



CONSOLIDATED ANNUAL REPORT

2019



AS MERKO EHITUS

GROUP

CONSOLIDATED ANNUAL REPORT

01.01.2019 – 31.12.2019

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 Entreprenør 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 5,000 apartments in Estonia, Latvia and Lithuania.



**2019 new contracts signed
EUR 169.6 mln**



**2019 revenue
EUR 326.8 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



**2019 EBITDA
EUR 21.9 mln**



**2019 net profit
EUR 16.3 mln**



**31 December 2019
694 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 ISO 45001



**Estonia's leading builder of
substations**

STATEMENT OF THE CHAIRMAN OF THE MANAGEMENT BOARD

Dear shareholders,

Developments on the Baltic construction and real estate market continued as we expected in 2019. The rapid growth in construction volumes in recent years stabilized and developers have become more cautious in launching new real estate investments. Although state investments into infrastructure remained at the same level as in years past, the share of the public sector orders on the construction market has grown.

The decrease in Merko Group's construction volumes, by more than 20% compared to the record level of 2018, was also expected. The group's sales revenue decreased year-over-year in Estonia and Latvia but remained at the same level in Lithuania and grew in Norway. Almost one-half of the group's revenue came from outside Estonia. In 2019, a number of outstanding major projects in all three Baltic capitals were completed, but new construction orders in the same volume did not take their place in the group's portfolio. The reason for the decrease in construction orders was both the growth of input prices in the construction sector and the group's strategy in selecting construction sites.



ANDRES TRINK
AS MERKO EHITUS
CHAIRMAN OF THE
MANAGEMENT BOARD

On the backdrop of decrease in sales revenue, we were however able to improve the group's profitability and profit before taxes grew by 2.8% compared to a year ago. Profitability was supported by the team's good work and everyday contribution to simplifying processes and reducing errors. Profitability was supported by the increased investments by the group into the apartment development business segment in all three Baltic states, and the greatest growth in investments last year was seen in Lithuania. In recent years, we have put the focus on larger development areas, where we can create an integrated residential environment and launch development projects stage by stage pursuant to demand. In 2019, close to 500 customers became owners of homes built by Merko. The largest projects launched or completed include, in Tallinn, Veerenni, Lahekalda, Noblessneri and Pikaliiva developments; in Riga, Viesturdārzs and Gaiļezera nami; and in Vilnius, Vilneles Slenis and Rinktinės Urban.

Merko's goal is to continue to be the preferred choice for construction service clients and apartment buyers who value quality and trustworthiness. Through the buildings and infrastructure we set up, we create a modern living environment and improve people's quality of life. To this end, we continue giving back to society, examples of which are our long-term cooperation projects in developing the network of Estonian Health Trails, cooperation with the Estonian Tennis Association and the Art Museum of Estonia as well as with various universities. We operate based on the long-term view and put value on quality and trust.

In connection with the global viral pandemic, the construction and real estate market outlook for the near future has become difficult. Risks have risen sharply in the world economy as well as financial markets, due to which near term negative developments with unforeseeable magnitude cannot be ruled out. Among other, banks' lending policy and conditions remain very important factors in market developments, but these depend also on the decisions and cooperation of companies and governmental institutions. We believe that strong capitalization and the capabilities of our team give Merko group a relative advantage in the execution of development and construction projects as well as in emerging from difficulties in the event of negative market developments.

I would like to thank all of Merko Group's employees and partners for a productive year, also our customers and home buyers who have put their trust in Merko.

Many thanks!



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.



TALLINN OLD TOWN FACADE LIGHTING

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.

In 2019, the group fulfilled the financial objectives set for both return on equity and equity ratio as a proportion of assets.

return on equity
12.9%

equity ratio
46%

The amount of dividends paid for the completed financial year and thus the dividend rate will be decided by the general meeting of shareholders.

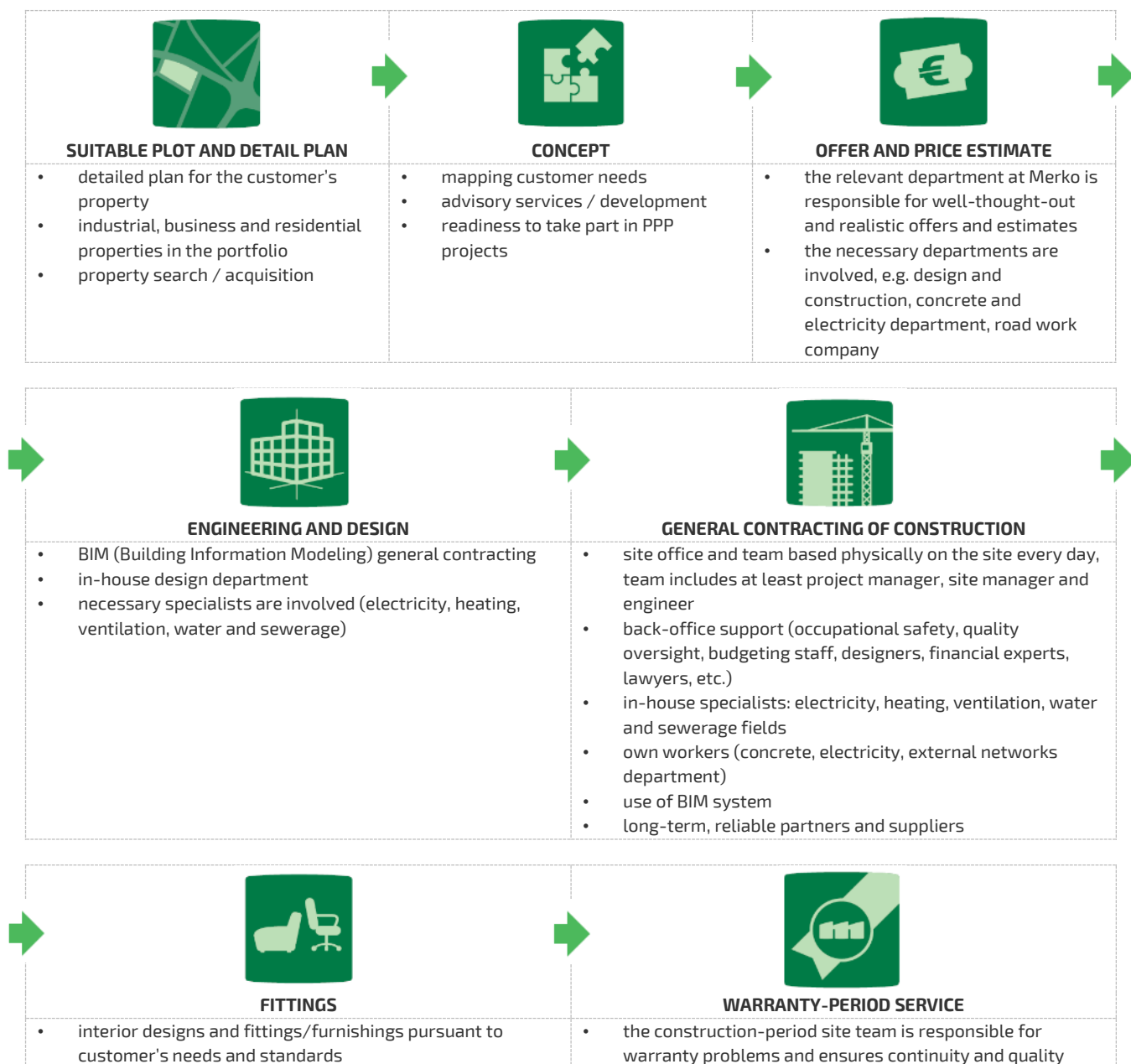
FULFILLMENT OF LONG-TERM FINANCIAL OBJECTIVES 2015-2019

	2019	2018	2017	2016	2015	AVERAGE
Return on equity, ROE (on yearly basis)	12.9%	15.3%	11.9%	5.0%	8.0%	10.6%
Dividend rate	*	92%	120%	119%	90%	105%
Equity ratio 31.12.	46.2%	48.9%	47.0%	51.6%	59.5%	50.6%

*The dividend rate for 2019 depends on the decision of the general meeting of shareholders to pay dividends

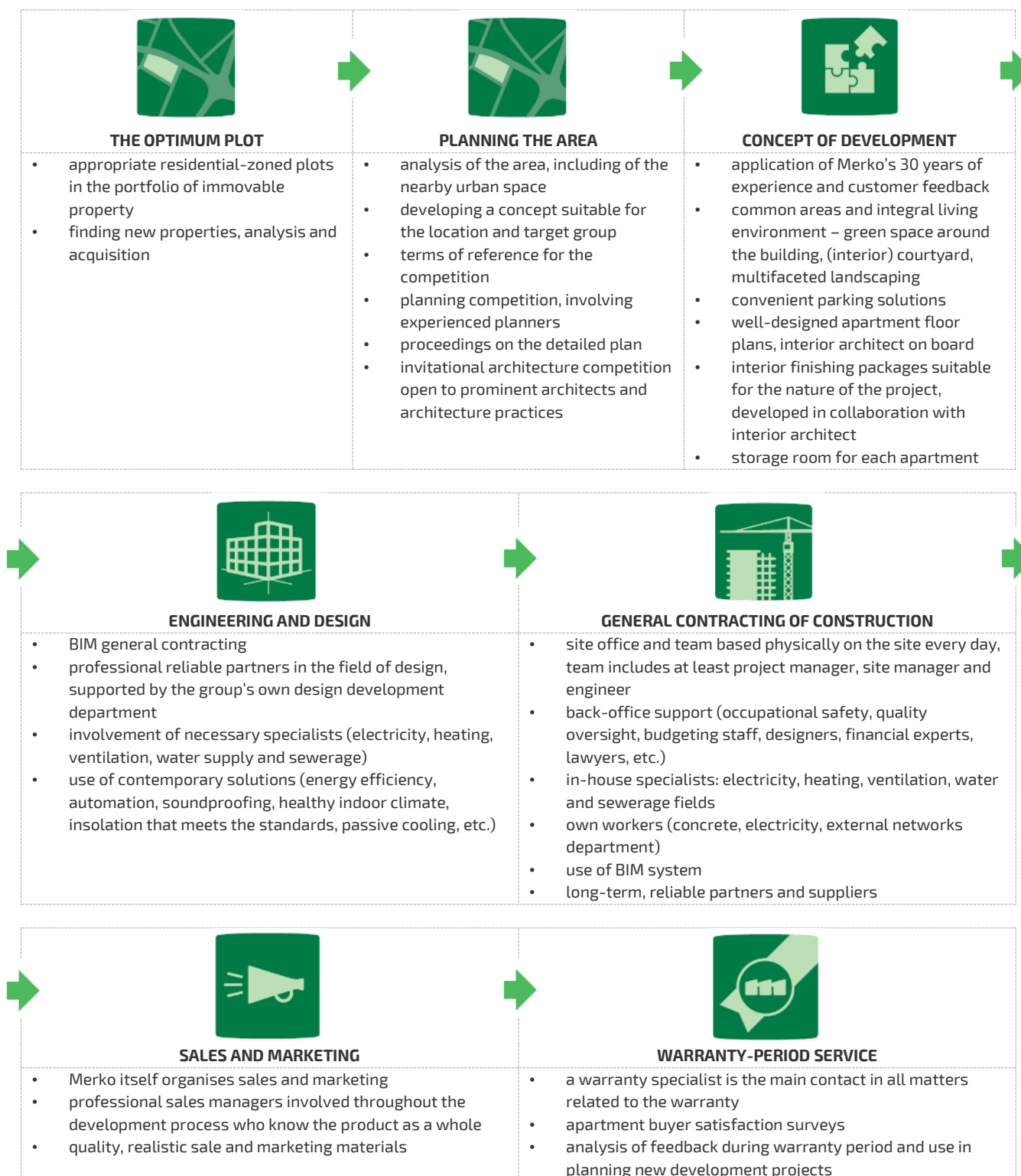
BUSINESS MODEL: CONSTRUCTION SERVICES TO CUSTOMERS

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 5,000 apartments in Estonia, Latvia and Lithuania, there are currently approximately 900 apartments in construction 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.



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RATIOS

(attributable to equity holders of the parent)

INCOME STATEMENT SUMMARY		2019	2018	2017
Revenue	million EUR	326.8	418.0	317.6
Gross profit	million EUR	34.8	33.0	30.9
Gross margin	%	10.7	7.9	9.7
Operating profit	million EUR	19.2	19.9	19.5
Operating profit margin	%	5.9	4.8	6.2
Profit before tax	million EUR	20.3	19.8	18.8
EBT margin	%	6.2	4.7	5.9
Net profit	million EUR	16.5	19.4	15.8
attributable to equity holders of the parent	million EUR	16.3	19.3	14.7
attributable to non-controlling interest	million EUR	0.2	0.1	1.1
Net margin	%	5.0	4.6	4.6
Other income statement indicators		2019	2018	2017
EBITDA	million EUR	21.9	21.9	22.2
EBITDA margin	%	6.7	5.2	7.0
General expense ratio	%	5.3	3.7	4.6
Labour cost ratio	%	11.4	8.2	10.1
Revenue per employee	thousand EUR	461	563	434
Other significant indicators		31.12.2019	31.12.2018	31.12.2017
Return on equity	%	12.9	15.3	11.9
Return on assets	%	5.6	6.9	5.8
Return on invested capital	%	11.1	11.5	11.4
Assets	million EUR	281.8	269.7	277.1
Equity	million EUR	134.6	136.3	134.7
Equity attributable to equity holders of the	million EUR	130.3	131.8	130.2
Equity ratio	%	46.2	48.9	47.0
Debt ratio	%	22.6	16.4	21.4
Current ratio	times	2.4	2.2	2.2
Quick ratio	times	0.8	1.1	1.1
Accounts receivable turnover	days	45	40	40
Accounts payable turnover	days	53	41	40
Average number of employees (total group)	people	709	743	732
Order book	million EUR	141.4	229.0	344.4

Calculation of ratios is provided on page 112 of the report.

THE MAIN FACTORS INFLUENCING THE CONSTRUCTION MARKET IN 2019

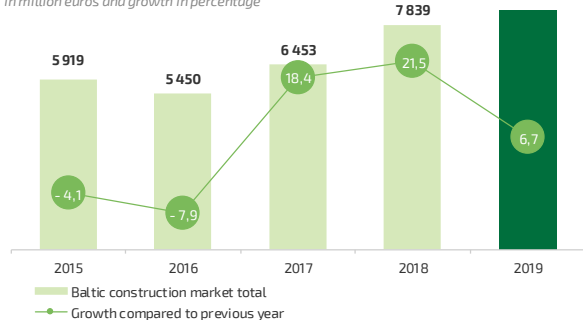
CONSTRUCTION SERVICES

	2019			2018		
	Estonia	Latvia	Lithuania	Estonia	Latvia	Lithuania
GDP annual change in current prices	+4.3%	+2.2%	+3.9%	+4.8%	+4.3%	+3.6%
Average monthly wage (gross) change	+7.4%	+7.2%	+8.8%	+7.3%	+8.4%	+10.1%
Construction price index annual change	+1.9%	+4.1%	+4.3%	+1.7%	+4.4%	+2.9%

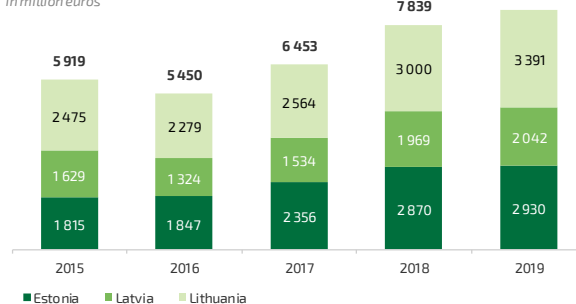
Source: Local national statistical offices / Eurostat.

In 2019, the economies of the Baltic states continued to outpace the average growth in the EU (+1.5%). Latvia's economic growth clearly slowed, however, being among the average European countries. In Estonia and Lithuania, growth continued at more or less the same pace as the previous year. The average monthly wage continued growing rapidly in all three Baltic states, deepening the imbalance between incomes and productivity. The growth of incomes has supported the overall economic activity, including real estate purchases, while it also means greater expenses for businesses, including in construction activity and investing into commercial real estate.

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



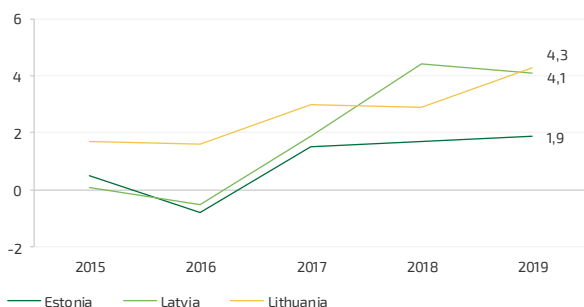
CONSTRUCTION MARKET VOLUMES (WITH OWN FORCES) IN THE BALTIC STATES BY GEOGRAPHICAL LOCATION
in million euros



Source: Local national statistical offices.

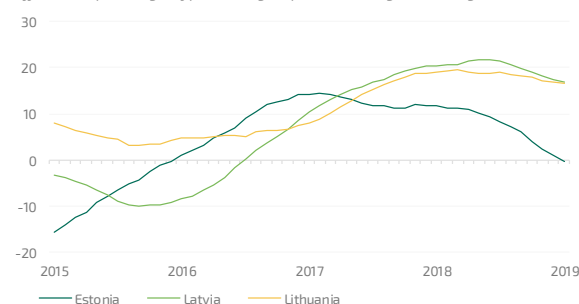
In 2019, a total of EUR 8,363 million of construction works were performed in the Baltic states. For the first time after the end of the last boom period, the 2008 peak level was reached (EUR 8,185 million). Above all, this stems from Estonia's contribution, which exceeded the 2007 peak by 17%. Latvia's and Lithuania's figures remained below the 2008 peak, by 15% and 6% respectively. Growth for the Baltics overall fell to barely +7% (2018: +21%). The volume of construction works grew in all three countries, most of all in Lithuania: +13%. Growth in Estonia and Latvia was limited: +2% in Estonia, +4% in Latvia.

CHANGE IN CONSTRUCTION PRICE INDEX
percentages



Source: Local national statistical offices / Eurostat.

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



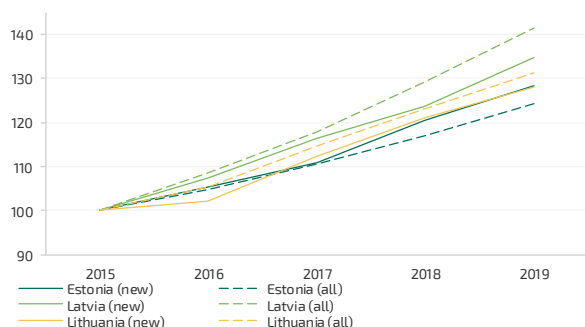
Construction prices continued to rise at the same rate as last year in Estonia (+1.9%) and in Latvia (+4.1%), but it sped up in Lithuania (+4.3%), supported by increasing volumes. Confidence in the construction sector (the average level for the last 12 months observed to eliminate seasonality) in Estonia fell over the course of the year to the long-term average level, remaining significantly higher in Latvia and Lithuania, although the rising trend also in those markets turned to a moderate decline.

APARTMENT DEVELOPMENT

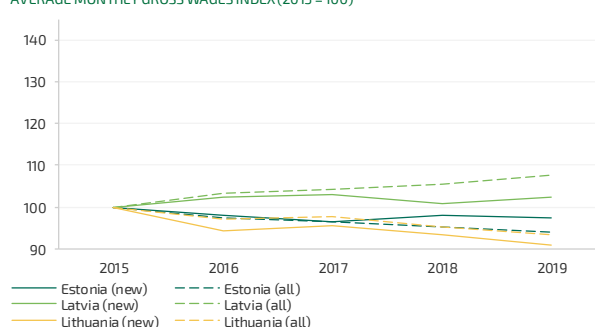
Housing prices have seen fairly consistent growth rates in all three Baltic states in recent years. Starting in 2015, the fastest price rise has been seen on the Latvian market: an average of close to 8% per year for new buildings and 9% for all buildings. Insofar as

the average income growth during the same period has been around 7%, people's purchasing power has somewhat decreased. In Estonia and Lithuania, prices have risen at a more moderate level (around 6-7% per year) falling a little short of wage growth. Thus, despite the constant price rise in Estonia and Lithuania, people's purchasing power has actually increased. Since by and large, real estate prices are rising at the same rate as incomes, there is no cause to see developments as amounting to a bubble.

NEW AND ALL (dotted line) DWELLINGS HOUSE PRICE INDEX (2015=100)

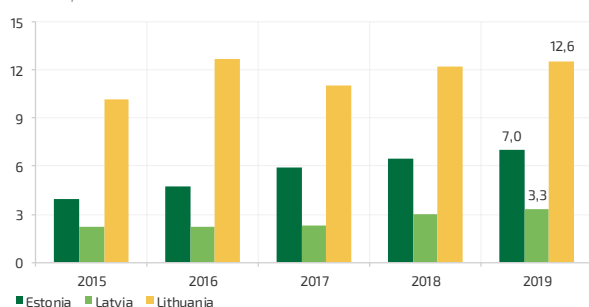
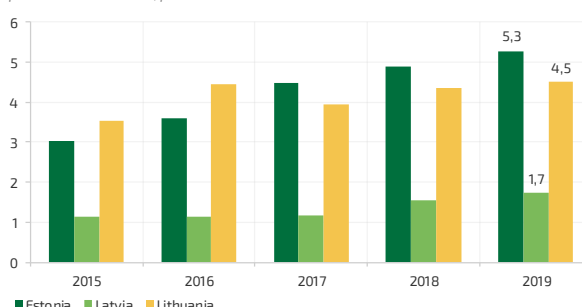


RATIO OF NEW AND ALL (dotted lines) DWELLINGS HOUSE PRICE INDEX TO AVERAGE MONTHLY GROSS WAGES INDEX (2015 = 100)



Source: Local national statistical offices / Eurostat.

Since 2012, Estonia has seen a continuous growth in the number of permits for use. In the last two years, the rate has slowed somewhat (annual growth less than 10%). Last year slightly more than 7,000 new residential units came on to the market (2018: ca 6,500), falling only slightly short of the boom-era peak (2007: ca 7,100). In Lithuania, a more energetic growth started in 2011, reaching its peak in 2016, when close to 12,700 permits for use were issued. At the height of the boom era in 2008, around 11,800 permits for use were issued in Lithuania. This level has now been exceeded in 2016, 2018 and 2019 (most recent figures: 12,600 permits). The greatest relative positive change in number of permits for use in the past two years has occurred in Latvia (2018 +31%, 2019 +12%). Still, Latvia's volumes remain modest compared to that of Estonia and Lithuania. At the height of the boom, in 2007, 9,300 permits were issued in Latvia, i.e. close to three times more than last year.

