Estonia	Latvia	Lithuania
GDP annual change in current prices	+3.9%	+4.8%	+3.4%	+4.9%	+4.6%	+4.1%
Construction price index annual change	+1.7%	+4.4%	+2.9%	+1.5%	+1.9%	+3.0%
<i>incl. labour force</i>	+4.0%	+8.3%	+6.2%	+2.4%	+4.5%	+8.3%
<i>construction machines</i>	+2.6%	+2.8%	+1.0%	+1.4%	+1.0%	+0.9%
<i>Building materials</i>	+0.4%	+3.7%	+1.4%	+1.0%	+1.4%	+0.7%

Source: Local national statistical offices / Eurostat.

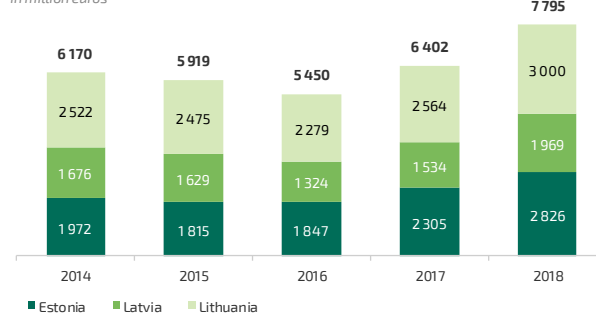
In 2018, strong economic growth in the Baltics continued, clearly exceeding the European Union average (+1.9%). Both in Europe as a whole and in Estonia and Lithuania, economic growth fell short of the pace of 2017 (EU +2.4%) while in Latvia, growth accelerated slightly. Estonia and Lithuania were chasing positions in the top 10 in the EU in terms of their 2018 results, while Latvia was in the top 5. Growth in the Baltic region has continued in the context of general developments in Europe, and among other things, the performance of export partners plays an important role. On the backdrop of increased salary growth (Estonia +7.3%, Latvia +8.4%, Lithuania +9.6%) and low unemployment, internal consumption remains strong, and investments have continued, including into buildings.

The rapid wage growth is also expressed in construction prices, being the greatest contributor to the overall growth figure after construction machinery and construction materials. As a whole, construction prices in Estonia rose +1.7%, +4.4% in Latvia and +2.9% in Lithuania, but their influence on market participants varies. Above all, the stiff competition between general contractors vying for a limited number of major construction projects and high construction activity have meant that subcontractor resources are being fully utilised. Thus, it has been complicated to find enough workforce at the right time for every stage of construction in order to keep the completion of projects on schedule. In addition, a shortage of resources became evident in regard to construction materials in 2018 – producers could not always keep up with market demand and queues for materials arose. All this resulted in a difficult situation for general contractors when it came to managing construction processes and resulted in additional expenses which are not necessarily expressed in the change in the construction price index.

CONSTRUCTION MARKET VOLUME (WITH OWN FORCES) AND GROWTH IN THE BALTIC STATES
in million euros



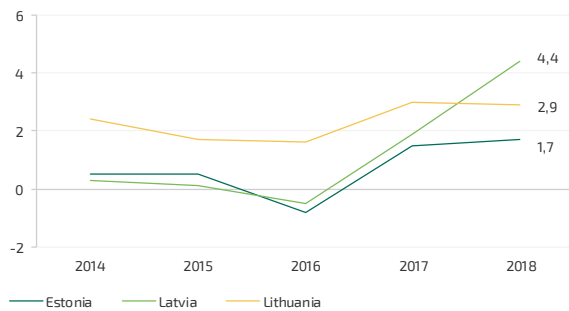
CONSTRUCTION MARKET VOLUMES (WITH OWN FORCES) IN THE BALTIC STATES BY GEOGRAPHICAL LOCATION
in million euros



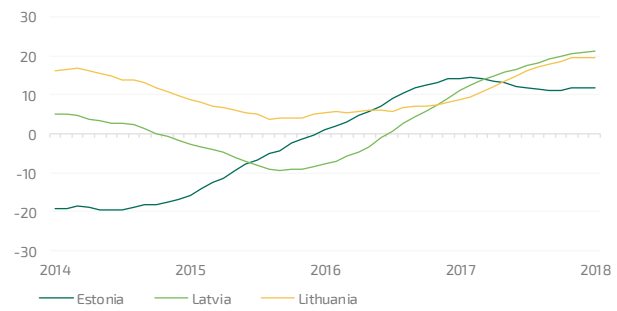
Source: Local national statistical offices.

In 2018, a total of EUR 7,795 million in construction work was performed using our own resources, which was close to EUR 1,400 million more than a year before (EUR 6,402 million). The construction market grew in current prices by +21.8% (2017: +17.5%). In this respect, the market as measured in current prices approached the peak boom-era levels, falling just 5% short (2008: EUR 8,185 million). In Estonia, the boom era peak was exceeded by 13% while Latvia and Lithuania fell 17-18% short. In terms of volume, Lithuania was still the leader, but its share has now fallen under 40% of the Baltic construction market (2018: 38.5%, 2017: 40.0%). Latvia's share has risen to 25.3% (2017: 24.0%) and Estonia's share to 36.3% (2017: 36.0%).

CHANGE IN CONSTRUCTION PRICE INDEX
percentages



CONSTRUCTION CONFIDENCE INDICATOR (12 month running average),
long-term average = 0
diff. between percentages of pos. and neg. responses less long-term average



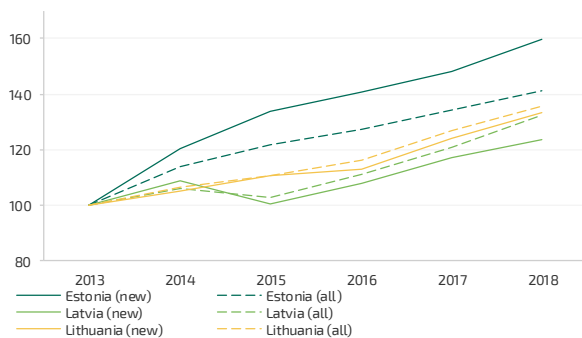
Source: Local national statistical offices / Eurostat.

Construction confidence indicator (in order to eliminate seasonality, 12 month running average is observed) has been considerably above the long-term average in all three countries. In Estonia the indicator remained stable last year, in Latvia and Lithuania the rise continued. Overall sentiment in the sector has been positive and by the end of the year, there were no real signs of changes in this trend. Considering that the construction volumes have increased during a rather short time period, especially in Estonia, but also in Lithuania, the growth rate might not continue at current level for much longer. The amount of issued construction permits decreased in 2018 compared to previous year in Estonia considerably both in terms of residential (ca -10%) and non-residential premises (ca -20%), while in Lithuania the amount of issued construction permits for residential premises remained the same and the amount of permits for non-residential premises increased (ca +10%). In Latvia the amount of issued construction permits increased both for residential and non-residential premises (ca +15...20%). In case a correction in construction volumes should take place, the fact that the construction confidence indicator remains on a high level creates questions whether market participants will be ready for it.

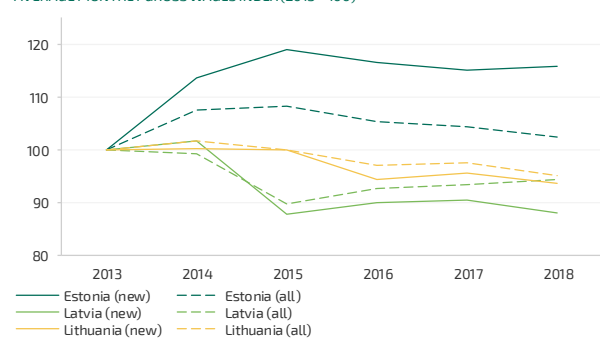
APARTMENT DEVELOPMENT

Housing prices have seen clear growth in all three Baltics in recent years although the dynamics have been somewhat different. Estonia saw strong growth in 2014 (+13.7%, including +20.2% in the case of new buildings) and in 2015 as well (all buildings +6.9%, new ones +11.1%), while Latvia saw a price correction in 2015 and Lithuania experienced a price rise of about +5%. Since then, the price dynamics have had greater similarities from one country to the next. In 2016-2017, it seemed that the price rise was tapering off in Estonia, but 2018 saw an additional +8% rise in the new housing price index and the rise in the price index for all buildings was +5%. In Latvia, the price rise in the last three years has been +8...9% annually and the prices for new buildings have gone up less. The trend is generally the opposite of Latvia in Estonia and Lithuania – the price of new residential units tends to grow faster than that of existing ones. Thus, the prices of new housing units in Lithuania rose +9.9% in 2017 and +7.4% in 2018, and the prices of all housing together rose +8.9% and +7.0% in those respective years.

NEW AND ALL (dotted line) DWELLINGS HOUSE PRICE INDEX (2013=100)



RATIO OF NEW AND ALL (dotted lines) DWELLINGS HOUSE PRICE INDEX TO
AVERAGE MONTHLY GROSS WAGES INDEX (2013 = 100)



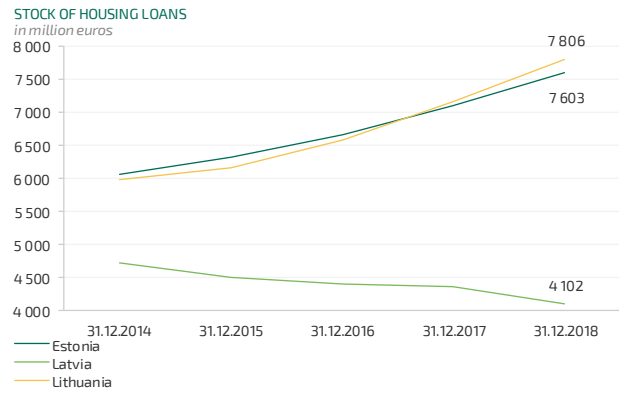
Source: Local national statistical offices / Eurostat.

Comparing the change in the average wage to the housing price index, we see that since 2014-2015, when the price rise clearly outstripped wage growth in Estonia, prices have risen in more or less the same tempo in the past three years. Wages have tended to grow more and thus housing prices have become even cheaper in relative terms. As Lithuania did not see a similar jump in prices in 2014-2015 as Estonia did, compared to the rise in wages, the prices of housing over the last five years have become rather more affordable there. In Latvia, after the correction of 2015 (a total of -3.4% for housing overall, and -7.7% for new housing), the prices in the last three years have tended to grow slightly faster with respect to wages even though the situation with new housing seems to indicate stability. Thus, even though prices have clearly risen (ca 20-60% over the last five years, depending on the country), the rise has generally been on a par with the rise in wages. Thus, the prices in Latvia and Lithuania today, compared to increase in income, are even 5-10% lower than five years ago.

Despite the rise of prices, today's situation cannot be compared – at least not in regard to prices on the residential real estate market – to the boom era of 2007-2008, when housing prices were growing significantly faster than wages and a clear price bubble

formed. Today we cannot see a similar bubble. It is a separate question, however, as to whether the rising wages to this point are a sustainable long-term trend and whether and when the trend will start to show up in employment indicators, which would in turn influence people's general sense of security and home buying decisions. Certainly, a large number of new development projects have been introduced to the market (especially in Tallinn and Vilnius), as a result of which the time needed to sell less attractive developments will likely become longer.

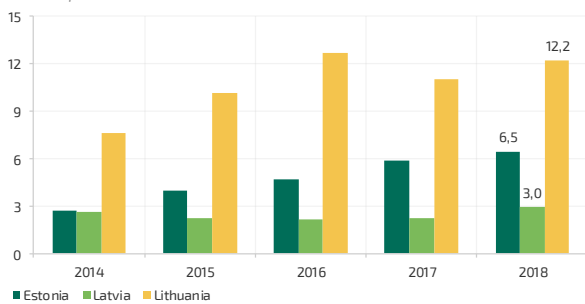
The housing loan balance continued growth in Estonia and Lithuania, in both cases at a rate comparable with 2017 (Lithuania 2018: +8.8%, 2017: +8.9%; Estonia 2018: +7.0%, 2017 +6.7%). In Latvia, the housing loan balance decreased by -6%, according to statistics by the Bank of Latvia (2017: -1.1%). However, this includes a one-off decrease due to excluding the loan portfolio of one bank, which lost its licence, from the statistics. Without this effect the balance of housing loan portfolio increased in Latvia for the first time since the crisis 10 years ago: the growth in 2018 was ca +1%. Compared to the end of 2008 (the peak of the boom), the balance of housing loans in Latvia was ca 38% lower at the end of 2018 (the effect of the bank, which lost its license, eliminated), even as the maximum decrease in the loan portfolio from the peak reached -6% in 2012 in Estonia and -3% in Lithuania. At the end of 2018, the housing loan balance in Estonia was 22% higher and in Lithuania 29% higher than at the end of 2008. Thus, the post-boom developments on the housing financing market for the past 10 years have been quite different in Latvia as compared to Estonia and Lithuania.



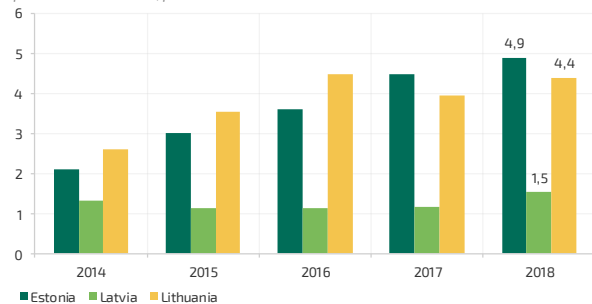
Source: Local central banks.

The availability of loans for purchasing a home continues to be solid on all three markets – although interest rates have risen somewhat in the last year, they are still low in the historical context, while the income and own financing requirements are not overly prohibitive. Compared to Estonia and Lithuania the overall demand for housing loans in Latvia has been low. However, the increase in the total balance of the housing loans in 2018 shows that also Latvian market is improving.

THE NUMBER OF USE AND OCCUPANCY PERMITS ISSUED FOR NEW RESIDENTIAL PREMISES thousand pcs



THE NUMBER OF USE AND OCCUPANCY PERMITS ISSUED FOR NEW RESIDENTIAL PREMISES per thousand residents, pcs



Source: Local national statistical offices.

In regard to the number of permits for use issued for new apartments, Estonia has seen constant growth since 2012. In 2018, the pace slowed somewhat, as the number of permits grew by just under 10 per cent, as opposed to the double-digit growth in previous years (9.9%; 2017: 24.5%). Last year, close to 6,500 new residential units came on to the market (2017: close to 5,900), while the figure was around 7,100 in 2007 at the peak of the boom period. Thus, the current level is 8% less than during the boom.

Lithuania saw the start of stronger growth in 2011 and it reached the crest in 2016, when about 12,700 permits for use were issued. In 2017, 13% fewer permits were issued (approx. 11,000) and last year, approx. 12,200 permits were issued. At the peak of the boom in 2008, approx. 11,800 permits were issued, so that this figure has been exceeded in two of the last three years.

In Latvia, the number of permits issued grew more than 30% last year, but the volume is still modest, being under 3,000 permits (2017: close to 2,300). In 2007 about 9,300 permits were issued in Latvia, so that the volumes last year were close to 68% lower than during the boom era.

Comparing the number of permits for use to population size, the ratio is highest in Estonia: 4.9 permits per thousand inhabitants (2017: 4.5), 4.4 in Lithuania (2017: 3.9) and just 1.5 in Latvia (2017: 1.2). Estonia and Lithuania are progressing at a similar speed in terms of relative numbers, while Latvia at just one-third of the pace.

OUTLOOK FOR 2019

In 2019, we expect that the economic growth in the Baltics will stay on a positive course, although likely to remain below last year's figures. The most important risks affecting the economic environment stem more from regional and global developments, not so much domestic factors, although there are questions at the local level about possible imbalances due to growth of income, changes in the political landscape or developments in the banking sector. Being small and open economic environments, Estonia, Latvia and Lithuania all depend on general developments in Europe, including especially developments of our primary export partners. As a whole, the EU economy, including statistics on the largest member states, has shown signs of growth tapering off in recent months. International organisations have downgraded their growth forecasts for Europe and other regions. The European Central Bank has postponed its thoughts of normalising monetary policy (such as by raising interest rates and ending bond buying programmes) to continue supporting the economy by supplying liquidity. In addition, global protectionist risks and geopolitical conflicts (including sanctions) remain and major regional organisational shakeups (such as Brexit) also add colour to the mix. The baseline scenario however continues to envision economic growth continuing in Europe and around in the world as well, which will keep Estonia, Latvia and Lithuania on their current positive course, even though the environment may be more volatile than before.

CONSTRUCTION SERVICES

The question in 2019 is whether the growth in construction volumes seen to date in the Baltics will continue or will there be an easing off and correction. Growth to this point has been fastest in Estonia, meaning that also the potential for correction is the most obvious on this market. In Latvia and Lithuania, construction volumes are still well under the boom-era peaks, and thus these markets have more potential for stronger developments in the near future. A possible correction in construction activity could have the effect of bringing greater order to the market, reducing the pressure from subcontractors on general contractors in terms of availability of resource and rising prices. If general contractors do not focus only on maintaining volumes but also on preserving profitability, there is hope that it will be possible to negotiate on reasonable conditions with customers even if volumes decrease. To this point, customers' demands have risen, among other things the construction periods have become shorter and stricter policies on penalties have been established. If the risk-to-return ratio for general contractors is not improved, it could mean a greater possibility of negative results becoming realised or that general contractors will become more passive on the market. In summary, such developments would be to the benefit of customers, either, as their own risks would grow (construction quality, projects would be prolonged or left unfinished due to financial difficulty, disputes would arise over compensation for changes and additional work, and so on). It would be reasonable for all parties to prioritise not only the lowest price but also mutual professionalism, a rational mindset and trustworthiness.

In the longer run, the big question is whether, how and according to what timetable the Rail Baltica project will be carried out. In terms of volume, this is a project that will significantly increase demand in the construction sector. In certain segments of the work, growth in demand may become evident to a level that exhausts the capability of the local market. This in turn will make it questionable whether other construction projects can be completed on time. If the additional demand from Rail Baltica coincides with a period when other demand is receding, it would help to reduce volatility in the sector. If the additional demand should crop up at a time when the construction sector is already active, overheating will be a clear possibility. Timing demand in the case of mammoth projects like this is practically impossible. However, it will contribute to developments on the construction market if plans are in place and made public as far in advance as possible, so that market participants can already start planning resources in a timely manner.

Merko Ehitus group's focus in construction activity will continue to remain on private capital investments into manufacturing, logistics and other business real estate. Because of high price competition the group has not been very successful in public procurements. We find that below a certain price level quality will suffer and we cannot compromise on that. We are looking to supply integral engineering, design and construction service, high-quality, optimum construction solutions, an efficient construction process, and the certainty that projects will be completed on schedule. We believe that a professional partner who shoulders responsibility for the entire construction process as a whole ensures more reliably a building that meets expectations. Considering the demands of customers in terms of guarantees and long payment terms, the burden on construction companies' current assets remains high, and to stay competitive it is important that companies be adept at managing cash flows. Merko companies are able to draw on group's relatively strong financial position as a competitive edge in negotiating payment terms.

Being one of the largest general contracting enterprises in the Estonian construction sector, AS Merko Ehitus's subsidiary AS Merko Ehitus Eesti competes effectively in all segments of activity. In the general construction segments, there are certainly many general contractors on the market, and the price competition will remain stiff also in 2019, often coming at the detriment of quality and contractual risks. In Latvia, the AS Merko Ehitus's subsidiary SIA Merks is among the leading general contractors and in Lithuania, AS Merko Ehitus's subsidiary UAB Merko Statyba has focused in its construction activity above all on apartment developments and the buildings (general construction) segment, where competition at procurements is still very high. The primary focus of Peritus Entreprenør AS, which operates in the Norwegian market, is the construction of buildings in the general construction field, where we are looking to expand our profile of services.

APARTMENT DEVELOPMENT

The Tallinn and Vilnius apartment markets will likely continue to display an activity level comparable to previous years, although in certain segments (above all the most expensive segment) both demand and supply could decline. Stabilisation and a certain better organisation of the market continues all the more clearly. The turnover period for lower-quality projects in weaker locations will grow longer. In such a situation, the positive features of stronger projects become more obvious. We consider Merko's position very strong, based on our good reputation over the long term, the high-quality projects we have carried out and our attractive projects – both the ones in progress and the ones going on sale – the relative competitive advantage will tend to increase on a stabilising market. Home buyers are increasingly conscious of construction quality and environmental aspects. They also have a wider range of choice when the supply is larger.

In Riga, the apartment market has shown certain signs of increased activity, but the activity level falls short of that of Tallinn and Vilnius. Developments on this market must be planned with particular care and implemented in line with market expectations. It must be borne in mind that turnover periods will be longer and buyers have become more demanding as to district and price.

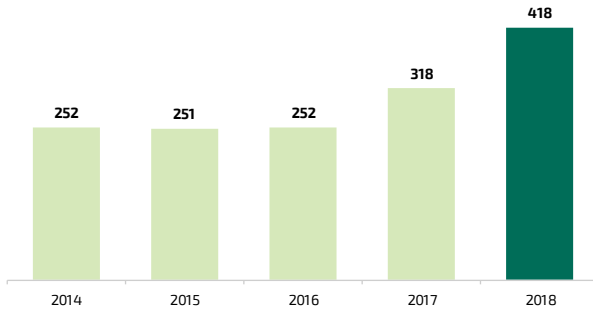
A key question will be whether banks are ready to continue financing developments. The conditions for securing a bank loan for development projects have become tighter over the last year (self-financing requirements, existence of preliminary contracts) and interest rates have gone up. Banks' readiness to provide financing is also impacted by recent general developments in competition between banks and on the regulatory front. First and foremost this will likely affect smaller developers whose owner-side capitalisation is lower and who are more dependent on a single large development. To this point, crowdfunding has been one way that developers have found additional funding in a situation where they do not meet the bank's conditions. Insofar as the general market situation has been favourable, we have not yet seen major unsuccessful projects that have attempted crowdfunding. Thus, there is not as yet a clear understanding of what potential losses investors might face in such cases and at least for now, investors still have an interest in financing projects in this manner.

The availability of bank loans for individuals looking to finance a home purchase is likely to remain good. Banks are well capitalised and the ratio of loans to deposits is at a good level. Prime interest rates will also remain low in the foreseeable future. People's incomes have risen and will continue to do so in the near future, savings have grown and unemployment remains low. People's purchasing power for buying homes is strong and Merko's goal is to offer them the kinds of apartments that are attractive to them. We will continue focusing on mainly the medium price class segment. We envision that it is precisely here that we can best apply our experience and understanding of what a quality apartment well equipped for living and its surrounding integral living environment should be. At the same time, we will also carry out, in the case of carefully selected projects, developments in other segments in which we are sure that we can realise them in a way that matches up buyers' expectations with our skill sets.

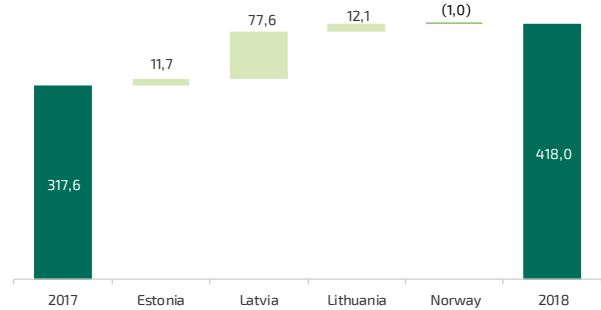
OPERATING RESULT

REVENUE AND PROFIT

GROUP REVENUE
in million euros



CHANGES IN GROUP REVENUE
in million euros

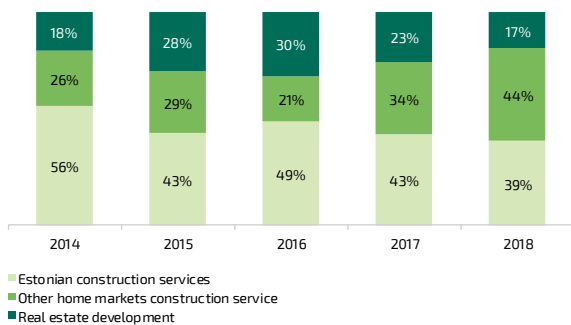


In 2018, the revenue of Merko Ehitus group was EUR 418.0 million, (2017: EUR 317.6 million) which exceeded the EUR 400 million threshold for the first time. 48.5% of the period's revenue was generated in Estonia, 37.7% in Latvia, 11.2% in Lithuania, and 2.7% in Norway (2017: 60.1% in Estonia, 25.2% in Latvia, 10.9% in Lithuania and 3.8% in Norway). Compared to 2017, the group's revenue increased by EUR 100 million or 31.6%, including a 6.1% increase in Estonia, 97.1% in Latvia and 35.0% in Lithuania. In Norway, the revenue decreased by 8.1%.

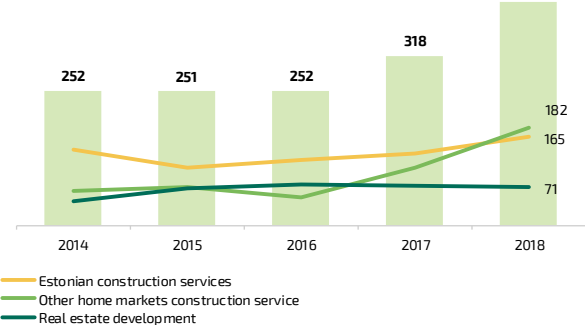
The group's revenue increased mostly because of the growth in construction contracts concluded with private sector customers in the last two years. Large construction objects have been put to work and revenue from those was partly recognised in 2018 and will also be recognised in 2019 according to construction schedule.

The main changes in the revenue structure compared to last year lie in the growth in revenue from other home markets construction services' general construction projects and in the moderate decrease in the sales revenue of the real estate development segment. The revenue growth in the other home markets construction services has been supported mainly by major construction contracts in Latvia. Merko Ehitus is focused on successfully completing these projects and keeping the future volumes stable. Considering the increasing price competition among main contractors in construction services in Estonia and on other home markets, the group is monitoring closely that when signing up for new construction projects, appropriate risk-reward ratio is maintained.

DISTRIBUTION OF GROUP REVENUE ACCORDING TO SEGMENTS
percentages



DISTRIBUTION OF GROUP REVENUE ACCORDING TO SEGMENTS
in million euros

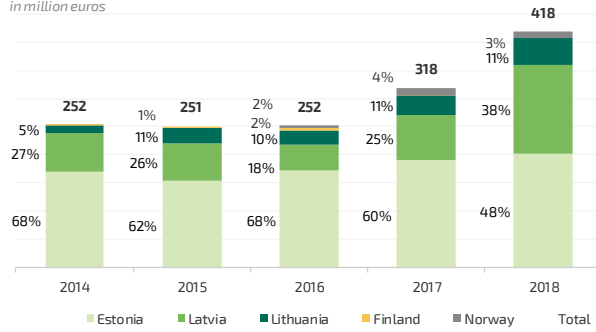


Estonian construction service segment contributed 39% (2017: 43%), other home markets construction service segment 44% (2017: 34%) and real estate development segment 17% (2017: 23%) of the group's revenue.

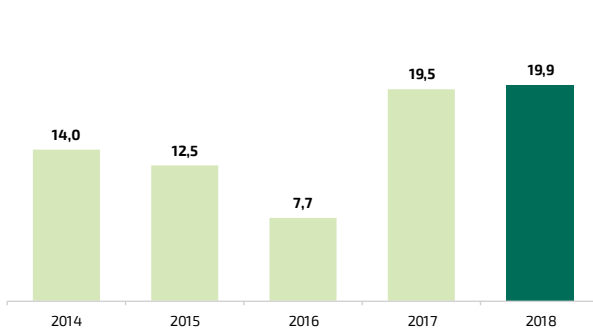
By country, Estonian sales continued to account for the largest share of revenue – 48% (2017: 60%) – at the same time the group's percentage of revenue from outside of Estonia increased to 52% (2017: 40%). Group's strategic aim is to diversify its operating portfolio by balancing the construction activities in Estonia with those abroad. Thus, the group continues to identify and strengthen its competitive advantages and is closely monitoring the development and opportunities in both the Baltic states and the Nordic countries, especially in Norway.

In 2018, the group's operating profit from development and construction activities totalled EUR 19.9 million (2017: EUR 19.5 million). The operating profit margin in 2018 (4.8%) decreased by 1.4 pp compared to last year (2017: 6.2%). The results for 2017 were influenced by one-off circumstances: sale of long-established land plots and inventory revaluations.

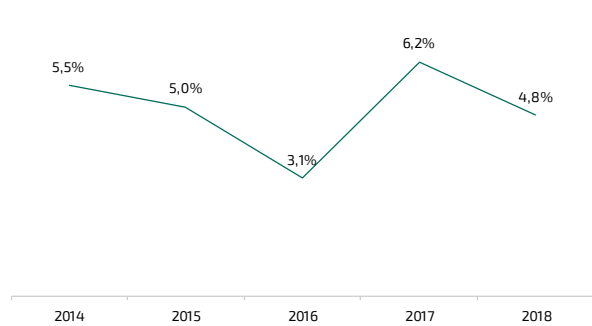
DISTRIBUTION OF GROUP REVENUE BY GEOGRAPHICAL LOCATION
in million euros



GROUP OPERATING PROFIT
in million euros



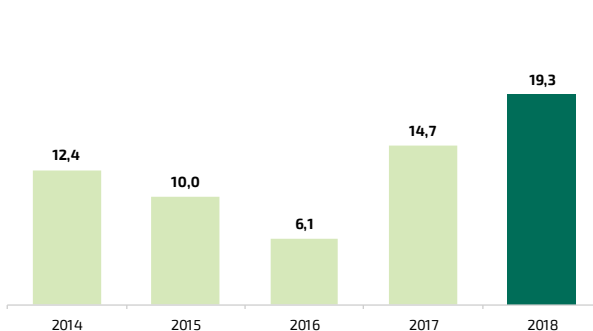
GROUP OPERATING PROFIT MARGIN
percentages



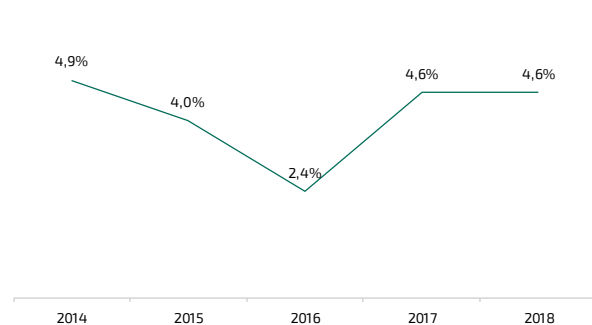
The group's aim is to preserve profitability in both the Estonian, but also other home markets' construction service domain, in spite of the prevailing competition situation between the main contractors, limited capabilities of sub-contractors and increasing input prices. Dependent on the demand of the construction market, the group continues to be geared towards moderate long term increase of operational volumes, but only in a capacity, which ensures that the risk profile of the business does not grow substantially more aggressive. Profitability is supported by apartment development, which remains the group's central business line.

In 2018, the group's pre-tax profit totalled EUR 19.8 million and the net profit attributable to owners of the parent company was EUR 19.3 million, compared to the pre-tax profit of EUR 18.8 million and net profit attributable to owners of the parent company of EUR 14.7 million in 2017. The group's profit before tax margin was 4.7% (2017: 5.9%) and net margin was 4.6% (2017: 4.6%).

GROUP NET PROFIT
in million euros



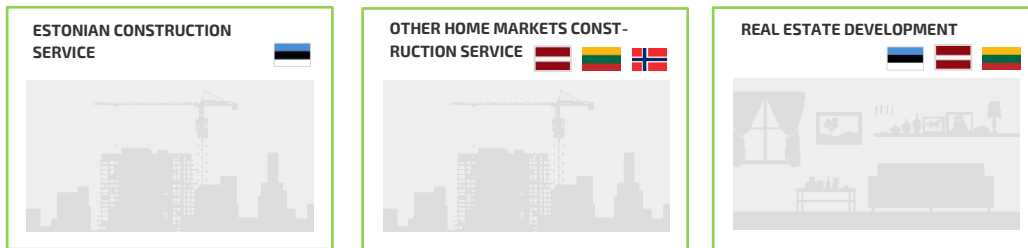
GROUP NET PROFIT MARGIN
percentages



In the second quarter of 2018, the group paid EUR 17.7 million in dividends. As these were paid from dividends received from foreign subsidiaries where the income had been taxed, the group did not incur additional income tax expenses. In the second quarter of 2017 the group paid EUR 7.3 million in dividends and incurred additional income tax expense in the amount of EUR 0.9 million.

BUSINESS ACTIVITIES

The group operates in Estonian, Latvian, Lithuanian and Norwegian market through its subsidiaries. See additionally the detailed management structure on page 46.



Pursuant to the international financial reporting standards (IFRS 8), the group discloses in the external financial reporting an aggregate overview of the business segments in countries that constitute a smaller share in operations, in accordance with the requirements established for the disclosure of business segments.

Depending on the country, the group provides construction and real estate development services in the following operating areas:

- **GENERAL CONSTRUCTION:** construction of various buildings, including commercial and office buildings, retail and entertainment centres, hotels and spas, as well as public buildings, dwellings and specific industrial buildings. In the context of main contracting, we provide high quality complete solutions to meet the client's needs.
- **CIVIL ENGINEERING:** design and construction of infrastructure facilities. The field includes port, waste handling and road infrastructure (bridges, tunnels, overpasses, roads), various environment protection facilities, drinking water and waste water treatment facilities, water and sewerage mains built using both open and no-dig methods, and various other engineering and technical sites.
- **ELECTRICAL CONSTRUCTION:** above all, medium and high voltage substation and cable line engineering configuration and construction. Merko has a professional project management team with good cooperation experience with local and international customers.
- **ROAD CONSTRUCTION:** various road maintenance services in Estonia: road construction, maintenance repair of roads, supervision of excavation works and the condition of roads, provision of repair services for machinery.
- **CONCRETE WORKS:** solutions for buildings and infrastructure constructed of prefabricated or concrete panels by group companies and out-of-house customer.
- **REAL ESTATE DEVELOPMENT:** development of apartment projects, long-term real estate investments and real estate projects for business purposes.

One of the keys to Merko's success 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 of project managers and engineers and experience in implementing complex projects using contemporary engineering solutions. Merko' strength is also in completing simultaneously various complex and long-term projects, while providing high quality construction services to customers with different requests.

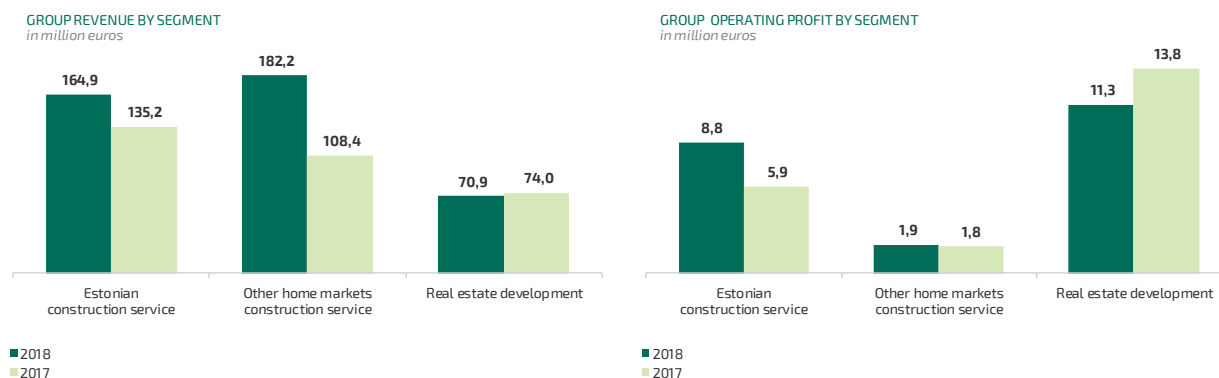


DEVELOPING DIGITAL CONSTRUCTION

AS Merko Ehitus Eesti joined the Estonian Digital Construction Cluster, which aims to carry out a paradigm shift in the construction sector, bringing into focus cooperation between construction stakeholders and implementing a mindset where a building is viewed throughout its lifecycle from the inception of the idea to the end of its useful service life.