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

Source: Local national statistical offices.

Estonia has issued the highest number of permits for use per capita with 5.3 per 1,000 inhabitants (2018: 4.9), while the figures were 4.5 in Lithuania (2018: 4.4) and just 1.7 in Latvia (2018: 1.5). Thus, Latvia is behind its neighbours by almost a factor of three.

OUTLOOK FOR 2020

2020 was expected to be a year of generally stable, moderate, albeit tapering, economic growth in the whole of the EU, including the Baltics. The main risks envisioned were the strained economic relations between the US vis-à-vis Europe and China (protectionism and sanctions), and, regionally, the after-effects of Brexit as well as developments in the banking sector (increasing amount of regulation, the knock-on effects of anti-money-laundering measures, the banks' waning risk appetite).

All of this has unfortunately changed dramatically with the global SARS-CoV-2 coronavirus pandemic originating in China and spreading around the entire world, causing the COVID-19 disease. By mid-March, many countries (including Estonia, Latvia, Lithuania and Norway) had declared a state of emergency with substantial restrictions on the normal operation of society. National borders are closed, freedom of movement has been halted, and service providers shuttered. At the time of preparing this report it remains unknown what all this will mean for the economy in the long run at the local, regional and global level. The main question is how long normal life will be disrupted and what the actual direct impact of the spread of the virus will be on public health.

It is clear that the previous forecasts are no longer valid and there will be a significant hole in the economic development around the entire world. At the minimum, it will mean slowing economic growth, and highly likely, recession. It will be very important how the commercial banks (grace periods, extensions of contracts), central banks (increasing the money supply and injections of liquidity, easing of regulatory requirements for commercial banks), governments (use of government debt to support the economy, timely

ending of lockdowns and restrictions) and international organizations (EU support measures, IMF financing, etc.) help the economy in recovering from this difficult situation. It is likely that consumer behaviour will change for longer than actual pandemic – life will become more stationary, people will travel less, consume less, save more, and economic confidence in regard to the future will be lower (fear of job loss, etc.). Sectors built on the free movement of people both within and across national borders will absorb the greatest impact – transport, lodging, entertainment, restaurants and catering. Industry and construction will face indirect impacts with the general economic activity being lower, and supply chains having become slower, less reliable and more costly.

CONSTRUCTION SERVICES

2019 witnessed a clear slowing of construction activity in Estonia and Latvia. In Lithuania, growth continued at a more than 10% pace. In an ordinary situation, the Estonian and Latvian construction volumes might have been forecasted to see a moderate decrease in 2020 (there were fewer large projects coming to market as the market was adjusting to previous greater supply) while Lithuanian growth was set to continue. Due to the pandemic, however, it is now unfortunately likely that all three markets will contract, with a setback in store for construction in Norway, too. The primary problems will be related to ensuring supply reliability of construction materials, also restrictions on free movement established by different countries as well as workers falling ill and being isolated may disrupt the construction activities. Longer-term impacts will come from increased cautiousness on the part of clients and investors. Investments will be postponed and business plans will be redrawn with a critical eye.

For main contractors, the key question in such a situation will be whether they have sufficient resources and that the usage of these resources is precisely planned. Market participants with a low level of capitalisation that makes it difficult for them to survive longer periods of inactivity, delays in delivery of materials and work will find themselves in a tight spot. It will also be important for the clients to adopt a generally responsible behaviour in the new and trying situation. If either side is too unbending on the issue of compliance with contracts and obligations, it could mean protracted court disputes, amplifying general problems, and crippling the economic environment more than minimally necessary. Because of this, all parties in the construction sector (clients, main contractors, subcontractors, government sector) must seriously consider the consequences of their activities, weighing them for the short-term and long-term perspective.

Public sector demand will play an even more important role than it has so far. With the initiative and capacity of the private sector to carry out projects and complete existing ones taking a downturn, it is possible for the public sector to soften the depth and duration of the shock for the construction sector by increasing demand. 2020 is the right time for the public sector to fast-track construction-related plans made for a longer time period. That applies to construction of buildings and infrastructure, general construction and civil engineering (highways, railway, power grid, etc.). Among other things, this pertains to Rail Baltica. This would be a critical period for plans related to the rail link to come into sharp focus and for clear progress to be made in enacting the plans in a timely fashion.

Merko Ehitus group is keeping a close eye on developments related to the spread of coronavirus, evaluating critically the course of every ongoing and planned construction project together with related risk aspects to be able to take timely important decisions pertaining to the practical organization as well as financial impacts of the construction activity. The group will continue to ensure the provision of professional high-quality service, at the same time taking into account the effects of the new reality beyond group's control, which may prevent work processes from being carried out per usual. Thanks to strong capitalization and long-term know-how among employees, Merko Ehitus group is capable of operating successfully also in a socio-economically challenging situation, so that the interests of the company as well as of the clients are both taken into consideration.

APARTMENT DEVELOPMENT

Apartment markets in Tallinn and Vilnius have shown a high level of activity and growing volumes thus far. The Latvian apartment market has also become more active in the last few years, although it remains well below Tallinn and Vilnius levels. The general trend also favoured the continuation of the current path in 2020 (low unemployment, growing incomes, reasonable loan terms, moderate, but continuing broad-based economic growth). The new situation posed by the spread of the coronavirus will unfortunately trim developments on the apartment market as well. First, the sale periods for projects that have reached or will reach completion will become longer. If rapid progress is not made in bringing the virus under control, we must also be prepared for decreasing prices, as demand will decrease from those who buy the apartments for own use (less confidence about the future) as well as from those who look at the apartments as investments (longer payback period, decreasing cross-border demand).

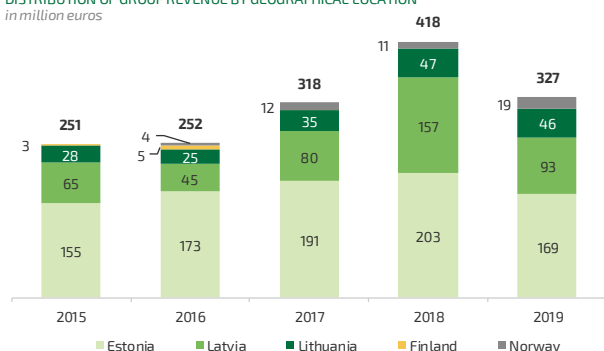
In such a situation it is important for developers to have sufficient financial reserves to ride out the lengthening sales periods without having to offload real estate developments at lower prices due to pressure from creditors. The position that the commercial banks take will have an especially important influence on the resilience of the real estate market. While still under the pandemic's influence, it is vital that the loans are not called in and the developers are granted longer time to sell the apartments. If banks are too rigid, it could trigger a faster and deeper market decline. It is also important for banks to have a long-term view when it comes to financing private homeowners' purchases. If the economy's bloodstream – lending – comes to a halt, it will probably have a greater acute impact on the health of the economy than the potential direct consequences of the virus itself.

The long-term view of Merko Ehitus for the apartment development remains on the same track. Now and in future, the group will continue to develop integral living environments, focusing on larger areas, offering reliable quality and expert solutions in spatial planning. In the shorter term, the group will continuously monitor the fast-changing environment and make investment decisions based on how the situation takes shape. Thanks to solid financial condition, Merko Ehitus can, if necessary, extend the sale periods for its developments and make investment decisions with a long-term positive influence on the group's financial state.

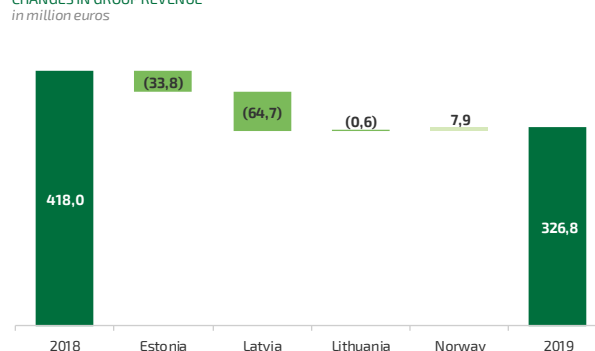
OPERATING RESULT

REVENUE AND PROFIT

DISTRIBUTION OF GROUP REVENUE BY GEOGRAPHICAL LOCATION
in million euros

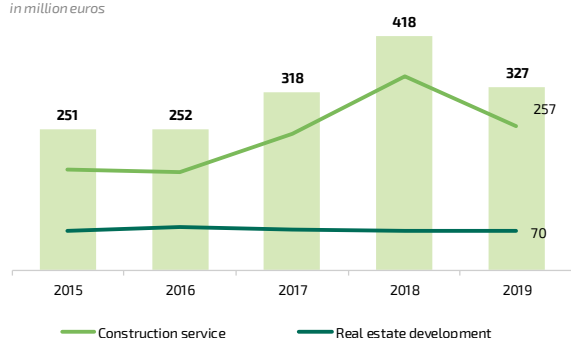


CHANGES IN GROUP REVENUE
in million euros

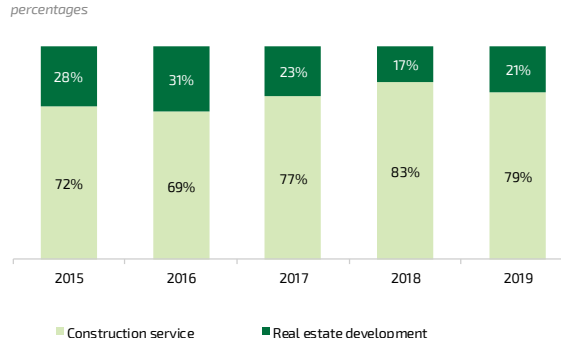


In 2019, the revenue of Merko Ehitus group was EUR 326.8 million, (2018: EUR 418.0 million). 51.7% of the period's revenue was generated in Estonia, 28.4% in Latvia, 14.1% in Lithuania, and 5.8% in Norway (2018: 48.5% in Estonia, 37.7% in Latvia, 11.2% in Lithuania and 2.7% in Norway). Compared to 2018, the group's revenue decreased by EUR 91 million or 21.8%, including a 16.7% decrease in Estonia, 41.1% in Latvia and 1.2% in Lithuania. In Norway, the revenue increased by 70.6%. The group's revenue decreased mainly due to unusually high sales revenue a year earlier – there were several major projects in operation that were not available in such volumes in 2019.

DISTRIBUTION OF GROUP REVENUE ACCORDING TO SEGMENTS
in million euros



DISTRIBUTION OF GROUP REVENUE ACCORDING TO SEGMENTS
percentages

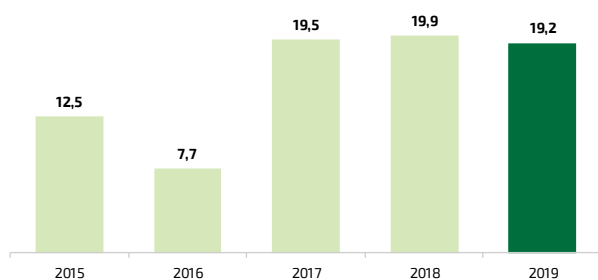


Real estate development accounted for a slightly larger share of the sales revenue due to the reduced volume of construction services, accounting for 21% (2018: 17%) of the group's total sales. The group will ensure that an appropriate risk-benefit ratio is ensured when engaging in new construction projects. It has been abandoned to enter into price competition rather than to increase the construction contract portfolio at high risk.

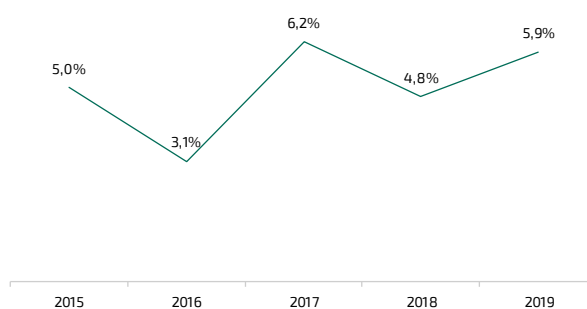
By country, Estonian sales continued to account for the largest share of revenue – 52% (2018: 48%). Estonia's share increased mainly on Latvia's expense, as there were extraordinarily large construction projects in Latvia in 2018, but not in such volume in 2019. The group finds it strategically important for the business operations to be diversified both geographically and in terms of business segments. Thus, the group continues to strengthen and implement its competitive advantages outside Estonia and is closely monitoring the development and opportunities in both the Baltic states and the Nordic countries, especially in Norway, as well as balancing construction activities with real estate development projects.

In 2019, the group's operating profit totalled EUR 19.2 million (2018: EUR 19.9 million). The operating profit margin in 2019 (5.9%) increased by 1.1 pp compared to last year (2018: 4.8%). Focus on increasing efficiency and signing construction contracts only in case the risks assumed are reasonable and the profitability is sufficiently robust has yielded results.

GROUP OPERATING PROFIT
in million euros

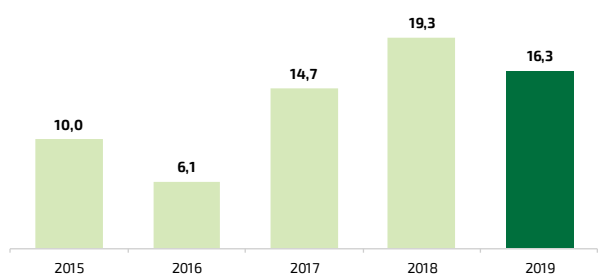


GROUP OPERATING PROFIT MARGIN
percentages

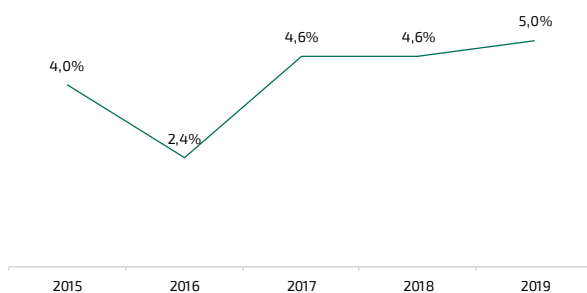


In 2019, the group's pre-tax profit totalled EUR 20.3 million and the net profit attributable to owners of the parent company was EUR 16.3 million, compared to the pre-tax profit of EUR 19.8 million and net profit attributable to owners of the parent company of EUR 19.3 million in 2018. The group's profit before tax margin was 6.2% (2018: 4.7%) and net margin was 5.0% (2018: 4.6%).

GROUP NET PROFIT
in million euros



GROUP NET PROFIT MARGIN
percentages



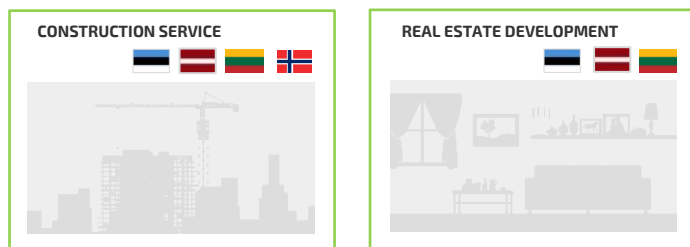
In the third quarter of 2019, the group paid EUR 17.7 million in dividends and incurred additional income tax expense in the amount of EUR 2.7 million. In the second quarter of 2018 the group paid EUR 17.7 million in dividends. As these were paid from dividends received from foreign subsidiaries where the income had been taxed, the group did not incur additional income tax expenses.



STUDENT HOME OF RAKVERE VOCATIONAL SCHOOL IN ESTONIA, COMPLETED IN 2019

BUSINESS ACTIVITIES

The group operates in Estonian, Latvian, Lithuanian and Norwegian market through its subsidiaries. See additionally the detailed management structure on page 39.



Starting from 2019, the management board of AS Merko Ehitus decided to change the segment reporting structure in the group's financial reports and harmonise it with the group's internal reporting structure.

As a result of the change, the Estonian construction service and other home market construction service will be merged and instead of three business segment there will be two:

- construction service;
- real estate development.

The change is due to the fact that over the years the volumes of construction services provided by group has grown significantly outside Estonia, therefore, the management board of AS Merko Ehitus is focusing on the construction service business segment as a whole and does not deem it necessary to treat Estonian construction service as a separate business segment.

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's strength is also in completing simultaneously various complex and long-term projects, while providing high quality construction services to customers with different requests.



SUSTAINABILITY STANDARDS

Merko group has extensive experience in designing and building in accordance with international sustainability standards. Completed in Vilnius in 2019, the Quadrum South business centre was awarded the BREEAM certificate at the level of "Excellent". A score of 75.3% is the highest score so far in Lithuania. In Latvia, the BREEAM certificate at the level of "Very Good" was awarded to the Akropole shopping centre in Riga, the first commercial building in Latvia with a "Very Good" BREEAM certificate. No projects matching the green label requirements were completed in Estonia in 2019.

CONSTRUCTION SERVICE

The construction service in Estonia consists of services in the field of general construction, civil engineering, electricity, external networks and road construction, as well as concrete works: in Latvia general construction, provision of civil engineering and electricity construction services; and in Lithuania and Norway general construction works.

million EUR

	2019	2018	CHANGE
Revenue	256.7	347.1	-26.0%
% of total revenue	78.6%	83.0%	
Operating profit	13.3	10.7	+23.9%
Operating profit margin	5.2%	3.1%	

In 2019, the revenue of the construction service segment was EUR 256.7 million (2018: EUR 347.1 million), having decreased by 26.0% from last year. The construction service segment revenue for 2019 made up 78.6% of the group's total revenue, having decreased by 4.4 pp in the yearly comparison (2018: 83.0%).

In 2019, the group earned an operating profit of EUR 13.3 million in this segment (2018: EUR 10.7 million). The operating profit margin was 5.2% (12M 2018: 3.1%). An increase in the profitability compared to the year before confirms that the approach to concentrate on increasing efficiency and to choose to sign only those construction contracts, which provide proper profitability with a sensible risk level, has been correct. Retaining the operating profitability level demands an increasingly stronger effort in finding efficiency as well as focusing on projects, in case of which it is possible to generate added value to the client through high quality of project management, and the provided service can be priced accordingly.

There continues to be strong competition among main contractors in the construction service market of the Baltic states. The number of larger construction objects on the market has decreased. Because of that the main contractors, at times, are willing to leave increasingly smaller or even non-existent buffers for unfavourable developments in order to secure the contract. At the same time the construction prices have been constantly rising, which increases costs for main contractors. In case of long-term construction contracts, the main contractors are assuming the risk of increasing costs. As a rule, this risk remains with the main contractor, as it cannot be shared with the client in a sensible way. Because of that the main contractors are in danger of destroying the profitability, which has been gradually accumulated for a longer period of time, with one unsuccessful contract. To turn profit, the main goal is to avoid such large mistakes.

Among the substantial projects in process that started in 2019 and earlier and will continue in 2020 were, in Estonia, the construction works of commercial building at Pärnu mnt 186, Terminal D parking house at the Tallinn passenger port, Türi Basic School buildings, construction of electric power cables of Suur Väin straits as well as high-voltage power cables in Tallinn, construction works of water supply and sewerage piping in Metsanurme, Kasemetsa and Üksnurme area, reconstruction of Aaspere-Haljala road section, and road repair and maintenance works in Tallinn. In Latvia, larger ongoing projects were the construction works of Lidl logistics centre, Laima chocolate factory and college building and dormitory in Pinki. In Lithuania, larger projects were the construction works of Neringa hotel, a private school building in Vilnius and Kaunas district Police headquarters. In Norway, mostly smaller scale contracts were in the works.

LARGEST PROJECTS COMPLETED IN 2019

PROJECT NAME		LOCATION	COUNTRY
Maakri Kvartal business complex	new	Maakri 19/21, Tallinn	Estonia
Tallink office building	new	Sadama st 9, Tallinn	Estonia
Residential building at Toom-Kuninga 21	new	Toom-Kuninga 21, Tallinn	Estonia
Student home of Rakvere Vocational School	new	Piiri 8, Rakvere	Estonia
Quay no 42 of Noblessner quarter	rec	Tallinn	Estonia
Roads in the Nursipalu target area	new	Rõuge rural municipality and Võru rural municipality, Võru county	Estonia
Kiini 110/20kV substation	new	Kiini village, Viljandi county	Estonia
Multifunctional Centre Akropole	new	Maskavas street 257, Riga	Latvia
Extension of Alfa shopping centre	new	Brīvības gatve 372, Riga	Latvia
Ventspils music school and concert hall	new	Lielais laukums 1, Ventspils	Latvia
Residential building at Aguonų st. 10	new	Aguonų st 10, Vilnius	Lithuania
Business centre Quadrum South	new	Konstitucijos prospekt 21, Vilnius	Lithuania
School building in Vilnius	new	Medeinos str 14, Vilnius	Lithuania
Tesla service centre	rec	Karihaugveien 100, Oslo	Norway
Office building Skippergata 3	rec	Skippergata 3, Oslo	Norway



NATIONAL DEFENSE OBJECTS

Merko has contributed to the completion of various national defence sites by building various objects at Ämari Air Base and Tapa Military Campus in Tapa over the years.

After the construction of the barracks at Ämari Air Base and the Nursipalu target area access and service roads in 2018, Merko completed a support building for the 1st Infantry Brigade's logistics centre, expanded the medical centre as well as built a helipad with an automated lighting system at the Tapa military campus in 2019.

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

	2019	2018	CHANGE
Revenue	70.1	70.9	-1.2%
incl. revenue from sale of apartments	63.8	41.3	
incl. construction service to joint venture projects	2.1	15.5	
incl. revenue from immovable properties	0.4	9.5	
% of total revenue	21.4%	17.0%	
Operating profit	8.1	11.3	-28.3%
Operating profit margin	11.6%	16.0%	

A total of 482 apartments (incl. 47 apartments in a joint venture) were sold in 2019 at the total value of EUR 63.8 million (excl. VAT), compared to same amount apartments- 482 (incl. 131 apartments in a joint venture) and EUR 41.3 million in 2018. In addition, the group sold 24 commercial areas (incl. 14 in a joint venture), in 2018 15 commercial areas (incl. 1 in a joint venture). Of the 482 apartments sold 289 were located in Estonia, 39 in Latvia, 154 in Lithuania. The construction service revenue from projects developed by joint ventures in 2019 was EUR 2.1 million (2018: EUR 15.5 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 2019, the share of revenue from the real estate development segment formed 21.4% of the group's total revenue (2018: 17.0%), having increased over the year by 4.4 pp. The main reason for the increase of the share is due to the reduced volume of construction services. Although the revenue from the sale of apartments increased by more than half, total revenue from real estate development fell by 1.2%: there was significantly less construction services for joint projects and no real estate sales.