The Digital Construction Cluster focuses on developing knowledge-based construction and increasing value added in the construction sector. The cluster unites real estate developers, architects, engineers, BIM software developers, consultants, representatives of builders and construction management, real estate owners, local governments, and institutions of higher education and competence centres.

CHANGE IN GROUP REVENUE AND OPERATING PROFIT ACROSS BUSINESS SEGMENTS



ESTONIAN CONSTRUCTION SERVICE

The Estonian construction service segment consists of services in the field of general construction, civil engineering, electricity, external networks and road construction, as well as concrete works. In previous periods (2015–2016) it has also included construction services on project basis in Finland. In 2017 and 2018 construction services were not provided in Finland.

million EUR

	2018	2017	CHANGE
Revenue	164.9	135.2	+22.0%
% of total revenue	39.4%	42.6%	
Operating profit	8.8	5.9	+50.3%
Operating profit margin	5.3%	4.3%	

In 2018, the revenue of the Estonian construction service segment was EUR 164.9 million (2017: EUR 135.2 million), having increased by 22.0% from last year. The increase in revenue in the segment is primarily influenced by the fact that several large-scale general construction projects launched in 2017.

The Estonian construction service segment revenues for 2018 were 39.4% of the group's revenue, forming the largest proportion in the group's revenue, having decreased by 3.2 pp in the yearly comparison (2017: 42.6%).

In 2018, the group earned an operating profit of EUR 8.8 million in this segment (2017: EUR 5.9 million). In 2018, the operating profit margin of the Estonian construction service segment was 5.3%, which increased by 1.0 pp compared to 2017 (4.3%). The profitability indicator has improved due to the increased efficiencies of internal project management processes.

The competition in main contracting in the area of general construction is getting increasingly tighter in the Estonian construction services market. The number of construction objects in the market is limited and therefore contractors tend to leave an increasingly small buffer for profitability and adverse developments when competing in price. This is particularly evident in public general construction procurements where Merko is finding it increasingly difficult to successfully participate. The stress in sales prices is accompanied by an increasing cost pressure from growing construction prices. The prices of labour, construction equipment and building materials have all increased. In order to ensure sustainable profitability, the group has to continue improving the efficiency of internal project management processes and optimizing the placement of resources and the cost base.

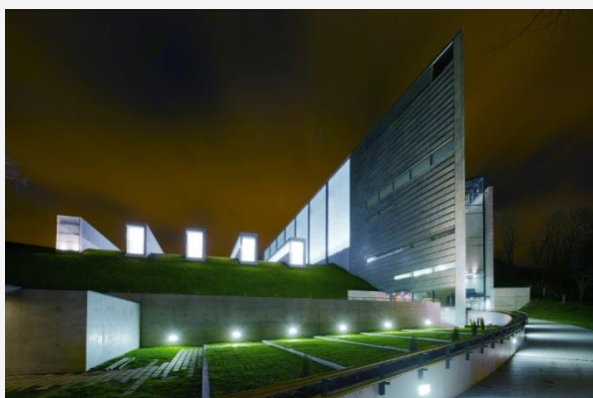
Among the substantial projects in process that started in 2018 and earlier and will continue in 2019 are the construction works of Maakri Kvartal business complex, Tallink office building, the first stage of office building at Tartu mnt 80, Kuressaare town centre, student home of Rakvere Vocational School and commercial building at Pärnu mnt 186, as well as renovation works of Tsirguliina 330kV substation, dredging and reconstruction works of Hundipea port and construction of electric power cables of Suur Väin and Väike Väin straits and also work arising from the road repair and maintenance agreement in Tallinn.

LARGEST PROJECTS COMPLETED IN 2018

PROJECT NAME		LOCATION
T1 MALL of Tallinn shopping centre	new	Peterburi st. 2, Tallinn
Õpiku office building B	new	Sepise 9/Valukoja 8, Tallinn
Pärnu road 22 office building	new	Pärnu mnt 22, Tallinn
Extension works of Wendre production building	new	Lina st 31, Pärnu
Extension works to the air traffic control centre	new, rec	Rae village, Rae municipality, Harjumaa

PROJECT NAME		LOCATION
Extension works to Embassy of the People's Republic of China residence	new, rec	Narva mnt 108, Tallinn
Viimsi State Gymnasium	new	Tammepõllu st 2, Haabneeme, Viimsi municipality, Harjumaa
Tapa close combat exercise area construction works	new	Tapa, Lääne-Viru county
Vändra 110KV substation	rec	Vändra parish, Pärnu county
Kuusalu 110KV substation	rec	Kuusalu, Harjumaa
Sindi 110KV switchgear	rec	Urge village, Sauga municipality, Pärnu county
The pipelines and bore hole pumping station for Tutermaa WS	rec	Kumna ja Tutermaa village, Harku municipality, Harjumaa
Tõrva town centre	new, rec	Tõrva city, Valgamaa
State highway 11125 Perila-Jäneda reconstruction	rec	Perila-Jäneda km 0,0-5,7 ja 5,8-10,7
Vana-Pirita road reconstruction and building a parking lot for Estonia History Museum	rec	Vana-Pirita st, Tallinn
State highway 13103 Lügause-Oandu-Tudu	new	Lügause-Oandu-Tudu km 0,0-3,0 and 3,9-6,1
Vesivärava st. reconstruction	rec	Vesivärava st, Tallinn

100 ESTONIAN BUILDINGS, 100 YEARS OF ESTONIA



On the occasion of the 100th birthday of the Republic of Estonia, the Estonian Association of Construction Entrepreneurs and the Association of Construction Material Producers of Estonia produced an exhibition and released a book entitled *100 Buildings – 100 years. The Story of Estonia in Buildings, 1918–2017*.

Seven projects built by Merko were selected as the buildings that best characterized the year in which they were completed. The recognition went to the renovated Rotermann Salt Storage (1996), the headquarters of Ühispank (1999), Kumu Art Museum of Estonia (2005), the extension of Tartu maantee along with parking lot and twin towers (2007), the runway and taxiing area of Ämari Air Base (2010), the Ülemiste traffic junction (2013) and the Tondiraba Ice Rink (2014).

OTHER HOME MARKETS CONSTRUCTION SERVICE

The other home markets construction service segment consists of general construction work in Latvia, Lithuania and Norway, as well as civil engineering and electricity construction services in Latvia.

million EUR

	2018	2017	CHANGE
Revenue	182.2	108.4	+68.1%
% of total revenue	43.6%	34.1%	
Operating profit (loss)	1.9	1.8	+7.1%
Operating profit margin	1.1%	1.7%	

The revenue of the other home markets construction service segment amounted to EUR 182.2 million in 2018 (2017: EUR 108.4 million), an increase of 68% compared to 2017. If the other home markets construction service segment revenues of 2017 formed 34.1% of the group's revenue, then during 2018 this has increased to 43.6%. The growth has been supported mainly by major projects in Latvia.

In 2018, the operating profit of the other home markets construction service segment amounted to EUR 1.9 million (2017: EUR 1.8 million) and the operating profit margin was 1.1% (2017: 1.7%). As in Estonia, strong competition is evident also in other home markets (especially in Latvia and Lithuania), input prices have increased and there is a lack of free resources of sub-contractors. Main

contractors have been in a situation where profitability has had to be maintained, regardless of ever-tightening construction schedules, contractual sanctions and increasing costs. Realization of risks associated with construction objects has a direct impact on business segment's financial results. In addition, the operating profitability of other home markets construction service segment in 2018 was influenced by major construction works carried out in consortium, in which case the revenue in the segment's results is accounted for in full, but the profit only for the part belonging to the group. The goal for the group is to improve the risk-reward ratio of the other home markets construction service. We participate in tenders only in case the tendering conditions correspond to our understanding of suitable risk level.

In Latvia, Merko has gained a strong position among general contractors, which provides opportunities to grow business volumes. In Lithuania, the group is continuing with a strategic plan to focus on foreign customers, who make up the predominant part of the group's Lithuanian secured order book. In Lithuania, we have also entered more widely the public procurement sphere in the field of general construction. In Norway, group signed two major construction contracts in 2018, in the amount of EUR 4.6 million and EUR 3.8 million, as well as performed several smaller-scale agreements.

Among the substantial projects in process that started in 2018 and earlier and will continue in 2019 are, in Riga, the construction works of Multifunctional Centre Akropole, Alfa Shopping Centre and Lidl logistics centre, as well as finishing works of Z-Towers business complex and, in Ventspils, the construction works of music school and concert hall. In Vilnius, the larger projects were the construction works of Neringa Hotel and Quadrum office building, as well as apartment buildings in Šaltiniu Namai quarter and two school buildings. In Norway, the larger projects included the design and construction works of Tesla service centre and renovation works of an office building in Oslo.

LARGEST PROJECTS COMPLETED IN 2018

PROJECT NAME		LOCATION	COUNTRY
Boksto 14 apartment building	new	Boksto st. 14, Vilnius	Lithuania
Magdalēna multifunctional building	new	Antonijas st. 17A, Riga	Latvia
Cēsu 9 apartment building	new	Cēsu st. 9, Riga	Latvia
Katlakalna 6D warehouse complex	new	Katlakalna st. 6D Riga	Latvia
Akersgata 8 office building	rec	Akersgata 8, Oslo	Norway
Extension works of Blakstad Hospital	new	Strandveien 35, Vette	Norway



SUSTAINABILITY STANDARDS

In 2018, the group completed several sites that received certification on the basis of international sustainability standards. Building B of the Ūpiku Office Building in Tallinn has a LEED Platinum certificate and building A of the same project, built in 2016, carries LEED Gold certification.

The expansion of the Radisson Blu Hotel Lietuva in Vilnius received a Very Good rating in the BREEAM certificate system for its design and it is also seeking the same status for the construction process. Vilnius Hotel IBIS received a Good rating in the BREEAM system for both design and construction process and the office building at Narbuto 5 in Vilnius was awarded a Very Good BREEAM rating for the construction process. Of the sites currently in progress, the Riga Akropole shopping centre and the Quadrum South office building in Vilnius are currently seeking BREEAM certification.

REAL ESTATE DEVELOPMENT

The real estate development segment includes residential real estate development and construction of joint venture projects, long-term real estate investments and commercial real estate projects in Estonia, Latvia and Lithuania. In the interests of the finest quality and maximum convenience and assurance for buyers, Merko handles all phases of development: acquisition of the real estate, planning, design of the development project, construction, sales and marketing, and warranty-period customer service.

million EUR

	2018	2017	CHANGE
Revenue	70.9	74.0	-4.1%
incl. revenue from sale of apartments	41.3	47.1	
incl. construction service to joint venture projects	15.5	18.5	
incl. revenue from immovable properties	9.5	5.2	
% of total revenue	17.0%	23.3%	
Operating profit	11.3	13.8	-17.7%
Operating profit margin	16.0%	18.6%	

A total of 482 apartments (incl. 131 apartments in joint ventures) were sold in 2018 at the total value of EUR 41.3 million (excl. VAT), compared to 392 apartments (incl. 17 apartments in joint ventures) and EUR 47.1 million in 2017. Of the 482 apartments sold 305 were located in Estonia, 72 in Latvia, 105 in Lithuania. The construction service revenue from projects developed by joint ventures in 2018 was EUR 15.5 million (2017: EUR 18.5 million). In 2018, the group sold "ibis" hotel, developed in Vilnius, together with parking lot and part of the land plot for a price of EUR 8.8 million, which in reporting is recognised under revenue from immovable properties.

In 2018, the share of revenue from the real estate development segment formed 17.0% of the group's total revenue (2017: 23.3%), having decreased over the year by 6.3 pp. The main reason for the decrease of the share is the rapidly grown volumes of construction services in the other home markets. At the same time, the sales revenue of real estate development declined by 4.1%, mainly due to decrease in the sales of own developed apartments. Demand for Merko developed apartments remains on a good level. In the light of that, the group in 2018 increased the number of apartments put in development, thus also increasing the apartment stock by the end of the year.

In 2018, operating profit of the real estate development segment amounted to EUR 11.3 million (2017: EUR 13.8 million) and the operating profit margin was 16.0% (2017: 18.6%), which decreased by 2.6 pp compared to the same period previous year. The profitability of the apartment development projects varies by project and depends greatly on the cost structure of the specific project, incl. the land acquisition price. In 2017, the segment's profitability was positively influenced by one-off factors: the sale of immovable properties that were strategically not needed by the group, and revaluation of inventories. At the same time, the operating profit margin has been affected by the volume of construction service projects developed by joint ventures. Profit from construction has been recognised in the course of construction and the profit from development is realised at a later stage, upon sale of apartments to the final customer, based on the equity method.



PAEPARGI RESIDENTIAL ENVIRONMENT

In 2008, work was completed on the Paepargi development – a 42-hectare area right on the outskirts of the Tallinn city centre, in the Lasnamäe district. Since 2008, Merko has been developing the park territory and the area around the heart of the area, Pae Lake, and has built 22 apartment buildings along with the streets between the buildings. The living environment encompasses 600 apartments and 680 parking spaces for inhabitants.

Paepargi's living environment is enhanced by a lighted bridge, connecting the two sides of Pae Lake, including a fountain, play areas in the park, jogging trails and exercise equipment, basketball court and a ping-pong table made of concrete.

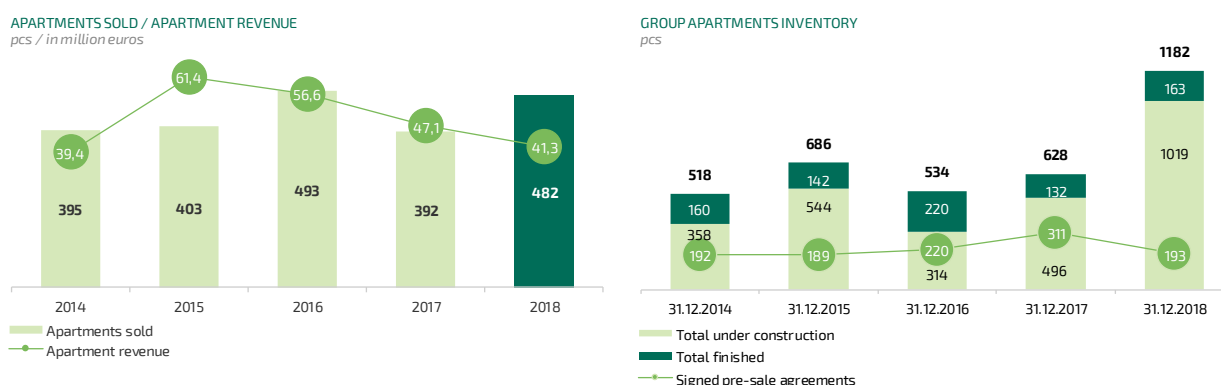
Managing a substantial portfolio of immovables requires careful and detailed planning of the whole process: the development of apartment buildings starts by organising the detailed planning, designing and construction, and ends with the sale of completed

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 property as developed real estate.

Merko manages all development phases of new housing – planning, designing, building and sales. Homes developed and built by Merko are characterised by integrated living environments, high energy efficiency, good sound insulation from indoor and outdoor noise as well as healthy interior climate.

Our objective is always 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 be of high quality and maintain its value in years to come.

In real estate development joint projects, Merko brings its knowledge and experience of real estate development and construction to the partnership and the other party provides the plot and/or investment. The relationships between the parties are regulated by a stakeholders' contract that specifies the liability, rights and responsibility of each partner.

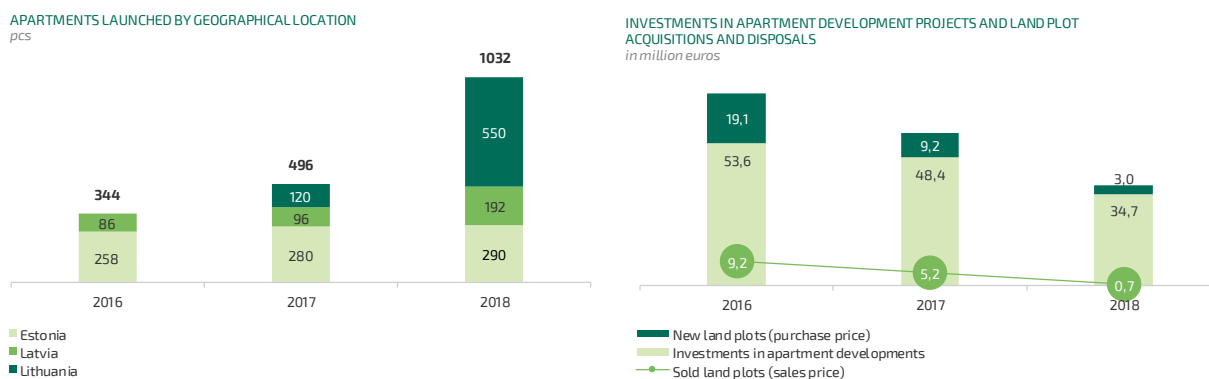


At the end of the period, Merko Ehitus group's inventory of apartments amounted to 1,182 units, of which 163 were completed and 1,019 in construction. 193 apartments were covered with preliminary agreements, incl. 41 completed apartments (34 in Estonia, 1 in Latvia and 6 in Lithuania) and 152 apartments under construction (110 in Estonia and 42 in Lithuania). The sale of these apartments had not yet been finalised and the apartments had not been delivered to customers, as the development sites are still under construction or the sites were completed at the end of the reporting period and the sales transactions have not all been finalised yet.

As at 31 December 2018, Merko Ehitus group had a total of 989 apartments for active sale (as at 31 December 2017: 317 apartments), for which there are no pre-sale agreements and of which 122 have been completed (27 in Estonia, 72 in Latvia and 23 in Lithuania) and 867 are under construction (169 in Estonia, 192 in Latvia and 506 in Lithuania). The number of apartments on sale as at 31 December 2018 has increased, compared to 31 December 2017, mainly due to the higher volume of projects launched in 2018: launch of construction of 1,032 new apartments (incl. 11 in joint venture), compared to 496 new apartments in 2017 (incl. 121 in joint venture).

After the reporting date, the group has launched one apartment development project – Matilda Maja project with 20 apartments, located at Paldiski st. 21 in Tallinn.

In 2018, the group invested a total of EUR 34.7 million (2017: EUR 48.4 million) in new development projects launched in 2018 as well as projects already in progress from previous year.



The group intends to continue investing in residential real estate projects also in 2019, maintaining the general annual planned development volumes at around 650-700 apartments. The actual volumes will depend on the developments on the apartment markets of the Baltic states and the pace of construction permit issuance. In 2018, construction of 1,032 apartments was started,

which is above 300 units more than the general annual target level. This was mainly due to delays in receiving building permits for projects in 2017, which were postponed to 2018. The planned investment level in 2019 in both development projects initiated in the previous years as well as new projects to be launched in 2019 is about EUR 100 million. Higher than usual investment level is due to the fact that in 2018 the construction of large part of the apartments was started in the second half of the year. Because of that also the investment amount of last year (EUR 34.7 million) was lower than initially planned (ca EUR 60 million). Substantial part of the investments to these apartments need to be made in 2019 and the majority of them will be finished in 2020.

One of the group's objectives is to keep the land plot portfolio at a level that ensures stable inventory of property development projects, considering the market conditions. As at 31 December 2018, the group's inventories included land plots with development potential, where the construction works had not started, of EUR 54.5 million (31.12.2017: EUR 63.6 million).

GROUP'S INVENTORIES WITH DEVELOPMENT POTENTIAL BY COUNTRY AS AT 31.12.

million EUR

	31.12.2018	31.12.2017
Estonia	26.9	28.9
Latvia	26.6	26.5
Lithuania	1.0	8.2
Total	54.5	63.6

In 2018, the group purchased new land plots at an acquisition cost of EUR 3.0 million for development purposes, incl. EUR 1.7 million in Estonia and EUR 1.3 million in Latvia (2017: acquired different new land plots in Estonia at an acquisition cost of EUR 5.1 million and in Latvia at an acquisition cost of EUR 4.1 million).

THE SPECIFICATIONS OF PROJECTS COMPLETED IN 2018

PROJECT		LOCATION	SIZE
Paepargi 43, 47	new	Tallinn, Estonia	4,227 m ² , 66 apartments
Paepargi 39, 41, 45	new	Tallinn, Estonia	5,695 m ² , 93 apartments
Staapli 3 *	new	Tallinn, Estonia	7,701 m ² , 103 apartments
Staapli 8 *	new	Tallinn, Estonia	1,991 m ² , 18 apartments
Staapli 12 *	New	Tallinn, Estonia	576 m ² , 11 apartments
Ceikiniu 3 (Rinktinės Urban)	new	Vilnius, Lithuania	6,727 m ² , 126 apartments
Gaiļezers 9, 11, 15	new	Riga, Latvia	6,943 m ² , 96 apartments

* A project developed by a joint venture.

Projects completed in 2018 had a total of 513 apartments with a total area of 33,860 square metres, of which 129 had not been sold by the year-end, and of those 40 apartments had a preliminary agreement signed, but the sales had not yet been finalised and the apartments not yet delivered to customers.



SATISFACTION SURVEYS CONDUCTED AMONG APARTMENT BUYERS

In 2018, Merko Ehitus Eesti conducted satisfaction surveys among people who had bought an apartment in the buildings at Staapli 4 in the Noblessner project and Paepargi 43, 47 and 53 in the Paepargi development. The results confirmed that the Merko trademark is highly valued among the buyers. In the study, Merko's general reference index (the customer loyalty index) was measured. The average result for the projects on a scale of -100 to +100 was +54. The research team also gauged customer satisfaction with sale and marketing materials, the purchasing process, the design quality and construction quality and the developed living environment. All of the projects posted an average score of more than 7 points out of 10, which can be considered a good result. The satisfaction surveys give Merko valuable feedback about how to improve the products and services further.

SECURED ORDER BOOK

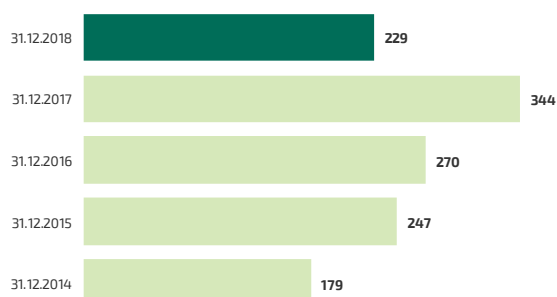
As at 31 December 2018, the group's secured order book (excluding own property developments) amounted to EUR 229.0 million as compared to EUR 344.4 million as at 31 December 2017. The secured order book excludes the group's proprietary residential development projects and work related to developing real estate investments.

In 2018, new construction contracts worth EUR 246.4 million were signed (excludes property developments), compared to EUR 334.9 million in the prior year.

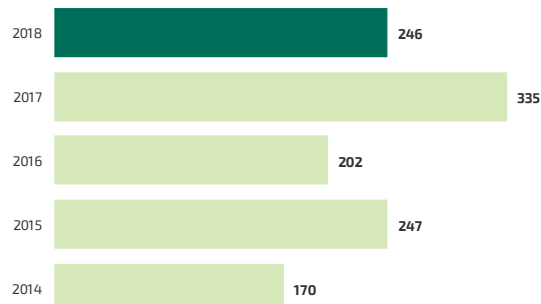
SECURED ORDER BOOK
in million euros



SECURED ORDER BOOK
in million euros



NEW CONTRACTS SIGNED
in million euros



LARGEST CONSTRUCTION CONTRACTS SIGNED IN 2018

in millions of euros (as announced during 2018 on Nasdaq Baltic stock exchange)

BRIEF DESCRIPTION OF CONTRACT	COUNTRY	COMPLETION DATE	COST
Long-term contract to carry out road repair and maintenance works in Tallinn	Estonia	End of 2023	26.0*
Design and construction contract for the construction of commercial building at Pärnu mnt 186, Tallinn	Estonia	March of 2020	16.0
Construction contract for the construction of new electric power cables between the mainland of Estonia and Muhu island in cooperation with AS Connecto Eesti. Leading partner in the contract is AS Merko Infra with 51:49 share	Estonia	December of 2020	9.0
Construction contract for the dredging and reconstruction works in Hundipea port	Estonia	January of 2020	6.8
Construction contract for the construction of new electric power cables between Muhu and Saaremaa islands in cooperation with AS Connecto Eesti. Leading partner in the contract is AS Connecto Eesti with 51:49 share	Estonia	December of 2020	5.4
Construction contract for the construction of Tsirguliina substation	Estonia	November of 2019	4.3
Construction contract for the construction of a student home at Piiri st. 8, Rakvere	Estonia	End of 2019	4.3
			71.8
Construction contract for the construction of a logistics centre for Lidl at Ulbrokas street in Riga	Latvia	January of 2020	42.5
			42.5
Construction contract for the construction of office building Quadrum at Konstitucijas ave. 21, Vilnius	Lithuania	October of 2019	12.0
Construction contract for the construction of a new private school building at Luksines st. 29, Vilnius	Lithuania	End of 2019	7.4
Construction contract for the construction of a new school building at Medeinos st. 14, Vilnius	Lithuania	July of 2019	4.0
			23.4

BRIEF DESCRIPTION OF CONTRACT	COUNTRY	COMPLETION DATE	COST
Design and construction contract for the construction of Tesla service centre at Karihaugveien st. 100, Oslo	Norway	April of 2019	4.5
Design and construction contract for the renovation of an office building at Møllergata st. 23-25, Oslo	Norway	July of 2019	3.6
Total			8.1
			145.8

* The contract value is approximately EUR 5.2 million per year.

Of the contracts signed in 2018, private sector orders continued to account for the vast majority, which is also represented in the group's secured order book as at the end of the reporting period, where private sector orders from projects in progress constitute 70% and public sector orders make up 30% (31.12.2017: 86% private sector and 14% public sector). The group continues to focus on comprehensive supply of the design and construction contracts.



SATISFACTION SURVEYS CONDUCTED AMONG CUSTOMERS

In 2018, a satisfaction survey conducted by AS Merko Ehitus Eesti among customers who contracted for construction services from Merko found that Merko had a general reference index score – also known as the customer loyalty index – of +50 (on a scale of -100 to +100).

All the topic areas covered received a score of at least 8 out of 10. Customers were most satisfied with Merko's employment culture and environment, the availability of key persons at Merko, and information provided in the building acceptance stage about use and maintenance of the building and the instructions for the warranty period.

CASH FLOWS

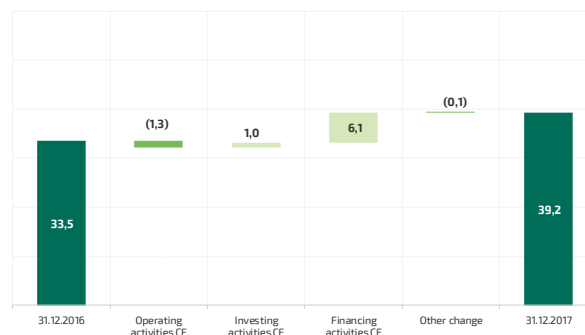
The change in short-term investments and cash equivalents in 2018 of Merko Ehitus group was positive EUR 0.8 million and as at 31 December 2018 the group had cash and cash equivalents in the amount of EUR 40.0 million (31.12.2017: EUR 39.2 million).

The operating cash flows of 2018 were positive by EUR 33.8 million (2017: negative by EUR 1.3 million), the cash flows from investment activities were EUR 0.0 million (2017: positive by EUR 1.0 million) and cash flows from financing activities were negative by EUR 33.0 million (2017: positive by EUR 6.1 million).

CHANGE IN CASH AND CASH EQUIVALENTS
in million euros



CHANGE IN CASH AND CASH EQUIVALENTS
in million euros



The cash flow from operating activity had positive impacts from EBITDA of EUR 21.9 million (2017: positive impact of EUR 22.2 million), from the positive changes in receivables and liabilities related to construction contracts of EUR 11.2 million (2017: negative change of EUR 8.5 million), change in the provisions of EUR 4.7 million (2017: positive change of EUR 0.6 million) and change in inventories of EUR 0.6 million (2017: negative change of EUR 4.9 million), while the negative impacts came from changes in trade and other receivables related to operating activities of EUR 1.3 million (2017: negative change of EUR 19.3 million), change in trade and other payables related to operating activities of EUR 1.8 million (2017: positive change of EUR 12.1 million) and change from the corporate income tax paid of EUR 0.4 million (12 months 2017: EUR 1.3 million).

Cash flows from investing activities include negative cash flow from the acquisition of non-current assets in the amount of EUR 1.0 million (2017: EUR 1.4 million) and the largest positive cash flow was from the sale of non-current assets in the amount of EUR 0.7 million (2017: EUR 1.9 million).

To support cash flows from operating activities, the group has raised additional external capital. At the same time, the debt ratio has remained at a moderate level (16.4% of total assets as at 31 December 2018; 21.4% as at 31 December 2017).

In cash flows from financing, the larger negative factors were dividend payment of EUR 17.8 million (2017: EUR 7.4 million) and negative change of loans received and repaid in connection with development projects in the amount of EUR 20.1 million (2017: net positive cash flow of EUR 7.7 million). Positive cash flow from financing activity were gained from net amount of loans received and repaid of project specific loans obtained using investment property as collateral in the amount of EUR 1.4 million (2017: negative cash flow in the net amount of EUR 0.6 million), as well as change in loans related to construction projects in the net amount of EUR 4.2 million (2017: net negative cash flow of EUR 2.8 million).

RATIOS

(attributable to equity holders of the parent)

INCOME STATEMENT SUMMARY		2018	2017	2016
Revenue	million EUR	418.0	317.6	252.0
Gross profit	million EUR	33.0	30.9	19.0
Gross margin	%	7.9	9.7	7.5
Operating profit	million EUR	19.9	19.5	7.7
Operating profit margin	%	4.8	6.2	3.1
Profit before tax	million EUR	19.8	18.8	7.3
EBT margin	%	4.7	5.9	2.9
Net profit	million EUR	19.4	15.8	6.0
attributable to equity holders of the parent	million EUR	19.3	14.7	6.1
attributable to non-controlling interest	million EUR	0.1	1.1	(0.1)
Net margin	%	4.6	4.6	2.4
Other income statement indicators				
EBITDA	million EUR	21.9	22.2	11.2
EBITDA margin	%	5.2	7.0	4.4
General expense ratio	%	3.7	4.6	5.3
Labour cost ratio	%	8.2	10.1	11.7
Revenue per employee	thousand EUR	563	434	325
Other significant indicators				
		31.12.2018	31.12.2017	31.12.2016
Return on equity	%	15.3	11.9	5.0
Return on assets	%	6.9	5.8	2.8
Return on invested capital	%	11.5	11.4	5.1
Equity ratio	%	48.9	47.0	51.6
Debt ratio	%	16.4	21.4	19.3
Current ratio	times	2.2	2.2	2.9*
Quick ratio	times	1.1	1.1	1.1*
Accounts receivable turnover	days	40	40	37
Accounts payable turnover	days	41	40	38
Average number of employees (total group)	people	743	732	776
Order book	million EUR	229.0	344.4	269.6

Calculation of ratios is provided on page 122 of the report.

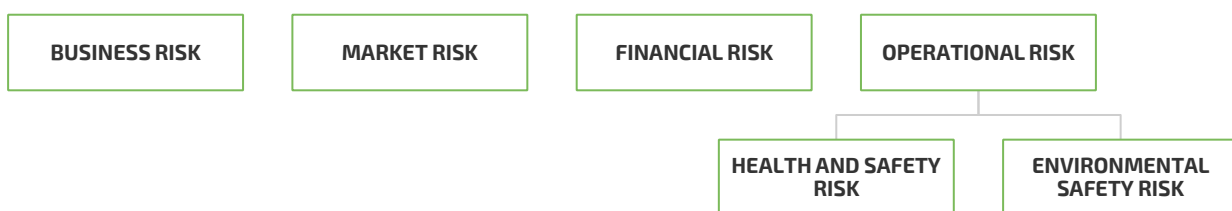
* As at 31 December 2016, in the formula for calculating the current ratio and the quick ratio, the amount of current liabilities has been reduced by EUR 12.5 million as a result of refinancing of the short-term loan received from the parent company AS Riverito at the end of 2016 with long-term bank loans at the beginning of 2017.

RISK MANAGEMENT

Risk management is part of strategic management and is inseparable from daily operations of the group. In managing risks, the main objective of the group is to determine larger and significant risks and to optimally manage these risks so that the group achieves its strategic and financial objectives. The group considers it important to assess aggregate group risks, instead of the impact factors of individual risks. Turning constant attention to risk management enables to exclude or minimise a possible financial loss. The following are deemed by the group to be the most significant risks: market risk, operational risk and financial risk, 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 35 of the financial statements. 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.

Group risk management is coordinated by the management board. In addition, the management board of each subsidiary develops, implements and maintains processes covering subsidiary's activities for the management of all material risks impacting the activity and results of the group. Each group company and business unit must ensure that risks are managed on an ongoing basis with reference to the objectives it has been assigned. Risk-taking is a normal part of business, but in doing so, one must be convinced that if the risk materialises, purposeful and sustainable activity is maintained with reference to the strategy of the company and business unit. The group assesses ongoing business risks and risks affecting investments in a calculated manner.

Merko Ehitus divides risks into four main categories:



Business risk

The group takes calculated risks for the purpose of increasing revenue. The biggest business risks relate to the entry of Merko Ehitus to new markets and segments, the management of existing inventories and investments and the execution of awarded construction contracts. 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.

Operating in several different markets requires orientation in the environments of various countries. The main areas of attention are the cyclical attributes of economies and legal, cultural and political differences. The main objective of Merko Ehitus is to expand into new segments in existing markets. When entering new markets, the company thoroughly studies local customs and peculiarities before making final investment decisions and makes sure that the environment is sufficiently stable and a competent team is assembled.

From the investments point of view, the main risks relate to the portfolio of properties and implementation of property development projects. Merko Ehitus carries out real estate development projects as an integrated process, comprising all activities from the acquisition of the property, proceedings related to the detailed plan, handling design and construction and finally sale of finished apartments to the customer and warranty service. The group uses standard policies for implementing real estate development projects in order to ensure the use of best practices that the entire group has accumulated over years. Merko Ehitus continuously analyses its existing inventory of land with development potential to ensure that the portfolio contains a sufficient number of properties to carry out developments suitable to the market. Investments in new properties or projects of up to EUR 3 million are decided on the supervisory board level of subsidiaries, while larger projects are further approved by the supervisory board of the group.

Market risk

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 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, increased income and savings, the demand and transaction activity on the apartment market has grown. Due to the selectiveness of the real estate market, setting the right sale price for new development projects in the given region has become very important. For managing 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 partially related to financial risks also includes *currency risk and interest rate risk*. The analysis of these risks is provided in Note 35 of the financial statements.

Financial risk

Financial risks include risks related to adequate capitalisation level and financing, currency, interest rate and credit risk. Financial risks are managed by the accounting and finance rules, as well as audit. The group's finance department is responsible for forecasting the cash flows of Merko Ehitus, continuously monitoring various subsidiaries' cash positions and forecasts. The group has enacted a regular budgeting procedure whereby the group's annual forecasts are updated as a minimum three times per year.

The analysis on *credit, liquidity and legal risks* is provided in Note 35 of the financial statements.

Operational risk

Operational risks are risks caused by inadequate or ineffective processes, people, equipment, systems or external events. The main goal of operational risk management is to reduce the effect of unwanted events. In order to meet the objective, the group is developing internal processes and control systems. In order to ensure the group's high level of project management, project teams are continuously trained, business processes are improved and results are monitored.

Considering the group's field of business, it is essential in operational risk management that the improvement and application of safety standards and regulations continues and that supervision of compliance with environmental requirements is increased. One measure for managing operational risks is the implementation of quality and environmental management systems. Risks related to occupational health and safety in construction are assessed and managed in all units and process stages of the group. The largest construction companies of the group, Merko Ehitus Eesti, Merko Infra, Tallinna Teede and and Latvian and Lithuanian subsidiaries, have implemented quality management system ISO 9001 and environmental management system ISO 14001 and health and safety management system OHSAS 18001. All management systems are certified. The group employs 8 (2017: 8) full-time quality specialists who are responsible for developing quality, safety and management systems and ensuring their functioning.

Insurance is used as additional mitigation of operational risks, especially for risks that cannot otherwise be mitigated. 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. The risks of the projects, which 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 specifics. 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 2018, indemnity applications submitted to insurance companies totalled EUR 0.91 million (2017: EUR 0.46 million), and insurance benefits were received in the amount of EUR 0.83 million (2017: EUR 0.43 million).

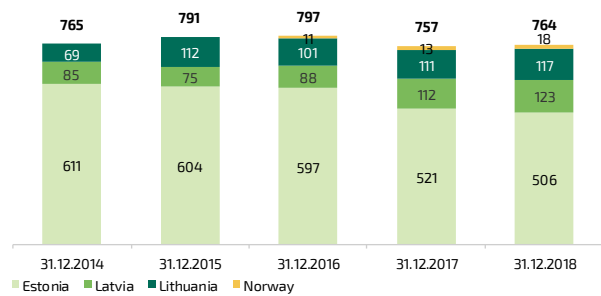
A warranty provision has been provided at the group to cover for the construction errors, which have become evident during the warranty period. In 2018, warranty provisions were set up at the group in the total amount of EUR 1.44 million (2017: EUR 1.15 million) and disbursements amounted to EUR 0.64 million (2017: EUR 0.74 million). As at the year-end, the group's warranty provision amounted to EUR 3.37 million (31.12.2017: EUR 2.87 million). With regard to work performed by subcontractors, the subcontractors are 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.

EMPLOYEES

Compared to the same period last year, the number of the group's employees increased by 7 (+0.9%) and as at 31 December 2018, the group had a total of 764 employees (including fixed-term and part-time employees).

166 people joined and 159 people left (2017: 159 people joined and 199 people left) Merko group in the financial year (including both termless and fixed-term contracts).

NO OF EMPLOYEES
people



TOTAL NUMBER OF EMPLOYEES BY EMPLOYMENT CONTRACT

	2018		2017	
	Count	%	Count	%
Permanent contract	699	91%	679	90%
Temporary contract	65	9%	78	10%
Total	764	100%	757	100%

TOTAL NUMBER OF EMPLOYEES BY GEOGRAPHICAL LOCATION

	2018		2017	
	Count	%	Count	%
Estonia	506	66%	521	69%
Latvia	123	16%	112	15%
Lithuania	117	15%	111	15%
Norway	18	3%	13	1%
Total	764	100%	757	100%

TOTAL NUMBER OF PERMANENT EMPLOYEES BY EMPLOYMENT TYPE

	2018		2017	
	Count	%	Count	%
Full-time	660	94%	644	95%
Part-time	39	6%	35	5%
Total	699	100%	679	100%

TOTAL NUMBER OF EMPLOYEES BY EMPLOYMENT POSITION

	2018		2017	
	Count	%	Count	%
Management	19	2%	19	2%
Middle management, specialists	493	65%	481	64%
Workers	252	33%	257	34%
Total	764	100%	757	100%

TOTAL NUMBER OF EMPLOYEES BY GENDER

	2018		2017	
	Count	%	Count	%
Male	646	85%	640	85%
Female	118	15%	117	15%
Total	764	100%	757	100%



SECTOR'S BIGGEST TAXPAYER

Merko places great value on doing honest business, including being a trustworthy and stable employer. We create a working environment that is conducive to good performance, one where occupational safety and development opportunities play an integral role.

The group's Estonian construction company AS Merko Ehitus Eesti employed over 500 people and, similarly to 2017, was also the biggest construction sector taxpayer and payer of labour taxes in Estonia. In 2018, the companies in AS Merko Ehitus Eesti group paid close to 17.5 million euros in state taxes and over 9.3 million euros in labour taxes.

PERSONNEL POLICY

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

We develop responsible management throughout the organisation, guided by group strategy, management system, applicable law, ethical values and good organisation management practice. We treat employees as partners, involving them in the decision-making process and perceiving that the right to make decisions includes responsibility. We support people's achievement of their professional goals and the advancement of their career in the group by encouraging existing employees to apply for vacant or new positions within the group. We ensure an adequate, fair and competitive salary and motivation package that corresponds to the contribution of the employee.

We provide employees with conditions for professional development and career opportunities by supporting studies and acquisition of professional knowledge and experience. We support our employees for developing their competence and skills.

In 2018, the number of new grievances about labour practices against Merko group amounted to 0 (2017: none), the number of grievances (both from current and previous years) addressed was 0 (2017: none) and the number of grievances (both from current and previous years) resolved was 0 (2017: none).

THE NUMBER OF EMPLOYEES WHO RECEIVED AN ANNUAL PERFORMANCE REVIEW

	2018		2017	
Estonia	126	25%	132	25%
Latvia	26	21%	35	31%
Lithuania	110	94%	111	100%
Norway	-	-	-	-
Total	262	34%	278	37%



INTERNS

In 2018, Merko Group had 23 interns. Seven of the students became our employees in Estonia and two in Latvia. In Estonia, 14 students from the Tallinn University of Technology, Tallinn University of Applied Sciences, the Võru County Vocational Education Centre and the Danish university VIA University College completed internships at Merko, getting an overview of the profession of skilled concrete worker and management of and work processes on complex projects (T1 Mall of Tallinn, Viimsi State Gymnasium, Pärnu mnt 22 office building, Tallink office building, Õpiku Business building, Noblessner Quarter, and others). Students in the electronic equipment speciality completed internships on various sites in the electrical work department. In Latvia, six interns were from the Riga University of Technology, one from the Latvia University of Life Sciences, civil engineering faculty and one from the Riga Technical College, who worked on construction sites and in the office. One intern was posted at our Lithuanian subsidiary.

HEALTH AND SAFETY

Since 2004, the construction companies in the group have followed the principles of the OHSAS 18001 occupational health and safety management system and the companies are certified accordingly. We consider it very important to take a contemporary approach to the field of occupational safety and health, and we have thus launched preparations for transition to the principles of the new ISO 45001 occupational health and safety standard and certification. We have also updated the risk analysis for our construction companies to determine the needs and possibilities for improving occupational health and safety and mapped the assessments of psychosocial risk factors for our employees. During 2018, the group conducted an obligatory in-depth occupational safety training in which about 100 employees took part.

The group companies have set the priority of establishing a safe working environment staffed by well-trained, healthy and motivated employees, both on construction sites and in offices. Our goal is to develop and furnish workplaces where on-the-job accidents and harm to health can be prevented in all respects and to preserve the long-term capacity for work and wellbeing of employees. To do so, we provide our employees with the necessary work and personal safety equipment and organise regular occupational health and safety training and in-service training; all new employees (including office staff) undergo occupational safety training when they start work. In addition, we notify our cooperation partners of our group's fire safety and occupational safety requirements and expect all of our contractual partners working on our sites to abide by them.

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 group, to allow employees to use the necessary health rehabilitation measures (e.g. treatment massage). Additionally, the group organises and provides free necessary vaccinations for its employees upon request.

77% of Merko Ehitus group's employees worked in companies with an international health and safety certificate OHSAS 18001 in 2018 (2017: 77%).

A balanced personal life and a healthy way of living provide a counterbalance to stressful work. In order to promote recreational sports and to maintain working ability we pay our employees sports and health allowance.



A COMPASSIONATE EMPLOYER

Merko cares about its employees and holds regular events for its workforce and their families, team-building events, and celebrates important occasions in its employees' lives.

Twice a year, AS Merko Ehitus Eesti organises an event for employees and their partners, a children's Christmas party and a bring-your-children-to-work day, offering them an exciting programme of activities. The company supports sports-minded active lifestyles by organising joint trainings, compensating expenses on sports and taking part in team sports (such as volleyball, ice hockey, football, mud run, Ironman basketball and tennis). The company also allows employees to work part-time and go on leave without pay. It pays employees their normal remuneration while they are participating in national defence exercises.

In accordance with the GRI guidelines, the rates of injury, occupational diseases, lost days, and absenteeism presented below are related to the number of employees, not the number of hours worked. The factor 200,000 is derived from 50 working weeks at 40 hours per week, per 100 employees.

TOTAL NUMBER AND RATES OF INJURIES, OCCUPATIONAL ILLNESSES, LOST AND ABSENTEE DAYS AND FATALITIES

	2018	2017	2016
Total number of injuries/accidents excluding minor (first-aid level) injuries/accidents	7	9	6
Total number of occupational illnesses	0	0	0
Total number of lost days due to occupational injuries/accidents or illnesses	406	282	510
Total number of absentee days	7,324	7,700	6,767
Total number of fatalities *	0	0	0
Injury rate (per 100 employees)	1.0	1.3	0.9
Occupational diseases rate (per 100 employees)	0.0	0.0	0.0
Lost days rate (per 100 employees)	60.7	41.2	72.9
Absentee rate per year (%)	4.4	4.5	3.9

Calculation of ratios is provided on page 122 of the report.

* In 2018, there was 1 work related accident, which resulted in injury to an employee of a subcontractor to which Merko group companies are liable for the general safety of the working environment (2017: 2; 2016: 0), and 0 fatal accidents to such employees (2017: 1; 2016: 0).

PERSONNEL DEVELOPMENT AND RECOGNITION

- we offer employees work they are trained to do and interested in, and which offers them opportunities for growth;
- we remunerate our employees fairly, taking into account their contribution to achieving the group's goals;
- we recognize employees who achieve or exceed the agreed-upon objectives.

The goal of the group's training and development activity is to support all facets of employees and develop and strengthen our teams. For the purpose of preserving and increasing employees' professional competence, we organise in-service training for our employees, preferring trainings that provide in-service training credit points needed to certify their competence.

The group's Estonian subsidiary has started a series of in-house trainings that cover topics that come up on construction sites, share experiences and provide an overview of the necessary standards and regulations in the field. The purpose of in-house training is to support the social development of employees on all levels and make teamwork more effective. The trainings also cover self-development, broadening horizons and mental health topics. In 2018, nearly 100 Estonian employees underwent a training called "Mental health in employment life". This in-house training series has been given its approval by the Estonian Association of Construction Engineers, and thus these trainings also confer in-service training credit points.

It is also important to raise awareness of health and occupational safety, and so employees in positions of responsibility regularly undergo occupational health and safety trainings (first aid givers, those performing work with open flame, slingers and others). In 2018, occupational safety trainings were held for all employees whose work involves presence on a construction site (engineering personnel, workers and apartment sale staff).

To train the young employees of the future, we have been engaged in developing and training students for years, offering them internships and visiting schools to deliver lectures. In addition, we have organised workshops and competitions, excursions to sites. We provide multifaceted support and recognition for teaching at school and acquiring a diploma.

We celebrate together with our employees their personal events. Group events for employees welcome everybody together with their spouses or companions and family events welcome the whole family. We offer additional benefits in the form of holiday days to our long-time employees and recognise them with the group's gold, silver and bronze pins.

We highly value teamwork and a strong sense of team identity. In order to recognise the most prominent employees of the company and the best business partners, employees annually elect AS Merko Ehitus Eesti and Tallinna Teede AS Achievers of the Year.



TRAINING

In 2018, AS Merko Ehitus Eesti held 21 briefings as part of in-house training (on average, they lasted 1.5 hours or 2 academic sessions per briefing). Employees attended these briefings a total of 381 times. Five different lecturers covered 16 different subjects.

The volume of external trainings organised in 2018 for managers, office staff and engineering staff at the Estonian subsidiary was 7,115 academic hours. In total, 209 employees took part and the number of training hours per person averaged 34.

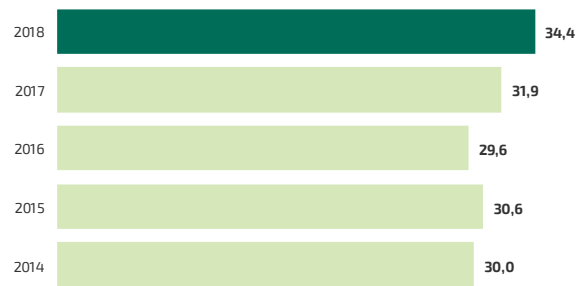
REMUNERATION

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

The group defines labour cost as salary (incl. fixed salary, additional pay (night work, overtime and public holidays), holiday pay and bonus), taxes based on salary, fringe benefits and taxes based on fringe benefits. In 2018, the labour cost was EUR 34.4 million (2017: EUR 31.9 million), up 7.6% from the previous year.

Benefits that are standard for full-time employees and not offered to part-time employees are not separately disclosed in Merko group companies, except with regard to part-time employees employed under a contract for a specified term, who are not entitled to all of the benefits offered to group employees.

LABOUR COST
in million euros



ETHICAL BUSINESS PRACTICES

Merko's core values include doing ethical business, as this helps to achieve profitable growth, maintain the trust of stakeholders, and support fair competition and equal treatment. AS Merko Ehitus group does not tolerate corruption in any form. All employees of the group must proceed from ethical principles in everything that they do.

In order to facilitate this, the group has enacted a Code of Business Ethics, which all Merko group employees are obliged to read and adhere to. The topic of business ethics has been thoroughly covered on the group's website <http://group.merko.ee/en/corporate-governance-2/responsibility/ethical-business-practices/>.

All employees, partners and customers can report clear or potential unethical conduct via various anonymous channels, of which the website provides an overview: <http://group.merko.ee/en/corporate-governance-2/responsibility/reporting-channels/>. The reporting and information analysis system implemented in AS Merko Ehitus ensures security, confidentiality and, if so desired, anonymity at every stage of the process. Each reported misconduct will be investigated by an independent cooperation partner – AS Merko Ehitus's contractual cooperation partner Ernst & Young – and will lead to appropriate action. In 2018, the group received two hints that led to an internal investigation (2017: no hints received).

In addition, key persons at Merko Ehitus are obliged to file a declaration of personal interests that covers data on holdings in companies, positions held on management bodies of companies and other legal persons, membership of professional organisations, information on valid registrations of economic activities and other data that might indicate a possible conflict of interest. In 2018, no conflict of interest cases of key persons were identified by the group.

ENVIRONMENT

Since 2004, the construction companies in the group have followed the principles of the ISO 14001 environmental management system and the companies are certified accordingly.

We consider dealing with group-wide environmental aspects to be a high-priority field where the main focus lies on organising handling of waste generated on construction sites and, where possible, ensuring separate collection of waste. Before starting work on a construction site, we prepare a waste plan for the site. Our policy is that waste can be handed over only to a waste handler with a waste permit. For years, Merko has kept systematic statistics on waste generated on sites and filed periodic waste reports that received approval from the Environmental Board.

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.

Our environment-related goals are the conservation-minded use of all resources (materials, fuel, energy and water), reducing the amount of waste generated and supporting recovery of materials. To achieve all this, we promote awareness among our employees and partners in cooperation of the environment as a whole. In designing and building, the group has followed the main principles of the Quality and Sustainable Real Estate Lifecycle standard, and in selecting materials we strive to make sure that the materials are VOC (*volatile organic compounds*) free and the producers hold an ISO 14001 certificate.

The Merko group sets the goal of constructing buildings that meet modern energy performance requirements. In the European Union, energy performance of buildings is regulated by Directive 2010/31/EU of the European Parliament and of the Council, which sets out the requirements for nearly zero-energy buildings.

Considering that energy costs are rising, Merko in cooperation with a number of customers has adopted the use of new technologies, materials and technical solutions and used various kinds of architectural techniques/measures/solutions to achieve a building that is designed to be as economical as possible without harming its office or residential environment in other aspects. The group's construction companies have experience in building according to the specifications of the American LEED (*Leadership in Energy and Environmental Design*) and the British BREEAM (*Building Research Establishment Environmental Assessment Method*) certificate. In addition, we have built for the first time in the last hundred years, a wooden school building made from the oldest environmentally friendly material, using mainly cross laminated timber and glued laminated timber elements as load-bearing structures.



WATER TREATMENT TEST DEVICE

As a result of cooperation between the specialists in its civil engineering division and TalTech engineers, AS Merko Ehitus Eesti built a water treatment testing device for the university that allows study of various technologies and materials for wastewater and drinking water treatment plants. The new device will enrich studies for students in the environmental technology field and offer practical information for companies engaged in water handling, giving a way of developing technologies to remove pharmaceutical or heavy metal residues from drinking water. The testing equipment has an automated controller connected to the internet, allowing experiments to be monitored and controlled remotely. The device is being tested at Tartu water treatment plant and in September 2019 it will be installed at TalTech's new laboratory.

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 2018, Merko Ehitus continued its long-term sponsorship projects in the same fields:

- we support sports and recreational sport projects that help create ways for entire communities to participate in sports and recreation;
- we support education in order to develop specialised education and plant the seeds for a new generation of professionals;
- we support keeping art and culture vital and make them available to more people, focusing on sites that are nationally important and have broad appeal.

During the year, the group supported sports, culture and education and made charitable donations in a total amount of EUR 0.20 million (2017: EUR 0.32 million).

SPORTS AND RECREATIONAL SPORTS

The group's largest sponsored project is the Estonian Health Trails (<https://terviserajad.ee/>) project founded in 2005 in collaboration with Swedbank and Eesti Energia. The aim of the project is to fix up and develop Estonian exercise and sports tracks to ensure the availability of year-round free of charge possibility for active exercise in nature for all interested people, and popularise sporty lifestyle. SA Eesti Terviserajad (Estonian Health Trails Foundation) has taken on a noteworthy role in shaping people's exercise habits and popularising active lifestyle through a network of health trails, various events and active outreach

Estonia now has 112 recreational trails all over the country and 1,100 km of footpaths and exercise tracks, of which soft-surfaced paths make up 900 km, hard-surfaced paths account for 200 km and illuminated paths make up around 250 km. Estonia has an average of 83.4 km (2017: 76 km) of maintained trails and tracks and 18.9 km of illuminated recreational trails or tracks per 100,000 people. They get approximately four million visits per year.

Three new health trails were added to the recreational trails network in 2018: a 2.7 km long trail in Orissaare, a 3 km long trail in Valjala, Saaremaa, and a 1.4 km long illuminated trail in Jõhvi. The biggest developments of the year took place on Narva Pähklimäe recreational trail, Nõmme Sports Centre, Pirita recreational trail, Valgehobusemäe and Kõrvemaa. Large-scale design project work continued for expanding Tallinn's network of bicycle and pedestrian paths and health trails. Investments were made into track grooming and snow making equipment at Pähklimäe in Narva, Kuningamäe in Põltsamaa, Lähte, Kuressaare, Rakvere, Võru, Tabasalu, Jõulumäe, Kuremaa and Värska.

To simplify navigation for the trail users, 80 large-format maps were installed and 62 trails use markings designed and installed by the foundation. All over Estonia 37 stretching walls have been installed for warm-up and cool-down stretching after exercise. The foundation has produced a total of 80 instructional videos in the Estonian and Russian language, in addition to inspirational video interviews with celebrities and video overviews from the trails and events. The videos received almost two million views in 2018.

With the aim of emphasising the importance of regular physical activity and to facilitate activity also inside the buildings, the foundation has developed a concept of an indoor health trail. In cooperation with various organisations, enterprises and schools, tracks suitable for the buildings have been prepared, taking advantage of staircases, corridors and the courtyard areas. As of the end of 2018, SA Eesti Terviserajad had laid out 70 indoor tracks that are used by 70,000 people every day. In 2018, the Estonian National Library and the North Estonia Medical Centre opened indoor tracks in their respective buildings.

TOTAL INVESTMENT INTO RECREATIONAL TRAILS: 40 MILLION EUROS



In the years 2005-2018, the SA Eesti Terviserajad foundation backed by its founders has invested 4.8 million euros into developing recreational trails. The investments have been made into all Estonian counties, most of them in Harju, Tartu and Ida-Viru counties. Based on the preferences of the population in the area where the trails are developed and used most actively, the biggest investments have been made at Pirita, Nõmme-Harku, Kõrvemaa and Jõulumäe centres and trails.

In the period 2004-2018, the total investment into the Estonian recreational trails network (in addition to the foundation's investment also includes state and local governments' investments and support from the European Union) amounts to close to 40 million euros.

In 2018, Merko also continued supporting professional sports, focusing on Estonian skiing and tennis as a gold sponsor of the Estonian Tennis Association. Merko also supported activities of the Latvian skier Patrīcija Eiduka and the Lithuanian Ice Hockey Federation.

CULTURE AND EDUCATION

In the field of culture, Merko values cultural heritage and supports the possibility to introduce different cultures and arts. We have enjoyed close cooperation with the Art Museum of Estonia since 2005. In 2018, we supported the development of a new exhibition solution for Notke's Danse Macabre in Tallinn, which included a design and engineering project, a multimedia solution that introduces the programmatic side and iconography of this medieval work, and an exhibition solution for visitors with special needs.

Merko supports the field of education with the aim of promoting professional education and training a future generation of civil engineers. Merko has close cooperation with the Tallinn University of Technology and the Estonian Academy of Arts, participating in their innovation and research projects.

Since 2007, we have awarded scholarships to engineering students and young teaching staff at the Tallinn University of Technology. In cooperation with the Tallinn University of Technology's Development Fund, close to 25 scholarships have been awarded to support the future of civil engineering. In 2018, the 3,500-euro scholarship handed out by Merko Ehitus Estonia to a young teaching staff member and researcher went to a senior researcher with the Faculty of Engineering's Institute of Civil Engineering and Architecture, Kalle Kuusk. The main areas of Kalle's research are full-scale renovation of residential buildings and nearly zero energy buildings. At the student scholarship competition held in spring, a 2,000-euro grant was awarded to a student in the industrial construction and civil engineering field, Risto Häelme, and in autumn, to Erik Teder, studying in the same field. At the last competition, the level of the applicants for the scholarship was so high that two additional 1,000-euro scholarships were awarded to Mari Stepanjan and Kaarel Juurma.

Also in 2018, a book supported by SIA Merks in Latvia was published – Construction in Latvia from 1918-2018. The three volume work gives an overview of the important buildings, events and people who have shaped and are shaping the future in construction in Latvia.



DIGITAL TOOLS STUDIO

Since 2016, Merko has been working closely with the Estonian Academy of Arts Faculty of Architecture. In autumn 2016, Merko Ehitus provided support for the opening of a unique energy performance professorship and, in the 2018/2019 academic year, a digital tools studio, which focuses on the design of large-scale energy-efficient buildings.

The digital tools studio opened in 2018 is led by professor Bernhard Sommer and associate professor Galo Moncayo and students are also supervised by the department's junior researchers and PhD students. The studio focuses on use of digital tools in the building design process, seeing the various components of a building as closely interconnected and if necessary, adaptable.

RECOGNITIONS 2018

In 2018, the following AS Merko Ehitus group companies were recognised:

MOST COMPETITIVE CONSTRUCTION COMPANY

The Estonian Chamber of Commerce and Industry recognized AS Merko Ehitus as the most competitive Estonian construction company of 2018. The competitiveness rankings have been compiled since 2003 with the goal of contributing to the rise in competitiveness of Estonian companies and faster development of the economy in general. Merko has won this recognition on 12 occasions.

THE BEST REAL ESTATE DEVELOPER

The world's leading business and investment magazine *Euromoney* selected Merko Ehitus as the best real estate developer in its Real Estate Survey 2018. The company came in first in the overall, residential and multipurpose real estate category. The results of the *Euromoney* review are based on assessments from other market participants and specialists – advisers, developers, investors, banks, business customers and end users. Merko has won the title of Estonia's best real estate developer for five years.

THE BEST-KNOWN REAL ESTATE BRAND

According to results of a survey conducted by Kantar Emor, Merko is one of Estonia's best-known real estate brands. A total of 233 people looking to buy an apartment in a new development in the Tallinn area and 150 people who had bought such a home in the last five years took part in the survey. The strengths of the Merko brand are considered to be trustworthiness, professionalism and quality.

ATTRACTIVE EMPLOYER

According to results of a survey conducted by the employer branding agency Instar in 2018, AS Merko Ehitus Eesti is seen by students in science and technology fields as among the most attractive companies to work for. In an Estonia-wide survey of work expectations and employer reputation perceived by students in higher education institutions, vocational schools and medical schools, more than 5,400 young people rated the attractiveness of 194 Estonian organisations as an employer. AS Merko Ehitus Estonia has been in the top three for two years in a row.

TALLINN'S NEATEST CONSTRUCTION SITE

The Tallinn City Municipal Engineering Services Department recognized Merko's construction of the office building at Pärnu mnt 22 as a role model for the best-maintained construction site. The purpose of the public competition held since 2005 was to verify the upkeep of construction sites in Tallinn, draw builders' attention to any shortcomings in the field of public maintenance and determine which company was most diligent in this field. Merko has won the title on four occasions.

BEST USE OF GLUE-LAMINATED TIMBER

The Viimsi State Gymnasium built by AS Merko Ehitus Eesti in Viimsi won the people's choice award in 2008 at the best wood building competition and an Arcwood special prize for best use of glue-laminated timber. The new Viimsi school building is the first public building in Estonia whose load-bearing structure relies mainly on GLT. The annual wood building competition is organised by the Estonian Forest and Wood Industries Association with the purpose of raising the popularity of wood in architectural, technical and construction aspects.

BEST BIM COOPERATION PROJECT

At the best construction projects competition, the Ministry of Economic Affairs and Communications awarded two special prizes for digital construction – Viimsi State Gymnasium built by AS Merko Ehitus Eesti won the prize for use of BIM technology, and the 4D/5D award went to the Noblessner Kodusadam project, on which Merko was the developer, head designer and builder. The Ministry of Economic Affairs and Communications has awarded a special prize for best BIM cooperation project in order to stimulate digital construction in Estonia. A year before, the Telia office building designed and built by AS Merko Ehitus Eesti won the award.

BEST WORK OF ENGINEERING AND ANNUAL PRIZE FOR ARCHITECTURE

At the 2018 Construction Project of the Year competition organised by the Estonian Association of Architectural and Consulting Engineering Companies, the central square of Tõrva built by AS Merko Infra took first prize in the field of infrastructure. The renovated central square and sculptural observation platform – the Tõrva smokestack – also won honourable mention at the Väike 2018 small-form architecture competition hosted by the Estonian Association of Architects.

ESTONIA'S MOST SUSTAINABLE BUILDING

Building B of the Öpiku Maja office complex – built by AS Merko Ehitus Eesti to meet LEED Platinum requirements – won second place in the competition Estonia's Most Sustainable Building 2018 organised by MTÜ Green Building Council. The building's utility systems were designed using thermal modelling and solar panels are mounted on the roof. To avoid excess use of material, flexible screen solutions were used on the office levels and utility systems that are capable of servicing various spatial solutions. Volatile-organic-compound-free materials were used in construction and the necessary measures were taken to limit the circulation of construction dust. Larger rooms have CO₂ detectors, which provide alerts as to when the room needs fresh air. Over 75% of the waste were in their second go-round during construction; the waste plan was followed carefully.

LATVIA'S BUILDING OF THE YEAR 2017

At the Latvian competition Building of the Year 2017, the buildings in the second phase of the Skanstes Parks development project, developed and built by SIA Merks, took top place in the new residential buildings category. The Relais le Chevalier Hotel renovated by SIA Merks, located at Kaļķu 20, won third place in the renovation category at the same competition.

BASIC BIM COMPETENCY LEVEL IN LATVIA

The Latvian Association for Construction Industry Digitalisation has evaluated the experience and processes used by SIA Merks in the field of BIM; awarding the company the first basic competency level to be awarded in general construction in Latvia.

THE BEST FUTURE PROJECT

The Rinktinės Urban development project developed and built by UAB Merko Statyba was recognized as the best future project at the sustainable development competition, organised by the Lithuanian Real Estate Developers Association.

LITHUANIAN CONSTRUCTION SECTOR LEADER 2018

In the rankings compiled by Lithuanian business newspaper *Verslo Žinios*, UAB Merko Statyba won the title of construction sector leader 2018. Six indicators from 2017 were considered in the comparison of companies in the sector: revenue, profitability, profit before taxes, annual change in profit before taxes and revenue (2017 vs. 2016), and the company's pay level compared to the average remuneration at other companies in the sector.

A NEW CENTRAL SQUARE IN TÕRVA



The town of Tõrva was the first to get a new central square as part of the Republic of Estonia 100 architecture programme "Public Space". AS Merko Infra carried out a complete renovation of the town's central square and built a new bus station building. In addition, they opened a view of and access to Lake Vesikjärv and built the Tõrva smokestack as the town's symbolic edifice. The existing large square was converted into smaller expanses more suited to a small town and more greenery was established on the square.

The project was recognized at the Construction Project of the Year 2018 competition and at the Association of Architects' small objects architecture competition "Väike 2018".

SHARE AND SHAREHOLDERS

The shares of Merko Ehitus are listed in the Main List of Nasdaq Tallinn. As at 31 December 2018, the company has 17,700,000 shares. The number of shares did not change during 2018.

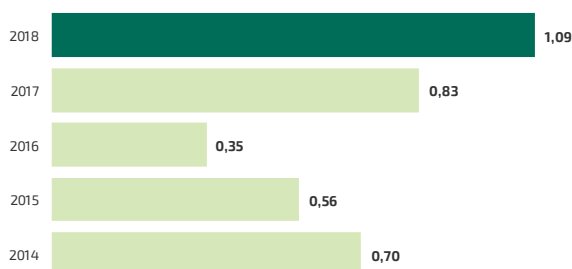
In 2018, 4,229 transactions were conducted with the shares of Merko Ehitus in the course of which 1.18 million shares were traded (6.7% of shares outstanding), with the total monetary value of transactions at EUR 12.2 million (comparative data for 2017: 2,203 transactions, in the course of which 0.51 million shares were traded (2.9% of shares outstanding) and the total monetary value of transactions was EUR 4.7 million). The lowest share price was EUR 8.70 and the highest share price was EUR 11.80 (2017: EUR 8.75 and EUR 9.69 respectively). The closing price of the share as at 31 December 2018 was EUR 9.20 (31.12.2017: EUR 8.81). As at 31 December 2018, by the Nasdaq Baltic stock exchange, the market capitalisation of AS Merko Ehitus was EUR 162.8 million, up 4.4% compared to the end of the equivalent period in the prior year (31.12.2017: EUR 155.9 million).

The number of shares that belong to the members of Supervisory Board and Management Board as at 31 December 2018 was 9,962,334 (31 December 2017: 9,962,334 shares) that accounted for 56.3% of the total number of shares (31 December 2017: 56.3%). 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 Report on Good Corporate Governance.