In 2019, operating profit of the real estate development segment amounted to EUR 8.1 million (2018: EUR 11.3 million) and the operating profit margin was 11.6% (2018: 16.0%), which decreased by 4.4 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. Profitability also depends on the distribution of sales revenue in the development business segment between sub-activities (sale of apartments, construction services for joint projects, sale of immovable properties). In case of construction services for joint projects, the profit from construction is 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.

VEERENNI RESIDENTIAL ENVIRONMENT



At the end of 2019, 12 buildings with a total of 137 apartments and 8 commercial spaces were completed as part of the first stage of the Uus-Veerenni development project. In total, homes for over a thousand families will be built in Uus-Veerenni over the next decade.

By the end of 2020, 8 new buildings with a total of 88 apartments and 4 commercial premises will be completed in Uus-Veerenni as part of the second stage.

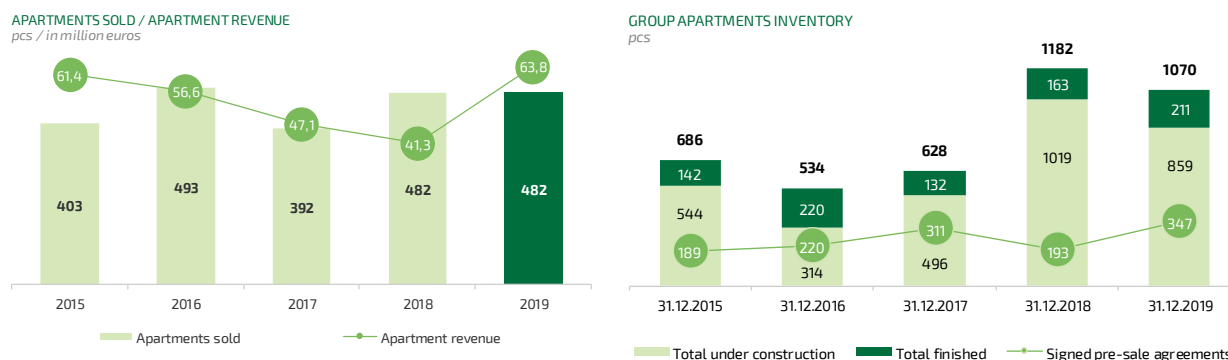
Uus-Veerenni is the largest comprehensive residential development area in Tallinn city centre. Green courtyards with recreational areas and playgrounds will be built between the apartment buildings, with in-quarter roads and an underground car park.

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.

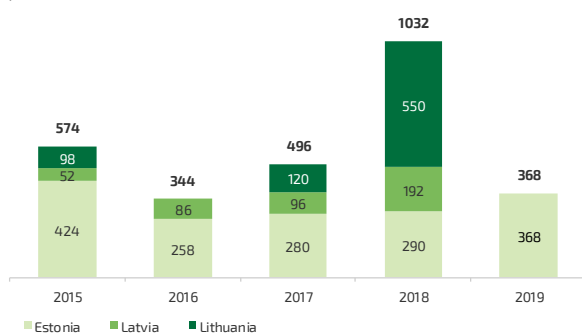
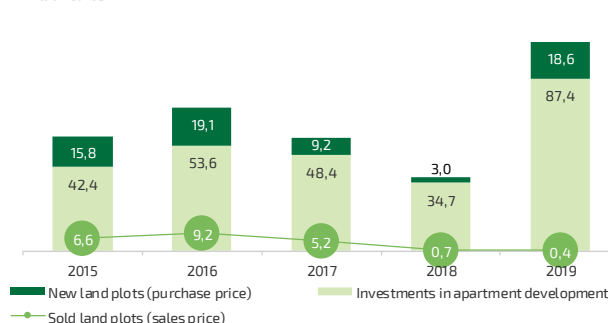
In real estate development joint projects, Merko brings its knowledge and experience of real estate development and construction to the partnership and the other party provides the plot and/or investment. The relationships between the parties are regulated by a stakeholders' contract that specifies the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



At the end of the period, Merko Ehitus group's inventory of apartments amounted to 1,070 units, of which 211 were completed and 859 in construction. 347 apartments were covered with preliminary agreements, incl. 29 completed apartments (8 in Estonia, 19 in Latvia and 2 in Lithuania) and 318 apartments under construction (113 in Estonia, 32 in Latvia and 173 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 2019, Merko Ehitus group had a total of 723 apartments for active sale (as at 31 December 2018: 989 apartments), for which there are no pre-sale agreements and of which 182 have been completed (43 in Estonia, 111 in Latvia and 28 in Lithuania) and 541 are under construction (255 in Estonia, 64 in Latvia and 222 in Lithuania). The number of apartments on sale as at 31 December 2019 has fallen, compared to 31 December 2018, as 368 new apartments launched in 2019, compared to 1,032 new apartments in 2018 (incl. 11 in joint venture).

In 2019, the group invested a total of EUR 87.4 million (2018: EUR 34.7 million) in new development projects launched in 2019 as well as projects already in progress from previous year. As in Latvia and especially in Lithuania the development of relatively many apartments started in 2018, in 2019 new projects were started only in Estonia.

APARTMENTS LAUNCHED BY GEOGRAPHICAL LOCATION
pcsINVESTMENTS IN APARTMENT DEVELOPMENT PROJECTS AND LAND PLOT
ACQUISITIONS AND DISPOSALS
in million euros

The group's long-term aim is to continue investing in residential real estate projects. The overall average annual planned development volumes could be around 650-700 apartments. The actual annual volumes depend, more broadly, on global developments and, more narrowly, on the situation of the apartment markets in the Baltic states as well as on the pace of construction permit issuance.

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 2019, the group's inventories included land plots with development potential, where the construction works had not started, of EUR 70.2 million (31.12.2018: EUR 54.5 million).

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

million EUR

	31.12.2019	31.12.2018
Estonia	29.3	26.9
Latvia	26.9	26.6
Lithuania	14.0	1.0
Total	70.2	54.5

In 2019, the group has purchased new land plots for real estate development purposes at an acquisition cost of EUR 18.6 million, including an acquisition of a real estate development area in Vilnius for EUR 13 million and land plots in Estonia for a total of EUR 5.6 million (in 2018, the group purchased new land plots at an acquisition cost of EUR 1.7 million in Estonia and EUR 1.3 million in Latvia)

THE SPECIFICATIONS OF PROJECTS COMPLETED IN 2019

PROJECT		LOCATION	SIZE
Tähepargi apartments	new	Tartu, Estonia	3,278 m ² , 45 apartments
Pikaliiva 18, 20	new	Tallinn, Estonia	3,907 m ² , 66 apartments
Suur-Patarei 20	new	Tallinn, Estonia	3,360 m ² , 31 apartments
Veerenni I stage	new	Tallinn, Estonia	9,169 m ² , 137 apartments
Fizikų 18	new	Vilnius, Lithuania	3,478 m ² , 70 apartments
Gaiļezers 5, 7, 13	new	Riga, Latvia	6,908 m ² , 96 apartments



SATISFACTION SURVEYS CONDUCTED AMONG APARTMENT BUYERS

In 2019, Merko conducted satisfaction surveys in Estonia among those who bought an apartment in Pikaliiva 18 and 20, Suur-Patarei 20 and the first stage of the Uus-Veerenni development project, i.e. Veerenni 36, Pille 7 and Tiit 3. The results confirm that the Merko brand is highly valued.

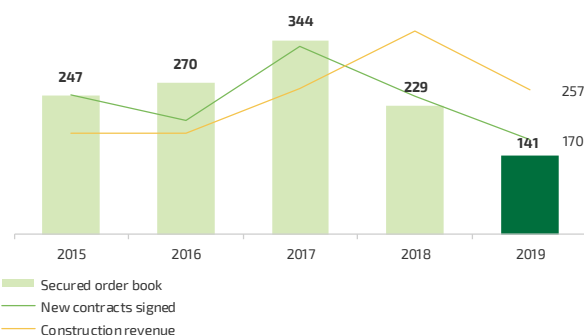
The survey measured Merko's Net Promoter Score or customer loyalty index. The average score for these projects was +63 (on a scale of -100 to +100). In addition, customer satisfaction with sales and marketing materials, the purchasing process, apartment design and construction quality, and the living environment were studied. All projects achieved an average score of more than 7.5 on a 10-point scale, which can be considered a good result. Satisfaction surveys give Merko valuable feedback on how to further improve its products and services.

SECURED ORDER BOOK

As at 31 December 2019, the group's secured order book (excluding own property developments) amounted to EUR 141.4 million as compared to EUR 229.0 million as at 31 December 2018. The secured order book excludes the group's proprietary residential development projects and work related to developing real estate investments.

In 2019, new construction contracts worth EUR 169.6 million were signed (excludes property developments), compared to EUR 246.4 million in the prior year.

SECURED ORDER BOOK
in million euros



LARGEST CONSTRUCTION CONTRACTS SIGNED IN 2019

in millions of euros (as announced during 2019 on Nasdaq Baltic stock exchange)

BRIEF DESCRIPTION OF CONTRACT	COUNTRY	COMPLETION DATE	COST
Construction contract for the reconstruction works of main road No. 1 (E20; Tallinn-Narva) Aaspere-Haljala section	Estonia	October of 2020	12.8
Construction contract for the construction of Türi Basic School buildings	Estonia	August of 2020	11.4
Design and construction works of water supply and sewerage piping in Metsanurme, Kasemetsa and Üksnurme area in Saku Parish, Harju County	Estonia	June of 2021	6.4
Construction contract for the construction of a support warehouse and the expansion of a medical centre in Tapa armed forces campus, in Lääne-Viru County	Estonia	January of 2020	5.5
Construction contract for the replacement of three 110 kV electric power lines with ground cables in Tallinn	Estonia	End of 2020	5.1
Construction contract for the reconstruction of Riga Technical University Civil Engineering Faculty building	Latvia	March of 2021	11.9
Construction contract for the construction of a new college building and a dormitory in Piņķi, Babītes county	Latvia	August of 2020	10.1
Construction contract for the new chocolate factory construction works in Latvia	Latvia	Q2 of 2020	8.9
Kaunas district Police headquarters building (Public-private partnership (PPP) contract for 15 years)	Lithuania	January of 2022	23.5
Construction contract for the amendment of the reconstruction and renovation works of the Neringa hotel building in Vilnius	Lithuania	Middle of 2020	5.0

The volume of private sector orders concluded in 2019 has declined, which is also reflected in the group's secured order book as at the end of the reporting period, where private sector orders from projects in progress constitute 36% and public sector orders make up 64% (31.12.2018: 70% private sector and 30% public sector). The group continues to focus on comprehensive supply of the design and construction contracts.



BETTER ENERGY SUPPLY TO THE ISLANDS

In 2019, Merko and Connecto installed a 110 kV submarine cable in the Väike Strait between the Muhu Island and the Saaremaa Island. The submarine cable, made without couplings, has a length of 4.7 km, a diameter of 190 mm and a weight of 67 kg per meter. For reliability reasons, the cable was recessed into the seabed to protect it from anchors, ice and other external influences.

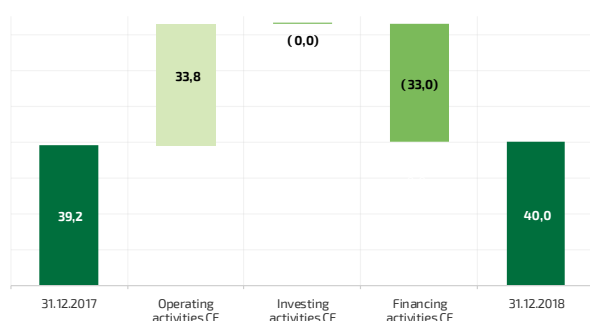
Thanks to the Väike Strait submarine cable, as well as the Suur Strait submarine cable connecting the mainland and the Muhu Island to be completed in 2020, the security of electricity supply of the largest islands in Estonia will be significantly improved.

CASH FLOWS

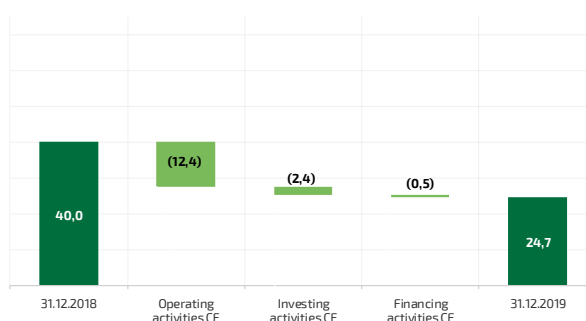
The change in short-term investments and cash equivalents in 2019 of Merko Ehitus group was negative by EUR 15.3 million and as at 31 December 2019 the group had cash and cash equivalents in the amount of EUR 24.7 million (31.12.2018: EUR 40.0 million).

The operating cash flows of 2019 were negative by EUR 12.4 million (2018: positive by EUR 33.8 million), cash flow from investing activity was negative by EUR 2.4 million (2018: EUR 0.0 million) and the cash flow from financing activity was negative by EUR 0.5 million (2018: negative by EUR 33.0 million).

CHANGE IN CASH AND CASH EQUIVALENTS
in million euros



CHANGE IN CASH AND CASH EQUIVALENTS
in million euros



The cash flow from operating activities had positive effect from EBITDA of EUR 21.9 million (2018: positive effect of EUR 21.9 million), from the changes in trade and other receivables related to operating activities of EUR 26.9 million (2018: negative effect of EUR 1.3 million), change in trade and other payables related to operating activities of EUR 1.8 million (2018: negative effect of EUR 1.8 million) and change in the provisions of EUR 0.3 million (2018: positive effect of EUR 4.7 million). The negative effects to cash flow from operating activities came from changes in receivables and liabilities related to construction contracts of EUR 10.7 million (2018: positive effect of EUR 11.2 million), change in inventories of EUR 48.1 million (2018: positive effect of EUR 0.6 million) and from the corporate income tax of EUR 3.1 million (2018: EUR 0.4 million). The group is focusing on investments to apartment development, which has brought about significant increase in the volume of inventories during the year 2019 therefore cash flow from operating activities is negative.

Cash flows from investing activities include negative effect from the acquisition of non-current assets and investment property in the amount of EUR 2.9 million (2018 EUR 1.1 million) and positive effect from the sale of non-current assets in the amount of EUR 0.5 million (2018: EUR 0.7 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 (22.6% of total assets as at 31.12.2019; 16.4% as at 31.12.2018).

In cash flows from financing, the larger negative factors were dividend payment of EUR 17.8 million (2018: EUR 17.8 million), repayments of lease liabilities in the amount of EUR 1.0 million (2018: net negative cash flow of EUR 0.6 million) and net amount of loans received and repaid of project specific loans obtained using investment property as collateral in the amount of EUR 0.5 million (2018: positive cash flow in the net amount of EUR 1.4 million), as well as from negative change in loans related to construction

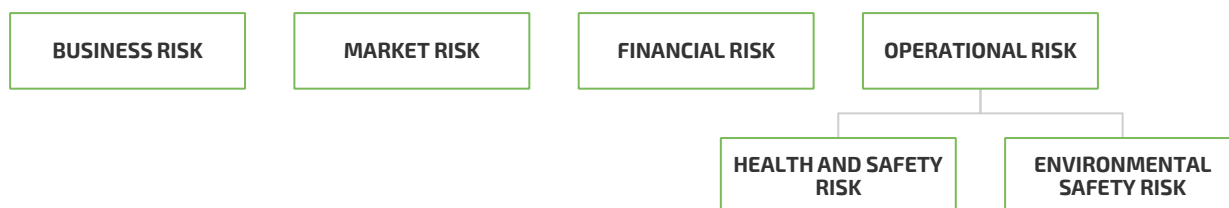
projects and other activities in the net amount of EUR 6.8 million (2018: net positive cash flow of EUR 4.2 million). Positive cash flow from financing activity was gained from net amount of loans received and repaid in connection with development projects in the amount of EUR 25.6 million (2018: net negative cash flow of EUR 20.1 million).

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.

Operating in several different markets requires orientation in the environments of various countries. The main areas of attention are the cyclicity 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 Latvian, Lithuanian and Norwegian subsidiaries, have implemented quality management system ISO 9001 and environmental management system ISO 14001 and health and safety management system ISO 45001 (Latvia is in the process of transition from OHSAS 18001). All management systems are certified. The group employs 8 (2018: 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 AS Merko Ehitus group company 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 2019, indemnity applications submitted to insurance companies totalled EUR 0.56 million (2018: EUR 0.91 million), and insurance benefits were received in the amount of EUR 0.21 million (2018: EUR 0.83 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 2019, warranty provisions were set up at the group in the total amount of EUR 1.36 million (2018: EUR 1.44 million) and disbursements amounted to EUR 1.09 million (2018: EUR 0.64 million). As at the year-end, the group's warranty provision amounted to EUR 3.50 million (31.12.2018: EUR 3.37 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.



MANAGEMENT SYSTEM OF THE GROUP'S NORWEGIAN SUBSIDIARY

In 2019, the management system of Peritus Entreprenør AS, a Norwegian construction company belonging to the group, was certified. The company was awarded all three certificates – ISO 9001, ISO 18001 and ISO 45001 – that the other construction companies of Merko group already possess.

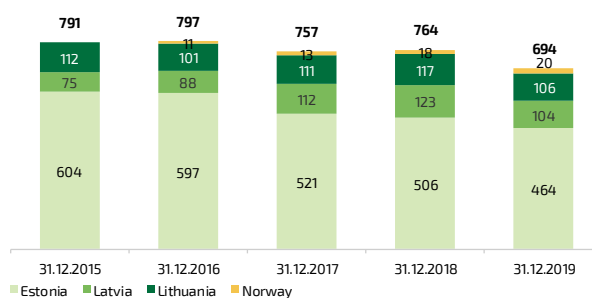
This addition to management system certificates confirms that the subsidiaries take the group's policies seriously in all of its home markets. Compliance with the international management system standard confirms that the company is a committed and trustworthy partner. The certificate also confirms that the quality, environment and health requirements and systematic management of these areas are respected.

EMPLOYEES

Compared to the same period last year, the number of the group's employees decreased by 70 (-9.2%) and as at 31 December 2019, the group had a total of 694 employees (including fixed-term and part-time employees).

92 people joined and 162 people left (2018: 166 people joined and 159 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

	2019		2018	
Permanent contract	642	93%	699	91%
Temporary contract	52	7%	65	9%
Total	694	100%	764	100%

TOTAL NUMBER OF EMPLOYEES BY GEOGRAPHICAL LOCATION

	2019		2018	
Estonia	464	67%	506	66%
Latvia	104	15%	123	16%
Lithuania	106	15%	117	15%
Norway	20	3%	18	3%
Total	694	100%	764	100%

TOTAL NUMBER OF PERMANENT EMPLOYEES BY EMPLOYMENT TYPE

	2019		2018	
Full-time	612	95%	660	94%
Part-time	30	5%	39	6%
Total	642	100%	699	100%

TOTAL NUMBER OF EMPLOYEES BY EMPLOYMENT POSITION

	2019		2018	
Management	17	2%	19	2%
Middle management, specialists	448	65%	493	65%
Workers	229	33%	252	33%
Total	694	100%	764	100%

TOTAL NUMBER OF EMPLOYEES BY GENDER

	2019		2018	
Male	589	85%	646	85%
Female	105	15%	118	15%
Total	694	100%	764	100%



SECTOR'S BIGGEST TAXPAYER

Merko values ethical business and strives to be a reliable and stable employer. We create a work environment conducive to good performance for our employees, an integral part of which is investing in occupational health and safety and providing development opportunities for our employees.

AS Merko Ehitus Eesti, the group's construction company in Estonia, employed almost 500 people and was the biggest contributor of state taxes and labour taxes in the Estonian construction sector in 2019, just like in 2018. In 2019, the companies belonging to the AS Merko Ehitus Eesti group paid nearly EUR 20.5 million in state taxes and EUR 10.9 million 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. Performance and development interviews as well as satisfaction surveys are regularly carried out to assess staff satisfaction and gather feedback.

THE NUMBER OF EMPLOYEES WHO RECEIVED AN ANNUAL PERFORMANCE REVIEW

	2019		2018	
Estonia	150	32%	126	25%
Latvia	72	69%	26	21%
Lithuania	99	93%	110	94%
Norway	-	-	-	-
Total	321	46%	262	34%

44 employees, including 13 office employees, 15 civil engineers and 16 construction workers, participated in the staff satisfaction survey carried out in the Lithuanian company UAB Merko Statyba in 2019. On a scale of 1 (completely satisfied) to 5 (completely unsatisfied), the average satisfaction index among those polled was 1.99. This means that staff members are satisfied with their job at the company.

In the Latvia based SIA Merks, a staff competence survey was conducted in 2019, measuring the level of satisfaction with the work arrangement and environment. The 72 staff members polled consider the company's working environment highly professional. They appreciate their versatile jobs and decision-making within the limits of their authorisation, and place high value in the company's dedication to staff training.

In 2019, the number of new grievances about labour practices against Merko group amounted to 0 (2018: none), the number of grievances (both from current and previous years) addressed was 0 (2018: none) and the number of grievances (both from current and previous years) resolved was 0 (2018: none).



INTERNS

Merko believes it is important to provide students with real work experience – over the past six years the group's subsidiaries have had more than 120 interns.

In 2019, Merko had eleven interns. Merko Ehitus Eesti provided practical work experience to ten young civil engineering students and one lawyer who took additional courses in construction law. The young people highly appreciated the experience gained at Merko and two students stayed in the company after their internship. In a job expectations and employer reputation survey conducted in 2019, with more than 5,300 respondents across Estonia, Merko Ehitus Eesti was recognized as an attractive employer by technology students.

HEALTH AND SAFETY

Group companies prioritise a safe working environment, preventing accidents at work and avoiding health damage. Merko has set its sights on maintaining a long-term capacity for work and ensuring staff's well-being. For this purpose, we provide our staff members with personal protective equipment required for work, and organise occupational health and safety training, along with in-service training. Depending on the level of occupational hazard, we ensure periodical health checks with our health service partners to prevent health problems, plan a safer working environment and ensure means of rehabilitation (e.g. massage therapy). As an additional measure for hedging health-related risks, we provide vaccination to our staff members, if they so desire. Furthermore, the company offers flexible working conditions, allowing employees to work part-time or from home office, take a winter holiday and maintain the salary during national defence drills.

Group construction companies adhere to the requirements established by the occupational health and safety laws and supplemented by the occupational health and safety management system. Group construction companies in Estonia and Lithuania were certified in 2019 under the ISO 45001 Occupational Health & Safety Management Standard. Our companies in Latvia are in the process of transitioning from OHSAS 18001 standards to ISO 45001 standards.