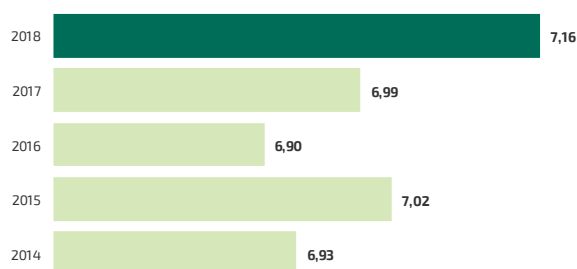
INFORMATION ON SECURITY

Issuer	AS Merko Ehitus
Name of security	Share of Merko Ehitus
Ticker	MRK1T
Residency of issuer	Estonia
Stock Exchange List	Nasdaq Tallinn, Baltic Main List
Industry	Construction
ISIN	EE3100098328
Nominal value	without nominal value
Number of securities	17,700,000
Volume of issue	12,000,000
Currency	EUR
Listing date	11.08.2008

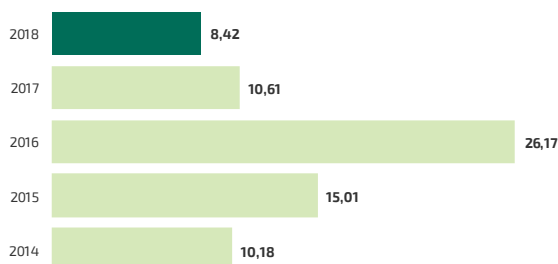
EARNINGS PER SHARE (EPS)
euros



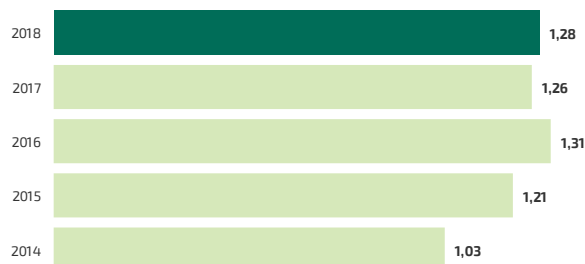
EQUITY PER SHARE
euros

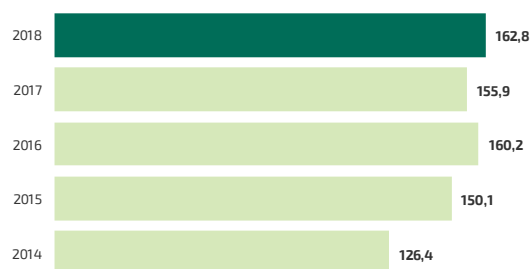
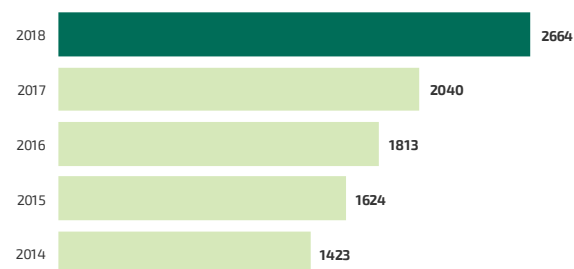
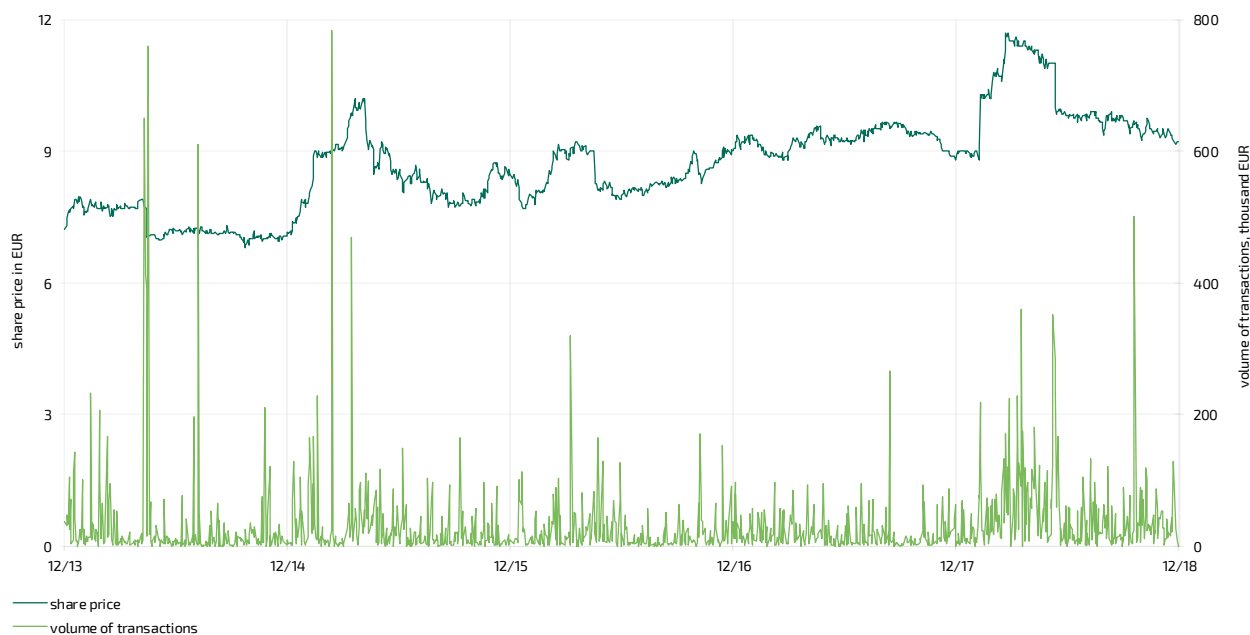


P/E RATIO
times



P/B RATIO
times



MARKET VALUE
in million euros

NUMBER OF SHAREHOLDERS AT YEAR-END
pcs

CHANGE IN THE PRICE AND VOLUME OF AS MERKO EHITUS SHARE AT NASDAQ TALLINN STOCK EXCHANGE

TRADING HISTORY OF SECURITY, IN EUROS

	2018	2017	2016
Highest	11.80	9.69	9.22
Lowest	8.70	8.75	7.60
Average	10.02	9.27	8.44
Closing at 31.12	9.2	8.81	9.05
Change at 31.12, %	+4.43	(2.65)	+6.72
Traded shares, pcs	1,178,232	508,339	633,185
Turnover, million EUR	12.16	4.69	5.35
Market value at 31.12, million EUR	162.8	155.9	160.2

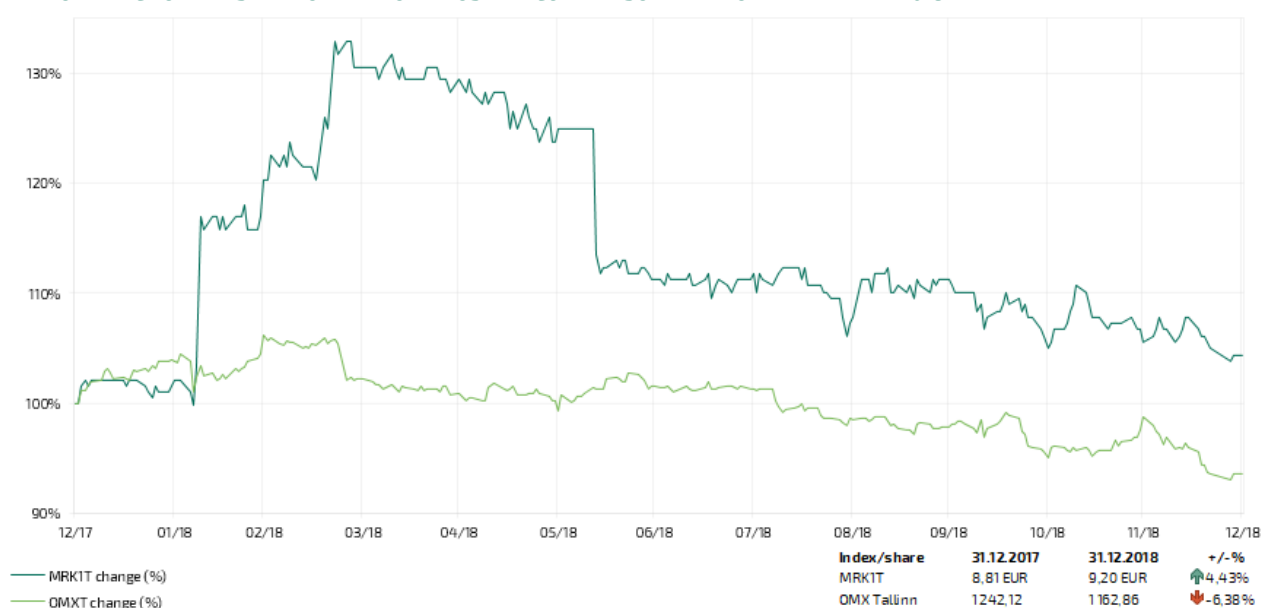
STRUCTURE OF SHAREHOLDERS ACCORDING TO NUMBER OF SHARES AS AT 31.12.2018

NUMBER OF SHARES	NUMBER OF SHAREHOLDERS	% OF SHAREHOLDERS	NUMBER OF SHARES	% OF SHARES
1 000 001 - ...	1	0.04%	12,742,686	71.99%
100 001 - 1 000 000	11	0.41%	2,474,700	13.98%
10 001 - 100 000	34	1.28%	881,041	4.98%
1001-10 000	373	14.00%	1,041,875	5.89%
101-1000	1,300	48.80%	508,960	2.87%
1-100	945	35.47%	50,738	0.29%
Total	2,664	100%	17,700,000	100%

STRUCTURE OF SHAREHOLDERS ACCORDING TO HOLDER CATEGORIES AS AT 31.12.2018

CATEGORY	NUMBER OF SHAREHOLDERS	% OF SHAREHOLDERS	NUMBER OF SHARES	% OF SHARES
Foreign controlled non-financial corporations	1	0.04%	500	0.00%
Insurance corporation	1	0.04%	142,887	0.81%
Non-profit institutions serving households	1	0.04%	100	0.00%
Pension funds	1	0.04%	7,883	0.04%
Public non-financial corporations	1	0.04%	8,000	0.05%
Non-MMF investment funds	3	0.11%	716,844	4.05%
Financial auxiliaries	7	0.26%	60,055	0.34%
Captive financial institutions and money lenders	15	0.56%	291,718	1.65%
Other financial intermediaries	22	0.82%	229,593	1.29%
Deposit-taking corporations except the central bank	23	0.86%	1,686,404	9.53%
National private non-financial corporations	269	10.10%	13,168,599	74.40%
Household	2,320	87.09%	1,387,417	7.84%
Total	2,664	100%	17,700,000	100%

PERFORMANCE OF THE SHARE OF MERKO EHITUS AND COMPARISON INDEX OMX TALLINN IN 2018



SHAREHOLDERS OF AS MERKO EHITUS AS AT 31.12.2018 AND CHANGE COMPARED TO THE PREVIOUS YEAR

	NUMBER OF SHARES	% OF TOTAL 31.12.2018	% OF TOTAL 31.12.2017	CHANGE
AS Riverito	12,742,686	71.99%	71.99%	-
ING Luxembourg S.A. AIF Account	670,695	3.79%	5.50%	(303,431)
Firebird Republics Fund Ltd	363,094	2.05%	2.05%	-
Firebird Avrora Fund Ltd	222,419	1.26%	1.25%	1,900
OÜ Midas Invest	210,680	1.19%	0.92%	47,655
SEB S.A. UCITS client assets	206,562	1.16%	1.31%	(25,660)
Skandinaviska Enskilda Banken AB, Swedish customers	159,559	0.90%	1.19%	(51,701)
State Street Bank and Trust Omnibus Account a Fund No OM01	153,018	0.87%	0.86%	-
SEB Elu- ja Pensionikindlustus AS	142,887	0.81%	0.81%	(1,000)
Firebird Fund L.P.	131,331	0.74%	0.74%	-
Total largest shareholders	15,002,931	84.76%	86.64%	(332,237)
Total other shareholders	2,697,069	15.24%	13.36%	332,237
Total	17,700,000	100%	100%	-

DIVIDENDS AND DIVIDEND POLICY

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.

According to AS Merko Ehitus long-term financial objectives, 50-70% of the annual profit are distributed to shareholders as dividends.

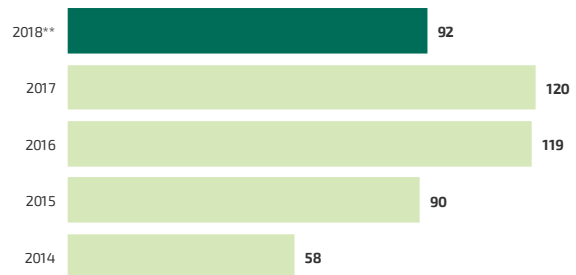
The annual general meeting of shareholders of AS Merko Ehitus held at 9 May 2018 approved the Supervisory Board's proposal to pay the shareholders the total amount of EUR 17.7 million (EUR 1.00 per share) as dividends from net profit brought forward, which is equivalent to a 120% dividend rate and a 11.4% dividend yield for the year 2017 (using the share price as at 31 December 2017). Comparable figures in 2017 were accordingly: EUR 7.3 million (EUR 0.41 per share) as dividends, which is equivalent to a 119% dividend rate and a 4.5% dividend yield for the year 2016 (using the share price as at 31 December 2016).

According to the Estonian Income Tax Law subsection 50 (1¹), AS Merko Ehitus can pay dividends, without any additional income tax expense and liabilities occurring, up to the amount it has received dividends from subsidiaries, which are resident companies of a Contracting State of the European Economic Area (EEA) Agreement subject to that state's income tax legislation. Taking into account the dividends already paid to the parent company by such foreign subsidiaries, the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018 (Q2 2017: EUR 0.9 million). The dividend payment to the shareholders took place on 15 June 2018.

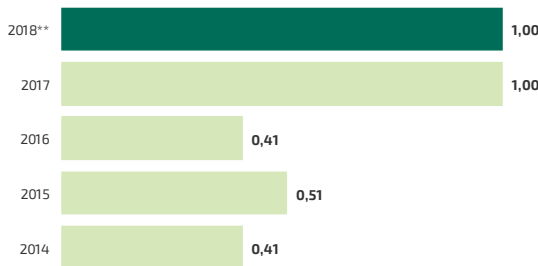
The Management Board proposes to pay the shareholders EUR 17.7 million as dividends from net profits brought forward (EUR 1.00 per share) in 2019, which is equivalent to a 92% dividend rate and a 10.9% dividend yield for the year 2018 (using the share price as at 31 December 2018). As the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018, the 20/80 regular rate of income tax is applied to dividends to be paid in 2019 and no additional income tax is withheld from dividends paid to shareholders that are resident natural persons.

In the past five years, the shareholders have received dividends from the net profit for the accounting year as follows:

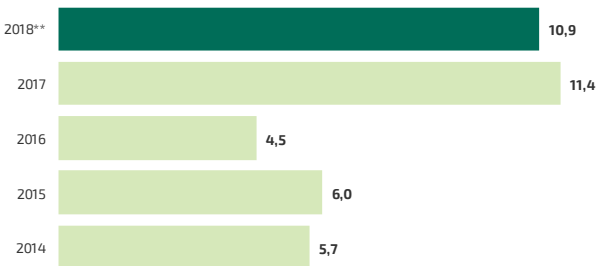
DIVIDEND RATE
percentages



DIVIDEND PER SHARE
euro



DIVIDEND YIELD*
percentages



* Using share price as at 31.12

** 2018 figures based on Management Board proposal regarding dividend payment.

Dividend payments are carried out in the next fiscal year in accordance with the decisions of the general meeting of the shareholders, regarding the previous fiscal year.

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 Nasdaq 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 2018.

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 to 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, Lithuania and Norway 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. The holding company AS Merko Ehitus has a two-member Management Board: Andres Trink and Tõnu Toomik.

It is important to maintain a simple organisational structure in the group, and in management to be guided primarily by the group's objectives and requirements. For the purposes of maximum efficiency in group management, we in some cases differentiate the management structure and legal structure. The group's management is carried out on a country basis. The group's country and business area detailed management structure as at 31 December 2018 is the following:



As at 31 December 2018, the group comprises of 31 companies (31.12.2017: 45). The group's legal structure is predominantly based on tax efficiency and there is not in all cases a direct linear relationship with the group's effective management structure. The detailed list of group companies is provided in Notes 19 and 20 of the financial statements.

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 general meeting of shareholders decides, among others, the appointment and recall of members of the Supervisory Board, appointment of the auditor, approval of the results of the financial year and the payment of dividends. The annual general meeting of shareholders is held at least once a year and shall approve the annual report within six months of the end of the financial year.

The general meeting of shareholders was held on 9 May 2018. The general meeting resolved to approve the annual report and the profit allocation proposal for 2017. The dividends in the sum of EUR 17.7 million (EUR 1 per share) were paid out to the shareholders on 15 June 2018.

In addition, the general meeting of shareholders decided to appoint the audit firm AS PricewaterhouseCoopers the auditor of AS Merko Ehitus for the financial years of 2018 through 2020 and to pay to the audit firm for auditing as per contract to be entered into with AS PricewaterhouseCoopers.

The Management Board made a presentation on the group's financial results and future prospects.

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 Nasdaq Tallinn Stock Exchange and by publishing a meeting call in one national daily newspaper and on its website 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 electronic means of communication equipment since the deployment of reliable solutions for the identification of shareholders, some of whom live abroad, while ensuring the privacy of participating shareholders, 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.

Annual and extraordinary general meeting of shareholders shall be chaired by an independent person. In 2018, 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 group'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 2018 was attended by Andres Trink (Chairman of the Management Board), Tõnu Toomik (Member of the Management Board), Priit Roosimägi (Head of Group Finance Unit) and Ago Vilu (Auditor).

SUPERVISORY BOARD

The Supervisory Board shall plan the activities of the group, organise the management of the group and supervise the activities of the Management Board. The Supervisory Board shall notify the general meeting of shareholders of the results of a review. The Chairman of the Supervisory Board organises the work of the Supervisory Board. The main duties of the Supervisory Board are to approve the group's material strategic and tactical decisions and to supervise the activities of the group's Management Board. The Supervisory Board's actions are guided by the company's articles of association, guidelines of the general meeting and law.

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.

As at 31 December 2018, the Supervisory Board of AS Merko Ehitus had three members. At the annual general meeting of shareholders held at 28 April 2017 the Supervisory Board members' terms of office were approved until 28 April 2020.

Toomas Annus

Chairman of the Supervisory Board

Positions held:

2011-... AS Merko Ehitus, Chairman of the Supervisory Board
 2014-... AS Kapitel, Chairman of the Supervisory Board
 2009-2014 AS Kapitel, Member of the Management Board
 2008-... Järvevana OÜ, Member of the Management Board
 1999-2009 AS Kapitel, Chairman of the Supervisory Board
 1997-2008 AS Merko Ehitus, Chairman of the Supervisory Board
 1996-... AS Riverito, Chairman of the Management Board
 1991-1996 AS EKE Merko, Chairman of the Management Board
 1989-1991 EKE MRK, director of the company

Education:

Tallinn University of Technology, industrial and civil engineering
 Tallinn Technical School of Building and Mechanics, industrial and civil engineering

Number of shares: 8,322,914 (AS Riverito)

Teet Roopalu

Member of the Supervisory Board

Positions held:

2004-... AS Merko Ehitus, Member of the Supervisory Board
 2010-... AS Riverito, Member of the Management Board
 2003-... AS Kapital, Member of the Supervisory Board
 2015-... Järvevana OÜ, Member of the Management Board
 2002-2004 AS Merko Ehitus, Adviser to the Management Board

Has worked for different construction companies, including as a director of finance. Has been in charge of economic activities in the EKE system as a chief economist; worked as a bank director; and has also worked in building design.

Member of Supervisory Boards of group subsidiaries.

Education:

Tallinn University of Technology, construction economics and organisation

Number of shares: -

Indrek Neivelt

Member of the Supervisory Board

Positions held:

2008-... AS Merko Ehitus, Member of the Supervisory Board
 2018-... AS Pocopay, Member of the Supervisory Board
 2015-2018 AS Pocopay, Member of the Management Board
 2016-... OÜ Poco Holding, Member of the Management Board

Has held various executive positions in Hansapank (now Swedbank), incl. Director General of the Group, Chairman of the Management Board and also in Bank Saint Petersburg as the Chairman of the Supervisory Board.

Belongs to Supervisory Boards of various companies.

Education:

Tallinn University of Technology, civil engineering economics and management

Stockholm University, banking and finance, MBA

Number of shares: 31,635 (Trust IN OÜ)

The meetings of the Supervisory Board generally take place once a month, except in summer months. In 2018, 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	15	100%
Teet Roopalu	14	93%
Indrek Neivelt	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 the 2018 and 2017 financial years, the members of the Supervisory Board were remunerated as follows (in euros):

NAME	2018	2017
Toomas Annus	35,152	42,182
Teet Roopalu	38,347	38,347
Indrek Neivelt	38,347	38,347
Olari Taal (until 30.04.2017)	-	12,782
TOTAL	111,846	131,658

Remuneration, less the statutory taxes, to the members of the Supervisory Board is paid on a monthly basis. As from 1 November 2018, the Chairman of the Supervisory Board has forwent the member's fee at his own request.

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 ensuring the group's sustainable development in accordance with set objectives and strategy. To ensure that the group'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 group's business operations, the fulfilment of the group'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. AS Merko Ehitus has a two-member Management Board: Andres Trink (Chairman of the Management Board) and Tõnu Toomik (Member of the Management Board).

Andres Trink

Chairman of the Management Board

Appointed: 1 January 2012

Term ends: 1 January 2021

Positions held:

2012-... AS Merko Ehitus, Chairman of the Management Board;
Chairman of the Supervisory Board of Merko Ehitus Eesti AS,
SIA Merks and UAB Merko Statyba

2016-... Swedbank Investeerimisfondid AS, Member of the
Supervisory Board

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 Hansapank (now Swedbank).

Education:

Tallinn University of Technology, automated management systems specialty (summa cum laude)
Estonian Business School, international business administration
Graduate of the INSEAD University (France), executive management programme

Number of shares: 600

Tõnu Toomik

Member of the Management Board

Appointed: 6 June 2013

Term ends: 6 June 2019

Positions held:

2013-... AS Merko Ehitus, Member of the Management Board

2014-... AS Kapitel, Member of the Supervisory Board

2011-2013 AS Merko Ehitus, Member of the Supervisory Board

2009-2014 AS Kapitel, Chairman of the Supervisory Board

2008-2011 AS Merko Ehitus, Chairman of the Supervisory Board

1999-2009 AS Kapitel, Member of the Supervisory Board

1997-1999 AS Kapitel, Chairman of the Supervisory Board

1997-2008 AS Merko Ehitus, Chairman of the Management Board

1996-... AS Riverito, Member of the Management Board

1993-1996 AS EKE Merko, Estonian Regional Director

1993-1993 AS EKE Merko, Project Manager

Member of the Supervisory Board of Merko Ehitus Eesti AS, SIA Merks and UAB Merko Statyba

Education:

Tallinn University of Technology, industrial and civil engineering

Number of shares: 1,607,185 (AS Riverito)

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 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, being responsible for business development and finance. Tõnu Toomik is responsible for the management of the portfolio of properties and coordination of construction segment development activities across the whole group.

Members of the Management Board have entered into 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 members depend on the financial state of the group and the fulfilment of strategic goals by the board member during the given financial year. The Supervisory Board takes into account the general economic environment as well as the present state and developments of the construction and real estate development markets when assessing the group's financial state.

In the 2018 and 2017 financial years, the Management Board members' remuneration incl. service fees and bonuses, accrued for the reporting year were as follows (in euros):

NAME	2018	2017
Andres Trink	305,633	254,257
Tõnu Toomik	267,842	237,698
TOTAL	573,475	491,955

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 and 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 as at 31 December 2018:

COMPANY *	SUPERVISORY BOARD	MANAGEMENT BOARD
AS Merko Ehitus Eesti (60,516,475 euros)	Andres Trink (Chairman), Teet Roopalu, Tõnu Toomik	Keit Paal (Chairman), Jaan Mäe, Alar Lagus, Veljo Viitmann
Tallinna Teede AS (17,819,768 euros)	Tõnu Toomik (Chairman), Keit Paal, Alar Lagus, Veljo Viitmann	Jüri Läll (Chairman), Jüri Helila
OÜ Merko Investments (21,580,029 euros)	-	Andres Trink, Priit Roosimägi
SIA Merks (22,626,236 euros)	Andres Trink (Chairman), Tõnu Toomik, Priit Roosimägi, Janis Šperbergs	Oskars Ozoliņš (Chairman), Andris Bišmeistars
SIA Merko Investments (814,934 euros)	-	Andres Trink (Chairman), Oskars Ozoliņš
UAB Merko Statyba (4,965,013 euros)	Andres Trink (Chairman), Tõnu Toomik, Priit Roosimägi	Saulius Putrimas (Chairman), Jaanus Rāstas

* The figures in brackets indicate the amount of equity held by the parent company's owners in significant subsidiaries as at 31 December 2018.

Changes in the management of group subsidiaries

On 8 January 2018, the Management Board of AS Merko Ehitus decided to extend the powers of the Members of the Supervisory Board of AS Merko Ehitus Eesti, Mr. Andres Trink, Mr. Tõnu Toomik and Mr. Teet Roopalu for three years, i.e. till 31 December 2020. The Supervisory Board of AS Merko Ehitus Eesti will continue in a former three-member panel: Mr. Andres Trink (The Chairman), Mr. Tõnu Toomik and Mr. Teet Roopalu.

On 18 April 2018, the Management Board of AS Merko Ehitus Eesti, part of AS Merko Ehitus group, decided to extend the powers of the Members of the Supervisory Board of AS Tallinna Teede, Mr. Veljo Viitmann and Mr. Alar Lagus for three years, i.e. till 18 April 2021. The Supervisory Board of AS Tallinna Teede will continue in a former four-member panel: Mr. Tõnu Toomik (The Chairman), Mr. Keit Paal, Mr. Veljo Viitmann and Mr. Alar Lagus.

On 1 November 2018, the general meeting of shareholders of SIA Merks, part of AS Merko Ehitus group, decided to extend the powers of the Member of the Management Board, Mr. Oskars Ozoliņš, until 1 February 2022 and to nominate Mr. Andris Bišmeistars as a new Member of the Management Board, starting from 1 November 2018 with the powers also until 1 February 2022. The Management Board of SIA Merks will continue with two members: Mr. Oskars Ozoliņš (The Chairman) and Mr. Andris Bišmeistars. The general meeting of shareholders also decided to dismiss Mr. Janis Šperbergs from the duties of the Member of the Management Board as of 1 November 2018 and to appoint him as a Member of the Supervisory Board, effective as of the same date. The Supervisory Board of SIA Merks will continue with four members: Mr. Andres Trink (Chairman), Mr. Tõnu Toomik, Mr. Priit Roosimägi and Mr. Janis Šperbergs.

On 3 December 2018, the Supervisory Board of Tallinna Teede AS, part of AS Merko Ehitus group, decided to extend the powers of a Member of the Management Board of the company, Mr. Jüri Helila, for two years, i.e. until 30 January 2021. The Management Board of Tallinna Teede AS will continue with two members: Mr. Jüri Läll (The Chairman) and Mr. Jüri Helila.

The fees to the members of the management board of the major subsidiaries is provided in Note 33 of the financial statements.

AUDIT COMMITTEE

The Supervisory Board of AS Merko Ehitus has formed an audit committee as its work body. The responsibility of the audit committee is advising the Supervisory Board in supervision related issues. The Committee executes supervision over the whole group (incl. subsidiaries): 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. Subsidiaries have not formed audit committees.

As at 10 January 2011, the company's Supervisory Board set up a 3-member audit committee. From November 1, 2017, the Supervisory Board of AS Merko Ehitus members are: Teet Roopalu (the Chairman), Indrek Neivelt and Viktor Mõisja.

A member of the committee is elected for a term of indefinite period, but at the decision of the Supervisory Board, a member of the committee may be recalled at any given time.

Members of the audit committee are not separately remunerated.

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 group'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 Baltic and that are available to all shareholders, potential investors and analysts covering the company.

On the other hand, management reporting is meant for the group'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. The refinement of reporting is a continuous process during which indicators affecting the achievement of agreed objectives are reviewed. 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 2018, the financial auditor for annual reports of 2018–2020 is AS PricewaterhouseCoopers (PwC). Auditors authorised to sign the report differ, depending on the country of residence of the group company. 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 conflicts of interest. In 2018, PwC provided to AS Merko Ehitus tax and other advisory services permitted under Estonian Audit Act. We find that the financial audit conducted in 2018 was in compliance with regulative acts, international standards and expectations. PwC presented the results in two stages: a) as part of an interim audit and b) with regard to the final audit before the independent auditor's report was issued. The auditor's report is presented on pages 109–115.

CONFLICT OF INTEREST AND HANDLING OF INSIDER INFORMATION

It is important to appropriately handle insider information in order to protect shareholders' interests 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 group'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.

As at 31 December 2018, the group's insider register lists 74 persons with permanent access (31.12.2017: 69 persons). The group keeps records on insiders in accordance with requirements set forth in the Securities Market Act and Nasdaq Tallinn rules and regulations.

To the best of our knowledge, in the financial year 2018 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.

OWNERSHIP INTERESTS OF AS MERKO EHITUS MEMBERS OF THE SUPERVISORY AND MANAGEMENT BOARD (OVER 5%) IN OTHER COMPANIES

NAME	RELATED COMPANY
Toomas Annus	AS Riverito, Kardispordi Arendamise OÜ, Kemental Grupp OÜ, OÜ Unisport Narva
Teet Roopalu	Teet Konsult OÜ
Indrek Neivelt	Trust IN OÜ
Andres Trink	None
Tõnu Toomik	AS Riverito, Loode Kalur OÜ

No members of the company's supervisory or management board hold shares in an entity that operates in the core business area of AS Merko Ehitus – construction sector.

An overview of transactions with related parties in 2018 is provided in Note 33 of the financial statements.

DISCLOSURE OF INFORMATION

In disclosing information, AS Merko Ehitus shall follow Estonian law, the rules and regulations of Nasdaq Tallinn Stock Exchange and guidelines of the Financial Supervision Authority of Estonia and immediately disclose important information regarding the group'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 group and its business partners.

The main principles of communication with investors and the general public are stated in the group's disclosure policy, which is available on the website: <https://group.merko.ee/en/investors/stock-exchange-news/disclosure-policy/>

The group discloses information about its financial condition and strategy in its financial statements, annual report and interim reports pursuant to the schedule that has been set. The disclosure dates of each next financial year will be announced before the end of the previous financial year.

Merko immediately discloses all decisions, issues and events that in the group's view may significantly change the price of the securities issued by the company and that are to be disclosed pursuant to laws and regulations. Stock exchange releases are published in Estonian and English.

Stock exchange releases are always published regarding the following subjects:

- financial statements, interim reports;
- amendments to previously published strategies and financial objectives;
- profit warnings;
- major projects and construction contracts;
- major investments and financial arrangements;
- significant corporate reorganisations and partnership agreements;
- significant reorganisation, streamlining or discontinuation of functions or operations;
- management board's proposals to the annual general meeting and resolutions adopted in the annual meeting;
- significant legal actions, legal proceedings or actions of the authorities.

Important information shall be disclosed through the stock exchange system and on the group's website. In 2018, AS Merko Ehitus published 44 stock exchange releases through the stock exchange system.

NUMBER OF RELEASES	CONTENT OF RELEASE
18	New construction contracts
11	New development projects
5	Operating results
3	Changes in structure and management
2	General meeting
5	Other releases

We will publish 2019 consolidated interim reports as follows:

DATE	EVENT
09.05.2019	2019 3 months and I quarter unaudited interim report
08.08.2019	2019 6 months and II quarter unaudited interim report
07.11.2019	2019 9 months and III quarter unaudited interim report

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.

The investor calendar published on the AS Merko Ehitus website <http://group.merko.ee/en/investors/investor-calendar/> provides an overview of investor meetings both past and upcoming. Current shareholders can request their participation in planned meetings shown on the investor calendar. Requests should be made in a timely fashion. In addition to the investor meeting date, time and names of participants, Merko's website has a section with the presentations used at the meetings. In 2018, AS Merko Ehitus organised 9 investor meetings (2017: 12), including 1 investor tour (2017: 1).

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	AS LHV PANK
Liivalaia 8, 15040 Tallinn, Estonia	Tartu mnt 2, 10145 Tallinn, Estonia
phone +372 631 0310	phone +372 680 0457
e-mail info@swedbank.ee	e-mail research@lhv.ee
www.swedbank.ee	www.lhv.ee

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

ANDRES TRINK	PRIIT ROOSIMÄGI	AS MERKO EHITUS
Chairman of the Management Board	Head of Group Finance Unit	Delta Plaza, 7th Floor
phone +372 650 1250	phone +372 650 1250	Pärnu mnt 141, 11314 Tallinn, Estonia
fax +372 650 1251	fax +372 650 1251	phone +372 650 1250
e-mail andres.trink@merko.ee	e-mail priit.roosimagi@merko.ee	group.merko.ee

DECLARATION OF CONFORMITY TO RECOMMENDATIONS OF GOOD CORPORATE GOVERNANCE CODE

The Corporate Governance Code (CGC) is based on the principle of follow or explain, according to which a publicly traded company 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 Corporate 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 Corporate Governance Code. Also, our activities comply with the Estonian legislation that regulates several principles provided in the code in more detail. We hereby declare that AS Merko Ehitus has followed all the recommendations of CGC, with the following exceptions:

CORPORATE GOVERNANCE RECOMMENDATIONS**EXPLANATIONS BY MANAGEMENT AND SUPERVISORY BOARDS**

1.3.2 Members of the Management Board, the Chairman of the Supervisory Board and if possible also the members of the Supervisory Board and at least 1 of the auditors attend the general meeting.	The Chairman of the Supervisory Board did not attend the annual general meeting held in 2018 as he was not in Estonia at the time.
1.3.3 In the existence of such technical means and in case it is not overly costly for the Issuer, the Issuer makes it possible to observe and attend the general meeting through means of communication (e.g. the Internet).	AS Merko Ehitus does not provide the possibility to observe and attend the general meeting through means of communication as such need has not been identified so far.
2.2.7 Basic wages, performance pay, severance packages, other benefits payable 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 the 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.	AS Merko Ehitus publishes in its annual report the total amount of remuneration and bonuses paid to member of the Management Board, as it believes that public disclosure of individual income items does not create value added for shareholders, but does violate the privacy of members of the Management Board.
5.2 The Issuer discloses the dates on which the information to be disclosed (incl. annual report, interim reports, notice calling general meeting) are going to be disclosed during the year in the beginning of the financial year in a separate announcement, so-called financial calendar.	AS Merko Ehitus disclosed the financial calendar for 2019 on 12 December 2018. It did not include the date on which the notice calling general meeting is going to be disclosed, as this will become known as the result of decisions by the Management Board and the Supervisory Board later during the year.
6.1.1 Also the Issuer's auditor attends the Supervisory Board meeting where the annual report is reviewed, at the invitation by the Supervisory Board.	The auditor does not usually attend the AS Merko Ehitus Supervisory Board meeting. Auditor presents an overview about the results of the carried out audit as a written report to the audit committee, which has been formed by the Supervisory Board as its work body. In case the members of the audit committee find it necessary to receive additional explanations, they may turn to the auditor using means of communication or invite the auditor to the audit committee meeting to provide explanations.

MANAGEMENT DECLARATION

The Management Board declares and confirms that according to their best knowledge, the year 2018 annual accounts, prepared in accordance with International Financial Reporting Standards as adopted by the European Union, present a correct and fair view of the assets, liabilities, financial position and profit or loss 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



29.03.2019

Tõnu Toomik

Member of the Management Board



29.03.2019

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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

in thousands of euros

	Note	2018	2017
Revenue	4	418,011	317,598
Cost of goods sold	5	(384,962)	(286,747)
Gross profit		33,049	30,851
Marketing expenses	6	(3,285)	(3,215)
General and administrative expenses	7	(12,304)	(11,289)
Other operating income	8	3,527	3,793
Other operating expenses	9	(1,115)	(601)
Operating profit		19,872	19,539
Finance income	10	8	4
Finance costs	11	(696)	(849)
Profit (loss) from sale and liquidation of subsidiary	19	(62)	14
Profit (loss) from joint ventures	20	653	64
Profit before tax		19,775	18,772
Corporate income tax expense	12	(375)	(3,020)
Net profit for financial year		19,400	15,752
incl. net profit attributable to equity holders of the parent		19,343	14,694
net profit attributable to non-controlling interest		57	1,058
Other comprehensive income (loss), which can subsequently be classified in the income statement			
Currency translation differences of foreign entities		(6)	(74)
Comprehensive income for the period		19,394	15,678
incl. attributable to equity holders of the parent		19,324	14,637
attributable to non-controlling interest		70	1,041
Earnings per share for profit attributable to equity holders of the parent (basic and diluted, in EUR)	13	1.09	0.83

The notes set out on pages 61-107 are an integral part of these consolidated financial statements.

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CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	Note	31.12.2018	31.12.2017
ASSETS			
Current assets			
Cash and cash equivalents	15	39,978	39,210
Trade and other receivables	16	76,183	75,844
Prepaid corporate income tax		224	492
Inventories	18	117,992	118,421
		234,377	233,967
Non-current assets			
Investments in joint ventures	20	732	79
Other long-term loans and receivables	21	10,391	17,163
Deferred income tax assets	22	-	5
Investment property	23	13,771	15,719
Property, plant and equipment	24	9,715	9,665
Intangible assets	25	671	497
		35,280	43,128
TOTAL ASSETS		269,657	277,095
LIABILITIES			
Current liabilities			
Borrowings	27	19,900	24,218
Payables and prepayments	28	77,016	74,972
Income tax liability		381	413
Short-term provisions	29	8,100	4,569
		105,397	104,172
Non-current liabilities			
Long-term borrowings	27	24,266	35,138
Deferred income tax liability	22	1,481	1,259
Other long-term payables	30	2,179	1,789
		27,926	38,186
TOTAL LIABILITIES		133,323	142,358
EQUITY			
Non-controlling interests	19	4,577	4,567
Equity attributable to equity holders of the parent			
Share capital	32	7,929	7,929
Statutory reserve capital		793	793
Currency translation differences		(721)	(702)
Retained earnings		123,756	122,150
		131,757	130,170
TOTAL EQUITY		136,334	134,737
TOTAL LIABILITIES AND EQUITY		269,657	277,095

The notes set out on pages 61-107 are an integral part of these consolidated financial statements.