Intensive work in the construction area is balanced by our contribution to the personal lives of staff members and healthy lifestyle. In order to promote recreational sports and maintain the capacity for work, we endorse a healthy and active way of life, compensate recreational sports and health expenses of staff members, and organise joint sports competitions. Twice a year, AS Merko Ehitus organises a festive gathering for its staff members and their partners in life – a grand Christmas gala in the winter and an entertaining celebration of the Builders' day at the end of summer. A separate Christmas party is held for the children of our employees, along with Merko's children's day at the beginning of summer, giving the children a good overview of their parents' work and the construction area in general.

79% of Merko Ehitus group's employees worked in companies with an international health and safety certificate ISO 45001/OHSAS 18001 in 2019 (2018: 77%).



A COMPASSIONATE EMPLOYER

In 2019, Merko Ehitus Eesti continued with traditional employee events and trainings and launched new ones. For example, there were tennis tournaments for Merko employees in the spring and autumn with very active participation as Merko is the golden sponsor of the Estonian Tennis Association.

In 2019, a "Stranger friend" counselling programme was launched for the company employees. The counselling – a preventive measure for work stress and burnout – allows the employee to have an employer-paid counselling session with mental health professionals, providing the employee with support in coping with difficult situations, impartial feedback, and a confidential and trusting environment for self-analysis.

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

	2019	2018	2017
Total number of injuries/accidents excluding minor (first-aid level) injuries/accidents	3	7	9
Total number of occupational illnesses	0	0	0
Total number of lost days due to occupational injuries/accidents or illnesses	138	406	282
Total number of absentee days	4,451	7,324	7,700
Total number of fatalities *	0	0	0
Injury rate (per 100 employees)	0.5	1.0	1.3
Occupational diseases rate (per 100 employees)	0.0	0.0	0.0
Lost days rate (per 100 employees)	21.6	60.7	41.2
Absentee rate per year (%)	2.8	4.4	4.5

Calculation of ratios is provided on page 112 of the report.

* In 2019, 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 (2018: 3; 2017: 2), and 0 fatal accidents to such employees (2018: 0; 2017: 1).



OCCUPATIONAL SAFETY

Merko continued developing the area of occupational safety in 2019. Among other activities, the quality department of Merko Ehitus Eesti sought inspiration in Europe's first construction sector occupational safety training park in Espoo, Finland.

In 2019, the occupational health and safety concept was developed for the Merko Ehitus Eesti management system, along with the new occupational safety plan. Occupational safety coordinators received comprehensive training with regard to the renewed principles, with 48 staff members participating.

PERSONNEL DEVELOPMENT AND RECOGNITION

Merko's greatest value lies in its people. As an employer,

- we provide our staff members with the work for which they are prepared and have an interest in, and which offers them the opportunity to grow and develop;
- we remunerate our employees fairly, in line with their contribution to the achievement of corporate goals;
- we recognise staff members who have achieved or exceeded the agreed-upon goals.

Merko's training and development activities aim at supporting broad-based education of the employees as well as developing and enhancing teamwork. In order to maintain and enhance professional competence, we organise in-service training, with a preference on training which provides the in-service training points required for competence certification.

The Estonian subsidiary has launched a series of in-service trainings, addressing various issues relevant to construction sites, sharing knowledge and providing an overview of the regulations and standards to be adhered to. Internal training also serves the purpose of supporting the growth of social skills of the employees and enhancing teamwork. Training sessions also cover personal development, broadening horizons and topics of mental health. Our internal training series have been approved by the Estonian Association of Civil Engineers, allowing to gain in-service training credits.

We also lay emphasis on enhancing occupational health and safety-related knowledge. The persons responsible for or key employees engaging in the area (first aid administrators, work involving open flame, toolmakers, etc.) are regularly subjected to occupational health and safety training.

In order to secure the next generation of staff required, we have been involved, for a number of years, in developing and supporting the training of students, offering apprenticeships and giving lectures at schools. Furthermore, we have organised workshops and competitions for students, and tours of our construction sites. We provide broad support to our staff members' educational activities and acknowledge the pursuit of further education and diplomas whilst working.

We celebrate our staff members' personal life events - birthdays, birth of children and start of school. Our corporate events welcome employees' life partners, with family events organised for entire families. We offer additional benefits, such as an extra holiday, to those with long-term service in the company, recognising their contribution with an honorary ornamental pin.

We place high value in teamwork and a strong team spirit. In order to recognise the most prominent employees, teams and the best business partners, employees annually elect AS Merko Ehitus Eesti Achievers of the Year.



INTERNAL TRAINING

In 2019, the keyword for Merko Ehitus Eesti's internal training programme was sharing experiences. Initiated by the Quality Department, a training series was launched in which the on-site teams shared experiences and lessons learned in solving complicated situations. In addition, briefings were organized for the company's employees to introduce legal changes in the construction industry and details of engineering issues.

In 2019, the development programme for the top and middle managers at Merko Ehitus Eesti was launched in cooperation with the TalTech School of Business and Governance.

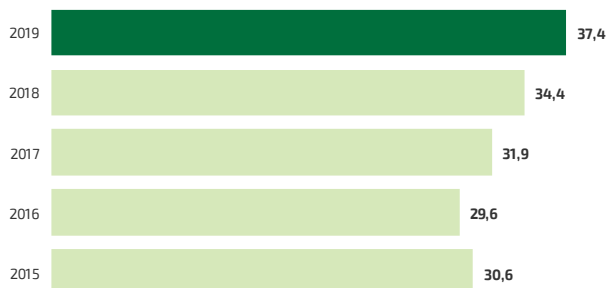
REMUNERATION

The group's objective is to pay its employees a competitive salary. In addition to basic remuneration, performance-based remuneration is paid.

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 2019, the labour cost was EUR 37.4 million (2018: EUR 34.4 million), up 8.8% 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 2019, the group received one hint, but no separate internal investigation was initiated – the complaint was based on a business-related contractual relationship with a third party and did not refer to unethical conduct that should have been addressed separately. Issues concerning contractual relations will be resolved in the ordinary course of business. (2018: 2 hints received that led to an internal investigation).

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 2019, no conflict of interest cases of key persons were identified by the group.

ENVIRONMENT

The activities of Merko group construction companies shape the urban environment and landscapes, with the main environmental impact generated through construction waste on construction sites. We therefore consider dealing with environmental aspects to be a high-priority area, organising the handling of waste and, where possible, ensuring separate collection of waste on the construction sites. We make sure that any waste generated on Merko's construction sites are handed over only to a waste handler with a waste permit, and keep systematic statistics on waste generated on the sites.

Our environment-related goals include sustainable use of all resources (materials, fuel, energy and water), reducing the amount of waste generated and supporting recovery of materials, where possible. To achieve all this, we promote among our employees and business partners awareness of the environment as a whole. We are the driving engine behind shaping the principles of recycling construction waste in the construction sector. In designing and building, we have set our sights on the main principles of the Quality and Sustainable Real Estate Lifecycle standard. In selecting building materials, we make an effort to ensure that the materials are VOC (volatile organic compounds) free and the manufacturers hold an ISO 14001 certificate.

Group construction companies adhere to the requirements established by the environmental laws and supplemented by the environmental management systems. Group construction companies are certified under ISO 14001.



ENVIRONMENTAL PROTECTION FACILITIES

Merko carried out the clean-up of residual pollution of two former asphalt concrete plants. On Saaremaa, the largest island of Estonia, the Maadevahe factory had polluted the surrounding soil, the aquifer and the Maadevahe River. In Valga, the soil and groundwater in the Priimetsa factory's territory were contaminated, and the pollution was threatening the Pedeli River.

The decontamination of asphalt concrete plants at Maadevahe and Priimetsa began in 2018 in cooperation with KMG Insenerihituse AS. More than 21,000 m³ of contaminated soil was disposed of in Maadevahe and nearly 11,000 m³ in Priimetsa. As part of the second phase of cleaning up the former Maadevahe factory, an additional 17,500 m³ of contaminated soil will be disposed of and work will be completed in 2020.

SOCIAL RESPONSIBILITY

The group has an impact on its employees, customers and partners as well as local communities, environment and society in general. We take responsibility for our decisions and activities that have an impact.

In 2019, 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.

In the financial year, the group supported sports, education and culture with donations amounting to a total of EUR 0.15 million (2018: EUR 0.2 million).

SPORTS AND RECREATIONAL SPORTS

Merko's largest sponsored project was the Eesti Terviserajad health trails project launched in 2005 in cooperation with Swedbank and Eesti Energia (<https://terviserajad.ee/>). The aim of the project is to renew and develop Estonian exercise and sports tracks, so as to ensure the availability of year-round free of charge possibility for active exercise in nature for all Estonian people, and popularise a sporty lifestyle. Over the last 15 years, SA Eesti Terviserajad (Estonian Health Trails Foundation) has taken on a noteworthy role in shaping people's exercising habits and popularising an active lifestyle through a network of health trails, various events and active outreach.

There are nearly four million visits to the health trails every year. Motion detectors were installed in 2019 on 40 health trails to collect more detailed statistics. Furthermore, weather sensors and 11 web cameras have been installed on the most popular trails. The foundation continued its active training, organising seminars and training sessions for the network and offering consulting to track masters. A practical training session was organised in cooperation with Czech bicycle track masters with regard to construction of bicycle trails, which were taken into focus in 2019.

86 trail maps have been installed for navigation purposes along with 38 stretching walls for preparatory and follow-up stretching, and trail marking developed by the foundation for 70 health trails. The foundation has produced more than 90 training videos in both Estonian and Russian languages, along with various promotional videos which were viewed nearly two million times via different channels in 2019.



STRONG NETWORK OF HEALTH TRAILS

In 15 years, 116 health trails and 1,110 km of exercise and sports tracks have been built all over Estonia, including 910 km of soft-covered trails, 200 km of hard-surfaced roads and 255 km of illuminated roads and trails. Per 100,000 inhabitants, Estonia has an average of 83.7 km of health trails with regular cleaning and snow clearance and 19.2 km of illuminated health trails.

Estonian Health Trails Foundation designed the Õismäe Bog health trail, the Ehitajate tee tunnel, the viaduct and tunnel as well as the light traffic road for the Järve health trail, all of which the city of Tallinn constructed in 2019. In addition to the Õismäe track, the Järta health trail in Märjamaa and the Pärnu-Jaagupi health trail in Pärnu County were added to the network in 2019.

With the aim of emphasising the importance of regular physical activity and to facilitate exercising within buildings, the foundation has developed the concept of indoor health trails. In cooperation with various organisations, enterprises and schools, suitable tracks have been laid out within buildings, taking advantage of staircases, corridors and courtyard areas. As at the end of 2019, there were a total of 75 indoor tracks in Estonia, providing daily access to more than 75,000 people.

Supported by its founders, the foundation invested EUR 5.1 million in the development of health trails between 2005 and 2019. The total investment made in the development of the Estonian health trail network between 2004 and 2019 (in addition to the foundation's own resources; also includes investments made by the state and local governments as well as EU funds) amounts to nearly EUR 50 million. Investments have been made in all Estonian counties, with the top three counties being Harjumaa, Tartumaa and Ida-Virumaa. Based on the preferences and usage of the local population, the largest investments have been made in the recreational centres and trails of Pirita, Nõmme-Harku, Kõrvemaa and Jõulumäe.

In 2019, the Ministry of Culture became the fourth equal partner, supporting the achievement of the objectives of the Estonian Health Trails. With the support measures launched in 2019 for regional recreational sports centres, the capacity for making artificial snow and maintaining tracks will be enhanced in 2019-2022, along with development of new tracks. In cooperation with the state and local governments, a total of EUR 4.8 million will be allocated to the 24 trails participating in the measure.

Merko also continued supporting professional sports in 2019, contributing to professional tennis and the organisation of international tournaments as a gold sponsor of the Estonian Tennis Association. To the home audience's delight, Merko Estonian Open, held in July 2019 in Pärnu, saw Estonian tennis players in all matches in the finals, with Jürgen Zopp succeeding in defending his title from 2017. Merko also supported the 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 options of promoting various cultures and arts. We have enjoyed close cooperation with the Art Museum of Estonia since 2005. In 2019, we celebrated the opening of the new exhibition solution for Notke's Danse Macabre. The solution for the exclusive and grandiose work of art was created by KOKO architects. For the first time in Estonia, the tailor-made exhibition solution utilises large-scale exhibition glass, specially prepared for the purpose. Over 8 m in length and weighing in at 600 kg, the special protective glass was made in Germany and allows to examine the painting in the most authentic form possible.

Merko supports education with the aim of promoting professional education and training the next generation of civil engineers. Merko cooperates closely with the Tallinn University of Technology and the Estonian Academy of Arts.

Since 2007, we have awarded scholarships to engineering students and young teaching staff at the Tallinn University of Technology with the aim of supporting the next generation of civil engineers and allowing the teaching staff to provide them with the best educational background possible. In 2019, the Merko scholarship was awarded to Ergo Pikas, a researcher with the department of civil engineering, who has actively participated in scientific research and several research projects in both Estonia and abroad. The engineering scholarship was awarded to Jane Kikojan, a 5th year student in the faculty of design and construction management, who stands out as an extremely focused student. Her internship in Merko showed that her diligence and ambition to challenge herself is bound to support her path towards becoming a top player in the field.

In the Estonian Academy of Arts, the digital tools studio was opened with the help of Merko in the academic year 2018/2019, focusing on designing a large-scale energy efficient building.

In Latvia, Merks supported, for the second year in a row, the Student Association of Riga Technical University's Civil Engineering Faculty, participating in the "Step into the Engineer's Shoes" initiative. The initiative involves a job shadowing day, allowing students to spend a day with the construction site team and to experience its everyday work. In total, the Merks staff accepted 20 students - 15 in the Laima plant site, 3 in the Lidl logistics centre site and 2 in the Riga Technical University site.

Merks also supported the City of Riga's participation in MIPIM, the world's largest real estate fair, as well as BREL, the Baltic States real estate forum, held annually in Riga.



EDUCATIONAL OBJECTS

In 2019, Merko contributed to the construction of educational facilities in Estonia, Latvia and Lithuania. For Rakvere Vocational School, Merko built a student accommodation for 200 students, the most modern in Estonia, and a multifunctional sports field with all the necessary facilities. The Ventspils Music School and Concert Hall, seating 600 people, were completed in Ventspils, Latvia in 2019. Two schools were opened in Vilnius: a new Catholic school building for 240 students and 80 nursery school children, and a general education school for 800 students and pre-school children.

The construction of educational buildings will continue. In 2020, the new study and sports building for Türi Basic School will be completed and the construction works of Tallinn Arte Gymnasium and Tallinn Music and Ballet School will begin.

RECOGNITIONS 2019

In 2019, the following AS Merko Ehitus group companies were recognised:

MOST COMPETITIVE CONSTRUCTION COMPANY AND LARGE ENTERPRISE

The Estonian Chamber of Commerce and Industry recognized AS Merko Ehitus as the most competitive Estonian construction company in 2019, for the thirteenth time. Merko also received the Most Competitive Estonian Large Enterprise award in 2019 (previously in 2015). The competitiveness rankings have been compiled since 2003 with the aim of contributing to the enhancement of the competitiveness of Estonian companies as well as faster development of the economy in general.

ESTONIA'S BEST-KNOWN REAL ESTATE DEVELOPER

According to the results of the real estate brand survey conducted by Kantar Emor in 2019, Merko is Estonia's best-known real estate developer. The survey studied both the reputation and awareness of the brand, with 59% of those requested to spontaneously recall real estate developers naming Merko. A total of 600 people were polled, including 267 respondents intending to purchase an apartment in a new residential development in Tallinn or its vicinity, and 214 buyers, who have recently purchased an apartment in the capital or Harju County.



URBAN SPACE DEVELOPMENT AT NOBLESSNER

Former Tsarist Russia submarine factory in Noblessner, Tallinn, has become a port area open to people and the sea, and Merko, in cooperation with BLRT, has created a modern living environment there.

In addition, Merko has also helped to design a beautiful public space. In conjunction with the construction of the Staapli residential quarter, Krusenstern Square was built, and in 2019 the reconstruction of the Noblessner quay and completion of a long-awaited seaside promenade were completed. For boats visiting the marina, the breakwater built with Insenerihituse AS makes sailing safer.

BUILDER OF THE YEAR

The jury set up by the Estonian Association of Construction Entrepreneurs declared Sergei Strigin, deputy director of the general construction division of AS Merko Ehitus Eesti, the winner of the Builder of the Year 2019 competition. The victory can be attributed to Sergei Strigin's contribution in the management of the construction work on the Tallink office building. The purpose of the competition is to honour the best construction manager, whose work has received recognition from the contracting entity, the architect, the designer as well as by the party conducting owner supervision. The Builder of the Year award was handed out for the eleventh time, with employees of Merko declared winners on five occasions.

CONSTRUCTION PROJECT OF THE YEAR AND THE BEST DIGITAL INNOVATION PROJECT

The Construction Project of the Year 2019 award of the Estonian Association of Architectural and Consulting Engineering Companies went to Maakri Kvartal in the buildings category, with the special prize for the Best Digital Innovation Project 2019 awarded by the Ministry of Economic Affairs and Communications to the T1 Mall of Tallinn shopping centre project. The Construction Project of the Year award serves to draw attention to fascinating buildings and facilities, and to recognise the designers behind the creation of the same. Last year, the central square of Tõrva, built by Merko, won the title of the Best Civil Engineering Facility. The special prize of digital construction was handed out by the Ministry of Economic Affairs and Communication for the third time. On all occasions, a project related to Merko has been declared the winner.

ATTRACTIVE EMPLOYER AMONG SCIENCE AND TECHNOLOGY STUDENTS

The employer branding agency Instar carried out a job expectations and employer reputation survey in 2019, with more than 5,300 people polled all over Estonia. The survey studied the attractiveness of 220 Estonian organisations. Merko Ehitus Eesti ranked sixth among students in science and technology fields, and was also the highest-ranking employer among construction enterprises. Instar has conducted employer attractiveness surveys since 2010. Merko has received the Attractive Employer label on every year since 2016.

STUDENT PRIZES OF THE ESTONIAN CONCRETE ASSOCIATION

Two employees of Merko Ehitus Eesti were awarded the student prizes of the Estonian Concrete Association in 2019. Kerdo Kütt (with co-author), junior designer in model design, received an award for the diploma paper in the field of construction in the Tallinn University of Applied Sciences. Klaid Melnikov, junior site manager of the South Estonia division received an award for the master's thesis in rural building in the Estonian University of Life Sciences. The Estonian Concrete Association has recognised the best concrete-related student theses since 2007, with the aim of enhancing academic work on materials and concrete building.

MOST ENERGY EFFICIENT BUILDING IN LATVIA

In the Most Energy Efficient Building in Latvia 2019 competition, the Merks Gaiļezera nami building at Gaiļezera 15 in Riga, developed and constructed by SIA Merks, ranked second in the Most Energy Efficient Apartment Building (New Construction) category. The competition is organised by the Latvian Ministry of Economy, the Ministry of Environmental Protection and Regional Development and the Būvzinieris magazine.

CONSTRUCTION INDUSTRY GRAND PRIX 2019

In the Construction Industry Grand Prix 2019 competition organised by the Latvian Association of Civil Engineers, SIA Merks's employee Janeks Joma received the Project Manager of the Year award, with a special prize awarded to Zigmunds Urtāns. Merks set up the candidates based on their experience in the company, and the feedback gathered from colleagues and partners.

LATVIA'S BUILDING OF THE YEAR 2018

In 2019, the first stage of development of the Magdelēna quarter in Riga received several acknowledgments. The project was awarded first prize in the category "New residential building" of the competition "Latvian Construction Awards 2018" organized by the Building Design and Construction Council, and in the category "New residential building" of the competition "The Best Building of the Year in Latvia in 2018" organized by the Latvian Builders Association. In the same competition, the building at Rūpniecības Street 25 of the development project Merks Viesturdārzs in Riga received a nomination in the category "Innovation in Construction".

BEST BIM PROJECT IN LITHUANIA

The apartment development project Vilnelės slėnis received first prize in the residential buildings category of the Lithuanian BIM projects 2019 competition.

MOST ATTRACTIVE EMPLOYER IN THE LITHUANIAN CONSTRUCTION SECTOR

In the Personnel 2019 competition, the most attractive employers in different sectors were announced. Merko Statyba was recognised as the most attractive employer in the Lithuanian construction sector. The top list prepared by the Verslo Žiniose business magazine and the cv.lt portal took account of the financial indicators of companies, as well as wage and employee dynamics indicators.

SHARE AND SHAREHOLDERS

The shares of Merko Ehitus are listed in the Main List of Nasdaq Tallinn. As at 31 December 2019, the company has 17,700,000 shares. The number of shares did not change during 2019.

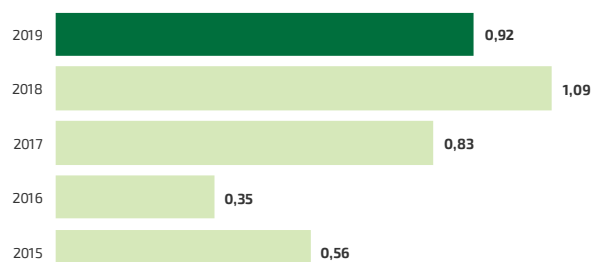
In 2019, 8,558 transactions were conducted with the shares of Merko Ehitus in the course of which 2.23 million shares were traded (12.6% of shares outstanding), with the total monetary value of transactions at EUR 21.3 million (comparative data for 2018: 4,299 transactions, in the course of which 1.18 million shares were traded (6.7% of shares outstanding) and the total monetary value of transactions was EUR 12.2 million). The lowest share price was EUR 8.74 and the highest share price was EUR 10.30 (2018: EUR 8.70 and EUR 11.80 respectively). The closing price of the share as at 31 December 2019 was EUR 9.38 (31.12.2018: EUR 9.20). As at 31 December 2019, by the Nasdaq Baltic stock exchange, the market capitalisation of AS Merko Ehitus was EUR 166.0 million, up 2.0% compared to the end of the equivalent period in the prior year (31.12.2018: EUR 162.8 million).

The number of shares that belong to the members of Supervisory Board and Management Board as at 31 December 2019 was 9,962,334 (31 December 2018: 9,962,334 shares) that accounted for 56.3% of the total number of shares (31 December 2018: 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.