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

in thousands of euros

	Equity attributable to equity holders of the parent				Total	Non-controlling interest	Total
	Share capital	Statutory reserve capital	Currency translation differences	Retained earnings			
Balance as at 31.12.2016	7,929	793	(645)	114,713	122,790	3,692	126,482
Profit (loss) for the financial year	-	-	-	14,694	14,694	1,058	15,752
Other comprehensive income (loss)	-	-	(57)	-	(57)	(17)	(74)
Total comprehensive income (loss) for the financial year	-	-	(57)	14,694	14,637	1,041	15,678
Transactions with owners							
Non-controlling interest of sold subsidiary	-	-	-	-	-	123	123
Option over shares relating to non-controlling interests	-	-	-	-	-	(182)	(182)
Dividends (Note 14)	-	-	-	(7,257)	(7,257)	(107)	(7,364)
Total transactions with owners	-	-	-	(7,257)	(7,257)	(166)	(7,423)
Balance as at 31.12.2017	7,929	793	(702)	122,150	130,170	4,567	134,737
Balance as at 31.12.2017	7,929	793	(702)	122,150	130,170	4,567	134,737
Profit (loss) for the financial year	-	-	-	19,343	19,343	58	19,401
Other comprehensive income (loss)	-	-	(19)	-	(19)	13	(6)
Total comprehensive income (loss) for the financial year	-	-	(19)	19,343	19,324	71	19,395
Transactions with owners							
Non-controlling interest of purchased subsidiary	-	-	-	(37)	(37)	36	(1)
Option over shares relating to non-controlling interests	-	-	-	-	-	19	19
Dividends (Note 14)	-	-	-	(17,700)	(17,700)	(116)	(17,816)
Total transactions with owners	-	-	-	(17,737)	(17,737)	(61)	(17,798)
Balance as at 31.12.2018	7,929	793	(721)	123,756	131,757	4,577	136,334

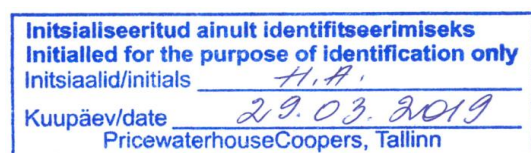
The notes set out on pages 61-107 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

in thousands of euros

	Note	2018	2017
Cash flows from (used in) operating activities			
Operating profit		19,872	19,539
Adjustments:			
Depreciation and impairment	23-25	2,073	2,675
(Profit)/loss from sale of non-current assets	8	(473)	(571)
(Profit)/loss from sale of a business unit		-	(474)
Change in receivables and liabilities related to construction contracts	4	11,153	(8,488)
Interest income from operating activities	8	(2,351)	(1,979)
Change in provisions	29	4,732	572
Change in trade and other receivables related to operating activities		(1,256)	(19,301)
Change in inventories	18	571	(4,851)
Change in trade and other payables related to operating activities		(1,759)	12,058
Interest received	8, 10, 16, 21	2,450	1,709
Interest paid	11, 28	(799)	(879)
Other finance income (costs)	11	(44)	(28)
Corporate income tax paid		(383)	(1,284)
Total cash flows from (used in) operating activities		33,786	(1,302)
Cash flows from investing activities			
Acquisition of subsidiaries		-	328
Disposal of subsidiary	19	385	(7)
Liquidation of subsidiary		(3)	-
Purchase of investment properties	23	(92)	(6)
Purchase of property, plant and equipment	24, 27	(712)	(1,186)
Proceeds from sale of property, plant and equipment	8, 24	664	1,924
Purchase of intangible assets	25	(281)	(181)
Sale of a business unit		-	113
Interest received	10, 16	3	6
Total cash flows from investing activities		(36)	991
Cash flows from (used in) financing activities			
Proceeds from borrowings	27	30,139	61,651
Repayments of borrowings	27	(44,670)	(47,380)
Finance lease principal payments	27	(605)	(818)
Contributions to the subsidiary's share capital from non-controlling shareholder	19	(1)	-
Dividends paid	14	(17,816)	(7,364)
Total cash flows from (used in) financing activities		(32,953)	6,089
Net increase/decrease in cash and cash equivalents		797	5,778
Cash and cash equivalents at the beginning of the period	15	39,210	33,544
Effect of exchange rate changes		(29)	(112)
Total at the end of the period	15	39,978	39,210

The notes set out on pages 61-107 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 collectively the group) for the financial year ended 31 December 2018 were signed by the Management Board on 29 March 2019.

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, Lithuania and Norway. Its main activities are construction and real estate development.

From 22 July 1997, the shares of AS Merko Ehitus are listed on Nasdaq Tallinn Stock Exchange. As at 31 December 2018, the majority shareholder AS Riverito owned 71.99% of the Company's shares through which the ultimate controlling person is Toomas Annus.

Since 1 January 2012, AS Merko Ehitus operates as a holding entity with no independent production activities, and which owns 100% ownership interests in construction entities in Estonia, Latvia and Lithuania and a majority holding in a construction entity in Norway.

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, 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 turn out to be inaccurate. 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 the statement of financial position. Current assets include assets that are expected to be realized in the course of group's ordinary operating cycle. 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 and the Norwegian krone. 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)

ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

The following new or revised standards or interpretations which became effective for the group from the financial year starting 1 January 2018:

NEW ACCOUNTING STANDARDS, INTERPRETATIONS AND CHANGES

Certain new or revised standards and interpretations have been issued that are mandatory for the group's annual periods beginning on or after 1 January 2018, and which the group has not early adopted:

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IFRS 9, Financial Instruments: Classification and Measurement. Key features of the new standard are:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity's business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets' cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets, but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.

IFRS 15, Revenue from Contracts with Customers. The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed.

Amendments to IFRS 15, Revenue from Contracts with Customers

The amendments do not change the underlying principles of the standard but clarify how those principles should be applied. The amendments clarify how to identify a performance obligation (the promise to transfer a good or a service to a customer) in a contract; how to determine whether a company is a principal (the provider of a good or service) or an agent (responsible for arranging for the good or service to be provided); and how to determine whether the revenue from granting a licence should be recognised at a point in time or over time. In addition to the clarifications, the amendments include two additional reliefs to reduce cost and complexity for a company when it first applies the new standard.

The implementation of IFRS 15 and IFRS 9 did not have a material impact on the group's financial statements as of 1 January 2018. See also a more detailed analysis in Note 2.

There are no other new or revised standards or interpretations that are effective for the first time for the financial year beginning on or after 1 January 2018 that would be expected to have a material impact to the group.

NEW ACCOUNTING STANDARDS, INTERPRETATIONS AND CHANGES

Certain new or revised standards and interpretations have been issued that are mandatory for the group's annual periods beginning on or after 1 January 2019, and which the group has not early adopted:

IFRS 16, Leases (effective for annual periods beginning on 1 January 2019). The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.

The group implemented the standard from 1 January 2019, applying the modified retrospective approach, as a result of which the impact of the implementation of the standard was recognised as of the date of initial implementation (1 January 2019) and the comparative data from 2018 were not restated.

The group uses simplifications for short-term leases and rent of low value assets. Cancellable vehicle leasing contracts with a term of up to 31 December 2019 are not recognised as assets, as all new vehicle leasing contracts are signed under the financial lease terms and their volume is immaterial (ca EUR 880 thousand).

As a result of implementing the new standard, the assets and liabilities as of 1 January 2019 increase from leasing of other assets in the amount of appr. EUR 1,760 thousand, including machinery and equipment appr. EUR 1,000 thousand and office premises appr. EUR 750 thousand. Leased assets ("right of use assets") are reflected in the statement of financial position in the same line item together with similar owned assets (tangible non-current assets) using acquisition cost less depreciation method. The depreciation period is usually the same as the lease period. The group assesses the impact of the change on retained earnings as immaterial (Note 26).

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Long-term Interests in Associates and Joint Ventures – Amendments to IAS 28 (effective for annual periods beginning on 1 January 2019). The amendments clarify that reporting entities should apply IFRS 9 to long-term loans, preference shares and similar instruments that form part of a net investment in an equity method investee before they can reduce such carrying value by a share of loss of the investee that exceeds the amount of investor's interest in the investee. The group assesses the impact of the amendments on its financial statements immaterial as of the preparation of this report and in the light of existing investments.

Amendments to the Conceptual Framework of Financial Reporting (effective for reporting periods beginning on 1 January 2020 or after; not yet adopted by the EU). The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance - in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting. The group is assessing the impact of these amendments to the financial statement.

Definition of materiality – Amendments to IAS 1 and IAS 8 (effective for annual periods beginning on or after 1 January 2020; not yet adopted by the EU). The amendments clarify the definition of material and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS. In addition, the explanations accompanying the definition have been improved. Finally, the amendments ensure that the definition of material is consistent across all IFRS Standards. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. The group is assessing the impact of these amendments to the financial statement.

There are no other new or revised standards or interpretations that are not yet effective that would be expected to have a material impact on the group.

1.4. CONSOLIDATION

Subsidiaries include all entities under the control of the group. The group controls the entity, if it receives or is entitled to variable profits arising from its role in the entity and the group can influence the amount of profit by exerting influence over the entity.

Subsidiaries are consolidated in the financial statements from the date of acquiring control until the date at which control ceases. The financial figures of the parent company and the subsidiaries have been consolidated on a line-by-line basis in the consolidated annual financial statements. Upon consolidation, intra-group transactions, balances and unrealised profits arising from intra-group transactions have been eliminated. Unrealised losses have also been eliminated, unless a loss is caused by impairment. Group entities use uniform accounting policies.

Investments are recognised in the parent company's unconsolidated financial statements at acquisition cost, less any accumulated impairment losses.

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 1.10).

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.

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TRANSACTIONS WITH NON-CONTROLLING INTERESTS

The group treats transactions with non-controlling interests as transactions with equity owners of the group. 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. 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.

1.7. JOINTLY CONTROLLED OPERATIONS

Under IFRS 11 Joint Arrangements, 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.

In 2018 and 2017, the group had no jointly controlled operations.

1.8. 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 statement 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.

1.9. FINANCIAL ASSETS

Accounting policies from 1 January 2018

The group classifies its financial assets in those to be measured at amortised cost measurement category. The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows.

Purchases and sales of financial assets conducted in normal market conditions are recognised on trade-date – the date on which the group commits to purchase or sell the asset.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the group has transferred substantially all the risks and rewards of ownership.

At initial recognition, the group measures the financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss. Subsequent measurement of debt instruments depends on the group's business model for managing the asset and the cash flow characteristics of the asset.

All group's debt instruments are classified in amortised cost measurement category.

Amortised cost: assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest on the unpaid principal are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other income/expenses. Foreign exchange gains and losses and impairment losses are presented as separate line items in the statement of profit or loss.

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As at 1 January 2018 and 31 December 2018, all the group's financial assets (trade receivables, contractual assets, loans granted, bank deposits, cash and cash equivalents, and other financial assets) were classified in this category.

The group has no investments in equity instruments.

Accounting policies until 31 December 2017

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 group 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 1.10).

1.10. 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;
- the future outlook of the debtor's business, including the future outlook for the particular economic sector and as well the general economic developments;
- probability that the debtor will enter bankruptcy;
- disappearance of an active market for that financial asset because of financial difficulties;
- 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.

The abovementioned accounting principles, which are implemented starting from 1 January 2018 do not substantially differ from those, which were used until 31 December 2017. Therefore, there have been no substantial changes in recognition of financial assets deriving from the accounting principles implemented starting from 1 January 2018.

NON-FINANCIAL ASSETS

Signs, which could give evidence to decrease in the value of assets are assessed critically on each reporting date. If such signs are identified, a recoverable value test is carried out for these assets. Losses deriving from the decrease in the value of assets is

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recognised, if the book value of the asset or the cash generating unit of such asset is above the recoverable value. Losses deriving from the decrease of value of assets is recognised in the expenses of that reporting period.

The recoverable value of group's non-current assets is the higher of the following two figures: the fair value (minus sales costs) of the asset or its value in use. In assessing the value in use of the asset the assumed future cash flows are discounted to their current value, using a discount rate, which reflects both the current market assessment of the change in the time value of money, as well as the specific risks associated with the asset. In case of an asset, which does not generate independent cash flows, the recoverable value is determined for the cash generating unit to which the asset belongs.

In case of non-current assets, prior write-downs are cancelled, if there are indicators, according to which the decrease in the value of the asset has ceased to exist and there have been changes in the assessments, which were the basis for the determination of the recoverable value of the asset. Prior write-down is cancelled only in such amount, which does not increase the post-cancellation value of the asset above the residual value, which would have been reached, taking into account normal depreciation, if the write-down had not been made.

1.11. INVENTORIES

Inventories are initially 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 measured in the statement of financial position at the lower of acquisition 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. Interest expenses associated with maintenance or usage of the property are not capitalised.

A completed real estate property is sold either in units (by houses, apartments, office spaces, etc.) or as a whole. Revenue is recognised as income from the sale of goods (Note 1.20). Upon the sale of real estate properties, the group and the acquirer enter into a notarised agreement for transferring the property, and a respective entry is made in the land register.

1.12. INVESTMENT PROPERTY

Investment property is 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.

1.13. PROPERTY, PLANT AND EQUIPMENT

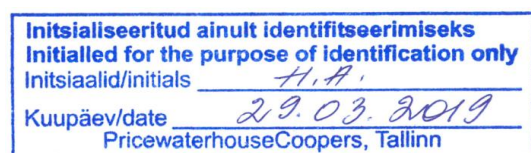
An item of property, plant and equipment is an asset used for production, provision of services or administrative purposes over a period longer than one year.

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 group 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 are 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.

1.14. INTANGIBLE ASSETS

Intangible assets are recognised in the statement of financial position when the asset can be controlled by the group, the expected future benefits attributable to the asset will flow to the group 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).

1.15. FINANCE AND OPERATING LEASES

Leases of property, plant and equipment that 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 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.

1.16. 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 recognised at their fair value and are subsequently carried 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.

1.17. 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. From 1 January 2015, the tax rate on dividends payable is 20/80 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. From 2019, tax rate of 14/86 can be applied to dividend payments. The more beneficial tax rate can be used for dividend payments in the amount of up to the average dividend payment during the three preceding years that were taxed with the tax rate of 20/80. When calculating the average dividend payment of three preceding years, 2018 will be the first year to be taken into account.

Corporate income tax on profits and deferred income tax expense or income of the subsidiaries located in Lithuania and Norway as well as corporate income tax on dividends and deferred income tax cost 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.

CORPORATE INCOME TAX IN LATVIA

In accordance with the tax law effective until 2017, profits of entities in Latvia were taxable with income tax. Therefore, until that, deferred tax was provided for on all temporary differences arising between the tax bases of assets and liabilities of Latvian subsidiaries and their carrying amounts in the consolidated financial statements. In accordance with the new Corporate Income Tax Law, starting from 1 January 2018, corporate income tax with a rate of 20/80 is levied on profits arisen after 2017 only upon their distribution. Transitional provisions of the law allow for reductions in the income tax payable on dividends, if the entity has unused tax losses or certain provisions recognised by 31 December 2017.

Due to the new tax law, there are no longer differences between the tax bases and carrying amounts of assets and liabilities, and hence, deferred income tax assets and liabilities no longer arise in respect of subsidiaries in Latvia. All deferred tax assets and liabilities recognised in previous periods were derecognised in 2017 and related income tax expense/income was recorded in the statement of profit or loss.

Legal entities in Latvia, Lithuania, Finland, Norway and Russia 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, the Republic of Finland, the Kingdom of Norway and the Russian Federation. The profit in the Republic of Latvia are taxed upon their distribution with a rate of 20/80 (2017: the profits of entities 15%). The profits of entities located in the Republic of Lithuania at the rate of 15% (2017: 15%), in the Republic of Finland at the rate of 20% (2017: 20%), in the Kingdom of Norway at the rate of 23% (2017: 24%) and in Russian Federation at the rate of 20% (2017: 20%).

1.18. 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 group 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.

1.19. 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.

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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 must be immediately recognised as an expense. A provision is recognised for onerous construction contracts, which have not yet been completed.

A provision for expenses yet to be incurred and invoices not yet received is formed for sold apartment projects, which is recognised in the income statement as an expense and in the balance sheet as a liability.

1.20. REVENUE

REVENUE FROM CONTRACTS WITH CUSTOMERS

Accounting policies from 1 January 2018

Revenue is income arising in the course of the group's ordinary activities. Revenue is measured in the amount of transaction price. Transaction price is the amount of consideration to which the group expects to be entitled in exchange of transferring control over promised goods or services to a customer, excluding the amounts collected on behalf of third parties. The group recognises revenue when it transfers control of a good or service to a customer.

REVENUE FROM CONTRACTS WITH CUSTOMERS – CONSTRUCTION SERVICES

The group provides construction services under fixed price contracts. Revenue from providing services is recognised in the accounting period in which the services are rendered. For fixed-price contracts, revenue is recognised based on the actual service provided until the end of the reporting period as a proportion of the total services to be provided, because the customer receives and uses the benefits simultaneously. The proportion of services actually provided is recognised based on the ratio of contract's actual costs and contract's estimated total costs, i.e. based on the stage of completion of the project.

If the customer has ordered construction services together with the installation of specific equipment and this is delivered directly from the factory to the customer's project site, the revenue from the sale of the equipment is recognised during the reporting period as part of the construction contract as a joint performance obligation. The customer does not benefit separately from the construction service and the equipment and is interested in purchasing only the full solution.

Estimates of revenue, costs or extent of progress toward completion of the contract are revised, if circumstances change. Any resulting increases or decreases in estimated revenues or costs are reflected in the statement of profit or loss in that period in which the circumstances that gave rise to the revision became known to the management.

In case of fixed-price contracts, the customer pays the fixed amount based on a payment schedule. If the services rendered by the group exceed the payment, a contract asset is recognised (in the annual report as „accrued income from construction services“). If the payments exceed the services rendered, a contract liability is recognised (in the annual report as „prepayments for construction services“).

The contract asset and contract liability arising from the same contract are presented net in the financial statements. If the contract includes variable consideration, revenue is recognised only to the extent that it is highly probable that there will be no significant reversal of such consideration.

CONSTRUCTION OF RESIDENTIAL PROPERTIES

The group develops and sells residential properties. Revenue is recognised when control over the property has been transferred to the customer. The properties have generally no alternative use for the group due to contractual restrictions. However, an enforceable right to payment does not arise until legal title has passed to the customer. Therefore, revenue is recognised at a point in time when the legal title has passed to the customer.

FINANCING COMPONENT

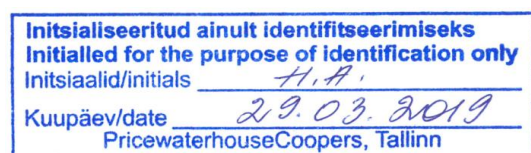
The group does not have any contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. Consequently, the group does not adjust any of the transaction prices for the time value of money.

Income 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.

Accounting policies until 31 December 2017

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

Sale of construction services is recognised as revenue under the stage of completion method 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 that 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 exchanged, adjusted by the amount of any cash or cash equivalents received or paid.

Sale of services is recognised based on the stage of completion of the service at the balance sheet date.

Income 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.

The state of completion is recognised based on the ratio of contract's actual costs incurred until the reporting date and contract's estimated total costs. The actual costs include direct and indirect costs of the construction contract.

If the customer has been presented with invoices for a larger or smaller sum than the recognised revenue as per state of completion method by the reporting date, the difference is recorded in the statement of financial position as an obligation or receivable.

If it is probable that the total costs of the contract exceed the total revenue of the contract, the expected loss is immediately reflected in profit or loss statement.

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

1.22. LOANS GRANTED

Loans granted are recognised in the group based on business principles and the loans are issued to companies with whom contracts are in place for the purpose of co-financing development projects. Real estate developers are granted loans on condition that the group receives an opportunity to provide construction service in the developments being financed. Due to the direct link between the loans and the group's business activity, the said loans and the related interests received are recognised in the cash flow statement under cash flows from operating activities (Note 17).

1.23. CONTINGENT LIABILITIES

Contingent liabilities are those liabilities the realisation of which is less probable than non-realisation or 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 (Note 34).

1.24. STATUTORY RESERVE CAPITAL

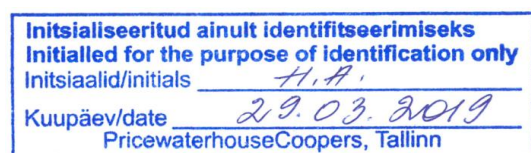
Reserve capital is formed to comply with the requirements of the Commercial Code. During each financial year, at least one-twentieth of the net profit shall be entered in reserve capital, until reserve capital reaches one-tenth of share capital. Reserve capital may be used to cover a loss, or to increase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

1.25. EVENTS AFTER THE BALANCE SHEET DATE

The financial statements of the reporting period include material circumstances affecting the assessment of assets and liabilities that 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.

1.26. 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.



1.27. SEGMENT REPORTING

According to IFRS 8 Operating Segments, segment reporting is applicable to operating segments whose results are regularly reviewed by the group'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.

NOTE 2 CHANGES IN ACCOUNTING POLICIES

This note explains the impact of the adoption of IFRS 9 Financial instruments and IFRS 15 Revenue from contracts with customers on the group's financial statements.

2.1. IFRS 9 FINANCIAL INSTRUMENTS

IFRS 9 replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and financial liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

The adoption of IFRS 9 Financial Instruments from 1 January 2018 resulted in changes in accounting policies, although no adjustments were recognised to the amounts in the financial statements. The new accounting policies are set out in note 1. In accordance with the transitional provisions in IFRS 9, comparative figures have not been restated.

On 1 January 2018 (the date of initial application of IFRS 9), the group's management has assessed which business models apply to the financial assets held by the group and has classified its financial instruments into the appropriate IFRS 9 categories. On the date of initial application, 1 January 2018, the financial instruments of the group were as follows, with any reclassifications noted (the reclassifications of the financial instruments on adoption of IFRS 9 did not result in any changes to measurements):

in thousands of euros

	Measurement category		Carrying amount 01.01.2018		Difference
	Original (IAS 39)	New (IFRS 9)	Original	New	
Financial assets					
Current					
Cash and cash equivalents	Amortised cost	Amortised cost	39,210	39,210	-
Trade and other receivables	Amortised cost	Amortised cost	66,274	66,274	-
Non-current					
Trade and other receivables	Amortised cost	Amortised cost	17,163	17,163	-
Total Financial assets			122,647	122,647	-

2.2. IMPAIRMENT OF FINANCIAL ASSETS

The group has the following types of financial assets that are subject to IFRS 9's new expected credit loss model:

- trade receivables;
- contract assets;
- loans granted;
- bank deposits;
- cash and cash equivalents and;
- other financial assets.

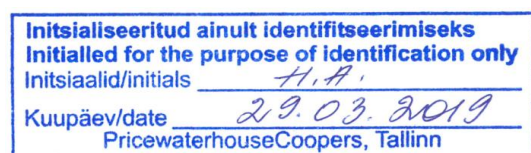
The group revised its impairment methodology for each of these classes of assets. As a result of the change in the impairment methodology there was no material changes in the loss allowance on 1 January 2018, thus no adjustments were made to the retained earnings nor equity.

2.3. IFRS 15 REVENUE FROM CONTRACTS WITH CUSTOMERS

The group has adopted IFRS 15 Revenue from Contracts with Customers from 1 January 2018, applying the modified retrospective approach, with the effect of initially applying this standard recognised at the date of initial application (i.e. 1 January 2018). Accordingly, the information presented for 2017 has not been restated – i.e. it is presented, as previously reported, under IAS 18 or IAS 11 and related interpretations. Additionally, the disclosure requirements in IFRS 15 have not been applied to comparative information.

As a result of the application no adjustments were recognised to the amounts in the financial statements at 1 January 2018.

A comprehensive check-list based on IFRS 15 standard has been prepared by the group, based on which the group entities assess and report revenue from contracts with customers according to the new standard. Group's management finds the impact of the amendments to existing construction contracts and also to new contracts with customers immaterial.



NOTE 3 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 where assumptions and estimates have an impact on the consolidated financial statements of Merko Ehitus group, are disclosed below. The effect of changes in management's estimates are reported in the income statement of the period of the change.

REVENUE FROM CONSTRUCTION SERVICES

Revenue from contracts with customers related to providing construction services is recognised based on the ratio of contract's actual incurred costs and the contract's estimated costs, which also assumes that the stage of completion of the construction contracts can be reliably assessed as of the reporting period. 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 December 2018, the amount of the provision for onerous contracts was EUR 247 thousand (2017: EUR 224 thousand), which was determined after the evaluation of the stage of completion of construction contracts (Note 28). 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 -20,209/+19,652 thousand (2017: EUR -24,077/+11,277 thousand).

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 group's write-down of inventories (work-in-progress, finished goods, acquisition of real estate properties for sale) would have been EUR 1,127 thousand higher in 2018 (2017: EUR 1,977 thousand higher), incl. real estate properties for sale in the amount of EUR 1,015 thousand (2017: EUR 1,383 thousand), work-in-progress in the amount of EUR 112 thousand (2017: EUR 524 thousand) and finished goods in the amount of EUR 0 thousand (2017: EUR 70 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 2018 would have been EUR 170 thousand lower (2017: EUR 293 thousand), incl. finished goods in the amount of EUR 170 thousand (2017: EUR 293 thousand).

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 collateral provided, the solutions offered to pay off the debt and the previous payment behaviour of the debtor are considered taking also into account the future outlook of the debtor, including its business logic and how that corresponds to the general economic developments as well as to the developments of particular economic sector (Note 16).

PROVISION FOR WARRANTY OBLIGATIONS

For determining the provision for warranty obligations, the historical cost of the group's warranty works is considered (Note 29).

VALUATION OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLES

An impairment test is carried out for property, plant and equipment and intangible assets when an event or change in circumstances indicates that impairment may have occurred. Based on management estimates, as at 31 December 2018 and 2017, no impairment tests were performed, as there were no indications of impairment of assets. As at 31 December 2018, the carrying amount of property, plant and equipment was EUR 9,715 thousand euros (31.12.2017: EUR 9,665 thousand) and the carrying amount of intangible assets was EUR 671 thousand (31.12.2017: EUR 497 thousand) (Note 24, 25).

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 December 2018 does not significantly differ from their fair value, with the exception of book value of land reclassified from inventories in the amount of EUR 11,940 thousand, the fair value of which by expert opinion was EUR 27,410 thousand (31 December 2017: the carrying amount of investment properties did not significantly differ from

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their fair value, with the exception of book value of land reclassified from inventories in the amount of EUR 11,851 thousand, the fair value of which by expert opinion was EUR 27,410 thousand). 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 its market value. External experts were not involved in the estimation of the fair value of investment properties, with the exception of land reclassified from inventories. Market value estimates are mostly based on market transactions, with the exception of real estate that is estimated using discounted cash flow method. As at 31 December 2018, the carrying amount of investment property was EUR 13,771 thousand (31.12.2017: EUR 15,719 thousand) (Note 23).

NOTE 4 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 countries and operating segments.

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

- Estonian construction service,
- other home markets construction service,
- real estate development.

Estonian construction service and other home markets construction service segments include all projects of the respective countries in general construction, civil engineering and road construction. Other operating areas (management services, supervision service, etc.) are insignificant to the group and they are recognised within the construction service segment. Other home markets construction service segment includes construction services in Latvia, Lithuania and Norway. The real estate segment primarily consists of the group's own real estate development – construction and sale, to a lesser degree, it also includes real estate maintenance and leasing. The amount of each cost item disclosed in segment reporting is a figure presented to the group's management for decision-making purposes regarding allocation of resources to segments and assessing the performance of the segment. Unallocated expenses and income after the profit of reporting segments are accounted in segment reporting using the same principles as in the financial statements and are not used for evaluation of the results of operating segments by the group's management.

Based on the resolution of the AS Merko Ehitus management board to monitor the revenue and the operating profit (loss) as the main financial indicators in the segment reporting, the operating profit (loss) has been presented as financial result according to segments since the financial statements of 2017. In addition to the cost item of the segment, undistributed marketing and general expenses, other operating income and expenses and financial income and costs have also been assigned to the segment's operating profit in proportion to the segment's revenue.

The business result is assessed based on external revenue, operating profit and profit before tax of the business segment. The operating profit and profit before tax of the segment is composed of the income and expenditure related to the segment. Other income and expenses not related to the segments are attributable to the activities of holding companies and are monitored at group level.

In the segment reporting, all intra-segment income and expenses have been eliminated from the pre-tax profit of the segments and all unrealised internal profits have been eliminated from the segment assets.

Additional information on the segments is provided in the Business activities chapter of the Management report.

in thousands of euros

2018	Estonian construction service	Other home markets construction service	Real estate development	Total segments
Revenue	164,947	182,153	85,343	432,443
Inter-segment revenue	(48)	11	(14,395)	(14,432)
Revenue from clients	164,899	182,164	70,948	418,011
incl. clients whose revenue is at least 10% of the group's consolidated revenue:				
client A (Estonian state)	54,547	-	-	54,547
client B	42,978	-	-	42,978
client C	-	70,311	-	70,311
Timing of revenue recognition at a point in time	1,695	531	52,846	55,072
Timing of revenue recognition over time	163,204	181,633	18,102	362,939

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2018	Estonian construction service	Other home markets construction service	Real estate development	Total segments
Operating profit (-loss)	8,796	1,923	11,319	22,038
Segment pre-tax profit (loss)	8,718	1,679	11,658	22,055
incl. interest income from operating activities (Note 8)	289	-	2,061	2,350
depreciation (Notes 5, 6, 7)	(1,575)	(143)	(290)	(2,008)
impairment of assets (Note 9)	(66)	-	-	(66)
impairment of inventories (Notes 5, 18)	-	-	(300)	(300)
recognition of provisions (Notes 5, 7, 29)	(1,240)	(3,904)	(480)	(5,624)
reversal of provisions (Note 5, 7, 29)	-	350	20	370
profit (loss) from joint ventures (Note 20)	-	-	653	653
other finance income (costs) (Notes 10, 11)	(11)	(16)	(223)	(250)
incl. interest expenses	(11)	(17)	(206)	(234)
Segment assets 31.12.2018	29,331	42,442	161,151	232,924
incl. joint ventures (Note 20)	-	-	732	732
2017	Estonian construction service	Other home markets construction service	Real estate development	Total segments
Revenue	135,338	108,446	98,388	342,172
Inter-segment revenue	(125)	(55)	(24,394)	(24,574)
Revenue from clients	135,213	108,391	73,994	317,598
incl. client (Estonian state), whose revenue is at least 10% of consolidated revenue	42,681	-	-	42,681
Timing of revenue recognition at a point in time	1,688	473	54,397	56,558
Timing of revenue recognition over time	133,525	107,918	19,597	261,040
Operating profit (-loss)	5,853	1,795	13,760	21,408
Segment pre-tax profit (loss)	5,822	1,552	13,426	20,800
incl. interest income from operating activities (Note 8)	18	-	1,654	1,672
depreciation (Note 5)	(1,873)	(48)	(271)	(2,192)
impairment of inventories (Notes 5, 18)	-	-	(2,360)	(2,360)
reversal of impairment of inventories (Notes 5, 18)	-	-	5,276	5,276
recognition of provisions (Notes 5, 7, 29)	(1,095)	(1,305)	(365)	(2,765)
reversal of provisions (Note 5, 7, 29)	191	-	-	191
profit (loss) from joint ventures (Note 20)	-	-	64	64
other finance income (costs) (Notes 10, 11)	(31)	9	(357)	(379)
incl. interest income	-	9	-	9
interest expenses	(18)	-	(341)	(359)
Segment assets 31.12.2017	29,422	49,162	157,058	235,642
incl. joint ventures (Note 20)	-	-	79	79

In addition to the segment assets, as at 31 December 2018 the group holds assets in the amount of EUR 36,733 thousand (31 December 2017: EUR 41,453 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, tax prepayments, other receivables and an unallocated portion of property, plant and equipment.

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RECONCILIATION OF THE PRE-TAX PROFIT OF SEGMENTS AND THE GROUP

	2018	2017
Pre-tax profit from reporting segments	22,055	20,800
Other operating profit (loss)	(2,166)	(1,869)
incl. recognition of provisions (Notes 7, 29)	(7)	(98)
finance income (costs)	(114)	(159)
incl. interest income	1	1
interest expenses	(146)	(147)
Total profit before tax	19,775	18,772

Other finance income and costs, not associated with any segment, includes financial income from bank deposits, profit (loss) from exchange rate changes, non-capitalized loan interest costs and other finance income and costs.

As the basis for the figure, that is allocated to segments based on revenue proportion, is the sum of group's unallocated costs, the interest income (expenses) in the sum of EUR -276 thousand (31 December 2017: EUR -246 thousand) has not been presented separately in the respective cost item.

REVENUE BY CLIENT LOCATION

in thousands of euros and percentage

	2018		2017	
Estonia	202,627	48%	190,928	60%
Latvia	157,496	38%	79,914	25%
Lithuania	46,765	11%	34,629	11%
Norway	11,123	3%	12,104	4%
Finland	-	0%	23	0%
Total	418,011	100%	317,598	100%

CONTRACT ASSETS AND LIABILITIES

in thousands of euros

	31.12.2018	31.12.2017
Accrued income from construction services (Note 16)	9,847	17,780
Prepayments for construction services (Note 28)	(16,912)	(13,749)
Advance payments received for construction contract works (Note 28)	(3,363)	(10,743)
Recognised provision for onerous construction contracts (Note 29)	(248)	(224)

During the accounting year advance payments received prior for construction contract works in a sum of EUR 10,743 thousand (2017: EUR 3,825 thousand) were recognised as revenue. As of 31 December 2018 the group's secured order book stood at EUR 228,950 thousand, for which the revenue is recognised in future periods. According to management estimation, 83% of revenue is going to be recognised in 2019 and 17% in 2020.

NON-CURRENT ASSETS (EXCEPT FOR FINANCIAL ASSETS AND DEFERRED INCOME TAX ASSETS) BY LOCATION OF ASSETS

in thousands of euros

	31.12.2018	31.12.2017
Estonia	11,970	13,446
Latvia	12,782	12,390
Lithuania	13	5
Norway	124	119
Total	24,889	25,960

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NOTE 5 COST OF GOODS SOLD

in thousands of euros

	2018	2017
Construction services and properties purchased for resale	262,190	186,352
Materials	60,096	50,983
Staff costs	23,666	22,255
Construction mechanisms and transport	10,214	9,317
Design	8,345	4,544
Real estate management costs	190	265
Depreciation (Note 4)	1,554	2,192
Impairment of inventories (Notes 4, 18)	300	2,360
Reversal of impairment of inventories (Notes 4, 18)	-	(5,276)
Provisions (Notes 4, 29)	5,242	2,574
Other expenses	13,165	11,181
Total cost of goods sold	384,962	286,747

NOTE 6 MARKETING EXPENSES

in thousands of euros

	2018	2017
Staff costs	2,454	2,326
Advertising, sponsorship	352	337
Transport	214	208
Depreciation	47	48
Other expenses	218	296
Total marketing expenses	3,285	3,215

NOTE 7 GENERAL AND ADMINISTRATIVE EXPENSES

in thousands of euros

	2018	2017
Staff costs	8,252	7,358
Office expenses, communication services	554	657
Consulting, legal, auditing *	481	680
Transport	410	364
Computer equipment and software	690	526
Depreciation	406	435
Provisions (Notes 4, 29)	20	98
Other expenses	1,491	1,171
Total general and administrative expenses	12,304	11,289

* Customer contract fees of the audit firms accounted for during the accounting year were EUR 101 thousand for audit fees (2017: EUR 130 thousand) and EUR 20 thousand for other business activities, including tax advisory services (2017: EUR 39 thousand).