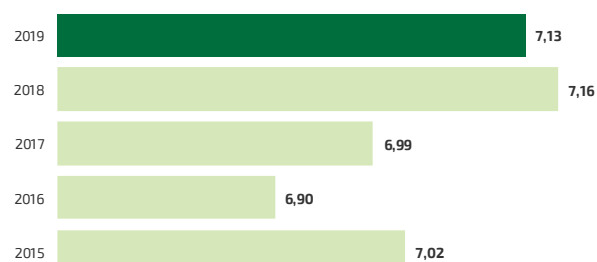
INFORMATION ON SECURITY

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 issued securities	17,700,000
Number of listed securities	17,700,000
Currency	EUR
Listing date	11 August 2008

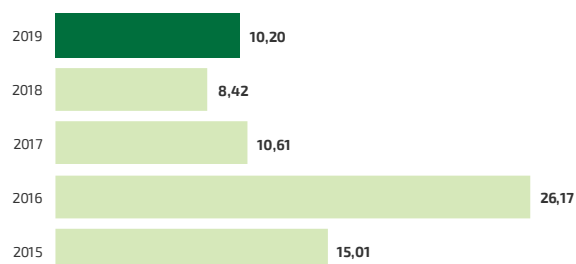
EARNINGS PER SHARE (EPS) euros



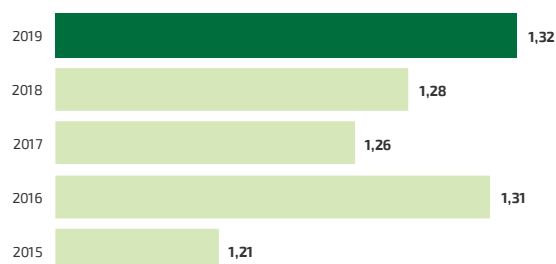
EQUITY PER SHARE euros

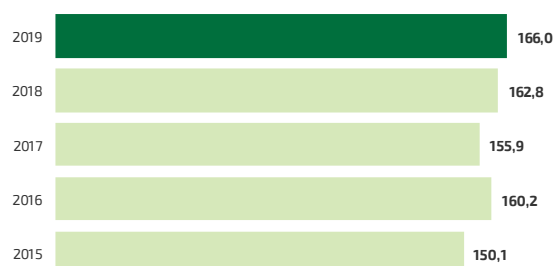
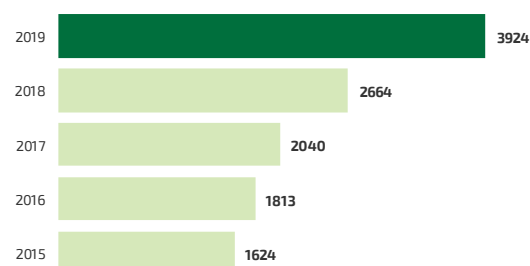
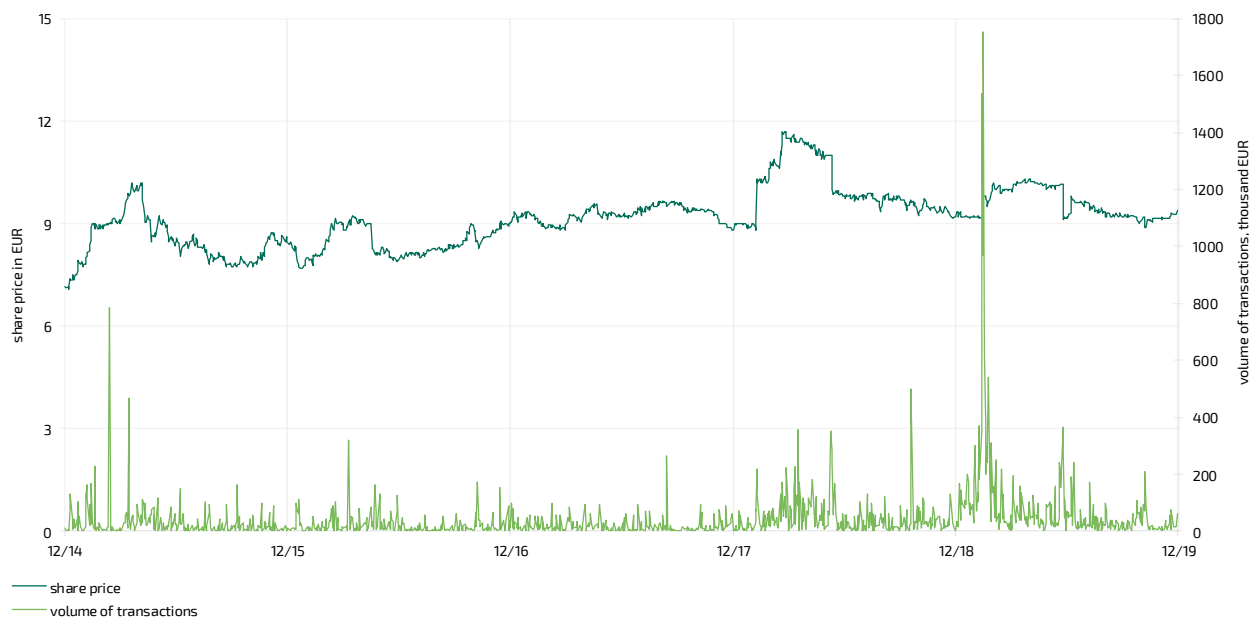


P/E RATIO times



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

	2019	2018	2017
Highest	10.30	11.80	9.69
Lowest	8.74	8.70	8.75
Average	9.55	10.02	9.27
Closing as at 31.12	9.38	9.20	8.81
Change as at 31.12, %	+2.00	+4.43	(2.65)
Traded shares, pcs	2,231,912	1,178,232	508,339
Turnover, million EUR	21.31	12.16	4.69
Market value as at 31.12, million EUR	166.0	162.8	155.9

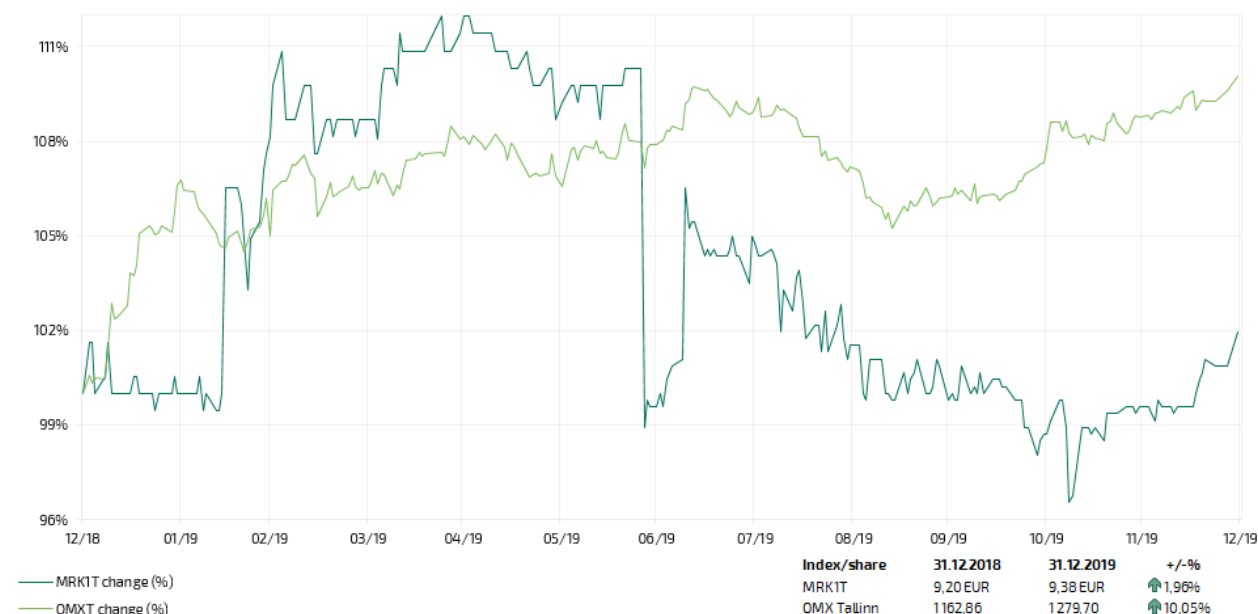
STRUCTURE OF SHAREHOLDERS ACCORDING TO NUMBER OF SHARES AS AT 31.12.2019

NUMBER OF SHARES	NUMBER OF SHAREHOLDERS	% OF SHAREHOLDERS	NUMBER OF SHARES	% OF SHARES
1 000 001 - ...	1	0.03%	12,742,686	71.99%
100 001 - 1 000 000	9	0.23%	1,615,685	9.13%
10 001 - 100 000	43	1.10%	1,037,150	5.86%
1001-10 000	516	13.15%	1,484,002	8.38%
101-1000	1,932	49.24%	746,499	4.22%
1-100	1,423	36.25%	73,978	0.42%
Total	3,924	100%	17,700,000	100%

STRUCTURE OF SHAREHOLDERS ACCORDING TO HOLDER CATEGORIES AS AT 31.12.2019

CATEGORY	NUMBER OF SHAREHOLDERS	% OF SHAREHOLDERS	NUMBER OF SHARES	% OF SHARES
Insurance corporations	1	0.03%	148,787	0.84%
Non-profit institutions serving households	1	0.03%	1,500	0.01%
Pension funds	1	0.03%	7,883	0.04%
Foreign controlled non-financial corporations	2	0.05%	1,500	0.01%
Public non-financial corporations	2	0.05%	8,315	0.05%
Non-MMF investment funds	3	0.07%	633,114	3.58%
Financial auxiliaries	7	0.18%	192,917	1.09%
Deposit-taking corporations except the central bank	22	0.56%	687,393	3.88%
Other financial intermediaries	22	0.56%	252,579	1.43%
Captive financial institutions and money lenders	23	0.58%	379,306	2.14%
National private non-financial corporations	370	9.43%	13,322,444	75.27%
Households	3,470	88.43%	2,064,262	11.66%
Total	3,924	100%	17,700,000	100%

PERFORMANCE OF THE SHARE OF MERKO EHITUS AND COMPARISON INDEX OMX TALLINN IN 2019



SHAREHOLDERS OF AS MERKO EHITUS AS AT 31.12.2019 AND CHANGE COMPARED TO THE PREVIOUS YEAR

	NUMBER OF SHARES	% OF TOTAL 31.12.2019	% OF TOTAL 31.12.2018	CHANGE
AS Riverito	12,742,686	71.99%	71.99%	-
Firebird Republics Fund Ltd	329,602	1.86%	2.05%	(33,492)
OÜ Midas Invest	296,100	1.67%	1.19%	85,420
Firebird Aurora Fund Ltd	188,927	1.07%	1.26%	(33,492)
Skandinaviska Enskilda Banken AB, Swedish customers	161,438	0.92%	0.90%	1,879
State Street Bank and Trust Omnibus Account a Fund No OM01	153,018	0.86%	0.86%	-
SEB Elu- ja Pensionikindlustus AS	148,787	0.84%	0.81%	5,900
Siseinfo OÜ	115,000	0.65%	0.57%	15,000
Firebird Fund L.P.	114,585	0.65%	0.74%	(16,746)
Clearstream Banking AG	108,228	0.61%	-	108,228
Total largest shareholders	14,358,371	81.12%	80.37%	132,697
Total other shareholders	3,341,629	18.88%	19.63%	(132,697)
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.

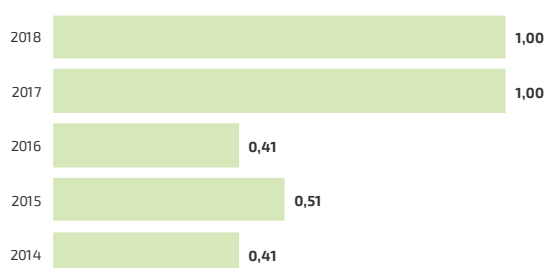
According to AS Merko Ehitus long-term financial objectives, 50-70% of the annual profit are distributed to shareholders as dividends.

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. As the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018, only the 20/80 regular rate of income tax was applied to dividends paid in 2019 (i.e. the rate of 14/86 on regularly payable dividends was not applied) and no additional income tax was withheld from dividends paid to shareholders that were natural persons. The dividend payment to the shareholders took place on 1 July 2019.

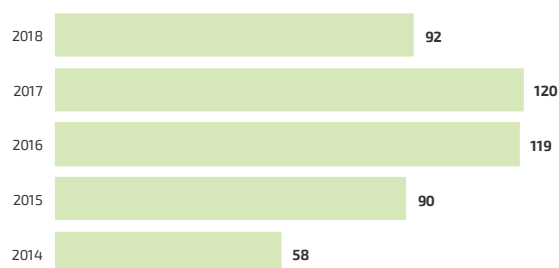
While the group did not incur income tax expenses arising in connection with disbursement of dividends in Estonia in 2018, it did incur these in 2019 in the case of EUR 10.3 million of paid dividends. Due to that, in 2020, the group will apply the 14/86 income tax rate on regularly payable dividends on one third of the EUR 10.3 million, i.e. EUR 3.4 million, of the possible (net) dividends paid. The group will withhold additional 7% income tax from dividends paid to shareholders that are natural persons and on which the 14/86 income tax rate has been applied. The decision to pay dividends for the year 2019 shall be taken by the general meeting of shareholders.

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

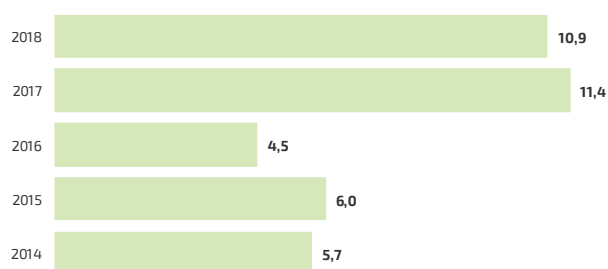
DIVIDEND PER SHARE
euro



DIVIDEND RATE
percentages



DIVIDEND YIELD *
percentages



* Using share price as at 31.12

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.

CORPORATE GOVERNANCE RECOMMENDATIONS REPORT

CORPORATE GOVERNANCE AND STRUCTURE

Adherence to the principles of Corporate Governance Recommendations 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 Corporate Governance Recommendations 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 2019.

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, SIA Merks, UAB Merko Statyba, AS Peritus Entreprenør and the companies belonging to the AS Merko Ehitus Eesti group: Tallinna Teede AS and AS Merko Infra.

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 2019 is the following:



As at 31 December 2019, the group comprises of 33 companies (31.12.2018: 31). 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, amendments to the articles of association, 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. In amending the articles of association, the general meeting of shareholders follows the regulation as per the Estonian Commercial Code. A resolution on amendment of the articles of association shall be adopted if at least two-thirds of the votes represented at a general meeting are in favour. 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 8 May 2019. The general meeting resolved to approve the annual report and the profit allocation proposal for 2018. The dividends in the sum of EUR 17.7 million (EUR 1 per share) were paid out to the shareholders on 1 July 2019.

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 Corporate Governance Recommendations, 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 2019, 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 2019 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 Janno Hermanson (Auditor).

The group is not aware of any agreements between its shareholders on the coordination of exercising the shareholders' rights.

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 2019, 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 Kapital (AS E.L.L. Kinnisvara until 2017), Chairman of the Supervisory Board
 2009-2014 AS E.L.L. Kinnisvara, Member of the Management Board
 2008-... Järvevana OÜ, Member of the Management Board
 1999-2009 AS E.L.L. Kinnisvara, 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 controlled: 12,742,686 (AS Riverito)

Toomas Annus holds the majority of the votes represented by shares in AS Riverito directly and through holding companies (176,351 shares out of a total of 270,000 shares). With that the votes held by AS Riverito in AS Merko Ehitus (12,742,686 shares) are deemed to belong to Toomas Annus.

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 Kapitel (AS E.L.L. Kinnisvara until 2017), 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)

According to the requirements of the Corporate Governance Recommendations Indrek Neivelt was an independent member of the Supervisory board.

The meetings of the Supervisory Board generally take place once a month, except in summer months. In 2019, the Supervisory Board held 11 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	10	91%
Teet Roopalu	11	100%
Indrek Neivelt	11	100%

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 2019 and 2018 financial years, the members of the Supervisory Board were remunerated as follows (in euros):

NAME	2019	2018
Toomas Annus	-	35,152
Teet Roopalu	38,347	38,347
Indrek Neivelt	38,347	38,347
TOTAL	76,694	111,846

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 forgone 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 UAB Merko Statyba and UAB Merko Bustas

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: 5 June 2022

Positions held:

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

2014-... AS Kapitel (AS E.L.L. Kinnisvara until 2017), Member of the
Supervisory Board

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

2009-2014 AS E.L.L. Kinnisvara, Chairman of the Supervisory Board

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

1999-2009 AS E.L.L. Kinnisvara, Member of the Supervisory Board

1997-1999 AS E.L.L. Kinnisvara, 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,
UAB Merko Statyba and UAB Merko Bustas, Chairman of the
Supervisory Board of Tallinna Teede AS

Education:

Tallinn University of Technology, industrial and civil engineering

Number of shares controlled: -

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. Bonuses are paid to the Management Board members once a year.

In the 2019 and 2018 financial years, the Management Board members' gross remuneration incl. service fees and bonuses, accrued for the reporting year were as follows (in euros):

NAME	2019	2018*
Andres Trink	329,702	312,674
Tõnu Toomik	276,568	278,483
TOTAL	606,270	591,157

**the figures for 2018 have been adjusted: the remuneration awarded for the financial year have been reported here, instead of the previously reported costs on remuneration reserve.*

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 2019:

COMPANY *	SUPERVISORY BOARD	MANAGEMENT BOARD
AS Merko Ehitus Eesti (62,868,838 euros)	Andres Trink (Chairman), Teet Roopalü, Tõnu Toomik, Martin Rebane	Keit Paal (Chairman), Jaan Mäe, Alar Lagus, Veljo Viitmann
Tallinna Teede AS (11,778,565 euros)	Tõnu Toomik (Chairman), Keit Paal, Alar Lagus, Veljo Viitmann	Jüri Läll (Chairman), Jüri Helila
OÜ Merko Investments (21,579,141 euros)	-	Andres Trink, Priit Roosimägi
SIA Merks (23,307,046 euros)	Andres Trink (Chairman), Tõnu Toomik, Priit Roosimägi, Janis Šperbergs	Oskars Ozoliņš (Chairman), Andris Bišmeistars
UAB Merko Bustas (7,997,711 euros)	Andres Trink (Chairman), Tõnu Toomik, Priit Roosimägi	Saulius Putrimas (Chairman)

* The figures in brackets indicate the amount of equity held by the parent company's owners in significant subsidiaries as at 31 December 2019.

Changes in the management of group subsidiaries

The Management Board of AS Merko Ehitus appointed Mr. Martin Rebane as a Member of the Supervisory Board of AS Merko Ehitus Eesti, part of AS Merko Ehitus group, starting from 30 April 2019. The Supervisory Board of AS Merko Ehitus Eesti will continue with four members: Mr. Andres Trink (Chairman), Mr. Tõnu Toomik, Mr. Teet Roopalü and Mr. Martin Rebane. According to the articles of association of AS Merko Ehitus Eesti, a Member of the Supervisory Board is appointed for three years.

The Supervisory Board of AS Merko Ehitus Eesti, part of AS Merko Ehitus group, extended the powers of the Chairman of the Management Board, Mr. Keit Paal, until 31 December 2019, and appointed Mr. Ivo Volkov as the new Chairman of the Management Board starting from 1 January 2020. The powers of Mr. Ivo Volkov as the Chairman of the Management Board of AS Merko Ehitus Eesti are in place from 1 January 2020 until 31 December 2022. Mr. Jaan Mäe, Mr. Alar Lagus and Mr. Veljo Viitmann remain as members of the Management Board of AS Merko Ehitus Eesti.

Mr. Teet Roopalü, Member of the Supervisory Board of AS Merko Ehitus Eesti, part of AS Merko Ehitus group, notified the Management Board of AS Merko Ehitus of his resignation from the position of the Member of the Supervisory Board starting from 1 January 2020. As per the decision of the Management Board of AS Merko Ehitus, the Supervisory Board of AS Merko Ehitus Eesti will continue with three members starting from January 1 2020: Mr. Andres Trink (The Chairman), Mr. Tõnu Toomik and Mr. Martin Rebane.

On 23 January 2020, the Management Board of AS Merko Ehitus Eesti, part of AS Merko Ehitus group, decided to make the following changes in the Supervisory Board of subsidiary Tallinna Teede AS: to remove Mr. Keit Paal as a member; to appoint Mr. Ivo Volkov as a member for a three years' period starting from 23 January 2020, and to extend the powers of the member Mr. Tõnu Toomik for three years starting from 23 January 2020. The Supervisory Board of Tallinna Teede AS will continue with four members: Mr. Tõnu Toomik (The Chairman), Mr. Ivo Volkov, Mr. Veljo Viitmann and Mr. Alar Lagus.

On 30 January 2020, the Supervisory Board of Tallinna Teede AS – the subsidiary of AS Merko Ehitus Eesti, part of AS Merko Ehitus group – decided to extend the powers of the Chairman of the Management Board, Mr. Jüri Läll, from 31 January 2020 until 30 January 2023. The Management Board of Tallinna Teede AS will continue in the current two-member panel: Mr. Jüri Läll (The Chairman) and Mr. Jüri Helila.

There will be a change in the Management Board of SIA Merks – part of AS Merko Ehitus group – as of 1 April 2020. Mr. Oskars Ozoliņš, who has held the position of the Chairman of the Management Board since 2012, will leave the company and current Member of the Management Board and Construction Director Mr. Andris Bišmeistars will start as the new Chairman of the Management Board. The Management Board of SIA Merks will continue with one member. In addition, according to the decision of the general meeting of shareholders from 11 February 2020, the powers of the Member of the Supervisory Board, Mr. Janis Šperbergs are ending as of 1 April 2020. The Supervisory Board of SIA Merks will continue with three members: Mr. Andres Trink (Chairman), Mr. Tõnu Toomik, and Mr. Priit Roosimägi.

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 members of the audit committee of AS Merko Ehitus are: Mr. Teet Roopalu (the Chairman), Mr. Indrek Neivelt and Mr. 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 Tiit Raimla 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 2019, PwC provided to AS Merko Ehitus advisory services permitted under Estonian Audit Act. We find that the financial audit conducted in 2019 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 independent report is presented on pages 100-106.

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 2019, the group's insider register lists 77 persons with permanent access (31.12.2018: 74 persons). The group keeps records on insiders in accordance with requirements set forth in the Securities Market Act, the Regulation (EU) No 596/2014 of the European Parliament and of the Council (market abuse regulation) and Nasdaq Tallinn rules and regulations.

To the best of our knowledge, in the financial year 2019 there were no cases of any misuse of insider information or conflicts of interest. No transactions with related parties were made at other than market terms. No transactions between the company and its

member of the board, a person close to or connected to the member of the board were carried out in the financial year of 2019, which would be regarded as significant for the company.

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

NAME	RELATED COMPANY
Toomas Annus	AS Riverito, Kardispordi Arendamise OÜ, Kental 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 2019 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 2019, AS Merko Ehitus published 37 stock exchange releases through the stock exchange system.

NUMBER OF RELEASES	CONTENT OF RELEASE
14	New construction contracts
6	New development projects
5	Operating results
4	Changes in structure and management
2	General meeting
1	New development areas
5	Other releases

We will publish 2020 consolidated interim reports as follows:

DATE	EVENT
07.05.2020	2020 3 months unaudited interim report
06.08.2020	2020 6 months and II quarter unaudited interim report
05.11.2020	2020 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 presentations 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 2019, AS Merko Ehitus organised 9 investor meetings (2018: 9), including 1 investor tour (2018: 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

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

AS LHV PANK

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

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

ANDRES TRINK

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DECLARATION OF CONFORMITY TO CORPORATE GOVERNANCE RECOMMENDATIONS

The Corporate Governance Recommendations (CGR) are based on the principle of comply or explain, according to which a publicly traded company shall explain its standpoints and activities with regard to those CGR provisions, which it does not comply with.

We have assessed the structure and functions of the management of AS Merko Ehitus on the basis of CGR. 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 CGR. Also, our activities comply with the Estonian legislation that regulates several principles provided in the recommendations in more detail. We hereby declare that AS Merko Ehitus has followed all corporate governance recommendations, with the following exceptions:

CORPORATE GOVERNANCE RECOMMENDATIONS ¹	EXPLANATIONS BY MANAGEMENT AND SUPERVISORY BOARDS
1.3.2 Members of the Management Board, the Chairman of the Supervisory Board and if possible, the members of the Supervisory Board and at least one of the auditors shall participate in the General Meeting.	The Chairman of the Supervisory Board did not attend the annual general meeting held in 2019 because of personal reasons.
1.3.3 Issuers shall make participation in the General Meeting possible by means of communication equipment (Internet) if the technical equipment is available and where doing so is not too cost prohibitive for the Issuer.	AS Merko Ehitus did not provide the possibility to observe and attend the regular general meeting in 2019 through means of communication as such need has not been identified so far.
2.2.7 Basic wages, performance pay, severance packages, other payable benefits and bonus schemes of a Management Board member as well as their essential features (incl. features based on comparison, incentives and risk) shall be published in clear and unambiguous form on website of the Issuer and in the Corporate Governance Recommendations Report. Information published shall be deemed clear and unambiguous if it directly expresses the amount of expense to the Issuer or the amount of foreseeable expense as of the day of disclosure.	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.
3.2.2. At least half of the members of the Supervisory Board of the Issuer shall be independent. If the Supervisory Board has an odd number of members, then there may be one independent member less than the number dependent members. An independent member is a person, who has no such business, family or other ties with the Issuer, a company controlled by the Issuer, a controlling shareholder of the Issuer, a company belonging to the Issuer's group or a member of a directing body of these companies, that can affect their decisions by the existence of conflict of interests. The independence requirements are presented in the annex of the Corporate Governance Recommendations. ANNEX. Requirements of independence Independent is the member of the Supervisory Board, who: (h) has not been an independent member of the Supervisory Board for more than ten (10) years;	The supervisory board of AS Merko Ehitus consists of three members, of which Indrek Neivelt is an independent member. Indrek Neivelt has been a member of the supervisory board since 6 November 2008, i.e. for more than ten years. Still, the management and supervisory boards are convinced that Indrek Neivelt remains independent from the Issuer, any company controlled by the Issuer, the controlling shareholder of the Issuer, any company belonging to the Issuer's group or any member of a directing body of these companies, when making decisions as the member of the supervisory board. Indrek Neivelt continues to comply with all other requirements of independence and as a member of the supervisory board acts in the best interests of all the shareholders.
5.2 The Issuer shall publish the disclosure dates of information subject to disclosure throughout a year (including the annual report, interim reports and notice calling a general meeting) at the beginning of the fiscal year in a separate notice, called financial calendar.	AS Merko Ehitus disclosed the financial calendar for 2020 on 9 December 2019. 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 On meeting of the Supervisory board, where the annual account shall be reviewed the auditor of the Issuer shall participate upon invitation of 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.

¹ Corporate Governance Recommendations, Finantsinspektsioon (FSA in Estonia), https://www.fi.ee/failid/HYT_eng.pdf

According to subsection 24² (4) of the Accounting Act, a large undertaking whose securities granting voting rights have been admitted for trading on a regulated securities market of Estonia or another Contracting State shall describe in the corporate governance report the diversity policies carried out in the company's management board and senior management and the results of the implementation thereof during the accounting year. If no diversity policies have been implemented during the accounting year, the reasons for this should be explained in the corporate governance report.

Merko Ehitus has not deemed it necessary to implement diversity policies as it bases its decisions on onboarding, work assessments and remuneration of its managers and employees on the group's best interests as well as the education, competencies and work results of the managers and employees, and not on their sex and gender, age, ethnicity or other such characteristics. The group has enacted a code of business ethics, which also includes the principle of equal treatment of employees. In 2019, no such violations were identified in the group, which would have suggested discrimination of employees or violations of human rights. Also, no work related complaints were submitted to labour dispute committees against the group in 2019.

MANAGEMENT DECLARATION

The Management Board declares and confirms that according to their best knowledge, the year 2019 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	/ digitally signed /	31.03.2020
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Tõnu Toomik	Member of the Management Board	/ digitally signed /	31.03.2020
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CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

in thousands of euros

	Note	2019	2018
Revenue	4	326,779	418,011
Cost of goods sold	5	(291,958)	(384,962)
Gross profit		34,821	33,049
Marketing expenses	6	(4,260)	(3,285)
General and administrative expenses	7	(12,988)	(12,304)
Other operating income	8	2,983	3,527
Other operating expenses	9	(1,318)	(1,115)
Operating profit		19,238	19,872
Finance income	10	3	8
Finance costs	11	(684)	(696)
Profit (loss) from sale and liquidation of subsidiary	19	-	(62)
Profit (loss) from joint ventures	20	1,766	653
Profit before tax		20,323	19,775
Corporate income tax expense	12	(3,833)	(375)
Net profit for financial year		16,490	19,400
incl. net profit attributable to equity holders of the parent		16,270	19,343
net profit attributable to non-controlling interest		220	57
Other comprehensive income (loss), which can subsequently be classified in the income statement			
Currency translation differences of foreign entities		13	(6)
Comprehensive income for the period		16,503	19,394
incl. attributable to equity holders of the parent		16,281	19,324
attributable to non-controlling interest		222	70
Earnings per share for profit attributable to equity holders of the parent (basic and diluted, in EUR)	13	0.92	1.09

The notes set out on pages 55-99 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	Note	31.12.2019	31.12.2018
ASSETS			
Current assets			
Cash and cash equivalents	15	24,749	39,978
Trade and other receivables	16	50,413	76,183
Prepaid corporate income tax		104	224
Inventories	18	166,226	117,992
		241,492	234,377
Non-current assets			
Investments in joint ventures	20	2,498	732
Other long-term loans and receivables	21	11,094	10,391
Investment property	23	14,047	13,771
Property, plant and equipment	24	11,919	9,715
Intangible assets	25	777	671
		40,335	35,280
TOTAL ASSETS		281,827	269,657
LIABILITIES			
Current liabilities			
Borrowings	27	20,725	19,900
Payables and prepayments	28	69,585	77,016
Income tax liability		812	381
Short-term provisions	29	7,976	8,100
		99,098	105,397
Non-current liabilities			
Long-term borrowings	27	43,001	24,266
Deferred income tax liability	22	1,682	1,481
Other long-term payables	30	3,491	2,179
		48,174	27,926
TOTAL LIABILITIES		147,272	133,323
EQUITY			
Non-controlling interests	19	4,217	4,577
Equity attributable to equity holders of the parent			
Share capital	32	7,929	7,929
Statutory reserve capital		793	793
Currency translation differences		(710)	(721)
Retained earnings		122,326	123,756
		130,338	131,757
TOTAL EQUITY		134,555	136,334
TOTAL LIABILITIES AND EQUITY		281,827	269,657

The notes set out on pages 55-99 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

in thousands of euros

	Equity attributable to equity holders of the parent					Non-controlling interest	Total
	Share capital	Statutory reserve capital	Currency translation differences	Retained earnings	Total		
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
Balance as at 01.01.2019	7,929	793	(721)	123,756	131,757	4,577	136,334
Adjustment on the adoption of IFRS 16	-	-	-	-	-	-	-
Balance as at 01.01.2019 restated	7,929	793	(721)	123,756	131,757	4,577	136,334
Profit (loss) for the financial year	-	-	-	16,270	16,270	220	16,490
Other comprehensive income (loss)	-	-	11	-	11	2	13
Total comprehensive income (loss) for the financial year	-	-	11	16,270	16,281	222	16,503
Transactions with owners							
Option over shares relating to non-controlling interests	-	-	-	-	-	(510)	(510)
Dividends (Note 14)	-	-	-	(17,700)	(17,700)	(72)	(17,772)
Total transactions with owners	-	-	-	(17,700)	(17,700)	(582)	(18,282)
Balance as at 31.12.2019	7,929	793	(710)	122,326	130,338	4,217	134,555

For share capital see also Note 32.

The notes set out on pages 55-99 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT

in thousands of euros

	Note	2019	2018
Cash flows from (used in) operating activities			
Operating profit		19,238	19,872
Adjustments:			
Depreciation and impairment	23-25	2,707	2,073
(Profit)/loss from sale of non-current assets	8	(309)	(473)
Change in receivables and liabilities related to construction contracts	4	(10,697)	11,153
Interest income from operating activities	8	(2,190)	(2,351)
Change in provisions	29	282	4,732
Change in trade and other receivables related to operating activities		26,854	(1,256)
Change in inventories	18	(48,118)	571
Change in trade and other payables related to operating activities		1,811	(1,759)
Interest received	8, 10, 16, 21	2,265	2,450
Interest paid	11, 28	(1,039)	(799)
Other finance income (costs)	11	(129)	(44)
Corporate income tax paid		(3,093)	(383)
Total cash flows from (used in) operating activities		(12,418)	33,786
Cash flows from investing activities			
Disposal of subsidiary	19	-	385
Liquidation of subsidiary		-	(3)
Purchase of investment properties	23	(410)	(92)
Purchase of property, plant and equipment (excl. leased assets)	24, 27	(2,199)	(712)
Proceeds from sale of property, plant and equipment	8, 24	508	664
Purchase of intangible assets	25	(273)	(281)
Interest received	10, 16	2	3
Total cash flows from investing activities		(2,372)	(36)
Cash flows from (used in) financing activities			
Proceeds from borrowings	27	46,527	30,139
Repayments of borrowings	27	(28,211)	(44,670)
Repayments of lease liabilities	27	(1,006)	(605)
Contributions to the subsidiary's share capital from non-controlling shareholder	19	-	(1)
Dividends paid	14	(17,772)	(17,816)
Total cash flows from (used in) financing activities		(462)	(32,953)
Net increase/decrease in cash and cash equivalents		(15,252)	797
Cash and cash equivalents at the beginning of the period	15	39,978	39,210
Effect of exchange rate changes		23	(29)
Cash and cash equivalents at the end of the period	15	24,749	39,978

The notes set out on pages 55-99 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 2019 were signed by the Management Board on 31 March 2020.

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, while the shares listed as of the reporting date have been listed since 11 August 2008 – AS Järvevana (business register code 10068022, previously named AS Merko Ehitus, currently named OÜ Järvevana), the shares of which were listed, was divided on 1 August 2008, during which AS Merko Ehitus (business register code 11520257) was established and the assets and the enterprise of AS Järvevana, with certain exceptions, were transferred to the established company. As at 31 December 2019, 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, unless otherwise specified.

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 became effective for the group from 1 January 2019:

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 (Note 2).

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.

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 2020, and which the group has not early adopted:

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 assesses that there is no material impact of application of the amendments to its financial statements.

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 assesses that there is no material impact of application of the amendments to its financial statements.

Definition of a business – Amendments to IFRS 3 (effective for annual periods beginning on or after 1 January 2020 or after; not yet adopted by the EU). The amendments revise definition of a business. A business must have inputs and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present, including for early stage companies that have not generated outputs. An organised workforce should be present as a condition for classification as a business if there are no outputs. The definition of the term 'outputs' is narrowed to focus on goods and services provided to customers, generating investment income and other income, and it excludes returns in the form of lower costs and other economic benefits. It is also no longer necessary to assess whether market participants are capable of replacing missing elements or integrating the acquired activities and assets. An entity can apply a 'concentration test'. The assets acquired would not represent a business if substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets). The Group assesses that there is no material impact of application of the amendments to its financial statements.

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.

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.

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

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.

As at 31 December 2018 and 31 December 2019, 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.

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.

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 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 the property is commercially disposable, which cannot be later than when a permit for use is obtained for the property. 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. For right-of-use assets refer to note 1.15. Items of property, plant and equipment leased under the 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. LEASED ASSETS

Accounting policies from 1 January 2019

THE GROUP AS A LESSEE

Leases are classified in accordance with IFRS 16, effective 1 January 2019, in accordance with paragraph 1.3 of this Note.

Lease is a contract that conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The right to use an asset exists if the lessor is unable to substitute an asset, the lessee has the ability to determine how to use the underlying asset and the lessee is entitled to the majority of future economic benefits generated from that right of use. If the lessee has the right to use a part of an asset the contract is considered a lease if the part of an asset is physically identifiable (e.g. lease of one floor in a building). There are several conditions to consider when evaluating a lease term. Only the assets that have a lease term shorter than 12 months can be excluded from the balance sheet and recognised as an operating lease so far. Such payments are recognised as an expense in the income statement on a straight-line basis over the lease term.

According to IFRS 16 lease term is:

- non-cancellable period of a lease – a period during which the lessee has no option to terminate the lease;
- periods covered by an option to terminate the lease – if the lessee is reasonably certain not to exercise that option;
- periods covered by an option to extend the lease – if the lessee is reasonably certain to exercise that option and has an option to extend the lease during one more time period. The same applies to termination options: if the lessee is certain not to use the termination option, the option should not be used to reduce the lease term.

In assessing the lease term, all relevant facts and circumstances shall be considered that create an incentive for the lessee to use that option. Lease term starts from the moment when the lessee is able to use the asset. Likelihood to use the options is considered at the commencement date. The likelihood to use the options is considered from the perspective of the lessee and it is affected by:

- contractual terms and conditions for the optional periods compared with market rates
- costs relating to the penalties of using/not using the options as well as other similar costs such as negotiation costs, relocation costs etc. If such costs (including penalties) are significant it is unlikely that the lessee will exercise the option to terminate and it is likely, that the lessee will exercise the option to extend;
- significant leasehold improvements undertaken over the term of the contract are expected to increase the likelihood to extend (and not to terminate) the lease;
- Very short-term non-cancellable period indicates that the lessee intends to extend the lease term (to avoid costs related to obtaining a new lease);
- the importance of that underlying asset to the lessee's operations and business plan - if the underlying asset is a specialised asset or suitable alternatives are not available the lessee is more likely to exercise the option to extend.

In addition, lessee's earlier operating activities shall be considered to determine the likelihood to exercise options to extend or terminate.

Lease term does not include periods when both parties have an option to terminate the lease. The lessee might intend to use the option to extend the lease period, however, that option does not depend solely on the intention of the lessee.

Leased assets (the "right-of-use assets") are generally measured at the cost minus depreciation method.

Lease liability is remeasured on the balance sheet when there is a change in the estimation of lease payments. The lessee recognises the amount of revaluation of lease liability as an adjustment of the underlying right-of-use asset. If the residual value of the underlying asset is approaching zero and additional decrease is revaluation the lease liability is recognised, the remaining amount is recognised in the income statement.

THE GROUP AS THE LESSOR

Assets leased out under operating lease terms are recognised in the balance sheet analogously to property, plant and equipment. They are depreciated over their expected useful lives on a basis consistent with similar assets. Operating lease payments are recognised as income on a straight-line basis over the lease term.

Accounting policies until 31 December 2018

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, which are reflected 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.

Legal entities in Latvia, Lithuania, Norway and Finland 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 Kingdom of Norway and the Republic of Finland. The profits in the Republic of Latvia are taxed upon their distribution with a rate of 20/80 (2018: the profits are taxed upon their distribution with a rate of 20/80). The profits of entities located in the Republic of Lithuania are taxed at the rate of 15% (2018: 15%), in the Kingdom of Norway at the rate of 22% (2018: 23%) and in the Republic of Finland at the rate of 20% (2018: 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.

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

Revenue is income arising in the course of the group's ordinary activities. Revenue is recognized 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 contracts is recognised in the same period as the services are provided and accepted by the customer. 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 only very rarely has contracts where the period between the transfer of the promised goods or services to the customer and payment by the customer exceeds one year. The impact of time value of money for the group is immaterial.

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.

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 16 Leases on the group's financial statements.

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. There was no impact on the starting balance of retained earnings as of 01.01.2019.

The group uses simplifications for short-term leases and rent of low value assets. Cancellable vehicle leasing contracts with a leasing period up to 12 months are not recognised as assets and all new vehicle leasing contracts are signed under the financial lease terms.

For leases that were classified as finance leases applying IAS 17, the carrying amount of the right-of-use asset and the lease liability at the date of initial application shall be the carrying amount of the lease asset and lease liability immediately before that date measured applying IAS 17. As at 31 December 2018, the balance of vehicles acquired under the financial lease terms was 1,729 thousand euros.

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. Implementing the amendments, the amount of non-current assets in the group's statement of financial position increased by 1,009 thousand euros as at 1 January 2019 and the amount of liabilities increased by 1,009 thousand euros (Notes 26, 27). As the amount of lease liabilities for the group is immaterial, the group decided to use a simplified approach in implementing the standard, based on which the lease liability is not measured in the present value of the remaining lease payments using the alternative borrowing interest rate of the lessee as the discount rate on the lease liabilities.

In accordance with the principles of the IAS 17 standard previously in force, lease payments were recognized under cost of goods sold, marketing expenses or general and administrative expenses, which were taken into account for obtaining EBITDA. As a result of adoption of the IFRS 16, EBITDA rose by EUR 329 thousand for 12 months of 2019, because lease payments are recognized as depreciation and interest expense on lease liabilities.

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 2019, the amount of the provision for onerous contracts was EUR 1,295 thousand (2018: EUR 247 thousand), which was determined after the evaluation of the stage of completion of construction contracts. 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 -7,293/+7,718 thousand (2018: EUR -20,209/+19,652 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/development) would have been EUR 2,351 thousand higher in 2019 (2018: EUR 1,127 thousand higher), incl. real estate properties for sale/development in the amount of EUR 2,285 thousand (2018: EUR 1,015 thousand), work-in-progress in the amount of EUR 0 thousand (2018: EUR 112 thousand) and finished goods in the amount of EUR 66 thousand (2018: EUR 0 thousand). No impairment losses were recognized for inventories of work-in-progress, finished goods and acquisition of real estate properties for sale/development in 2019, therefore no impairment test has been performed. In 2018, if the value had been underestimated by 10% (income would be 10% higher upon the disposal of assets), the write-down of inventories would have been EUR 170 thousand lower, incl. finished goods in the amount of EUR 170 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 2019 and 2018, no impairment tests were performed, as there were no indications of impairment of assets. As at 31 December 2019, the carrying amount of property, plant and equipment was EUR 11,919 thousand (31.12.2018: EUR 9,715 thousand) and the carrying amount of intangible assets was EUR 777 thousand (31.12.2018: EUR 671 thousand) (Notes 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 2019 does not significantly differ from their fair value, with the exception of book value of land in the amount of EUR 11,940 thousand, the fair value of which by expert opinion was EUR 27,410 thousand (31 December 2018: the carrying amount of investment properties did not significantly differ from their fair value, with the exception of book value of land in the amount of EUR 11,940 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 2019, the carrying amount of investment property was EUR 14,047 thousand (31.12.2018: EUR 13,771 thousand) (Note 23).

NOTE 4 OPERATING SEGMENTS

in thousands of euros

In previous reporting periods of AS Merko Ehitus group, financial information was presented in segment reporting under the "Estonian construction service", "other home markets construction service" and "real estate development" segments. Due to the fact that over the years the volumes of construction services provided by group has grown significantly outside Estonia, the management board of AS Merko Ehitus is focusing on the construction service business segment as a whole in one segment.

The comparative data for previous periods has been adjusted according to new presentation of the segment reporting in 2019 consolidated annual report, including the fact that the recognition of the real estate development segment has not changed and the comparative data of this segment have not been adjusted.

The chief operating decision-maker, i.e. the Management Board of parent AS Merko Ehitus, monitors the business of the group by operating segments.

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

- construction service,
- real estate development.

Construction service segment includes all projects of the home markets 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. The real estate development 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.

AS Merko Ehitus management board monitors the revenue and the operating profit (loss) as the main financial indicators in the segment reporting. 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

2019

	Construction service	Real estate development	Total segments
Revenue	256,749	99,863	356,612
Inter-segment revenue	(47)	(29,786)	(29,833)
Revenue from clients	256,702	70,077	326,779
incl. clients whose revenue is at least 10% of the group's consolidated revenue:			
client A (Estonian state)	57,687	-	57,687
client B	37,179	-	37,179
Timing of revenue recognition at a point in time	2,155	66,384	68,539
Timing of revenue recognition over time	254,547	3,693	258,240
Operating profit (-loss)	13,276	8,115	21,391
Segment pre-tax profit (loss)	13,053	9,607	22,660
incl. interest income from operating activities (Note 8)	47	2,143	2,190
depreciation (Notes 5, 6, 7)	(2,264)	(443)	(2,707)
impairment of inventories (Notes 5, 18)	(175)	-	(175)
recognition of provisions (Notes 5, 7, 29)	(3,934)	(1,533)	(5,467)
reversal of provisions (Note 5, 7, 29)	257	-	257
profit (loss) from joint ventures (Note 20)	-	1,766	1,766
other finance income (costs) (Notes 10, 11)	(13)	(256)	(269)
incl. interest expenses	(17)	(239)	(256)
Segment assets 31.12.2019	54,944	195,073	250,017
incl. joint ventures (Note 20)	-	2,498	2,498

2018	Construction service	Real estate development	Total segments
Revenue	347,100	85,343	432,443
Inter-segment revenue	(37)	(14,395)	(14,432)
Revenue from clients	347,063	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	2,226	52,846	55,072
Timing of revenue recognition over time	344,837	18,102	362,939
Operating profit (-loss)	10,719	11,319	22,038
Segment pre-tax profit (loss)	10,397	11,658	22,055
incl. interest income from operating activities (Note 8)	289	2,061	2,350
depreciation (Notes 5, 6, 7)	(1,718)	(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)	(5,144)	(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)	(27)	(223)	(250)
incl. interest expenses	(28)	(206)	(234)
Segment assets 31.12.2018	71,773	161,151	232,924
incl. joint ventures (Note 20)	-	732	732

In addition to the segment assets, as at 31 December 2019 the group holds assets in the amount of EUR 31,810 thousand (31 December 2018: EUR 36,733 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.