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NOTE 8 OTHER OPERATING INCOME

in thousands of euros

	2018	2017
Interest income from operating activities	2,351	1,979
Profit from sale of non-current assets	473	571
Fines and penalties for delay received	200	133
Collection of doubtful receivables (Notes 16, 35)	94	238
Other income	409	872
Total other operating income	3,527	3,793

NOTE 9 OTHER OPERATING EXPENSES

in thousands of euros

	2018	2017
Fines, penalties	427	61
Gifts, donations	289	252
Doubtful receivables expense (Notes 16, 35)	292	243
Impairment of assets (Note 24)	66	-
Other expenses	41	45
Total other operating expenses	1,115	601

NOTE 10 FINANCE INCOME

in thousands of euros

	2018	2017
Interest income (Note 4)	3	3
Foreign exchange gains	5	-
Other finance income	-	1
Total finance income	8	4

NOTE 11 FINANCE COSTS

in thousands of euros

	2018	2017
Interest expense (Notes 4, 27)	652	745
Foreign exchange losses	-	1
Other finance costs	44	103
Total finance costs	696	849

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NOTE 12 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:

2018	Latvia	Lithuania	Other foreign countries	Estonia	Total
Profit (loss) before tax	3,130	3,591	214	12,840	19,775
Tax rate applicable to profits	0%	15%	23%	0%	
Tax calculated at domestic tax rates applicable to profits in the respective countries	(5)	(539)	(49)	-	(593)
Tax calculated on expenses not deductible for tax purposes	-	(30)	-	-	(30)
Tax effect of income not subject to tax	-	17	-	-	17
Tax losses of previous periods recognised in the reporting period	-	317	18	-	335
Tax losses not recognised in the reporting period	-	(104)	-	-	(104)
Total income tax expense	(5)	(339)	(31)	-	(375)
incl. income tax expense	(5)	(191)	(31)	-	(227)
deferred income tax expense (Note 22)	-	(148)	-	-	(148)

2017	Latvia	Lithuania	Other foreign countries	Estonia	Total
Profit (loss) before tax	5,263	3,003	918	9,588	18,772
Tax rate applicable to profits	15%	15%	24%	0%	
Tax calculated at domestic tax rates applicable to profits in the respective countries	(789)	(450)	(220)	-	(1,459)
Tax calculated on expenses not deductible for tax purposes	(647)	(990)	(11)	-	(1,648)
Tax effect of income not subject to tax	-	669	-	-	669
Tax losses of previous periods recognised in the reporting period	23	390	-	-	413
Tax losses not recognised in the reporting period	(71)	(42)	(2)	-	(115)
Income tax withheld on dividends	-	-	-	(880)	(880)
Total income tax expense	(1,484)	(423)	(233)	(880)	(3,020)
incl. income tax expense	(234)	(216)	(233)	(880)	(1,563)
deferred income tax expense (Note 22)	(1,250)	(207)	-	-	(1,457)

As at 31 December 2018, the parent company AS Merko Ehitus has EUR 2,879 thousand (31.12.2017: EUR 67 thousand) in dividends received from subsidiaries in previous periods and income from abroad, on which the income tax has been withheld.

As at 31 December 2018, it is possible to pay out dividends to shareholders from retained earnings in the amount of EUR 99,004 thousand (31.12.2017: EUR 97,172 thousand). Considering the taxed dividends received and income tax withheld on foreign income totalling EUR 720 thousand (31.12.2017: EUR 17 thousand), the corresponding income tax on dividends would amount to EUR 24,031 thousand (31.12.2017: EUR 24,276 thousand). As the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018, the 20/80 regular rate of income tax on net amounts paid out as dividends is applied in accounting for additional income tax on dividends. The income tax related to disbursement of dividends is recognised as a liability and income tax expense upon the announcement of dividends.

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NOTE 13 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.

	2018	2017
Net profit attributable to shareholders (in thousand EUR)	19,343	14,694
Weighted average number of ordinary shares (thousand pcs)	17,700	17,700
Basic earnings per share (in euros)	1.09	0.83

In 2018 and 2017, 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 14 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 parent company AS Merko Ehitus in 2019 will total EUR 17,700 thousand, i.e. EUR 1.00 per share. As the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018, the 20/80 regular rate of income tax is applied to dividends to be paid in 2019 and no additional income tax is withheld from dividends paid to shareholders that are resident natural persons.

In 2018, the parent company AS Merko Ehitus paid EUR 17,700 thousand in dividends, i.e. EUR 1.00 per share. On that, the company did not incur income tax obligation, as the dividend payments were covered by dividends already paid to the parent company by foreign subsidiaries.

In 2017, the parent company AS Merko Ehitus paid EUR 7,257 thousand in dividends, i.e. EUR 0.41 per share, incurring an income tax obligation of 20/80 of the amount disbursed, i.e. EUR 1,814 thousand, which was covered in part (EUR 934 thousand) from income tax withheld on taxed dividends received from subsidiaries in previous periods. In Q2 2017, the group incurred an additional income tax expense of EUR 880 thousand related to disbursement of dividends.

NOTE 15 CASH AND CASH EQUIVALENTS

in thousands of euros

	31.12.2018	31.12.2017
Cash on hand	-	1
Bank accounts	39,915	39,174
Short-term bank deposits	63	35
Total cash and cash equivalents (Note 35)	39,978	39,210

As at 31 December 2018, the weighted average interest on short-term bank deposits was 0.05% (31.12.2017: 5.35%).

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NOTE 16 TRADE AND OTHER RECEIVABLES

in thousands of euros

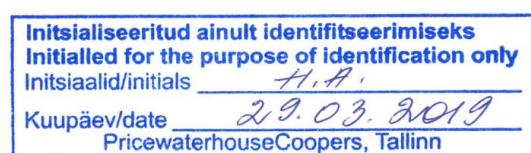
	31.12.2018	31.12.2017
Trade receivables (Note 35)		
Accounts receivable	42,835	36,768
Allowance for doubtful receivables	(81)	(103)
	42,754	36,665
Tax prepayments excluding corporate income tax		
Value added tax	944	733
Other taxes	2	2
	946	735
Accrued income form construction services (Notes 4, 35)	9,847	17,780
Other short-term receivables		
Short-term loans (Notes 17, 35)	14,590	10,590
Interest receivables (Note 35)	112	603
Other short-term receivables (Note 35)	271	636
	14,973	11,829
Prepayments for services		
Prepayments for construction services	7,064	8,075
Prepaid insurance	195	248
Other prepaid expenses	404	512
	7,663	8,835
Total trade and other receivables	76,183	75,844
incl. short-term loan receivables from related parties (Note 17)	9,000	9,000
other short-term receivables and prepayments to related parties (Note 33)	1,521	2,911

In 2018, the payment discipline of customers improved compared to last year. The share of overdue receivables decreased from 10.6% to 6.2% of total receivables, and as at the balance sheet date, the amount of overdue receivables was EUR 2,654 thousand (31 December 2017: 3,898 thousand). By 13 March 2019, overdue receivables had been collected in the amount of EUR 1,083 thousand. At the same time, in 2018, the share of receivables overdue for more than 180 days increased, which prolonged the average collection period of trade receivables to 40 days (2017: 40 days).

	2018	2017
Doubtful receivables at the beginning of the period	(103)	(265)
Reporting period doubtful receivables expenses (Note 9)	(90)	(114)
Reestablishment of receivables written off in previous years	-	(18)
Receivables written off during the year as uncollectible	18	56
Received doubtful receivables (Note 8)	94	238
Doubtful receivables at the end of the period	(81)	(103)

Additionally, in 2018, advance payments to suppliers were wrote down in the amount of EUR 202 thousand (2017: EUR 129 thousand), (Note 9). According to the management estimates, based on historical experience, there are sufficient reasons to conclude that the trade receivables reported in the financial statements will be collected from the buyers.

A more detailed overview of the group's credit risk is provided in Note 35.



NOTE 17 LOANS GRANTED

in thousands of euros

	Joint ventures (Note 33)	Unrelated legal entities	Total
2018			
Loan balance at beginning of the year	9,000	5,590	14,590
Reclassification of interest receivable into loan	366	-	366
Received	(366)	-	(366)
Loan balance at end of the year	9,000	5,590	14,590
incl. current portion (Notes 16, 35)	9,000	5,590	14,590
Average effective interest rate	6.0%	6.5% -15%	
2017			
Loan balance at beginning of the year	3,952	1,560	5,512
Granted	6,371	4,000	10,371
Reclassification of interest receivable into loan	138	30	168
Decrease of loan receivable in connection with sale of share in joint venture	(1,461)	-	(1,461)
Loan balance at end of the year	9,000	5,590	14,590
incl. current portion (Notes 16, 35)	9,000	1,590	10,590
non-current portion 2...5 years (Notes 21, 35)	-	4,000	4,000
Average effective interest rate	6.2%	8.0%	

Issued loans reported as at the reporting date had not yet fallen due, with the exception of a loan receivable in a sum of EUR 1,590 thousand for which mutual negotiations for loan contract prolongation and conclusion of construction contract are ongoing. Considering among other factors the mortgage collateralization of the contract, the value of which the management finds sufficient to cover the loan principal remaining if necessary, the management has not found it necessary to make a write-down for the remaining loan principal.

Loan in a sum of EUR 4,000 thousand was returned after the reporting date on 25.01.2019.

As at 31 December 2018 the loans granted to unrelated legal entities in a sum of EUR 5,590 thousand are secured by mortgages on the registered immovable properties at Tatari st. 6a, Sepapaja 3/Suur-Sõjamäe 12a and Sepapaja 5 in Tallinn in the amount of EUR 7,900 thousand.

NOTE 18 INVENTORIES

in thousands of euros

	31.12.2018	31.12.2017
Materials	797	238
Work-in-progress	43,081	36,023
Finished goods	15,991	17,612
Goods for resale		
Registered immovables purchased for resale	54,532	63,613
Other goods purchased for resale	705	747
	55,237	64,360
Prepayments for inventories		
Prepayments for real estate properties	1,300	-
Prepayments for other inventories	1,586	188
	2,886	188
Total inventories	117,992	118,421

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The inventories pledged as collateral as at 31 December 2018 for loans total EUR 50,374 thousand (2017: EUR 64,372 thousand) (Note 31).

In 2018, inventories have been written down to their net realisable value by EUR 300 thousand (2017: EUR 2,360 thousand) and previously made write-downs have not been reversed (2017: EUR 5,276 thousand, incl. EUR 660 thousand calculated proportionally to non-controlling interest) (Notes 3, 5, 19, 35). The reversal of write-downs is based on the updated valuation tests performed by the management, which took into consideration the fact that the economic environment has improved considerably compared to the time the write-downs were made, which has also brought about a recovery in real estate sales prices, according to comparable transactions known to management.

	Carrying amount before write-down	Write-down	Reversal of write- down	Carrying amount after write-down
31.12.2018				
Registered immovables purchased for resale	54,832	(300)	-	54,532
Total	54,832	(300)	-	54,532
31.12.2017				
Finished goods	19,972	(2,360)	-	17,612
Registered immovables purchased for resale	58,337	-	5,276	63,613
Total	78,309	(2,360)	5,276	81,225

NOTE 19 SHARES IN SUBSIDIARIES

	Ownership and voting rights %		Location	Area of operation
	31.12.2018	31.12.2017		
AS Merko Ehitus Eesti	100	100	Estonia, Tallinn	Construction
Tallinna Teede AS	100	100	Estonia, Tallinn	Road construction
AS Merko Infra	100	100	Estonia, Tallinn	Construction
AS Merko Tartu	-	100	Estonia, Tartu	Construction
OÜ Mineraal	-	100	Estonia, Tallinn	Mining
Kivimäe 32 OÜ	-	100	Estonia, Tallinn	Real estate
OÜ Tähelinna Kinnisvara	100	-	Estonia, Tallinn	Real estate
UAB Merko Statyba	100	100	Lithuania, Vilnius	Construction
UAB Statinių priežiūra ir administravimas	100	100	Lithuania, Vilnius	Real estate
UAB Timana	100	100	Lithuania, Vilnius	Real estate
OÜ Merko Property	100	100	Estonia, Tallinn	Real estate
UAB Balsiu mokyklos SPV	100	100	Lithuania, Vilnius	Real estate
UAB Merko Bustas	100	100	Lithuania, Vilnius	Real estate
UAB MN Projektas	100	100	Lithuania, Vilnius	Real estate
UAB Jurininku aikštele	100	100	Lithuania, Vilnius	Real estate
UAB Rinktinės projektai	100	100	Lithuania, Vilnius	Real estate
OÜ Jõgeva Haldus	-	100	Estonia, Tallinn	Real estate
OÜ Metsailu	-	100	Estonia, Tallinn	Real estate
OÜ Kiviaia Kinnisvara	100	100	Estonia, Tallinn	Real estate
OÜ Tähelinna Kinnisvara	-	100	Estonia, Tallinn	Real estate
Väike-Paekalda OÜ	-	100	Estonia, Tallinn	Real estate
Suur-Paekalda OÜ	-	100	Estonia, Tallinn	Real estate
Paekalda 2 OÜ	-	100	Estonia, Tallinn	Real estate
Paekalda 3 OÜ	-	100	Estonia, Tallinn	Real estate
Paekalda 7 OÜ	-	100	Estonia, Tallinn	Real estate
Paekalda 9 OÜ	-	100	Estonia, Tallinn	Real estate
OÜ Unigate	-	100	Estonia, Tallinn	Real estate
SIA Merko Investments	100	100	Latvia, Riga	Holding

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	Ownership and voting rights %		Location	Area of operation
	31.12.2018	31.12.2017		
ÜÜ Merko Investments	100	100	Estonia, Tallinn	Holding
SIA Merks	100	100	Latvia, Riga	Construction
SIA SK Viesturdarzs	100	100	Latvia, Riga	Real estate
SIA Merks Investicijas	100	100	Latvia, Riga	Real estate
SIA Industrialais Parks	100	100	Latvia, Riga	Real estate
SIA Ropažu Priedes	100	100	Latvia, Riga	Real estate
PS Merko-Merks	100	100	Latvia, Riga	Construction
SIA Žakusala Estates	75	75	Latvia, Riga	Real estate
PS Merks-Ostas celtnieks	65	65	Latvia, Riga	Construction
PS Merks Merko Infra	100	100	Latvia, Riga	Construction
Merko Finland Oy	100	100	Finland, Helsinki	Construction
Hartian Oy	100	75	Finland, Helsinki	Real estate
Lenko Stroi LLC	-	100	Russia, St. Petersburg	Construction
Merko Investments AS	100	100	Norway, Sofiemyr	Holding
Peritus Entreprenør AS	56	56	Norway, Sofiemyr	Construction

2018

On 20 November 2017, AS Merko Ehitus supervisory board decided to start liquidation procedures of 100% owned subsidiary based in Russia, 000 Lenko Stroi. The 000 Lenko Stroi liquidation was completed and company was deleted from the Commercial Register on 21 December 2018.

In connection with the improvement of efficiency of the business operations and the structure of the Estonian companies of AS Merko Ehitus group, on 21 December 2017, AS Merko Ehitus and AS Merko Ehitus Eesti, 100% subsidiary of AS Merko Ehitus, entered into a real right contract to transfer the right of ownership on real estate development segment's registered immovables and shareholdings in private limited companies on 1 January 2018. These companies were (a) 100% subsidiaries of AS Merko Ehitus: ÜÜ Tähelinna Kinnisvara, ÜÜ Metsailu, ÜÜ Paekalda 2, ÜÜ Paekalda 3, ÜÜ Paekalda 7, ÜÜ Paekalda 9, ÜÜ Unigate, Suur-Paekalda ÜÜ, Väike-Paekalda ÜÜ; and (b) a 50% joint venture ÜÜ Kodusadam. As per a merger contract signed prior, on balance sheet date 1 January 2018, AS Merko Ehitus Eesti merged AS Merko Tartu and aforementioned received subsidiaries with itself, with the exception of ÜÜ Tähelinna Kinnisvara. The final entry in the Commercial Register was made on 24 May 2018.

On 21 December 2017, a merger between AS Merko Infra and ÜÜ Mineraal, both belonging to AS Merko Ehitus group, was initiated. The acquiring company was AS Merko Infra. As a result of the merger, the company being acquired (ÜÜ Mineraal) wound up without liquidation proceedings and AS Merko Infra became the legal successor of the company being acquired. The merger date was 1 January 2018, after which all transactions of the acquired company will be deemed to be made on the account of the acquiring company. The final entry in the Commercial Register was made on 25 May 2018.

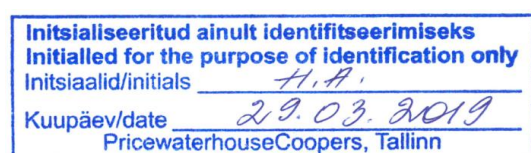
On 12 April 2018, AS Merko Ehitus disposed of its 100% shareholding in ÜÜ Jõgeva Haldus. The impact of the sale transaction on the consolidated result was a loss of EUR 59 thousand and increase of cash balance of EUR 385 thousand.

On 15 May 2018, Merko Finland Oy, fully owned subsidiary of AS Merko Ehitus, acquired an additional 25% share in the subsidiary Hartian Oy from the current co-shareholder with an acquisition price of EUR 1 thousand. After the transaction, Merko Finland Oy holds 100% of the shares of the subsidiary Hartian Oy.

On 29 October 2018, a merger between OY Merko Finland and Hartian OY, both belonging to AS Merko Ehitus group, was initiated. The acquiring company is OY Merko Finland. As a result of the merger, the company will being acquire (Hartian OY) wound up without liquidation proceedings and OY Merko Finland become the legal successor of the company being acquired. The merger date is 1 January 2019, after which all transactions of the acquired company will be deemed to be made on the account of the acquiring company. The final entry in the Commercial Register will be made in 2019.

In the first half of 2018, AS Merko Ehitus launched the dissolution of its branches in Latvia and Lithuania. The Latvian branch was deleted from the Commercial Register on 22 March 2018. The dissolution of the Lithuanian branch was completed and the branch was deleted from the Commercial Register on 21 January 2019.

On 17 December 2018, Merko Ehitus Eesti, fully owned subsidiary of AS Merko Ehitus, signed a notarised division plan. According to the plan, company ÜÜ Vahi Lastehoid will be established as a result of the division, to which apartment ownerships, located on Pärna allee in Tartu, will be transferred as per the division plan. The division will take effect as the entry is made in the Commercial Register presumably in the second quarter of 2019.



On 28 December 2018, AS Merko Ehitus launched a process for restructuring its fully owned subsidiary in Lithuania, UAB Merko Bustas. In accordance with the restructuring plan, UAB Merko Bustas's 100% subsidiary UAB Rinktinės projektai will be merged with the parent company. The restructuring is planned to be completed and the final merger entry made in the Commercial Register in the first quarter of 2019.

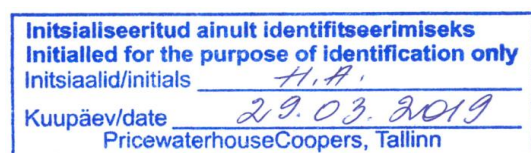
FINANCIAL INFORMATION REGARDING SIGNIFICANT SUBSIDIARY WITH A NON-CONTROLLING INTEREST

in thousands of euros

	SIA Zakusala Estates	
Statement of financial position	31.12.2018	31.12.2017
Cash	136	230
Trade and other receivables	12	6
Inventories	17,759	17,657
Total short-term assets	17,907	17,893
Short-term liabilities	70	22
Net assets	17,837	17,871
Equity	17,837	17,871
Non-controlling interest %	25%	25%
Non-controlling interest	4,459	4,468
Statement of comprehensive income	01.01-31.12.2018	01.01-31.12.2017
Reversal of impairment of inventories	-	2,643
Other expenses	(4)	(1)
Land tax	(29)	(117)
Net profit (loss) for the period	(33)	2,525
Comprehensive profit (loss) for the period	(33)	2,525
incl. attributable to equity holders of the parent	(25)	1,894
attributable to non-controlling interest	(8)	631
Cash flow statement	01.01-31.12.2018	01.01-31.12.2017
Operating profit	(33)	2,525
Change in receivables related to operating activities	(6)	3
Change in inventories	(102)	(2,669)
Change in payables related to operating activities	47	-
Total cash flow from operating activities	(94)	(141)
Repayments of borrowings	-	(70)
Total cash flow from financing activities	-	(70)
Change in cash and cash equivalents	(94)	(211)
Cash and cash equivalents in the beginning of the period	230	441
Cash and cash equivalents at the end of the period	136	230

In 2017, a previously made write-down on SIA Zakusala Estates immovable in the sum of EUR 2,643 thousand was reversed, of which 660 thousand euros was calculated proportionally to non-controlling interest.

As at 31 December 2018, the group's non-controlling interest in equity is EUR 4,577 thousand (31.12.2017: EUR 4,567 thousand), including SIA Zakusala Estates non-controlling interest in the amount of EUR 4,459 thousand (31.12.2017: EUR 4,468 thousand). The other companies with a non-controlling interest – totalling at EUR 118 thousand (31.12.2017: EUR 99 thousand) – do not separately constitute a significant item for the group.



NOTE 20 INVESTMENTS IN JOINT VENTURES

	Ownership and voting rights %		Location	Area of operation
	31.12.2018	31.12.2017		
Joint ventures				
Poolkoksimäe Sulgemise OÜ*	-	50	Estonia, Tallinn	Construction
Kodusadam OÜ	50	50	Estonia, Tallinn	Real estate

2018

* On 17 March 2017, AS Merko Ehitus and AS Ehitusfirma Rand ja Tuulberg initiated a process to dissolve joint venture Poolkoksimäe Sulgemise OÜ, in which each joint owner had a 50% share. The liquidation of the company was completed and the deletion entry to the Commercial Register made on 26 January 2018.

in thousands of euros

	Investment at 31.12.2017	Changes in 2018		Investment at 31.12.2018
		acquisition (sale)	profit (loss) on entities	
Joint ventures				
Kodusadam OÜ	79	-	653	732
Total joint ventures	79	-	653	732

in thousands of euros

	Investment at 31.12.2016	Changes in 2017		Investment at 31.12.2017
		acquisition (sale)	profit (loss) on entities	
Joint ventures				
OÜ Unigate	160	(92)	(68)	-
Poolkoksimäe Sulgemise OÜ	0	-	(0)	-
Kivimäe 32 OÜ	269	(327)	58	-
Kodusadam OÜ	5	-	74	79
Total joint ventures	434	(419)	64	79

JOINT VENTURES

in thousands of euros

	Assets 31.12.			Liabilities 31.12		Equity 31.12.	Income	Expenses	Net profit (loss)
	Cash	Other current assets	Non- current assets	Borrow- ings	Other current liabilities				
2018									
Kodusadam OÜ	9,056	15,100	1,956	18,000	6,648	1,464	27,975	(26,670)	1,305
Total	9,056	15,100	1,956	18,000	6,648	1,464	27,975	(26,670)	1,305
2017									
OÜ Unigate	-	-	-	-	-	-	-	(136)	(136)
Poolkoksimäe Sulgemise OÜ	-	-	-	-	-	-	-	(0)	(0)
Kivimäe 32 OÜ	-	-	-	-	-	-	189	(68)	121
Kodusadam OÜ	621	24,663	-	18,000	7,125	159	3,653	(3,503)	150
Total	621	24,663	-	18,000	7,125	159	3,842	(3,707)	135

In 2018, interest expenses have not been recognised in the joint venture's expenses (2017: OÜ Unigate EUR 136 thousand).

In connection with the joint venture, the group has contractual obligations to finance, as needed, the joint ventures' activities with loans totalling EUR 9,000 thousand (31.12.2017: EUR 9,000 thousand), of which the group has paid EUR 9,000 thousand in total (31.12.2017: EUR 9,000 thousand). In addition, the group has an obligation to provide construction services in future periods in amount of EUR 2,307 thousand (31.12.2017: EUR 18,083 thousand).

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NOTE 21 OTHER LONG-TERM LOANS AND RECEIVABLES

in thousands of euros

	31.12.2018	31.12.2017
Long-term loans (Notes 17, 35)	-	4,000
Long-term trade receivables (Note 35) *	10,391	13,163
Total other long-term loans and receivables	10,391	17,163

* incl. long-term receivables from buyer of Balsiu School in amount of EUR 10,253 thousand (31.12.2017: EUR 10,580 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:

31.12.2018	Latvia	Lithuania	Other foreign countries	Total
Deferred income tax liability				
effect of other payables	-	(1,407)	(74)	(1,481)
Deferred income tax expense of the financial year (Note 12)	-	(148)	-	(148)
31.12.2017	Latvia	Lithuania	Other foreign countries	Total
Deferred income tax liability				
effect of other payables	-	(1,259)	-	(1,259)
Deferred income tax assets				
incl. tax loss carryforwards	-	-	5	5
Total deferred income tax assets	-	-	5	5
Deferred income tax expense of the financial year (Note 12)	(1,250)*	(207)	-	(1,457)

* Elimination of deferred income tax assets in the sum of EUR 1,250 thousand is due to changes in the corporate income tax law in Latvia (Note 1.17).

NOTE 23 INVESTMENT PROPERTIES

in thousands of euros

	Land	Right of superficies	Buildings	Total
Cost at 31.12.2016	51	29	5,245	5,325
Accumulated depreciation 31.12.2016	-	(11)	(1,206)	(1,217)
Carrying amount at 31.12.2016	51	18	4,039	4,108
Acquisition	-	-	7	7
Reclassification	11,851	-	-	11,851
Depreciation	-	(1)	(246)	(247)
Carrying amount at 31.12.2017	11,902	17	3,800	15,719
Cost at 31.12.2017	11,902	29	5,252	17,183
Accumulated depreciation 31.12.2017	-	(12)	(1,452)	(1,464)
Carrying amount at 31.12.2017	11,902	17	3,800	15,719
Acquisition and improvements	89	-	2	91
Disposal in the course of business combination	-	-	(1,873)	(1,873)
Depreciation	-	0	(166)	(166)
Carrying amount at 31.12.2018	11,991	17	1,763	13,771
Cost at 31.12.2018	11,991	29	2,631	14,651
Accumulated depreciation 31.12.2018	-	(12)	(868)	(880)
Carrying amount at 31.12.2018	11,991	17	1,763	13,771

As at 31 December 2018, the carrying amounts of investment properties do not significantly differ from their fair values, with the exception of the reclassified land from the inventories, the fair value of which has been estimated by valuation expert at EUR 27,410 thousand (31.12.2017: the carrying amounts of investment properties did not significantly differ from their fair values, with the exception of the reclassified land from the inventories, the fair value of which has been estimated by valuation expert at EUR 27,410 thousand). Fair values have mainly been estimated based on comparable transactions (Level 2). Fair value measurement was carried out using Level 3 inputs of the fair value hierarchy.

Investment properties have been acquired for the purpose of earning rental income and/or for capital appreciation. Buildings located on the plot of land have temporarily been leased out under the operating lease terms. Information about the earned rental income and direct administrative expenses of investment properties leased out is disclosed in Note 26.

In the fourth quarter of 2017, the land at Skanstes in Riga totalling EUR 11,851 thousand was reclassified from inventories to investment property for long-term holdings for the purpose of capital appreciation, as the group does not have plans to carry out development operations on the premises.

As at 31 December 2018, investment properties pledged as collateral for loans total EUR 13,436 thousand (31.12.2017: EUR 15,333 thousand) (Note 31).). The Pärna avenue properties in Tartu and land at Skanstes in Riga have been pledged as collateral to bank loans.

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NOTE 24 PROPERTY, PLANT AND EQUIPMENT

in thousands of euros

	Land	Buildings	Machinery and equipment	Other fixtures	Construction in progress and prepayments	Total
Cost at 31.12.2016	821	5,650	17,625	5,190	1,093	30,379
Accumulated depreciation at 31.12.2016	-	(1,948)	(11,164)	(4,429)	-	(17,541)
Carrying amount at 31.12.2016	821	3,702	6,461	761	1,093	12,838
Unrealised exchange rate differences	-	-	-	(4)	-	(4)
Acquisition	-	2	767	319	166	1,254
Disposals	(4)	(71)	(1,357)	(3)	-	(1,435)
Disposal in the course of business combination	(6)	-	(903)	-	-	(909)
Reclassification	-	-	724	225	(949)	-
Write-offs	-	-	(3)	(12)	-	(15)
Depreciation	-	(180)	(1,440)	(444)	-	(2,064)
Carrying amount at 31.12.2017	811	3,453	4,249	842	310	9,665
Cost at 31.12.2017	811	5,530	13,707	5,561	310	25,919
Accumulated depreciation at 31.12.2017	-	(2,077)	(9,458)	(4,719)	-	(16,254)
Carrying amount at 31.12.2017	811	3,453	4,249	842	310	9,665
Acquisition and improvements	-	40	1,623	184	282	2,129
Disposals	(2)	(44)	(151)	(82)	-	(279)
Reclassification	-	313	148	21	(482)	-
Impairment	(66)	-	-	-	-	(66)
Write-offs	-	(1)	-	(1)	-	(2)
Depreciation	-	(176)	(1,160)	(396)	-	(1,732)
Carrying amount at 31.12.2018	743	3,585	4,709	568	110	9,715
Cost at 31.12.2018	743	5,765	14,473	5,474	110	26,565
Accumulated depreciation at 31.12.2018	-	(2,180)	(9,764)	(4,906)	-	(16,850)
Carrying amount at 31.12.2018	743	3,585	4,709	568	110	9,715

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

As at 31 December 2018, property, plant and equipment pledged as collateral for loans total EUR 2,639 thousand (31.12.2017: EUR 3,384 thousand) (Note 31). The group's most significant item of property, plant and equipment pledged as collateral to the loans is the Järvevana tee 9G property and the office building thereon.

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NOTE 25 INTANGIBLE ASSETS

in thousands of euros

	Goodwill *	Software	Prepayments	Total
Cost at 31.12.2016	970	1,137	213	2,320
Accumulated amortisation and impairment at 31.12.2016	(656)	(991)	-	(1,647)
Carrying amount at 31.12.2016	314	146	213	673
Unrealised exchange rate differences	(5)	(2)	-	(7)
Acquisitions	-	128	54	182
Reclassification	-	223	(223)	-
Amortisation and impairment	(235)	(116)	-	(351)
Carrying amount at 31.12.2017	74	379	44	497
Cost at 31.12.2017	74	1,471	44	1,589
Accumulated amortisation and impairment at 31.12.2017	-	(1,092)	-	(1,092)
Carrying amount at 31.12.2017	74	379	44	497
Unrealised exchange rate differences	(1)	-	-	(1)
Acquisitions	-	100	182	282
Reclassification	-	187	(187)	-
Amortisation and impairment	-	(107)	-	(107)
Carrying amount at 31.12.2018	73	559	39	671
Cost at 31.12.2018	73	1,716	39	1,828
Accumulated amortisation and impairment at 31.12.2018	-	(1,157)	-	(1,157)
Carrying amount at 31.12.2018	73	559	39	671

* In connection with the disposal of the road maintenance field of activity from AS Vooremaa Teed, a 100% subsidiary of Tallinna Teede AS belonging to AS Merko Ehitus group, and the merger of the companies in Q3 2017, the goodwill of AS Vooremaa Teed has been written down and written off the balance sheet.

NOTE 26 LEASED ASSETS

in thousands of euros

	31.12.2018	31.12.2017
Assets acquired under finance lease terms		
Machinery and equipment		
Cost	3,476	3,545
Accumulated depreciation	(1,747)	(2,585)
Carrying amount	1,729	960

On the basis of cancellable lease agreements, operating lease payments totalling EUR 521 thousand were paid for vehicles in 2018 (2017: EUR 599 thousand). The group does not intend to use a bargain purchase option for the assets leased under the operating lease terms in the reporting period.

Lease agreements do not set any limits to groups' dividend or financing policies. Rented assets have not been subleased.

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INVESTMENT PROPERTIES LEASED OUT UNDER NON-CANCELLABLE OPERATING LEASE TERMS

	31.12.2018	31.12.2017
Cost	2,682	5,320
Accumulated depreciation	(868)	(1,469)
Carrying amount	1,814	3,851
	2018	2017
Operating lease income received for investment properties (Note 22)	403	509
Future operating lease income:	1,384	1,446
Next year	302	512
In 2...5 years	857	927
Later than 5 years	225	7
Direct administrative expenses of investment properties (Note 23)	(213)	(307)

NOTE 27 BORROWINGS

in thousands of euros

	Finance lease liabilities at present value	Loans from					total	Total borrowings (Note 35)
		banks	parent company (Note 33)	entities under common control (Note 33)	other entities			
2018								
Balance at beginning of the year	863	50,383	-	6,000	2,110	58,493	59,356	
Received	1,477	20,399	-	-	9,740	30,139	31,616	
Repaid	(605)	(38,645)	-	-	(6,025)	(44,670)	(45,275)	
Sale to lessor	(88)	-	-	-	-	-	(88)	
Loan liability related to the disposals of subsidiary	-	(1,443)	-	-	-	(1,443)	(1,443)	
Loan balance at end of the year	1,647	30,694	-	6,000	5,825	42,519	44,166	
incl. current portion	524	12,551	-	1,000	5,825	19,376	19,900	
non-current portion 2...5 years	1,123	18,143	-	5,000	-	23,143	24,266	
Accrued interest of reporting period	21	617	-	145	-	762	783	
incl. capitalised interest cost	-	131	-	-	-	131	131	
Interest rate range	1.0%-3.55%+3-6 month euribor	0.65%-2.3%+1-6 month euribor; 1.69%+ Eonia	-	2.65%+6 month euribor	0%			
Base currencies	EUR	EUR, NOK	-	EUR	EUR			

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	Finance lease liabilities at present value	Loans from					Total borrowings (Note 35)
		banks	parent company (Note 33)	entities under common control (Note 33)	other entities	total	
2017							
Balance at beginning of the year	1,769	25,703	12,500	6,000	29	44,232	46,001
Received	68	59,541	-	-	2,110	61,651	61,719
Repaid	(818)	(34,880)	(12,500)	-	-	(47,380)	(48,198)
Sale to lessor	(156)	-	-	-	-	-	(156)
Loan liability related to the disposals of subsidiary	-	-	-	-	(7)	(7)	(7)
Reclassification of loan into other payables	-	22	-	-	(22)	-	-
Exchange rate	-	(3)	-	-	-	(3)	(3)
Loan balance at end of the year	863	50,383	-	6,000	2,110	58,493	59,356
incl. current portion	487	20,621	-	1,000	2,110	23,731	24,218
non-current portion 2...5 years	376	29,762	-	5,000	-	34,762	35,138
Accrued interest of reporting period	44	641	34	146	-	821	865
incl. capitalised interest cost	-	120	-	-	-	120	120
Interest rate range	1.6%-4.1%+3-6 month euribor	1.05%-2.3%+1-6 month euribor; 1.69%+eonia	4.0%	2.65%+6 month euribor	0%		
Base currencies	EUR	EUR, NOK	EUR	EUR	EUR, NOK		

	2018	2017
Minimum future payments under finance lease	1,703	870
incl. current portion	545	492
non-current portion with the term of 2...5 years	1,158	378

Borrowings with floating interest rates related to EURIBOR are divided by the interest rate changes and the contractual repricing dates as follows:

	2018	2017
Finance lease liabilities		
1-5 months	431	180
6-12 months	1,185	572
Bank loans		
1-5 months	13,809	12,265
6-12 months	16,850	38,070
Loans from entities under common control		
6-12 months	6,000	6,000
Total	38,275	57,087

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

	2018	2017
Finance lease liabilities	31	111
Loans from bank	35	48
Loans from other entities	5,825	2,110
Total	5,891	2,269

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Although different risk factors were evident in global financial markets throughout the year, it was generally a relatively stable year. The risk margins on loans did not significantly change as compared to last year, because EURIBOR was stable and other risk margins have not changed significantly since the loans were taken. Therefore, we can state that the fair value of bank loans to a material extent equals their carrying amount. The fair value of loans is measured using the discounted cash flow method and on the basis of Level 3 inputs of the fair value hierarchy (Note 35).

Among the loans from entities under common control, there is a loan from Järvevana OÜ, the interest of which is 6-month EURIBOR + 2.65%.

Loan collaterals and pledged assets are presented in Note 31.

NOTE 28 PAYABLES AND PREPAYMENTS

in thousands of euros

	31.12.2018	31.12.2017
Trade payables (Note 35)	38,327	35,356
Payables to employees	10,067	8,613
Tax liabilities, except for corporate income tax		
value added tax	1,102	532
personal income tax	648	554
social security tax	1,166	958
unemployment insurance tax	57	53
contributions to mandatory funded pension	42	43
other taxes	229	160
	3,244	2,300
Prepayments for construction services (Notes 4, 35)	16,912	13,749
Other liabilities (Note 35)		
interest liabilities	6	2
other liabilities	345	594
	351	596
Prepayments received *	8,115	14,358
Total payables and prepayments	77,016	74,972
incl. payables to related parties (Note 33)	293	17

* As of 31 December 2018 the balance of prepayments received consists of prepayments received in connection with construction contracts (advance payments received for construction contract works) in a sum of EUR 3,363 thousand (31.12.2017: EUR 10,743 thousand) and of prepayments received connection with residential properties (apartment buyers) in a sum of EUR 4,752 thousand (31.12.2017: EUR 3,615 thousand) (Note 4).

NOTE 29 PROVISIONS

in thousands of euros

	Provision for warranty obligation for construction	Provision for onerous construction contracts	Provision for legal costs and claims filed (Note 35) *	Provision for costs of projects sold and work-in-progress of projects	Other provisions	Total provisions
2018						
Balance at beginning of the year	2,874	224	120	1,221	130	4,569
Recognised (Notes 4, 5, 7)	1,442	282	-	3,878	29	5,631
Used during the year	(643)	(258)	-	(752)	(80)	(1,733)
Reversed (Notes 4, 7)	(300)	-	-	(20)	(50)	(370)
Exchange rate	-	-	-	3	-	3
Balance at end of the year	3,373	248	120	4,330	29	8,100
incl. current portion	3,373	248	120	4,330	29	8,100
2017						
Balance at beginning of the year	2,476	79	273	2,788	21	5,637
Recognised (Notes 4, 5, 7)	1,152	408	75	1,067	161	2,863
Used during the year	(736)	(263)	(228)	(2,455)	(52)	(3,734)
Reversed (Notes 4, 7)	(18)	-	-	(173)	-	(191)
Exchange rate	-	-	-	(6)	-	(6)
Balance at end of the year	2,874	224	120	1,221	130	4,569
incl. current portion	2,874	224	120	1,221	130	4,569

* Additional information is provided in subsection "Legal risk" in Note 35.

The basic principle for making provisions for warranty obligations are the historical trends in the statistical share of construction contract volumes. Historically, the amount of provision used has not varied significantly from the amount of provision recognised. The provisions for costs of projects sold are based on the total costs of projects as defined in business plans, which are constantly updated and realized pursuant to the work performed.

NOTE 30 OTHER LONG-TERM PAYABLES

in thousands of euros

	31.12.2018	31.12.2017
Trade payables (Note 35)	1,675	1,248
Other long-term payables (Note 35)	504	541
Total other long-term payables	2,179	1,789
incl. other long-term payables to related parties (Notes 33)	504	541

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NOTE 31 LOAN COLLATERALS AND PLEDGED ASSETS

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

in thousands of euros

Commercial pledges	31.12.2018	31.12.2017
Movable property	62,891	62,018
Term deposit	-	35
Financial assets *	12,425	12,643
Total	73,316	74,696

* The financial assets of UAB Balsiu mokyklos SPV, which OÜ Merko Property has pledged to secure the investment loan in the amount of EUR 7,657 thousand for the benefit of OP Corporate Bank plc Lithuanian branch (31.12.2017: EUR 5,311 thousand for the benefit of Luminor Bank AB Lithuanian branch).

Mortgages	31.12.2018	31.12.2017
Inventories (Note 18)	50,374	64,372
Land and buildings (Note 24)	2,639	3,240
Other non-current assets (Note 25)	-	144
Investment properties (Note 23)	13,436	15,333
Total	66,449	83,089

Pledges of shares

In addition to the commercial pledge on financial assets, OÜ Merko Property has pledged the shares of its wholly-owned subsidiary UAB Balsiu mokyklos SPV for the benefit of OP Corporate Bank plc Lithuanian branch. An investment loan in the amount of EUR 7,657 thousand (31.12.2017: EUR 5,311 thousand for the benefit of Luminor Bank AB Lithuanian branch) is secured by the pledge.

NOTE 32 SHARE CAPITAL

There were no changes in share capital during 2018 and 2017.

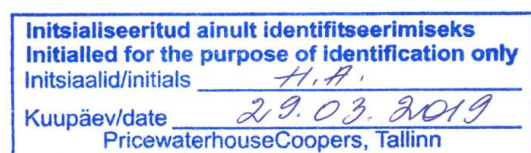
The Commercial Code of the Republic of Estonia specifies the following requirements for the share capital of the entities registered in Estonia:

- 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 ¼ 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 31.12.2018 and 31.12.2017, the share of capital of AS Merko Ehitus was EUR 7,929 thousand and the consolidated net assets of AS Merko Ehitus were EUR 131,757 thousand (31.12.2017: EUR 130,170 thousand), therefore the Company's equity and share capital were in compliance on both balance sheet date with the requirements established in the Republic of Estonia. The calculated value of the share was 0.447966 euros.



NOTE 33 RELATED PARTY TRANSACTIONS

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 or so-called sister companies, in this Note "Entities under common control";
- 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 31.12.2018 and 31.12.2017, 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

	2018	2017
Provided services and goods sold		
Parent company	15	15
Joint ventures *	16,505	15,763
Entities under common control	91	6,430
Members of the management	43	42
Other related parties	28	-
Total services provided and goods sold	16,682	22,250
Interest income		
Joint ventures	559	435
Purchased services and goods		
Parent company	90	90
Entities under common control	57	59
Total purchased services and goods	147	149
Interest expense		
Parent company	-	34
Entities under common control	145	146
Total interest expense	145	180

BALANCES WITH RELATED PARTIES

in thousands of euros

	31.12.2018	31.12.2017
Receivables from related parties		
Loans granted (Note 16, 17, 21)		
Joint ventures	9,000	9,000
Receivables and prepayments (Note 16)		
Parent company	4	4
Joint ventures	1,385	2,489
Entities under common control	88	418
Members of the management	44	-
Total receivables and prepayments	1,521	2,911
Total receivables from related parties	10,521	11,911

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	31.12.2018	31.12.2017
Payables to related parties		
Short-term loans received (Note 27)		
Entities under common control	1,000	1,000
Total short-term loans received	1,000	1,000
Payables and prepayments (Note 28)		
Parent company	9	9
Joint ventures	14	7
Entities under common control	1	1
Members of the management	269	-
Total payables and prepayments	293	17
Long-term loans received (Note 27)		
Entities under common control	5,000	5,000
Other long-term payables (Note 30)		
Other related parties	504	541
Total payables to related parties	6,797	6,558

* Provided services to joint ventures consist mainly of construction services

With regard to receivables from related parties, no impairments were performed in either 2018 or 2017.

REMUNERATION OF THE MEMBERS OF THE SUPERVISORY AND MANAGEMENT BOARDS

In 2018, the members of the Supervisory and Management Boards of AS Merko Ehitus and Management Boards of its significant subsidiaries were paid gross fees totalling EUR 2,643 thousand (2017: EUR 2,355 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 1,052 thousand (2017: EUR 882 thousand). In 2018, compensation was paid to the management board members in the amount of EUR 34 thousand (2017: EUR 147 thousand).

MEMBERS OF THE SUPERVISORY AND MANAGEMENT BOARD

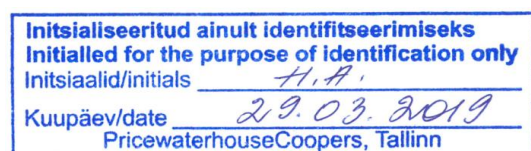
Track record and photographs of the members of the Supervisory Board can be found in the management report and on AS Merko Ehitus website at group.merko.ee.

Shares held by members of the Supervisory Board of AS Merko Ehitus as at 31 December 2018

		NO. OF SHARES	% OF SHARES
Toomas Annus (AS Riverito)	Chairman of the Supervisory Board	8,322,914	47.02%
Indrek Neivelt (OÜ Trust IN)	Member of the Supervisory Board	31,635	0.18%
Teet Roopalu	Member of the Supervisory Board	-	0.00%
		8,354,549	47.20%

Shares held by members of the Management Board of AS Merko Ehitus as at 31 December 2018

		NO. OF SHARES	% OF SHARES
Andres Trink	Chairman of the Management Board	600	0.00%
Tõnu Toomik (AS Riverito)	Member of the Management Board	1,607,185	9.08%
		1,607,785	9.08%



NOTE 34 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.

	31.12.2018	31.12.2017
Performance period's warranty to the customer	34,511	31,229
Tender warranty	655	2,201
Guarantee warranty period	17,666	18,197
Prepayment guarantee	12,098	16,249
Payment guarantee	30,500	31,019
Contracts of surety	7,734	4,215
Letter of credit	428	-
Total contingent liabilities	103,592	103,110

The "Payment guarantee" entry as at 31.12.2018 and 31.12.2017 includes a payment guarantee for the benefit of a financial institution, issued within the framework of a contract for construction, in order to secure the customer's contractual payment obligations in the total amount of up to EUR 30,500 thousand. The realisation of the payment guarantee is not considered likely by the group. To secure the customer's contractual obligations, a first-ranking mortgage of EUR 36,600 thousand with the financing institution as the beneficiary has been established on the registered immovable property of the building to be constructed in the framework of the construction agreement. To secure the group's payment guarantee, a second-ranking mortgage of EUR 8,500 thousand with the group as the beneficiary has been established.

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 eliminated.

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

Payment guarantee – guarantor guarantees repayments of the customer's/developer's loan.

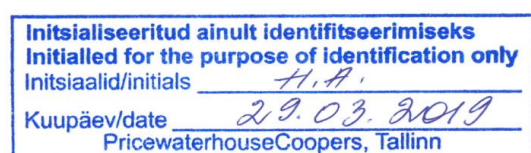
Contracts of surety – the group guarantees the timely fulfillment of group member's liabilities towards a third party (e.g. providing services by a certain date in the agreed amount).

Letter of credit – a letter of credit is the obligation of the buyer (i.e. the bank opening the letter of credit) to pay the seller (i.e. the receiver of the letter of credit) the amount of the letter of credit, if the seller fulfils and presents documentation to the bank regarding the fulfilment of the conditions fixed with the letter of credit.

As at 31 December 2018 the group has recognised a provision (Note 29) with regards to the guarantee for warranty period which is based upon historical experience and contractual volumes.

Tax authorities have the right to review the group's tax records within 5 years after submitting the tax declaration and upon detecting errors, impose additional taxes, interest and fines. The group's management estimates that there are no 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 35.



NOTE 35 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 have 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, the future outlook of these business are analysed, including business logic and its compliance with general economic developments as well as developments corresponding economic sector and also their financial position is analysed. 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 bank account or term deposits at banks, which are part of Swedbank, SEB, Luminor and OP Corporate Bank groups. Baltic banks, which are part of Swedbank and SEB group do not have separate ratings by Moody's. The parent company of Swedbank group, Swedbank AB, has a Moody's long-term credit rating Aa2 (2017: Aa3) and the parent company of SEB group, Skandinaviska Enskilda Banken AB, has a Moody's long-term credit rating Aa2 (2017: Aa3). OP Corporate Bank PLC has a Moody's long-term credit rating Aa3 (2017: Aa3). Luminor Bank has a Moody's long-term credit rating Baa1 (2017: did not have a rating, being jointly owned by DNB Bank ASA (Moody's credit rating Aa2) and Nordea Bank AB (Moody's credit rating Aa3).

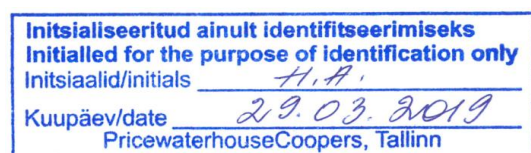
While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial as at 1 January 2018 and 31 December 2018. The management estimates that the group is not exposed to significant credit risk.

FINANCIAL ASSETS EXPOSED TO CREDIT RISK

in thousands of euros

	Allocation by due dates		Carrying amount	Collateral
	1-12 months	2-5 years		
31.12.2018				
Cash and cash equivalents (Note 15)	39,978	-	39,978	-
Trade receivables (Notes 16, 21)	42,754	10,391	53,145	-
Accrued income from construction service (Notes 4, 16)	9,847	-	9,847	-
Loans granted (Notes 16, 17, 21)	14,590	-	14,590	5,590
Interest receivables (Notes 16, 21)	112	-	112	-
Other short-term receivables (Note 16)	271	-	271	-
Total	107,552	10,391	117,943	5,590
31.12.2017				
Cash and cash equivalents (Note 15)	39,210	-	39,210	-
Trade receivables (Notes 16, 21)	36,665	13,163	49,828	1,500
Accrued income from construction service (Notes 4, 16)	17,780	-	17,780	-
Loans granted (Notes 16, 17, 21)	10,590	4,000	14,590	5,590
Interest receivables (Notes 16, 21)	603	-	603	-
Other short-term receivables (Note 16)	636	-	636	-
Total	105,484	17,163	122,647	7,090

The group's customers are primarily large local entities or public sector entities (as at 31 December 2018, the public sector proportion in accounts receivable amounted to 8.0% (31.12.2017: 12.2%) with well-known and sufficient creditworthiness.



TRADE RECEIVABLES BY DUE DATE

in thousands of euros

	31.12.2018		31.12.2017	
Not overdue	50,507	95.0%	45,930	92.2%
1-30 days overdue	1,006	1.9%	2,146	4.3%
31-60 days overdue	294	0.6%	397	0.8%
61-90 days overdue	64	0.1%	271	0.5%
91-120 days overdue	12	0.0%	44	0.1%
121-180 days overdue	16	0.1%	22	0.1%
More than 180 days overdue	1,246	2.3%	1,018	2.0%
Total trade receivables (Notes 16, 21)	53,145	100%	49,828	100%

* Trade receivables are presented in net amount, i.e. the sum of receivables also includes allowance for doubtful receivables from buyers.

As at the balance sheet date, the amount of overdue receivables was EUR 2,639 thousand (31.12.2017: EUR 3,898 thousand), of which EUR 1,083 thousand has been collected by 13 March 2019. In a year, the share of overdue short-term receivables in total receivables decreased from 7.8% to 5.0%. The group keeps running track of payment history for all customers separately for each receivable. According to management estimates, which are based on customers' historical payment behaviour, background assessment on the payment behaviour and business perspectives of new clients, the management estimates that there are sufficient reasons to conclude that the receivables reported in the financial statements will be paid off by the buyers. The receivables, which were not overdue at the balance sheet date, will be paid by due date. As well as invoiced trade receivables, management estimates the credit risk of accrued income from construction service to be low. The management bases its assessment on the regular monitoring of the financial position and payment behavior of the contractual partner and the outlook of the contractor's economic sector and general economic developments. 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 joint ventures, the economic activities of which the group has a good overview of, totalled EUR 9,000 thousand (31.12.2017: 9,000 thousand) and therefore, no additional collateral is required. As at 31 December 2018, loans granted to unrelated legal entities amounted to EUR 5,590 thousand (31.12.2017: 5,590 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. Additional information on loan guarantees is given in Note 17.

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 2018, the share of interest-bearing liabilities in the group's capital structure increased slightly and management considers this share to be moderate (as at 31 December 2018, 16.4% and as at 31 December 2017, 21.4% 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 months.

EFFECT OF CHANGES IN INTEREST RATE RISK ON FINANCE COSTS AND INCOME

As at 31 December 2018, the group's interest-bearing liabilities totalled EUR 44,166 thousand (31.12.2017: EUR 59,356 thousand), of which short-term loans and repayments of long-term liabilities in 2019 totalled EUR 19,900 thousand (31.12.2017: EUR 24,218 thousand) and long-term loans and finance lease liabilities totalled EUR 24,266 thousand (31.12.2017: EUR 35,138 thousand). As at 31 December 2018, the group's loans granted totalled EUR 14,590 thousand (31.12.2017: EUR 14,590 thousand), of which all were classified as short-term loans with repayments in 2019 (31.12.2017: EUR 10,590 thousand short-term and EUR 4,000 thousand as long-term loans). Loan interest depended on interbank 1-12 month loan base interest in the entity's domicile and Euribor. As at 31 December 2018, the break-down of interest-bearing borrowings and loans granted was as follows:

	31.12.2018	31.12.2017
Fixed rate liabilities	5,892	2,269
Liabilities with floating rate interests 1-5 months	14,239	12,445
Liabilities with floating rate interests 6-12 months	24,035	44,642
Total interest-bearing borrowings	44,166	59,356
Fixed rate receivables	14,590	14,590

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The management does not expect big changes in base interest rates, the market is stable and base interest rates remain low. Assuming that average EURIBOR is 10 pp 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 38 thousand (31.12.2017: EUR 57 thousand). All the loans granted have fixed interest rate and therefore a change in the reference rates would have no impact on the interest income.

In addition to risk arising from changes in Euribor, 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 and other unrelated third parties in the total limit amount of EUR 34,103 thousand, of which EUR 8,519 thousand was withdrawn. In 2019, the contracts in a total amount of EUR 17,103 thousand will expire, which renewal will be considered.

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, Latvia and Lithuania and kroner in Norway. Transactions within the group are conducted in euros as a rule. To eliminate foreign currency risks, close track is kept of the proportions of the group's assets and liabilities held in different currencies and, when it comes to entering into long-term construction contracts, the euro is the preferred currency in the Baltics, and, in Norway, the krone. The breakdown of financial assets and liabilities in local currencies as at the balance sheet date is as follows:

	In EUR	In NOK
31.12.2018		
Assets	96.1%	3.9%
Liabilities	97.1%	2.9%
31.12.2017		
Assets	96.2%	3.8%
Liabilities	96.9%	3.1%

Considering the fact that the materials and services used in construction are generally from the local market or supplied from within the EU, the currency risk in the group is currently minimal.

3. LIQUIDITY RISK

The group's liquidity or solvency represents its ability to settle its liabilities to creditors on time. As at 31 December 2018, the group's current ratio was 2.2 (31.12.2017: 2.2) and the quick ratio 1.1 (31.12.2017: 1.1). In addition to 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 and other unrelated third parties in the total amount of EUR 34,103 thousand, of which EUR 25,584 thousand was unused (31.12.2017: EUR 17,478 thousand, of which EUR 9,478 thousand was unused). In addition to the overdraft facility, the group has a current loan facility with the limit of EUR 3,500 thousand (31.12.2017: EUR 3,500 thousand) from AS Riverito, which was fully unused as at the end of current and previous financial years.

The management estimates that the group's capital structure – equity ratio of 48.9% (31.12.2017: 47.0%) and a moderate proportion of interest bearing liabilities at 16.4% (31.12.2017: 21.4%) of the balance sheet total – ensures the group's trustworthiness for creditors. It also enables to prolong existing financial liabilities and raise additional working capital funds, if needed.

FINANCIAL ASSETS/LIABILITIES

in thousands of euros

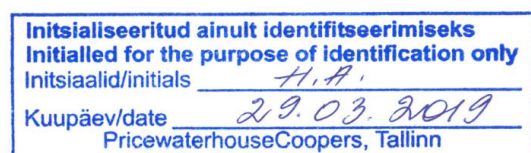
	Allocation by due date			Total	Carrying amount
	1-3 months	4-12 months	2-5 years		
31.12.2018					
Assets					
Cash and overnight deposits (Note 15)	39,978	-	-	39,978	39,978
Trade receivables (Notes 16, 21)	26,765	15,989	10,391	53,145	53,145
Accrued income from construction services (Notes 4, 16)	9,847	-	-	9,847	9,847
Loans and interest (Notes 16, 17, 21)	1,702	13,000	-	14,702	14,702
Other short-term receivables (Note 16)	129	142	-	271	271
Total	78,421	29,131	10,391	117,943	117,943
Liabilities					
Trade payables (Notes 28, 30)	25,199	13,128	1,675	40,002	40,002
Prepayments for construction services (Notes 4, 28)	16,912	-	-	16,912	16,912
Loan and finance lease liabilities (Note 27) *	3,646	16,254	24,266	44,166	44,166
Other liabilities (Note 28, 30)	255	96	504	855	855
Financial guarantees	30,500	-	-	30,500	-
Total	76,512	29,478	26,445	132,435	101,935
Net assets / liabilities	1,909	(347)	(16,054)	(14,492)	16,008

	Allocation by due date			Total	Carrying amount
	1-3 months	4-12 months	2-5 years		
31.12.2017					
Assets					
Cash and overnight deposits (Note 15)	39,210	-	-	39,210	39,210
Trade receivables (Notes 16, 21)	31,039	5,626	13,163	49,828	49,828
Accrued income from construction services (Notes 4, 16)	17,780	-	-	17,780	17,780
Loans and interest (Notes 16, 17, 21)	11,193	-	4,000	15,193	15,193
Other short-term receivables (Note 16)	322	314	-	636	636
Total	99,544	5,940	17,163	122,647	122,647
Liabilities					
Trade payables (Notes 28, 30)	35,356	-	1,248	36,604	36,604
Prepayments for construction services (Notes 4, 28)	13,749	-	-	13,749	13,749
Loan and finance lease liabilities (Note 27) *	11,225	12,993	35,138	59,356	59,356
Other liabilities (Note 28, 30)	436	160	541	1,137	1,137
Financial guarantees	31,872	-	-	31,872	-
Total	92,638	13,153	36,927	142,718	110,846
Net assets / liabilities	6,906	(7,213)	(19,764)	(20,071)	11,801

* 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.

4. FAIR VALUE ESTIMATION

According to the estimation of the group, the carrying values of financial assets at amortised cost (Notes 15, 16, 17, 21) and financial liabilities at amortised cost (Notes 27, 28, 30) in the consolidated balance sheet as at 31 December 2018 and 31 December 2017 do not vary significantly from their fair value.



The Management Board estimates that the fair value of long-term receivables does not materially differ from their carrying amount because no material changes have occurred in risk margins of the borrowers. The fair value of receivables is measured using the discounted cash flow method in accordance with IFRS 7 on the basis of Level 3 inputs of the fair value hierarchy.

The fair value of trade receivables (31.12.2018: EUR 10,235 thousand; 31.12.2017: EUR 10,580 thousand) related to Balsiu– equals their carrying amount, as the impact of discounting is not significant. The carrying amount of future receivables related to Balsiu School is EUR 23,986 thousand (31.12.2017: EUR 25,440 thousand) and the fair value of the mentioned receivables is equal to EUR 23,347 thousand using the effective interest rate of 0.31% (31 December 2017: EUR 24,724 thousand using the effective interest rate of 0.31%). As the amount receivable is due from the state institution, the interest rate used for the fair value calculation is a long-term borrowing rate at the end of the period applicable to the Republic of Lithuania (www.ecb.europa.eu/stats/financial_markets_and_interest_rates/long_term_interest_rates). Long-term receivables related to Balsiu School are valued on the basis of Level 2 inputs of the fair value hierarchy.

A significant part of the group's long-term payables have a floating interest rate, which changes according to fluctuations of the market interest rate. In the estimation of the management, the group's risk margins have not materially changed since the loans were obtained and the interest rates on the group's debt meet the market conditions. The fair value of long-term financial obligations is determined based on discounted future contractual cash flows using the market interest rate available to the group for the use of similar financial instruments (Level 3).

To provide an indication of the inputs used to determine fair value, the group has classified its financial instruments into three levels based on the requirements of accounting standards.

Level 1: Financial instruments valued at unadjusted prices on the stock market or other active regulated market. As at 31 December 2018 and 2017, the group did not have any Level 1 financial instruments.

Level 2: Financial instruments whose values are based on valuation methods based on observable inputs. This category includes e.g. financial instruments valued based on prices of identical instruments traded on an active regulated market or financial instruments which are revalued at regulated market price but have low liquidity on the stock market.

Level 3: Financial instruments where the valuation methods used for revaluation are based on non-observable inputs.

CAPITAL MANAGEMENT

The group considers borrowings and total equity as capital. As at 31 December 2018, the total equity attributable to equity owners of the parent was EUR 131,757 thousand (31.12.2017: EUR 130,170 thousand). The group's principle is to maintain a strong equity base for the purpose of 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 increase income for its shareholders and ensure its ability to pay dividends.

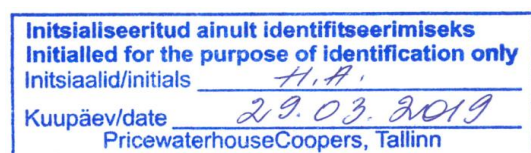
The group's equity is currently mainly tied up in the land plots portfolio invested in for the purpose of real estate development, which the group has realised according to the changes in the market primarily through its own developments. The group can additionally regulate the equity structure through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

The group considers it important to ensure an optimal capital structure. Therefore, it monitors that the group's equity to assets ratio is at least 40% (31.12.2018: 48.9%, 31.12.2017: 47.0%).

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

	31.12.2018	31.12.2017
Borrowings	44,166	59,356
Less: cash and cash equivalents and short-term deposits	(39,978)	(39,210)
Net debt	4,188	20,146
Total equity attributable to owners of the parent	131,757	130,170
Total net debt and equity attributable to equity owners of the parent	135,945	150,316
Share of net borrowings	3.1%	13.4%

The group's net debt at 31 December 2018 stood at EUR 4.2 million (31.12.2017: EUR 20.1 million).



MANAGEMENT OF OTHER RISKS

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 group's activities from the perspective of laws or contracts from a different position and dispute the legitimacy of the group's activities.

As at 31 December 2018, a provision has been set up at the group in the amount of EUR 120 thousand for covering potential claims and legal costs (31.12.2017: EUR 120 thousand) (Note 29).

An overview of the key legal disputes of group entities ended during 2018 and ongoing as of 31 December 2018 is presented below.

ESTONIA

Lawsuit against former employee

On 17 December 2014, AS Merko Infra filed a claim in Harju County Court against a former AS Merko Infra employee, Maksim Vihharev, seeking EUR 97 thousand in damages along with a petition to secure the action. The lawsuit relates to intentional damage caused by fictitious transactions concluded by Maksim Vihharev on behalf of AS Merko Infra while serving as electrical work project manager and purchase of items not necessary for contractual work. On 6 September 2018, a ruling of the Tallinn Circuit Court entered into force, under which Maksim Vihharev was ordered to pay AS Merko Infra damages of EUR 92 thousand, plus late interest on that amount starting from 17 December 2014 at the rate set forth in the second sentence of subsection 113 (1) of the Law of Obligations Act, until the payment of the damages. The circuit court also ordered Vihharev to pay AS Merko Infra procedural costs totalling EUR 34 thousand.

Appeal for the revocation of the order of the Minister of the Environment

Several court cases are ongoing in connection with Minister of the Environment regulation No 22 of 27 March 2015, which redrew the boundaries of species protection sites to exclude properties on Paekalda street owned by AS Merko Ehitus subsidiaries Suur-Paekalda OÜ and Väike-Paekalda OÜ (now merged with AS Merko Ehitus Eesti, part of AS Merko Ehitus group). On 2 February 2016, AS Merko Ehitus group companies, Suur-Paekalda OÜ and Väike-Paekalda OÜ, filed a complaint in Tallinn Administrative Court for compensation of damage. The plaintiffs are seeking a ruling ordering that the state pay damages of approximately EUR 3.2 million to Suur-Paekalda OÜ (exact amount to be determined) and approximately EUR 1.6 million to Väike-Paekalda (exact amount to be determined) as well as late interest at the rate specified in subsection 113 (1) of the Law of Obligations Act starting from 2 February 2016 until due compliance with the demand for compensation. The claims consist of direct patrimonial damage (reduction in the value of immovable property and expenditures made on development activity) and claims for revenue foregone (failed development activity in 2005-2007). In 2019, an interim court ruling by Tallinn Administrative Court is expected about the determination of the legal basis for the claim. After that the litigation will continue to determine the amount of the damage. The possible positive impact of the claim submitted has not been recognized by the group in its financial statements.

LATVIA

Lawsuit against former employee

On 5 May 2015, SIA Merks filed suit in Riga District Court against former SIA Merks employee Rolands Mēnesis in a claim for the compensation of damage amounting to EUR 337 thousand. The object of the statement of claim is damage deliberately caused by project manager Rolands Mēnesis by entering into fictitious transactions on behalf of SIA Merks and purchase of items not necessary for contractual work. The new court hearing is scheduled on 5 June 2019.

The possible effect of the potential positive outcome of this claim has not been taken into account in the group's financial reporting.

Starptautiskā lidosta "Rīga"

On 21 September 2017, SIA Merks has initiated court proceedings against VAS "Starptautiskā lidosta "Rīga"" (Riga International Airport). The basis of the court proceeding is a dispute with Riga International Airport on the terms and conditions of signing the final completion certificate of the new passenger terminal of Riga International Airport. SIA Merks seeks court decision requiring Riga International Airport to sign the final completion certificate and thus entitling SIA Merks for payment of EUR 449 thousand (EUR 414 thousand being the principal claim and EUR 35 thousand late interest) for the works.

On 5 March 2018, SIA Merks prepared an additional claim to the court to confirm that the works are fully and properly performed and should be duly accepted by Riga International Airport and, releasing the retention money for the warranty period guarantee in the amount of EUR 920 thousand.

On 8 June 2018, Riga International Airport paid partly the claim submitted on September 21, 2017, therefore SIA Merks reduced the claim to EUR 248 thousand (EUR 76 thousand being the principal claim and EUR 172 thousand late interest). On 11 December 2018 was decided to take independent expert and new court hearing is scheduled on 20 May 2019. No additional provisions are recognised in relation to the potential outcome of this claim.

LITHUANIA

Vilniaus vandenys

On 18 May 2016, AS Merko Ehitus and UAB Merko Statyba, acting pursuant to the joint venture agreement, filed an action against UAB Vilniaus vandenys in the total amount of EUR 183 thousand. The plaintiffs maintain that due to the actions of UAB Vilniaus vandenys,

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both the construction period became longer and also additional works were carried out – works that the customer later refused to pay for. By decision of 9 January 2018, the court appointed an expertise, the result of which was submitted on 14 December 2018. The next court hearing will take place on 9 May 2019. The potential positive outcome of this claim is not recognised in the group's financial reporting.

UAB Axis

On 3 September 2018, UAB Axis power (sub-contractor) filed an action against UAB Merko Statyba (main contractor), part of AS Merko Ehitus group, in the total amount of EUR 846 thousand as compensation for carrying out concrete works, which were more complicated than foreseen at signing of the contract. Court hearing is scheduled on 25 April 2019. The group finds the claim unsubstantiated and has not recognised provisions in relation to this claim.

VALUE OF ASSETS

Although the economic environment has attained certain stability, the effect of the real estate market risk remained material for assessing the group's activities. In 2018, the group recognised EUR 658 thousand (2017: EUR 2,838 thousand) in impairment losses on assets and inventories, incl. impairment loss of EUR 300 thousand (2017: EUR 2,360 thousand) on finished goods, EUR 66 thousand from the impairment of tangible assets (2017: EUR 235 thousand impairment of goodwill recognised under intangible assets, no impaired of tangible assets), EUR 90 thousand (2017: EUR 114 thousand) on the write-off of doubtful and irrecoverable receivables and EUR 202 thousand loss from write-off of prepayments to suppliers (2017: EUR 129 thousand). In 2018, no reversal of previous period impairment losses were made (2017: EUR 5,276 thousand). The receivables expensed in prior periods in the amount of EUR 94 thousand were collected (2017: EUR 238 thousand). See also Notes 16, 18, 24 and 25 for further details.

NOTE 36 SUPPLEMENTARY DISCLOSURES ON THE PARENT COMPANY

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

in thousands of euros

	2018	2017
Revenue	4,797	16,431
Cost of goods sold	(4,112)	(13,075)
Gross profit	685	3,356
Marketing expenses	(60)	(80)
General and administrative expenses	(1,891)	(1,713)
Other operating income	25,430	1,010
Other operating expenses	(245)	(158)
Operating profit (loss)	23,919	2,415
Finance costs	(182)	(355)
Finance income from investments in subsidiaries	20,322	7,324
Profit before tax	44,059	9,384
Deferred income tax expense	-	(14)
Net profit for the year	44,059	9,370

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STATEMENT OF FINANCIAL POSITION

in thousands of euros

	31.12.2018	31.12.2017
ASSETS		
Current assets		
Cash and cash equivalents	7,979	1,183
Receivables and prepayments	1,081	9,564
Inventories	746	25,730
	9,806	36,477
Non-current assets		
Investments in subsidiaries	123,332	136,111
Investments in joint ventures	-	5
Other long-term financial assets	44,831	3,599
Investment properties	-	17
Property, plant and equipment	155	44
Intangible assets	108	112
	168,426	139,888
TOTAL ASSETS	178,232	176,365
LIABILITIES		
Current liabilities		
Borrowings	1,032	12,004
Trade and other payables	1,516	15,133
Short-term provisions	16	27
	2,564	27,164
Non-current liabilities		
Long-term borrowings	5,115	5,007
	5,115	5,007
TOTAL LIABILITIES	7,679	32,171
EQUITY		
Share capital	7,929	7,929
Statutory reserve capital	793	793
Retained earnings	161,831	135,472
TOTAL EQUITY	170,553	144,194
TOTAL LIABILITIES AND EQUITY	178,232	176,365

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STATEMENT OF CHANGES IN EQUITY

in thousands of euros

Parent	Share capital	Statutory reserve capital	Retained earnings	Total
Balance as at 31.12.2016	7,929	793	133,359	142,081
Net profit for financial year	-	-	9,370	9,370
Dividends	-	-	(7,257)	(7,257)
Balance as at 31.12.2017	7,929	793	135,472	144,194
Carrying amount of holdings under control or significant influence				(136,116)
Value of holdings under control or significant influence under the equity method				122,092
Adjusted unconsolidated equity 31.12.2017				130,170
Net profit for financial year	-	-	44,059	44,059
Dividends	-	-	(17,700)	(17,700)
Balance as at 31.12.2018	7,929	793	161,831	170,553
Carrying amount of holdings under control or significant influence				(123,332)
Value of holdings under control or significant influence under the equity method				84,536
Adjusted unconsolidated equity 31.12.2018				131,757

Adjusted unconsolidated equity is used as the basis for verifying compliance with equity requirements set forth in the Commercial Code.