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

in thousands of euros

	2019	2018
Pre-tax profit from reporting segments	22,660	22,055
Other operating profit (loss)	(2,153)	(2,166)
incl. recognition of provisions (Notes 7, 29)	(9)	(7)
finance income (costs)	(184)	(114)
incl. interest income	-	1
interest expenses	(178)	(146)
Total profit before tax	20,323	19,775

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 -220 thousand (31 December 2018: EUR -276 thousand) has not been presented separately in the respective cost item.

REVENUE BY CLIENT LOCATION

in thousands of euros and percentage

	2019		2018	
Estonia	168,825	52%	202,627	48%
Latvia	92,772	28%	157,496	38%
Lithuania	46,202	14%	46,765	11%
Norway	18,980	6%	11,123	3%
Total	326,779	100%	418,011	100%

CONTRACT ASSETS AND LIABILITIES

in thousands of euros

	31.12.2019	31.12.2018
Accrued income from construction services (Note 16)	11,689	9,847
Prepayments for construction services (Note 28)	(8,058)	(16,912)
Advance payments received for construction contract works (Note 28)	(5,637)	(3,363)
Recognised provision for onerous construction contracts (Note 29)	(1,295)	(248)

During the accounting year advance payments received prior for construction contract works in a sum of EUR 5,637 thousand (2018: EUR 3,363 thousand) were recognised as revenue. As of 31 December 2019, the group's secured order book stood at EUR 141,434 thousand (2018: EUR 228,950 thousand), for which the revenue is recognised in future periods. According to management estimation, 82% of revenue is going to be recognised in 2020 and 18% in 2021.

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

in thousands of euros

	31.12.2019	31.12.2018
Estonia	15,289	11,970
Latvia	13,333	12,782
Lithuania	476	13
Norway	143	124
Total	29,241	24,889

NOTE 5 COST OF GOODS SOLD

in thousands of euros

	2019	2018
Construction services and properties purchased for resale	185,121	262,190
Materials	49,121	60,096
Staff costs	26,323	23,666
Construction mechanisms and transport	8,911	10,214
Design	4,394	8,345
Real estate management costs	401	190
Depreciation (Note 4)	1,835	1,554
Impairment of inventories (Notes 4, 18)	175	300
Provisions (Notes 4, 29)	4,939	5,242
Other expenses	10,738	13,165
Total cost of goods sold	291,958	384,962

NOTE 6 MARKETING EXPENSES

in thousands of euros

	2019	2018
Staff costs	2,560	2,454
Advertising, sponsorship	1,166	352
Transport	187	214
Depreciation	105	47
Other expenses	242	218
Total marketing expenses	4,260	3,285

NOTE 7 GENERAL AND ADMINISTRATIVE EXPENSES

in thousands of euros

	2019	2018
Staff costs	8,506	8,252
Office expenses, communication services	462	554
Consulting, legal, auditing *	497	481
Transport	415	410
Computer equipment and software	570	690
Depreciation	767	406
Provisions (Notes 4, 29)	280	20
Other expenses	1,491	1,491
Total general and administrative expenses	12,988	12,304

* Customer contract fees of the audit firms accounted for during the accounting year were EUR 140 thousand for audit fees (2018: EUR 101 thousand) and EUR 26 thousand for other business activities (2018: EUR 20 thousand).

NOTE 8 OTHER OPERATING INCOME

in thousands of euros

	2019	2018
Interest income from operating activities	2,190	2,351
Foreign exchange gains	2	-
Profit from sale of non-current assets	309	473
Fines and penalties for delay received	114	200
Collection of doubtful receivables (Notes 16, 35)	1	94
Other income	367	409
Total other operating income	2,983	3,527

NOTE 9 OTHER OPERATING EXPENSES

in thousands of euros

	2019	2018
Fines, penalties	211	427
Gifts, donations	181	289
Doubtful receivables expense (Notes 16, 35)	795	292
Impairment of assets (Note 24)	-	66
Other expenses	131	41
Total other operating expenses	1,318	1,115

NOTE 10 FINANCE INCOME

in thousands of euros

	2019	2018
Interest income (Note 4)	2	3
Foreign exchange gains	-	5
Other finance income	1	-
Total finance income	3	8

NOTE 11 FINANCE COSTS

in thousands of euros

	2019	2018
Interest expense (Notes 4, 27)	656	652
Other finance costs	28	44
Total finance costs	684	696

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:

2019	Latvia	Lithuania	Norway	Estonia	Total
Profit (loss) before tax	319	4,806	1,684	13,514	20,323
Tax rate applicable to profits	0%	15%	22%	0%	
Tax calculated at domestic tax rates applicable to profits in the respective countries	(1)	(721)	(371)	-	(1,093)
Tax calculated on expenses not deductible for tax purposes	-	48	-	-	48
Tax effect of income not subject to tax	-	(235)	-	-	(235)
Tax losses of previous periods recognised in the reporting period	-	214	(2)	-	212
Tax losses not recognised in the reporting period	-	(16)	-	-	(16)
Income tax withheld on dividends	(161)	-	-	(2,588)	(2,749)
Total income tax expense	(162)	(710)	(373)	(2,588)	(3,833)
incl. income tax expense	(162)	(573)	(309)	(2,588)	(3,632)
deferred income tax expense (Note 22)	-	(137)	(64)	-	(201)

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)

As at 31 December 2019, the parent company AS Merko Ehitus has EUR 1 thousand (31.12.2018: EUR 2,879 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 2019, it is possible to pay out dividends to shareholders from retained earnings in the amount of EUR 97,533 thousand (31.12.2018: EUR 99,004 thousand). Considering the taxed dividends received and income tax withheld on foreign income totalling EUR 0 thousand (31.12.2018: EUR 720 thousand), the corresponding income tax on dividends would amount to EUR 24,083 thousand (31.12.2018: EUR 24,031 thousand). Regarding the additional income tax on dividends, the 14% tax rate on regularly payable dividends (14/86 on net dividends), which is applied on the average amount of the paid dividends taxed in Estonia during the previous 3 years, has been taken into consideration, including the fact that the income tax on regularly payable dividends is applied to dividends taxed in Estonia starting only from 2018, and therefore in 2020 the sum of dividends that shall be taxed using the 14% rate is one third of the total sum of dividends that have been taxed in Estonia during 2018 and 2019. Above that sum, a regular 20% tax rate is applied to the dividends (i.e. a 20/80 tax rate applied to the sum paid out as net dividends). The income tax related to disbursement of dividends is recognised as a liability and income tax expense upon the announcement of dividends.

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.

	2019	2018
Net profit attributable to shareholders (<i>in thousand EUR</i>)	16,270	19,343
Weighted average number of ordinary shares (<i>thousand pcs</i>)	17,700	17,700
Basic earnings per share (<i>in euros</i>)	0.92	1.09

In 2019 and 2018, 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. While in 2018, no income tax cost for the group arose in Estonia in connection with the payment of dividends, in 2019 it did arise in connection with EUR 10.3 million worth of paid dividends. Pursuant to that, in 2020, the group shall recognise income tax cost on possible payable dividends using the tax rate for regularly payable (net) dividends of 14/86 on a sum of EUR 3.4 million, i.e. one third of the aforementioned 10.3 million. As per the Estonian Income Tax Act, the group shall withhold an additional 7% income tax from the dividends taxed with the 14/86 rate that are paid to shareholders who are natural persons.

In accordance with the profit allocation decision, dividends were paid by parent company AS Merko Ehitus in 2019 in the amount of EUR 17,700 thousand, i.e. EUR 1.00 per share. The group incurred income tax expenses in 2019 in connection with dividend payments in an amount of 2,749 thousand euros.

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.

NOTE 15 CASH AND CASH EQUIVALENTS

in thousands of euros

	31.12.2019	31.12.2018
Cash on hand	6	-
Bank accounts	24,743	39,915
Short-term bank deposits	-	63
Total cash and cash equivalents (Note 35)	24,749	39,978

NOTE 16 TRADE AND OTHER RECEIVABLES

in thousands of euros

	31.12.2019	31.12.2018
Trade receivables (Note 35)		
Accounts receivable	34,148	42,835
Allowance for doubtful receivables	(856)	(81)
	33,292	42,754
Tax prepayments excluding corporate income tax		
Value added tax	695	944
Other taxes	3	2
	698	946
Accrued income from construction services (Notes 4, 35)	11,689	9,847
Other short-term receivables		
Short-term loans (Notes 17, 35)	1,700	14,590
Interest receivables (Note 35)	3	112
Other short-term receivables (Note 35)	172	271
	1,875	14,973
Prepayments for services		
Prepayments for construction services	2,441	7,064
Prepaid insurance	117	195
Other prepaid expenses	301	404
	2,859	7,663
Total trade and other receivables	50,413	76,183
incl. short-term loan receivables from related parties (Note 17)	1,650	9,000
other short-term receivables and prepayments to related parties (Note 33)	89	1,521

In 2019, the share of overdue receivables increased from 6.2% to 15.8% of total receivables, and as at the reporting date (31.12.2019), the amount of overdue receivables was EUR 5,257 thousand (31 December 2018: 2,639 thousand). By 12 March 2020, out of the receivables that were in overdue as of the reporting date, EUR 1,142 thousand remained in overdue, i.e. 3.4% of total receivables at the reporting date. In 2019, the share of receivables overdue for more than 180 days decreased, but the share of receivables over 30 and 60 days increased which prolonged the average collection period of trade receivables to 45 days (2018: 40 days).

	2019	2018
Doubtful receivables at the beginning of the period	(81)	(103)
Reporting period doubtful receivables expenses (Note 9)	(794)	(90)
Receivables written off during the year as uncollectible	18	18
Received doubtful receivables (Note 8)	1	94
Doubtful receivables at the end of the period	(856)	(81)

Additionally, in 2019, advance payments to suppliers were wrote down in the amount of EUR 1 thousand (2018: EUR 202 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
2019			
Loan balance at beginning of the year	9,000	5,590	14,590
Received	(7,350)	(5,540)	(12,890)
Loan balance at end of the year	1,650	50	1,700
incl. current portion (Notes 16, 35)	1,650	50	1,700
Interest rate	6.0%	10%	
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%	

NOTE 18 INVENTORIES

in thousands of euros

	31.12.2019	31.12.2018
Materials	236	797
Work-in-progress	65,550	43,081
Finished goods	28,252	15,991
Goods for resale		
Registered immovables purchased for resale/development	70,193	54,532
Other goods purchased for resale	133	705
	70,326	55,237
Prepayments for inventories		
Prepayments for real estate properties	-	1,300
Prepayments for other inventories	1,862	1,586
	1,862	2,886
Total inventories	166,226	117,992

The inventories pledged as collateral as at 31 December 2019 for loans total EUR 95,719 thousand (2018: EUR 50,374 thousand) (Note 31).

In 2019, inventories have been written down to their net realisable value by EUR 175 thousand (2018: EUR 300 thousand) and previously made write-downs have not been reversed (2018: EUR 0 thousand).

	Carrying amount before write-down	Write-down	Carrying amount after write-down
31.12.2019			
Other goods purchased for resale	308	(175)	133
Total	308	(175)	133
31.12.2018			
Registered immovables purchased for resale/development	54,832	(300)	54,532
Total	54,832	(300)	54,532

NOTE 19 SHARES IN SUBSIDIARIES

	Ownership and voting rights %		Location	Area of operation
	31.12.2019	31.12.2018		
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
OÜ Tähelinna Kinnisvara	100	100	Estonia, Tallinn	Real estate
OÜ Vahi Lastehoid	100	-	Estonia, Tallinn	Real estate
OÜ Merko Kaevandused	100	-	Estonia, Tallinn	Mining
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
UAB VPSP 2	100	-	Lithuania, Vilnius	Real estate
UAB VPSP Projektas	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 Jurininkų aikštele	100	100	Lithuania, Vilnius	Real estate
UAB Rinktinės projektai	-	100	Lithuania, Vilnius	Real estate
UAB MB Projektas	100	-	Lithuania, Vilnius	Real estate
OÜ Kiviaia Kinnisvara	100	100	Estonia, Tallinn	Real estate
SIA Merko Investments	-	100	Latvia, Riga	Holding
OÜ 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 Investīcijas	100	100	Latvia, Riga	Real estate
SIA Industriālais 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 Zakusala 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	Finland, Helsinki	Real estate
Merko Investments AS	100	100	Norway, Sofiemyr	Holding
Peritus Entreprenør AS	56	56	Norway, Sofiemyr	Construction

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 was OY Merko Finland. As a result of the merger, the company being acquired (Hartian OY) wound up without liquidation proceedings and OY Merko Finland became the legal successor of the company being acquired. The merger date was 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 was made on 30 April 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 OÜ Vahi Lastehoid was established as a result of the division, to which apartment ownerships, located on Pärna allee in Tartu, transferred as per the division plan. The division came into force with the entry in the Commercial Register made on 20 June 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 was merged with the parent company. The restructuring was completed and the final merger entry was made in the Commercial Register on 27 November 2019.

On 14 January 2019, UAB Merko Statyba, fully owned subsidiary of AS Merko Ehitus, established a company UAB VPSP 2 in Lithuania, through which the public-private partnership (PPP) project for the design and construction works of the new Kaunas district Police headquarters of the Police Department under the Ministry of the Interior of the Republic of Lithuania is being carried out in Kaunas.

On 1 April 2019, UAB Merko Bustas, fully owned subsidiary of AS Merko Ehitus in Lithuania established a fully owned subsidiary UAB MB Projektas.

On 5 April 2019, AS Merko Ehitus management board decided to start liquidation procedures of a fully owned subsidiary OÜ Kiviaia Kinnisvara. The liquidation of the company was completed and deleted from the Commercial Register on 4 March 2020.

On 10 April 2019, UAB Merko Statyba, fully owned subsidiary of AS Merko Ehitus in Lithuania, established a 100% subsidiary UAB VPSP Projektas.

On 10 May 2019, AS Merko Ehitus management board decided to start liquidation procedures of 100% owned subsidiary SIA Merko Investments. The liquidation of the company was completed and deleted from the Commercial Register on 2 September 2019.

On 17 September 2019, the supervisory board of AS Merko Infra, part of AS Merko Ehitus group, decided to start liquidation procedures of AS Merko Infra branch in Latvia. The liquidation was completed and the branch deleted from the Commercial Register on 2 December 2019.

On 18 December 2019, AS Merko Ehitus Eesti, fully owned subsidiary of AS Merko Ehitus, established a 100% subsidiary OÜ Merko Kaevandused.

On 27 December 2019, AS Merko Infra and OÜ Merko Kaevandused, fully owned subsidiaries of AS Merko Ehitus Eesti, signed a notarised division plan under which AS Merko Infra (company being divided) will divest the assets related to the mine to OÜ Merko Kaevandused (recipient company). The balance sheet date of the division and transfer of assets shall be 1 January 2020. The final entry of the division in the Commercial Register shall be made during 2020.

FINANCIAL INFORMATION REGARDING SIGNIFICANT SUBSIDIARY WITH A NON-CONROLLING INTEREST

in thousands of euros

SIA Zakusala Estates		
Statement of financial position	31.12.2019	31.12.2018
Cash	122	136
Trade and other receivables	30	12
Inventories	18,001	17,759
Total short-term assets	18,153	17,907
Short-term liabilities	348	70
Net assets	17,805	17,837
Equity	17,805	17,837
Non-controlling interest %	25%	25%
Non-controlling interest	4,451	4,459
Statement of comprehensive income	01.01-31.12.2019	01.01-31.12.2018
Other expenses	(3)	(4)
Land tax	(29)	(29)
Net profit (loss) for the period	(32)	(33)
Comprehensive profit (loss) for the period	(32)	(33)
incl. attributable to equity holders of the parent	(24)	(25)
attributable to non-controlling interest	(8)	(8)
Cash flow statement	01.01-31.12.2019	01.01-31.12.2018
Operating profit	(32)	(33)
Change in receivables related to operating activities	(18)	(6)
Change in inventories	(242)	(102)
Change in payables related to operating activities	278	47
Total cash flow from operating activities	(14)	(94)
Change in cash and cash equivalents	(14)	(94)
Cash and cash equivalents in the beginning of the period	136	230
Cash and cash equivalents at the end of the period	122	136

As at 31 December 2019, the group's non-controlling interest in equity is EUR 4,217 thousand (31.12.2018: EUR 4,577 thousand), including SIA Zakusala Estates non-controlling interest in the amount of EUR 4,451 thousand (31.12.2018: EUR 4,459 thousand). The other companies with a non-controlling interest – totalling at EUR -234 thousand (31.12.2018: EUR 118 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
	31.12.2019	31.12.2018		
Joint ventures				
Kodusadam OÜ	50	50	Estonia, Tallinn	Real estate

in thousands of euros

	Investment at 31.12.2018	Changes in 2019 profit (loss) on entities	Investment at 31.12.2019
Joint ventures			
Kodusadam OÜ	732	1,766	2,498
Total joint ventures	732	1,766	2,498

in thousands of euros

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

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	Short-term borrowings	Other current liabilities				
2019									
Kodusadam OÜ	1,718	7,060	262	3,300	744	4,996	19,961	(16,429)	3,532
Total	1,718	7,060	262	3,300	744	4,996	19,961	(16,429)	3,532
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

In 2019, interest expenses have not been recognised in the expenses of joint ventures (2018: 0 thousand) as the loan usage costs are capitalized during construction period.

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 (31.12.2018: EUR 9,000 thousand), of which the group has paid EUR 1,650 thousand in total (31.12.2018: EUR 9,000 thousand). In addition, the group has an obligation to provide construction services in future periods in amount of EUR 264 thousand (31.12.2018: EUR 2,307 thousand).

NOTE 21 OTHER LONG-TERM LOANS AND RECEIVABLES

in thousands of euros

	31.12.2019	31.12.2018
Long-term trade receivables (Note 35) *	11,094	10,391
Total other long-term loans and receivables	11,094	10,391

* incl. long-term receivables from buyer of Balsiu School in amount of EUR 10,293 thousand (31.12.2018: EUR 10,253 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:

31.12.2019	Lithuania	Norway	Total
Deferred income tax liability			
effect of other payables	(1,544)	(138)	(1,682)
Deferred income tax expense of the financial year (Note 12)	(137)	(64)	(201)

31.12.2018	Lithuania	Norway	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)

NOTE 23 INVESTMENT PROPERTIES

in thousands of euros

	Land	Right of superficies	Buildings	Total
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
Acquisition and improvements	409	-	-	409
Depreciation	-	(1)	(132)	(133)
Carrying amount at 31.12.2019	12,400	16	1,631	14,047
Cost at 31.12.2019	12,400	29	2,631	15,060
Accumulated depreciation 31.12.2019	-	(13)	(1,000)	(1,013)
Carrying amount at 31.12.2019	12,400	16	1,631	14,047

As at 31 December 2019, the carrying amounts of investment properties do not significantly differ from their fair values, with the exception of land, the fair value of which has been estimated by valuation expert at EUR 27,410 thousand (31.12.2018: the carrying amounts of investment properties did not significantly differ from their fair values, with the exception of land, the fair value of which had 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.

As at 31 December 2019, investment properties pledged as collateral for loans total EUR 13,816 thousand (31.12.2018: EUR 13,436 thousand) (Note 31).

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 31.12.2017	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
incl. leased assets	-	-	1,418	-	-	1,418
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
IFRS 16 initial application (Note 2)	-	770	239	-	-	1,009
Adjusted carrying value as at 01.01.2019	743	4,355	4,948	568	110	10,724
Acquisition and improvements	-	23	2,599	394	591	3,607
incl. leased assets	-	23	1,384	-	-	1,407
Disposals	-	-	(348)	(17)	-	(365)
Reclassification	(31)	-	189	401	(199)	360
Write-offs	-	-	(21)	(2)	-	(23)
Depreciation	-	(449)	(1,667)	(268)	-	(2,384)
Carrying amount at 31.12.2019	712	3,929	5,700	1,076	502	11,919
Cost at 31.12.2019	712	6,558	14,371	4,018	502	26,161
Accumulated depreciation at 31.12.2019	-	(2,629)	(8,671)	(2,942)	-	(14,242)
Carrying amount at 31.12.2019	712	3,929	5,700	1,076	502	11,919
incl. leased assets (Note 26)		526	2,456	-	-	2,982

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

As at 31 December 2019, property, plant and equipment pledged as collateral for loans total EUR 3,021 thousand (31.12.2018: EUR 2,639 thousand) (Note 31).

NOTE 25 INTANGIBLE ASSETS

in thousands of euros

	Goodwill	Software	Prepayments	Total
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
Acquisitions	-	112	161	273
Reclassification	-	200	(200)	-
Write-offs	-	(2)	-	(2)
Amortisation and impairment	-	(165)	-	(165)
Carrying amount at 31.12.2019	73	704	-	777
Cost at 31.12.2019	73	2,024	-	2,097
Accumulated amortisation and impairment at 31.12.2019	-	(1,320)	-	(1,320)
Carrying amount at 31.12.2019	73	704	-	777

NOTE 26 LEASED ASSETS

in thousands of euros

	Office space and warehouses	Vehicles and equipment	Total
31.12.2018			
Cost	-	3,476	3,476
Accumulated depreciation	-	(1,747)	(1,747)
Carrying amount	-	1,729	1,729
01.01.2019			
Initial recognition on IFRS 16 adoption	770	239	1,009
2019			
Additions	23	1,384	1,407
Termination of lease contracts	-	(246)	(246)
Depreciation	(267)	(650)	(917)
31.12.2019			
Cost	793	3,665	4,458
Accumulated depreciation	(267)	(1,209)	(1,476)
Carrying amount (Note 24)	526	2,456	2,982

The group's consolidated statement of profit or loss and other comprehensive income includes the following amounts relating to leases:

in thousands of euros

	2019	Note
Interest expense	33	11
Expense relating to short-term leases	357	5, 6, 7
Expense relating to leases of low-value assets	112	5, 6, 7

Consideration paid for leases recognised as fixed assets (including the leases that ended during the period) amounted to EUR 1,208 thousand in 2019.