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CASH FLOW STATEMENT

in thousands of euros

	2018	2017
Cash flows from operating activities		
Operating profit (loss)	23,919	2,415
Adjustments:		
Depreciation and impairment	46	38
(Profit)/loss from sale of non-current assets	(3)	-
(Profit) from transfer of the field of real estate development	(24,519)	-
Change in receivables and liabilities related to construction contracts	-	80
Interest income from business activities	(900)	(683)
Change in provisions	22	(1,010)
Change in trade and other receivables related to operating activities	(19,592)	(3,241)
Change in inventories	4,006	10,394
Change in trade and other payables related to operating activities	(168)	1,231
Interest received	216	531
Interest paid	(169)	(415)
Other finance income and costs	(17)	-
Corporate income tax paid	(7)	-
Total cash flows from operating activities	(17,166)	9,340
Cash flows from investing activities		
Acquisition of subsidiaries	-	(2,743)
Investments in subsidiaries	(38,601)	(13,636)
Disposal of subsidiary	400	-
Reduction of equity in subsidiary	17,387	12,417
Purchase of property, plant and equipment	-	(5)
Proceeds from sale of property, plant and equipment	6	-
Purchase of intangible assets	(15)	(38)
Transfer of the field of real estate development	53,322	-
Interest received	1	4
Dividends received	20,165	7,324
Total cash flows from investing activities	52,665	3,323
Cash flows from financing activities		
Proceeds from borrowings	-	26,771
Loan repayments received	(10,974)	(32,409)
Finance lease principal payments	(29)	(19)
Dividends paid	(17,700)	(7,257)
Total cash flows from financing activities	(28,703)	(12,914)
Net increase/decrease in cash and cash equivalents	6,796	(251)
Cash and cash equivalents in the beginning of period	1,183	1,434
Cash and cash equivalents at end of the period	7,979	1,183

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SIGNATURES OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD TO THE 2018 ANNUAL REPORT

The Management Board of AS Merko Ehitus has prepared the management report, the consolidated financial statements and the profit allocation proposal for 2018.

Andres Trink	Chairman of the Management Board		29.03.2019
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Tõnu Toomik	Member of the Management Board	29.03.2019
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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 independent 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		09.04.2019
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Teet Roopalu	Member of the Supervisory Board	09.04.2019
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Indrek Neivelt	Member of the Supervisory Board	09.04.2019
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Independent auditor's report

To the Shareholders of AS Merko Ehitus

(Translation of the Estonian original)*

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of AS Merko Ehitus and its subsidiaries (together the Group) as at 31 December 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2018;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated cash flow statement for the year then ended;
- the consolidated statement of changes in equity for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report.

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

Independence

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Auditors Activities Act of the Republic of Estonia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the ethical requirements of the Auditors Activities Act of the Republic of Estonia.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Group are in accordance with the applicable law and regulations in the Republic of Estonia and that we have not provided non-audit services that are prohibited under § 591 of the Auditors Activities Act of the Republic of Estonia. During 2018, we have provided to the Group tax and general advisory services.

Our audit approach

Overview



Materiality

Overall group audit materiality is EUR 3,5 million, which represents approximately 0.8% of consolidated total revenue.

Audit scope

A full scope audit was performed by us or, under our instructions, by PwC network firms for Group entities covering 97% of the Group's revenues and 97% of the Group's assets. Selected audit procedures were performed on remaining balances to ensure we obtained sufficient appropriate audit evidence to express an opinion on the Group's financial statements as a whole.

Key audit matters

- Revenue recognition on construction contracts
- Valuation of inventory relating to property developments

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where the Management Board made subjective judgments; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgment, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall group audit materiality	EUR 3,5 million
How we determined it	0.8% of total revenues
Rationale for the materiality benchmark applied	We have used revenue as in our view this is one of the key metrics used both internally by management as well as, we believe, externally by investors and lenders, in evaluating the performance of the Group.



Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters

How our audit addressed the key audit matters

Revenue recognition on construction contracts (refer to Note 1 'Summary of significant accounting policies – subsections 1.20 'Revenue' and Note 4 'Operating Segments' for further details).

In 2018 the Group has recognised revenue of EUR 418 million, EUR 362.9 million of which is related to construction services.

New revenue standard, IFRS 15, that changed certain aspects of revenue recognition, became effective from 1 January 2018.

The Group's revenues from construction services are generated from a large portfolio of contracts with different terms regarding service fee, use of subcontractors or partners and profit sharing. Revenue from construction contracts is recorded by reference to the progress towards satisfaction of performance obligations (stage of completion). Determining the stage of completion requires the management to estimate the cost to complete the contract, as well as any possible adjustments to the contractual fee, at each measurement date.

Accounting estimates have subjective nature and rely on many sources of information, both within the Group and external, about the expected outcome of a contract. The complexity resulting from both the large number of varying contractual terms and estimation uncertainties regarding the expected outcome of construction contracts could lead to errors that may become material, when aggregated.

As such, revenue recognition on construction contracts requires significant time and resource to audit due to both its magnitude and complexity, and is therefore considered to be a key audit matter.

We audited revenue recognition on construction contracts through a combination of controls testing and substantive testing.

We assessed if Group had appropriately applied the guidance in the new revenue standard, IFRS 15 regarding accounting for revenue, including for revenue recognised over time.

We performed testing of the design, implementation and operating effectiveness of controls supporting identification of contractual terms, selection of suitable accounting policies and assessment of the stage of completion. We did not identify any exceptions that impacted our audit approach.

The controls testing was supported by substantive audit procedures. We selected a sample of contracts and performed substantive procedures that included, but were not limited to:

- reconciling the contract fee used in calculating the revenue based on the stage of completion to the contract;
- reconciling incurred contract costs included in revenue calculation to accounting records and testing the proper allocation of costs to individual contracts;
- testing correct periodisation of contract costs;
- checking the formula used for calculation of revenue based on stage of completion;
- investigating the estimates of margins during current and comparative periods applied for revenue calculation of the same contracts to identify potential management bias.

We also evaluated the correctness of disclosures in relation to the construction contracts. As a result of our work, we found no material exceptions.



Valuation of inventory relating to property developments (refer to Note 1 'Summary of significant accounting policies – subsection 1.11 'Inventories', Note 18 'Inventories' and Note 35 'Risk management' subsection 'value of assets' for further details).

As at 31 December 2018 the Group's balance sheet includes inventory in the amount of EUR 118 million, of which EUR 16 million were finished apartments, EUR 43.1 million unfinished apartments and EUR 54.5 million land purchased for development and resale (mostly with the aim of being developed as residential property).

Inventories are carried at the lower of cost and net realisable value.

With property prices, especially those of residential property, following the economic cycle and exhibiting substantial fluctuation over time, net realisable value of the inventory of finished and unfinished apartments and property for resale needs to be carefully monitored against the carrying amount. Should the net realisable value of a property fall below its carrying amount, a write-down to net realisable value is necessary. Determining the net realisable value of property requires estimates of the expected selling price and may require estimates of the cost to complete the development of the property.

Due to the magnitude and related estimation uncertainty, valuation of inventory of finished and unfinished apartments and land to be developed for sale is considered a key audit matter.

We assessed the management's expertise to perform valuation of property. The management is experienced in property valuation and the outcomes of completed development projects have usually met the profitability estimates.

We evaluated the model prepared by the management for determining the net realisable value and identifying any necessary write-down. We validated that the valuation model is in accordance with IFRS requirements.

We performed testing of the inputs used in the valuation model. Our work targeted individual properties on our assessment of the risk, based on the location, carrying amount and any specific conditions related to a property. For inputs based on estimates, which include unit costs applicable for completing the construction and sales price, we assessed the reasonableness of the inputs by comparing them with historical data from completed projects and available market information such as construction price indexes. Where available, we compared the estimated sales prices with comparable market transactions.

It was evident from our work that sufficient attention had been paid to each property's individual characteristics including their construction quality, geographic location and relevant legal or contractual obligations.

We also read the disclosures provided in respect of net realisable value of inventory, including sensitivity analysis, and found them to comply with IFRS requirements.

We concluded that the assumptions used in the management's valuations were supportable in light of available property-specific and market evidence. As a result of our work, we noted no material exceptions.

How we tailored our audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

The Group comprises a number of subsidiaries that are further disclosed in Note 19. A full scope audit was performed by PwC Estonia or, under our instructions, by other PwC network firms for entities covering 97% of the Group's assets and 97% of the Group's revenues. The remaining entities of the Group were immaterial, therefore we only performed selected audit procedures on these components relating to specified account balances or disclosures.



Where work was performed by component auditors from another PwC network firm, we determined the level of involvement we needed to have to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group financial statements as a whole. The nature, timing and extent of the work impacting the Group audit opinion is set and monitored in Estonia, with input from the teams outside Estonia at the risk assessment stage.

At the Group level we also audited the consolidation process. We also evaluated whether significant risk of material misstatement existed, using analytical procedures in relation to the aggregated financial information of the remaining entities not subject to audit or audit of specified account balances, including comparing their account balances to those present at the time of deciding the audit scope.

Other information

The Management Board is responsible for the other information contained in the Group's Consolidated Annual Report in addition to the consolidated financial statements and our auditor's report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Management Board and those charged with governance for the consolidated financial statements

The Management Board is responsible for the preparation and fair presentation of the 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.

In preparing the consolidated financial statements, the Management Board is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Management Board either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.



As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management Board.
- Conclude on the appropriateness of the Management Board's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.



Report on other legal and regulatory requirements

Appointment and period of our audit engagement

We were first appointed as auditors of AS Merko Ehitus, as a public interest entity, for the financial year ended 31 December 2008. Our appointment has been renewed by tenders and shareholder resolutions in the intermediate years, representing the total period of our uninterrupted engagement appointment for AS Merko Ehitus, as a public interest entity, of 11 years.

AS PricewaterhouseCoopers

A handwritten signature in blue ink, appearing to read 'Ago Vilu', with a long horizontal stroke extending to the right.

Ago Vilu

Certified auditor in charge, auditor's certificate no.325

A handwritten signature in blue ink, appearing to read 'Janno Hermanson', with a large, looping initial 'J' and a long horizontal stroke extending to the right.

Janno Hermanson

Auditor's certificate no.570

29 March 2019

** 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.*

PROFIT ALLOCATION PROPOSAL

in euros

Total retained earnings as at 31.12.2018	123,756,119
incl. net profit for 2018	19,342,762

The Management Board proposes profit allocation as follows:

Dividends (EUR 1.00 per share)	17,700,000
Retained earnings after profit allocation	106,056,119

Andres Trink

Chairman of the Management Board



29.03.2019

Tõnu Toomik

Member of the Management Board



29.03.2019

OTHER NOTES TO THE ANNUAL REPORT

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KEY FINANCIAL INDICATORS IN 2014-2018

CONSOLIDATED INCOME STATEMENT

in thousands of euros

	2018	2017	2016	2015	2014
Revenue	418,011	317,598	251,970	251,012	252,323
Cost of goods sold	(384,962)	(286,747)	(232,961)	(228,044)	(227,591)
Gross profit (loss)	33,049	30,851	19,009	22,968	24,732
<i>% of revenue</i>	7.9%	9.7%	7.5%	9.1%	9.8%
Marketing expenses	(3,285)	(3,215)	(3,281)	(3,230)	(3,190)
General and administrative expenses	(12,304)	(11,289)	(10,076)	(8,907)	(9,128)
Other operating income	3,527	3,793	2,466	1,943	1,901
Other operating expenses	(1,115)	(601)	(399)	(278)	(340)
Operating profit (loss)	19,872	19,539	7,719	12,496	13,975
<i>% of revenue</i>	4.8%	6.2%	3.1%	5.0%	5.5%
Finance income	8	4	46	120	143
Finance costs	(696)	(849)	(649)	(786)	(680)
Profit (loss) from joint ventures	591	78	163	(138)	(130)
Profit (loss) before tax	19,775	18,772	7,279	11,692	13,308
<i>% of revenue</i>	4.7%	5.9%	2.9%	4.7%	5.3%
Corporate income tax expense	(375)	(3,020)	(1,275)	(1,857)	(1,055)
Net profit (loss) for the financial year	19,400	15,752	6,004	9,835	12,253
incl. attributable to equity holders of the parent	19,343	14,694	6,122	10,000	12,417
<i>% of revenue</i>	4.6%	4.6%	2.4%	4.0%	4.9%
Attributable to non-controlling interests	57	1,058	(118)	(165)	(164)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	31.12.2018	31.12.2017	31.12.2016	31.12.2015	31.12.2014
ASSETS					
Current assets					
Cash and cash equivalents	39,978	39,210	33,544	39,905	51,583
Trade and other receivable	76,183	75,844	45,566	24,854	46,382
Prepaid corporate income tax	224	492	617	421	3
Inventories	117,992	118,421	123,364	109,090	117,638
	234,377	233,967	203,091	174,270	215,606
Non-current assets					
Investments in joint ventures	732	79	434	284	67
Other long-term loans and receivables	10,391	17,163	15,371	16,419	11,409
Deferred income tax assets	-	5	1,325	1,423	1,535
Investment properties	13,771	15,719	4,108	4,371	4,619
Property, plant and equipment	9,715	9,665	12,838	13,442	15,003
Intangible assets	671	497	673	879	1,011
	35,280	43,128	34,749	36,818	33,644
TOTAL ASSETS	269,657	277,095	237,840	211,088	249,250
LIABILITIES					
Current liabilities					
Borrowings	19,900	24,218	21,485	5,525	14,287
Payables and prepayments	77,016	74,972	56,259	43,266	71,122
Corporate income tax liability	381	413	278	711	352
Short-term provisions	8,100	4,569	5,637	5,013	6,239
	105,397	104,172	83,659	54,515	92,000
Non-current liabilities					
Long-term borrowings	24,266	35,138	24,516	25,660	23,359
Deferred income tax liability	1,481	1,259	1,122	788	738
Other long-term payables	2,179	1,789	2,061	1,159	1,671
	27,926	38,186	27,699	27,607	25,768
TOTAL LIABILITIES	133,323	142,358	111,358	82,122	117,768
EQUITY					
Non-controlling interests	4,577	4,567	3,692	3,268	4,455
Equity attributable to equity holders of the parent					
Share capital	7,929	7,929	7,929	7,929	12,000
Statutory reserve capital	793	793	793	1,200	1,200
Currency translation differences	(721)	(702)	(645)	(663)	(665)
Retained earnings	123,756	122,150	114,713	117,232	114,492
	131,757	130,170	122,790	125,698	127,027
TOTAL EQUITY	136,334	134,737	126,482	128,966	131,482
TOTAL LIABILITIES AND EQUITY	269,657	277,095	237,840	211,088	249,250

OTHER KEY FIGURES

attributable to equity holders of the parent

		2018	2017	2016	2015	2014
EBITDA	million EUR	21.9	22.2	11.2	15.5	16.4
EBITDA margin	%	5.2	7.0	4.4	6.2	6.5
General expense ratio	%	3.7	4.6	5.3	4.8	4.9
Staff costs ratio	%	8.2	10.1	11.7	12.2	11.9
Revenue per employee	thousand EUR	563	434	325	322	319
ROE	%	15.3	11.9	5.0	8.0	10.1
ROA	%	6.9	5.8	2.8	4.4	5.0
ROIC	%	11.5	11.4	5.1	7.9	8.8
Equity ratio	%	48.9	47.0	51.6	59.5	51.0
Debt ratio	%	16.4	21.4	19.3	14.8	15.1
Current ratio	times	2.2	2.2	2.9*	3.2	2.3
Quick ratio	times	1.1	1.1	1.1*	1.2	1.1
Accounts receivable turnover	days	40	40	37	39	56
Accounts payable turnover	days	41	40	38	39	39
Number of employees 31.12	people	764	757	797	791	765
Average number of employees	people	743	732	776	779	790
Secured order book	million EUR	229	344	270	247	179
New contracts signed	million EUR	246	335	202	247	170

* As at 31 December 2016, in the formula for calculating the current ratio and the quick ratio, the amount of current liabilities has been reduced by EUR 12.5 million as a result of refinancing of the short-term loan received from the parent company AS Riverito at the end of 2016 with long-term bank loans at the beginning of 2017.

SHARE-RELATED KEY FIGURES

attributable to equity holders of the parent

		2018	2017	2016	2015	2014
Earnings per share (EPS)	EUR	1.09	0.83	0.35	0.56	0.70
Equity per share	EUR	7.16	6.99	6.90	7.02	6.93
Dividend per share	EUR	1.00*	1.00	0.41	0.51	0.41
Dividend rate	%	92*	120	119	90	58
Dividend yield	%	10.9*	11.4	4.5	6.0	5.7
P/E ratio	times	8.42	10.61	26.17	15.01	10.18
P/B ratio	times	1.28	1.26	1.31	1.21	1.03
Share price trend						
Average	EUR	10.02	9.27	8.44	8.47	7.33
Highest	EUR	11.80	9.69	9.22	10.50	7.99
Lowest	EUR	8.70	8.75	7.60	7.06	6.70
Share price 31.12	EUR	9.20	8.81	9.05	8.48	7.14
Market value 31.12	million EUR	162.8	155.9	160.2	150.1	126.4
Share turnover trend						
Share turnover	million EUR	12.16	4.69	5.35	7.71	7.62
Transactions	pcs	4,299	2,203	2,312	2,829	1,699
Shares traded	million pcs	1.18	0.51	0.63	0.90	1.03
Ratio of shares traded	%	6.7	2.9	3.6	5.1	5.8
Number of shares	million pcs	17.70	17.70	17.70	17.70	17.70
Number of shareholders 31.12	pcs	2,664	2,040	1,813	1,624	1,423

* Pursuant to the Management Board's proposal regarding dividend payment.

DEFINITIONS OF RATIOS

Gross profit margin (%)	=	$\frac{\text{Gross profit}}{\text{Revenue}}$
Operating profit margin (%)	=	$\frac{\text{Operating profit}}{\text{Revenue}}$
EBT margin (%)	=	$\frac{\text{Earnings before tax}}{\text{Revenue}}$
Net profit margin (%)	=	$\frac{\text{Net profit (attributable to equity holders of the parent)}}{\text{Revenue}}$
Return on equity, ROE (%)	=	$\frac{\text{Net profit (attributable to equity holders of the parent) of the current 4 quarters}}{\text{Shareholders equity (average of the current 4 quarters)}}$
Return on assets, ROA (%)	=	$\frac{\text{Net profit (attributable to equity holders of the parent) of the current 4 quarters}}{\text{Total assets (average of the current 4 quarters)}}$
Return on invested capital, ROIC (%)	=	$\frac{\text{(Profit before tax + interest expense - foreign exchange gain (loss) + other financial income) of the current 4 quarters}}{\text{(Shareholders equity (average) + interest-bearing liabilities (average)) of the current 4 quarters}}$
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)	=	$\frac{\text{Trade receivables of the current 4 quarters (average)} \times 365}{\text{Revenue of the current 4 quarters}}$
Accounts payable turnover (days)	=	$\frac{\text{Payables to suppliers of the current 4 quarters (average)} \times 365}{\text{Cost of goods sold of the current 4 quarters}}$
EBITDA (million EUR)	=	Operating profit + depreciation
EBITDA margin (%)	=	$\frac{\text{Operating profit + depreciation}}{\text{Revenue}}$
General expense ratio (%)	=	$\frac{\text{Marketing expenses + General and administrative expenses}}{\text{Revenue}}$
Labour cost ratio (%)	=	$\frac{\text{Labour costs}}{\text{Revenue}}$
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)	=	$\frac{\text{Shareholders equity (average of the current 4 quarters)}}{\text{Number of shares}}$
Dividend per share (EUR)	=	$\frac{\text{Payable dividends}}{\text{Number of shares}}$
Dividend rate (%)	=	$\frac{\text{Payable dividends} \times 100}{\text{Net profit (attributable to equity holders of the parent)}}$
Dividend yield (%)	=	$\frac{\text{Dividends payable per share}}{\text{Share price 31.12}}$
P/E	=	$\frac{\text{Share price 31.12}}{\text{Earnings per share of the current 4 quarters}}$
P/B	=	$\frac{\text{Share price 31.12}}{\text{Equity per share (average of the current 4 quarters)}}$
Market capitalisation	=	Share price 31.12 x Number of shares
Ratio of shares traded	=	$\frac{\text{Number of shares traded during the year}}{\text{Number of shares in total}}$
Injury rate (per 100 employees)	=	$\frac{\text{Total number of injuries/accidents excluding minor (first-aid level) injuries/accidents} \times 200\,000}{\text{Total number of working hours per year}}$
Occupational diseases rate(per 100 employees)	=	$\frac{\text{Total number of occupational illnesses} \times 200\,000}{\text{Total number of working hours per year}}$
Lost days rate (per 100 employees)	=	$\frac{\text{Total number of lost days due to occupational illnesses/injuries/accidents} \times 200\,000}{\text{Total number of working hours per year}}$
Absentee rate per year	=	$\frac{\text{Total number of absentee days}}{\text{Calculated number of total working days per year}}$

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 2018 is presented according to Estonian Classifications of Economic Activities (EMTAK 2008), as required under the Commercial Code § 4 p.6:

in thousands of euros

EMTAK code		2018	2017
	Rendering of construction services		
4221	construction of utility projects for fluids	-	58
	Real estate activities		
6810	sales of own real estate	4,735	16,261
6820	renting and operating of own or leased real estate	62	112
		4,797	16,431
	Total revenue	4,797	16,431

SUSTAINABLE DEVELOPMENT REPORT

SUSTAINABILITY REPORTING PRINCIPLES



The Annual Report of Merko Ehitus group is prepared based on the international integrated reporting framework and the Global Reporting Initiative (GRI) Standards. The purpose of the Annual Report is to provide a clear overview and description of how Merko Ehitus creates additional value to its customers, shareholders and other stakeholders, while highlighting the key factors of the value chain process. The Annual Report does not focus only on past events, but is more focused, through integrated reporting, on the horizon ahead. We aim to give the reader a better overview of the strategy, long-term objectives and sustainability of AS Merko Ehitus group as a whole.

Key economic, social responsibility and environmental aspects have been presented by using the integrated reporting principle, in the different sections and notes to the annual report.

Compared to the 2017 report, the transition from the GRI G4 guidelines to the GRI Standards took place, resulting in changes in the wording and data (indexes) of key topics. In preparing the report, Merko Ehitus has focused on the key subjects of the group companies, depending on the specifics of their business, which are:

- Economic Performance;
- Market Presence;
- Indirect Economic Impacts;
- Procurement Practices;
- Anti-corruption;
- Materials;
- Energy;
- Waste;
- Environmental Compliance;
- Employment;
- Occupational Health and Safety;
- Training and Education;
- Local Communities;
- Political Contributions.

Further information on the internationally integrated reporting framework and GRI Standards can be acquired on websites www.integratedreporting.org and www.globalreporting.org.

STAKEHOLDERS

The Merko Ehitus group has mapped its primary stakeholder groups: Merko group employees, shareholders and investors, customers for construction service and apartment buyers, local government units and public organisations, cooperation partners, subcontractors and suppliers and the public. Stakeholders are mapped and selected based on the standpoint of both the company and the stakeholder, taking into account cooperation between the parties and the impact of the company on the stakeholder.

The primary principles for disclosure of information at Merko are continuity, neutrality, transparency, integrity and fairness and preventive approach. Various channels have taken shape for communicating with different stakeholders:

Employees	Everyday cooperation and communication with the company's colleagues and managers at various levels, annual performance reviews, company's website, Intranet and newsletter, company information days and other events, in-house trainings and social media.
Shareholders, investors, banks	Stock market system and press releases, website section aimed at investors, investor meetings, materials and events.
Customers and apartment buyers	Everyday cooperation and communication in the course of the construction process, feedback from customers and satisfaction surveys, company's website, public communication. Additional communication channels for apartment buyers: apartment development project website and sales materials, sales director and, in the case of some projects, sales office, customer days, model apartment, social media, satisfaction surveys.
Partners in cooperation, subcontractors and suppliers	Everyday cooperation and communication in the course of the construction process, meetings and events, public communication.
Local governments and public organisations	Meetings, public communication.
Broader public	Social responsibility and support and cooperation projects, cooperation with different organisations, public communication, social media.

GRI CONTENT INDEX

Standard	Disclosure	Page	Information
GRI 102: General Disclosures			
ORGANISATIONAL PROFILE			
102-1	Name of the organisation	p. 2	
102-2	Products, services and trademarks	p. 4, 8-9, 19, note 4	
102-3	Location of headquarters	p. 2	
102-4	Location of operations	p. 4, 19, note 19	
102-5	Ownership and legal form	p. 4, 42-44, 46-50	
102-6	Markets served	p. 4, 19, note 4	
102-7	Scale of the organisation	p. 4, 11, 32	
102-8	Basic information on employees	p. 32	
102-9	Supply chain		Merko Ehitus group companies use suppliers and subcontractors extensively in its operations in all of the countries it operates. The materials used in construction come from an extensive network of suppliers located mainly in Europe, particularly in the group's current operating countries. Merko Ehitus group companies mainly act as general contractors hence the large extent of the workforce used in construction, with the exception of project management, comes from the subcontractor network. Subcontractors and their workforce are largely from the group's operating countries.
102-10	Significant changes during the reporting period		-
102-11	Precautionary Principle or approach	p. 30-31, 36-37	
102-12	External initiatives		No significant commitments to voluntary charters and other initiatives.
102-13	Memberships in associations		Merko Ehitus group companies are members in the following associations and organisations: Estonian Chamber of Commerce and Industry Estonian Association of Construction Entrepreneurs Estonian Waterworks Association Estonia Concrete Association Estonian Association of Electrical Enterprises Estonian Society for Electrical Power Engineering Estonian Asphalt Pavement Association Latvian Chamber of Commerce and Industry Latvian Partnership of Building Contractors Latvian National Real Estate Developers Alliance Latvian Construction Industry Digitalization Association Latvian Association of Civil Engineers Skanste Development Agency Latvian Builders Association Lithuanian Builders Association
STRATEGY			
102-14	CEO's statement	p. 5	The statement does not cover the relevance and strategy of sustainability.
ETHICS AND INTEGRITY			
102-16	Organisation's values, principles, standards, norms of behaviour and codes of ethics	p. 6, 36-39	In addition to Merko Ehitus values, mission and vision, our operations are guided by responsible management and business principles. These are included in the orientation of new personnel and also highlighted in various events and materials for personnel.
GOVERNANCE			
102-18	Governance structure	p. 46-49	
STAKEHOLDER ENGAGEMENT			
102-40	List of stakeholders	p. 124	
102-41	Collective bargaining agreements		Merko Ehitus group does not have general collective bargaining agreements, it complies with company-specific agreements in line with local legislation
102-42	Identification and selection of stakeholders	p. 124	

102-43	Approach to stakeholder engagement	p. 124	
102-44	Key topics and concerns raised	p. 25, 27, 33	Customer satisfaction, grievances about labour practices
REPORTING PRACTICE			
102-45	Entities included in the consolidated financial statements		The report covers all of the Merko Ehitus group's functions, unless otherwise mentioned.
102-46	Defining report content and topic Boundaries	p. 124	
102-47	List of material topics	p. 124	
102-48	Restatements of information		-
102-49	Changes in reporting	p. 124	
102-50	Reporting period		The reporting period is the calendar year, January 1, 2018 – December 31, 2018
102-51	Date of most recent previous report		The most recent previous integrated annual report was published on April 03, 2018.
102-52	Reporting cycle		The report is published annually.
102-53	Contact point		Priit Roosimägi, Head of Group Finance Unit
102-54	Claims of reporting in accordance with the GRI Standards		This report has been prepared in accordance with the GRI Standards (<i>Global Reporting Initiative</i>) Core option.
102-55	GRI Content Index	p. 125-129	
102-56	External assurance		The GRI report has not been assured by a third party.

MATERIAL TOPICS**GRI 201: Economic Performance 2016**

GRI 103-1 to GRI 103-3	Management approach 2016	p. 32	The activities of Merko Ehitus group have a significant economic impact on society and the company's main stakeholders. The group companies are important employers and taxpayers, and the company creates business opportunities for suppliers and subcontractors by its activities. The business activities of Merko Ehitus are long-term by nature. We have made considerable investments into assets, the realisation horizon of which we measure in years. Cooperation with stakeholders is important for the group in order to ensure the sustainability of business activities.
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Direct economic value generated and distributed for stakeholders 2018 (2017)

201-1	Direct economic value generated and distributed	Revenue EUR 418.0 million (317.6)	Suppliers Materials and goods, EUR 70.3 million (60.3) External services EUR 262.2 million (186.4)	Employees 764 employees (757) Labour costs EUR 34.4 million (31.9)
			Investors Dividends EUR 17.7 million (7.3)	Public sector Corporate income tax expense EUR 0.4 million (3.0)

Merko Ehitus group approach to taxes

Group is committed to being a responsible taxpayer in all of its operating countries. It complies with local and international tax regulations, practices and interpretations, as well as requirements concerning tax returns and other documentation. Merko Ehitus group applies the market price principle pursuant to the OECD Transfer Pricing Guidelines and local transfer pricing regulations in the group's internal business transactions.

PAID* TAXES BY COUNTRIES

in thousands of euros

	2018	2017
Estonia	17,999	22,321
Latvia	2,559	4,108
Lithuania	4,706	2,382
Norway	1,234	649
Total	26,498	29,460

* Actually paid and not calculated tax amounts.

PAID* TAXES BY TAX TYPES

in thousands of euros

	2018	2017
Value added tax	12,108	13,978
Taxes on employee wages and fringe benefits	12,894	12,563
Other taxes	1,107	1,667
Corporate income tax	389	1,252
Total	26,498	29,460

* Actually paid and not calculated tax amounts.

GRI 202: Market Presence 2016			
GRI 103-1 to GRI 103-3	Management approach		The success of group's business operations in each home country (Estonia, Latvia, Lithuania, Norway) depends on the local people who are familiar with the business environment and cultures of each country. Although the group's structure is international, in each country we operate as local companies
202-2	Proportion of management hired from the local community at significant locations of operation	p 46-50	The management of the group takes place on a national basis, where managers are generally local and national citizens.
GRI 203: Indirect Economic Impacts 2016			
GRI 103-1 to GRI 103-3	Management approach		As the leading construction company in the Baltics, our economic activity influences the local economic environment significantly. We erect new houses, construct and maintain public roads, install power lines and build substations, also we cooperate with local governments in shaping public spaces. All this renews and improves the overall environment where also economic relations can develop more efficiently and closely, through which value can be created for other market participants.
203-1	Infrastructure investments and services	p. 20-21, 37-38, 41	
203-2	Significant indirect economic impacts	p. 20-23, 37-39	
GRI 204: Procurement Practices 2016			
GRI 103-1 to GRI 103-3	Management approach		The group's business is based on fair and transparent business ethics.
204-1	Proportion of spending on local suppliers at significant locations of operation	p. 4, 76	The materials and services used in construction are generally from the local market or supplied from within the EU. Detailed data is not reported at group level.
GRI 205: Anti-corruption 2016			
GRI 103-1 to GRI 103-3	Management approach		Merko's core values include ethical business activities, and any forms of corruption are unacceptable for the group. All employees of the group have to comply with ethical principles and observe the code of business ethics established in the group.
205-2	Communication and training on anti-corruption policies and procedures	p. 36	Merko continuously provides training and orientation to its personnel on the prevention of corruption and other illegal operating practices. The content and scope of the training depends partly on the role of the persons concerned.

205-3	Confirmed incidents of corruption and actions taken		There were no confirmed incidents of corruption in 2018. In addition to the prevention of corruption, Merko Ehitus group has a principle of investigating all suspected cases of misconduct and deciding on further action based on the results of the investigation.
GRI 301: Materials 2016			
GRI 103-1 to GRI 103-3	Management approach		Due to the fact that construction activities involve the use of many different building materials and products, the efficiency of such use is a significant cost-related area that is constantly in focus. Each construction project is unique; therefore, it is difficult to develop a uniform material efficiency indicator that would accurately reflect the actual level of efficiency. Thus, material efficiency is monitored and managed on an individual project basis. Besides project-bases analysis, Merko Ehitus is also engaged in the broader development of design organisation and technical calculation preparation practices from the viewpoint of material efficiency, focusing on the optimisation of building structures and the choice of materials. In choosing building materials and products, the construction companies in the Merko group follow the principles of ensuring the requirements of Regulation (EU) No 305/2011 and the national legal acts.
GRI 302 Energy 2016			
GRI 103-1 to GRI 103-3	Management approach		The group's main activity is construction management, which is not particularly energy-intensive compared to production activities. The group's business activities include many projects of different types and volume, and energy consumption can therefore vary considerably across periods. In conducting its activities, the company primarily focuses on energy efficiency on a project and unit level, developing various energy-efficient work methods and replacing its vehicles and tools as energy efficiency improves.
301-1	Energy consumption within the organisation	p. 36-37	The group's construction companies comply with the principles of environmental management system standard ISO 14001 and hold the respective certificate. The European Union Member States are obliged to comply with the Energy Efficiency Directive (2012/27/EU), which requires large companies to conduct regular energy audits. The regular energy audits of the Merko group companies have been regularly submitted and declared to be in conformity. An accredited energy auditor would be engaged should the need arise to conduct further energy audits of a large company.
301-2	Energy consumption outside of the organisation	p. 22	The group's energy consumption outside of the organisation is mainly of a local nature and is based on the principles of construction management – sites with larger numbers of workers are mainly located near capitals, i.e. close to where the workers live, while the project management of smaller projects that are located farther away from the headquarters is often concentrated. Such projects are managed from the headquarters, which reduces overall energy consumption, fuel consumption and CO ² emissions. Until 2018, Regulation No. 55 of the Minister of Economic Affairs and Communication was applied in the design of buildings in Estonia. In the future, the design of buildings will be based on Regulation No. 63 of the Minister of Entrepreneurship and Information Technology, the application of which ensures the energy necessary for low energy buildings.
GRI 306: Waste 2016			
GRI 103-1 to GRI 103-3	Management approach		Construction activities, particularly at sites that involve demolitions works, generate large quantities of waste. Similarly to the question of materials and energy, the issue of re-using waste, reducing the volumes of waste and recycling waste is an issue of cost-efficiency for the group, which is managed on a project and unit basis. The waste generated at construction sites is sorted and delivered to a waste handler who holds a waste permit. If possible, waste is re-used depending on local recycling methods. Merko maintains systemic statistical records of the waste generated and submits regular annual waste reports.
GRI 307: Environmental Compliance 2016			
GRI 103-1 to GRI 103-3	Management approach	p. 36-37	
307-1	Non-compliance with environmental laws and regulations		No significant fines and sanctions for non-compliance with environmental regulations during the period.
GRI 401: Employment 2016			

GRI 103-1 to GRI 103-3	Management approach	p.32-36	
401-1	New employee hires and employee turnover	p. 32	The age groups are not gathered at group level.
401-2	Benefits provided to full time employees	p. 35	
GRI 403: Occupational Health and Safety 2016			
GRI 103-1 to GRI 103-3	Management approach	p. 34	
403-2	Rates of injury, fatalities and absenteeism	p. 34	
GRI 404: Training and Education 2016			
GRI 103-1 to GRI 103-3	Management approach	p. 35	
404-2	Programs for skills management and lifelong learning that support the continued employability of employees and assist them in managing career endings	p. 35	
404-3	Employees receiving regular performance and career development reviews	p. 33	
GRI 413: Local Communities 2016			
GRI 103-1 to GRI 103-3	Management approach		Operating in the construction and real estate development sector requires good relations with local communities on whom the company's business activities have an effect. Works at construction sites are organised so as to keep the disturbance of the surrounding residents, businesses and passers-by to a minimum, and those directly affected by construction works are given prior notice of plans to carry out construction works. Upon preparing new real estate developments, consideration is given to the practices of the former users of the development area, and the constructed buildings are surrounded with integral environments that correspond to the expectations of the local communities and suit the overall urban environment.
413-1	Percentage of operations with implemented local community engagement, impact assessments, and development programs	p. 8-9, 37-39, 124	
413-2	Operations with significant actual and potential negative impacts on local communities	p. 37-39, 124	
GRI 415: Political Contributions 2016			
GRI 103-1 to GRI 103-3	Management approach		The group's principle is not to make political donations.
415-1	Contributions to political parties and related institutions		Merko Ehitus group does not support any politicians, political parties or other political institutions.