Consideration paid for short-term cancellable leases for vehicles as right-of-use assets amounted to EUR 308 thousand in 2019 (2018: EUR 521 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. Rented assets have not been subleased.

LEASES - THE GROUP AS A LESSEE (INVESTMENT PROPERTIES LEASED OUT UNDER NON-CANCELLABLE OPERATING LEASE TERMS)

	31.12.2019	31.12.2018
Cost	2,682	2,682
Accumulated depreciation	(1,000)	(868)
Carrying amount	1,682	1,814

	2019	2018
Operating lease income received for investment properties (Note 23)	303	403
Future operating lease income:	914	1,384
Next year	246	302
In 2...5 years	660	857
Later than 5 years	7	225
Direct administrative expenses of investment properties (Note 23)	(153)	(213)

NOTE 27 BORROWINGS

in thousands of euros

	Lease liabilities at present value	Loans from				Total borrowings (Note 35)
		banks	entities under common control (Note 33)	other entities	total	
Loan balance as at 31.12.2018	1,647	30,694	6,000	5,825	42,519	44,166
IFRS 16 initial application (Note 2)	1,009	-	-	-	-	1,009
Adjusted carrying value as at 01.01.2019	2,656	30,694	6,000	5,825	42,519	45,175
2019						
Received	1,406	45,827	-	700	46,527	47,933
Repaid	(1,006)	(21,686)	-	(6,525)	(28,211)	(29,217)
Sale to lessor	(165)	-	-	-	-	(165)
Loan balance as at 31.12.2019	2,891	54,835	6,000	-	60,835	63,726
incl. current portion	806	18,919	1,000	-	19,919	20,725
non-current portion 2...5 years	2,085	35,916	5,000	-	40,916	43,001
Accrued interest of reporting period	33	829	145	-	974	1,007
incl. capitalised interest cost	-	351	-	-	351	351
Interest rate range	1.0%-3.55% +3-6 month euribor	0.65%-2.3% +1-6 month euribor; 1.69%+Eonia 6.46%-7.26%	2.65%+6 month euribor	0%		
Base currencies	EUR	EUR, NOK	EUR	EUR		

	Lease liabilities at present value	Loans from				Total borrowings (Note 35)
		banks	entities under common control (Note 33)	other entities	total	
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 6.46%-7.26%	2.65%+6 month euribor	0%		
Base currencies	EUR	EUR, NOK	EUR	EUR		

	2019	2018
Minimum future payments under lease liabilities	2,974	1,703
incl. current portion	839	545
non-current portion with the term of 2...5 years	2,135	1,158

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

	2019	2018
Lease liabilities		
1-5 months	522	431
6-12 months	1,840	1,185
Bank loans		
1-5 months	26,864	13,809
6-12 months	27,945	16,850
Loans from entities under common control		
6-12 months	6,000	6,000
Total	63,171	38,275

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

	2019	2018
Lease liabilities	529	31
Loans from bank	26	35
Loans from other entities	-	5,825
Total	555	5,891

Loan collaterals and pledged assets are presented in Note 31.

NOTE 28 PAYABLES AND PREPAYMENTS

in thousands of euros

	31.12.2019	31.12.2018
Trade payables (Note 35)	30,681	38,327
Payables to employees	10,647	10,067
Tax liabilities, except for corporate income tax		
value added tax	4,270	1,102
personal income tax	485	648
social security tax	1,146	1,166
unemployment insurance tax	48	57
contributions to mandatory funded pension	33	42
other taxes	205	229
	6,187	3,244
Prepayments for construction services (Notes 4, 35)	8,058	16,912
Other liabilities (Note 35)		
interest liabilities	5	6
other liabilities	218	345
	223	351
Prepayments received *	13,789	8,115
Total payables and prepayments	69,585	77,016
incl. payables to related parties (Note 33)	12	293

* As of 31 December 2019 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 5,637 thousand (31.12.2018: EUR 3,363 thousand) and of prepayments received connection with residential properties (apartment buyers) in a sum of EUR 8,152 thousand (31.12.2018: EUR 4,752 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
2019						
Balance at beginning of the year	3,373	248	120	4,330	29	8,100
Recognised (Notes 4, 5, 7)	1,361	1,381	202	2,454	78	5,476
Used during the year	(1,090)	(334)	-	(3,890)	(29)	(5,343)
Reversed (Notes 4, 7)	(137)	-	(120)	-	-	(257)
Balance at end of the year	3,507	1,295	202	2,894	78	7,976
incl. current portion	3,507	1,295	202	2,894	78	7,976
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

* 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

	31.12.2019	31.12.2018
Trade payables (Note 35)	2,476	1,675
Other long-term payables (Note 35)	1,015	504
Total other long-term payables	3,491	2,179
incl. other long-term payables to related parties (Notes 33)	1,015	504

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	31.12.2019	31.12.2018
Movable property	49,413	62,891
Financial assets *	12,356	12,425
Total	61,769	73,316

* The financial assets of UAB Balsiu mokyklos SPV, which OÜ Merko Property has pledged to secure the investment loan in the amount of EUR 7,132 thousand for the benefit of OP Corporate Bank plc Lithuanian branch (31.12.2018: EUR 7,657 thousand for the benefit of OP Corporate Bank plc Lithuanian branch).

Mortgages	31.12.2019	31.12.2018
Inventories (Note 18)	95,719	50,374
Land and buildings (Note 24)	3,021	2,639
Investment properties (Note 23)	13,816	13,436
Total	112,556	66,449

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 7,132 thousand (31.12.2018: EUR 7,657 thousand for the benefit of OP Corporate Bank plc Lithuanian branch) is secured by the pledge.

NOTE 32 SHARE CAPITAL

There were no changes in share capital during 2019 and 2018.

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 31.12.2019 and 31.12.2018, the share of capital of AS Merko Ehitus was EUR 7,929 thousand and the consolidated net assets of AS Merko Ehitus were EUR 130,338 thousand (31.12.2018: EUR 131,757 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 31.12.2019 and 31.12.2018, 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

	2019	2018
Provided services and goods sold		
Parent company	15	15
Joint ventures *	2,770	16,505
Entities under common control	847	91
Members of the management **	2,441	43
Other related parties	-	28
Total services provided and goods sold	6,073	16,682
Interest income		
Joint ventures	377	559
Purchased services and goods		
Parent company	90	90
Entities under common control	137	57
Total purchased services and goods	227	147
Interest expense		
Entities under common control	145	145
Total interest expense	145	145

BALANCES WITH RELATED PARTIES

in thousands of euros

	31.12.2019	31.12.2018
Receivables from related parties		
Loans granted (Note 16, 17, 21)		
Joint ventures	1,650	9,000
Receivables and prepayments (Note 16)		
Parent company	4	4
Joint ventures	64	1,385
Entities under common control	9	88
Members of the management	12	44
Total receivables and prepayments	89	1,521
Total receivables from related parties	1,739	10,521
Payables to related parties		
Lease liabilities (Note 27)		
Entities under common control	124	-
Short-term loans received (Note 27)		
Entities under common control	1,000	1,000
Payables and prepayments (Note 28)		
Parent company	9	9
Joint ventures	-	14
Entities under common control	3	1
Members of the management	-	269
Total payables and prepayments	12	293
Long-term loans received (Note 27)		
Entities under common control	5,000	5,000
Other long-term payables (Note 30)		
Other related parties	1,015	504
Total payables to related parties	7,151	6,797

* Provided services to joint ventures consist mainly of construction services.

** Apartments were sold and handed over to members of management in 2019. These did not constitute significant transactions for the group.

With regard to receivables from related parties, no impairments were performed in either 2019 or 2018.

REMUNERATION OF THE MEMBERS OF THE SUPERVISORY AND MANAGEMENT BOARDS

In 2019, 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 3,212 thousand (2018: EUR 2,643 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 1,084 thousand (2018: EUR 1,052 thousand). In the 12 months of 2019, the Management Board members of major subsidiaries did not receive benefits (2018: EUR 34 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 2019

		NO. OF SHARES	% OF SHARES
Toomas Annus (AS Riverito) *	Chairman of the Supervisory Board	12,742,686	71.99%
Indrek Neivelt (OÜ Trust IN)	Member of the Supervisory Board	31,635	0.18%
Teet Roopalu	Member of the Supervisory Board	-	-
		12,774,321	72.17%

* Toomas Annus holds the majority of the votes represented by shares in AS Riverito directly and through holding companies (176,351 shares out of a total of 270,000 shares). With that the votes held by AS Riverito in AS Merko Ehitus (12,742,686 shares) are deemed to belong to Toomas Annus.

The Management Board of the holding company AS Merko Ehitus has two members: Andres Trink and Tõnu Toomik

Shares held by members of the Management Board of AS Merko Ehitus as at 31 December 2019

		NO. OF SHARES	% OF SHARES
Andres Trink	Chairman of the Management Board	600	0.00%
Tõnu Toomik	Member of the Management Board	-	-
		600	0.00%

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 significant expenses related to these guarantees are unlikely.

	31.12.2019	31.12.2018
Performance period's warranty to the customer	24,896	34,511
Tender warranty	916	655
Guarantee warranty period	19,964	17,666
Prepayment guarantee	6,835	12,098
Payment guarantee	-	30,500
Contracts of surety	7,783	7,734
Letter of credit	-	428
Total contingent liabilities	60,394	103,592

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 fulfilment 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 2019 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 their businesses is analysed, including business logic and its compliance with general economic developments and the developments of the corresponding economic sector, as well as their financial position. 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 (2018: Aa2) and the parent company of SEB group, Skandinaviska Enskilda Banken AB, has a Moody's long-term credit rating Aa2 (2018: Aa2). OP Corporate Bank PLC has a Moody's long-term credit rating Aa3 (2018: Aa3). Luminor Bank has a Moody's long-term credit rating Baa1 (2018: Baa1).

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 2019 and 31 December 2019. The management estimates that the group cash and cash equivalents are 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		
31.12.2019				
Cash and cash equivalents (Note 15)	24,749	-	24,749	-
Trade receivables (Notes 16, 21)	33,292	11,094	44,386	-
Accrued income from construction service (Notes 4, 16)	11,689	-	11,689	-
Loans granted (Notes 16, 17, 21)	1,700	-	1,700	50
Interest receivables (Notes 16, 21)	3	-	3	-
Other short-term receivables (Note 16)	172	-	172	-
Total	71,605	11,094	82,699	50
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

The group's customers are primarily large local entities or public sector entities (as at 31 December 2019, the public sector proportion in accounts receivable amounted to 13.3% (31.12.2018: 8.0%)) with well-known and sufficient creditworthiness.

TRADE RECEIVABLES BY DUE DATE

in thousands of euros

	31.12.2019		31.12.2018	
Not overdue	39,128	88.2%	50,507	95.0%
1-30 days overdue	2,376	5.3%	1,006	1.9%
31-60 days overdue	2,419	5.4%	294	0.6%
61-90 days overdue	86	0.2%	64	0.1%
91-120 days overdue	58	0.1%	12	0.0%
121-180 days overdue	30	0.1%	16	0.1%
More than 180 days overdue	289	0.7%	1,246	2.3%
Total trade receivables (Notes 16, 21)	44,386	100%	53,145	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 5,257 thousand (31.12.2018: EUR 2,639 thousand), of which EUR 2,632 thousand has been collected by 12 March 2020. In a year, the share of overdue short-term receivables in total receivables increased from 5.0% to 11.8%. The group keeps running track of payment history for all customers separately for each receivable. Customers who have exceeded the payment deadline are handled personally in order to find solutions that ensure the best possible protection of the group's interests. 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 behaviour 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 1,650 thousand (31.12.2018: 9,000 thousand) and therefore, no additional collateral is required. As at 31 December 2019, loans granted to unrelated legal entities amounted to EUR 50 thousand (31.12.2018: 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.

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 2019, 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 2019, 22.6% and as at 31 December 2018, 16.4% 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 2019, the group's interest-bearing liabilities totalled EUR 63,726 thousand (31.12.2018: EUR 44,166 thousand), of which short-term loans and repayments of long-term liabilities in 2020 totalled EUR 20,725 thousand (31.12.2018: EUR 19,900 thousand) and long-term loans and finance lease liabilities totalled EUR 43,001 thousand (31.12.2018: EUR 24,266 thousand). As at 31 December 2019, the group's loans granted totalled EUR 1,700 thousand (31.12.2018: EUR 14,590 thousand), of which all were classified as short-term loans with repayments in 2020 (31.12.2018: EUR 14,590 thousand short-term loan). Loan interest depended on interbank 1-12 month loan base interest in the entity's domicile and Euribor. As at 31 December 2019, the break-down of interest-bearing borrowings and loans granted was as follows:

	31.12.2019	31.12.2018
Fixed rate liabilities	555	5,892
Liabilities with floating rate interests 1-5 months	27,668	14,239
Liabilities with floating rate interests 6-12 months	35,503	24,035
Total interest-bearing borrowings	63,726	44,166
Fixed rate receivables	1,700	14,590

The management estimates that there will be no changes in the base interest rates, which could have a significant impact on the financial position of the group: the market continues to have low (including negative) base interest rates. Assuming that average Euribor would rise 10 basis points above the zero level 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 63 thousand (31.12.2018: EUR 38 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 37,603 thousand, of which EUR 7,563 thousand was withdrawn. In 2020, the contracts in a total amount of EUR 25,000 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 break-down of financial assets and liabilities in local currencies as at the balance sheet date is as follows:

	In EUR	In NOK
31.12.2019		
Assets	94.5%	5.5%
Liabilities	97.9%	2.1%
31.12.2018		
Assets	96.1%	3.9%
Liabilities	97.1%	2.9%

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 2019, the group's current ratio was 2.4 (31.12.2018: 2.2) and the quick ratio 0.8 (31.12.2018: 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 37,603 thousand, of which EUR 30,040 thousand was unused (31.12.2018: EUR 34,103 thousand, of which EUR 25,584 thousand was unused). In addition to the overdraft facility, the group has a current loan facility with the limit of EUR 3,500 thousand (31.12.2018: 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 46.2% (31.12.2018: 48.9%) and a moderate proportion of interest bearing liabilities at 22.6% (31.12.2018: 16.4%) 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		
31.12.2019					
Assets					
Cash and overnight deposits (Note 15)	24,749	-	-	24,749	24,749
Trade receivables (Notes 16, 21)	25,758	7,534	11,094	44,386	44,386
Accrued income from construction services (Notes 4, 16)	11,689	-	-	11,689	11,689
Loans and interest (Notes 16, 17, 21)	53	1,650	-	1,703	1,703
Other short-term receivables (Note 16)	172	-	-	172	172
Total	62,421	9,184	11,094	82,699	82,699
Liabilities					
Trade payables (Notes 28, 30)	14,739	15,942	2,476	33,157	33,157
Prepayments for construction services (Notes 4, 28)	8,058	-	-	8,058	8,058
Loan and finance lease liabilities (Note 27) *	4,380	16,345	43,001	63,726	63,726
Other liabilities (Note 28, 30)	79	144	1,015	1,238	1,238
Total	27,256	32,431	46,492	106,179	106,179
Net assets / liabilities	35,165	(23,247)	(35,398)	(23,480)	(23,480)

	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

* 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 2019 and 31 December 2018 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 (31.12.2019: EUR 10,239 thousand; 31.12.2018: EUR 10,253 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 22,532 thousand (31.12.2018: EUR 23,986 thousand) and the fair value of the mentioned receivables is equal to EUR 21,966 thousand using the effective interest rate of 0.31% (31 December 2018: EUR 23,347 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 has 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 2019 and 2018, 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 2019, the total equity attributable to equity owners of the parent was EUR 130,338 thousand (31.12.2018: EUR 131,757 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% (31.12.2019: 46,2%, 31.12.2018: 48,9%).

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

	31.12.2019	31.12.2018
Borrowings	63,726	44,166
Less: cash and cash equivalents and short-term deposits	(24,749)	(39,978)
Net debt	38,977	4,188
Total equity attributable to owners of the parent	130,338	131,757
Total net debt and equity attributable to equity owners of the parent	169,315	135,945
Share of net borrowings	23.0%	3.1%

The group's net debt at 31 December 2019 stood at EUR 39.0 million (31.12.2018: EUR 4.2 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 2019, a provision has been set up at the group in the amount of EUR 202 thousand for covering potential claims and legal costs (31.12.2018: EUR 120 thousand) (Note 29).

An overview of the key legal disputes of group entities ended during 2019 and ongoing as of 31 December 2019 is presented below.

ESTONIA

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

The court cases 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). On April 22, 2019 the Tallinn Administrative Court partially satisfied the appeal and ordered the Republic of Estonia to pay AS Merko Ehitus Eesti EUR 760 thousand and late interest until the principal claim is duly discharged. The court also ordered that procedural costs of EUR 12 thousand should be paid to AS Merko Ehitus Eesti. Both sides filed an appeal to the Tallinn District Court, which partially annulled the decision of the Tallinn Administrative Court and sent the case back to Administrative Court to determine the amount of compensation. Both parties have appealed in cassation to the Supreme Court. The impact of this claim has not been taken into account in the group's reporting.

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 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). The parties have reached a settlement, which provides that SIA Merks will deliver negotiated works to Riga International Airport by 31 March 2020, after which Riga International Airport will sign the final acceptance act. Deriving from the settlement, the parties have asked the court to suspend the case, and the next court hearing is scheduled on 7 May 2020. No additional provisions are recognised in relation to the potential outcome of this claim.

Latvian Competition Council administrative proceeding

On 3 September 2019, Latvian Competition Council (Konkurences padome) officials carried out administrative proceeding activities in the office of SIA Merks. As part of the activities the Chairman of SIA Merks's Management Board was interviewed by the officials. To the group's knowledge, the purpose of the on-going proceeding is to ascertain whether there have been infringements of competition law in Latvia by construction companies. SIA Merks is among the construction companies involved in the proceeding. As of this report, the management has no information about the future of the proceeding. As to the management's knowledge the Competition Council has decided to prolong the term of the proceeding until 1 August 2020 and according to the law, after that term, the council has the right to prolong the term of the proceeding for an additional one year. No provisions are recognised in relation to the effect of this proceeding.

SIA Ostas celtnieks

On 6 November 2019, SIA Merks filed an action against SIA "Ostas celtnieks" in the amount of EUR 230 thousand and additional EUR 21 thousand for late interests. The basis for this claim is the loss incurred from the construction of Ventspils music school and concert hall carried out as per consortium contract of which 35% is to be covered by SIA "Ostas celtnieks" according to its share in the contract. So far, SIA "Ostas celtnieks" has not covered its share of the loss. The court hearing is scheduled on 27 April 2020. The impact of this claim has not been taken into account in the group's reporting.

LITHUANIA

UAB 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, 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 to the court on 14 December 2018. By the decision of 7 June 2019, the court dismissed the claim. On 5 July an appeal was presented to the higher court. 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. By the decision of 18 August 2019, the court appointed court expertise, the expected term of which is up to 6 months. 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 2019, the group recognised EUR 970 thousand (2018: EUR 658 thousand) in impairment losses on assets and inventories, incl. impairment loss of EUR 175 thousand (2018: EUR 0 thousand) on other goods purchased for resale, EUR 794 thousand (2018: EUR 90 thousand) on the write-off of doubtful and irrecoverable receivables and EUR 1 thousand loss from write-off of prepayments to suppliers (2018: EUR 202 thousand). The receivables expensed in prior periods in the amount of EUR 1 thousand were collected (2018: EUR 94 thousand). See also Notes 16 and 18 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

	2019	2018
Revenue	336	4,797
Cost of goods sold	(234)	(4,112)
Gross profit	102	685
Marketing expenses	(32)	(60)
General and administrative expenses	(2,022)	(1,891)
Other operating income	2,059	25,430
Other operating expenses	(129)	(245)
Operating profit (loss)	(22)	23,919
Finance costs	(183)	(182)
Finance income from investments in subsidiaries	14,477	20,322
Profit before tax	14,272	44,059
Deferred income tax expense	(87)	-
Net profit for the year	14,185	44,059

STATEMENT OF FINANCIAL POSITION

in thousands of euros

	31.12.2019	31.12.2018
ASSETS		
Current assets		
Cash and cash equivalents	103	7,979
Receivables and prepayments	3,441	1,081
Inventories	560	746
	4,104	9,806
Non-current assets		
Investments in subsidiaries	123,120	123,332
Other long-term financial assets	48,776	44,831
Property, plant and equipment	246	155
Intangible assets	96	108
	172,238	168,426
TOTAL ASSETS	176,342	178,232
LIABILITIES		
Current liabilities		
Borrowings	3,058	1,032
Trade and other payables	1,068	1,516
Short-term provisions	9	16
	4,135	2,564
Non-current liabilities		
Long-term borrowings	5,169	5,115
	5,169	5,115
TOTAL LIABILITIES	9,304	7,679
EQUITY		
Share capital	7,929	7,929
Statutory reserve capital	793	793
Retained earnings	158,316	161,831
TOTAL EQUITY	167,038	170,553
TOTAL LIABILITIES AND EQUITY	176,342	178,232

STATEMENT OF CHANGES IN EQUITY

in thousands of euros

Parent	Share capital	Statutory reserve capital	Retained earnings	Total
Balance as at 31.12.2017	7,929	793	135,472	144,194
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 as at 31.12.2018				131,757
Net profit for financial year	-	-	14,185	14,185
Dividends	-	-	(17,700)	(17,700)
Balance as at 31.12.2019	7,929	793	158,316	167,038
Carrying amount of holdings under control or significant influence				(123,120)
Value of holdings under control or significant influence under the equity method				86,420
Adjusted unconsolidated equity as at 31.12.2019				130,338

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

CASH FLOW STATEMENT

in thousands of euros

	2019	2018
Cash flows from operating activities		
Operating profit (loss)	(22)	23,919
Adjustments:		
Depreciation and impairment	108	46
(Profit)/loss from sale of non-current assets	-	(3)
(Profit) from transfer of the field of real estate development	-	(24,519)
Interest income from business activities	(2,058)	(900)
Change in provisions	160	22
Change in trade and other receivables related to operating activities	(6,969)	(19,592)
Change in inventories	186	4,006
Change in trade and other payables related to operating activities	(613)	(168)
Interest received	2,722	216
Interest paid	(178)	(169)
Other finance income and costs	(2)	(17)
Corporate income tax paid	(86)	(7)
Total cash flows from operating activities	(6,752)	(17,166)
Cash flows from investing activities		
Investments in subsidiaries	(204)	(38,601)
Disposal of subsidiary	-	400
Liquidation of subsidiary	365	-
Reduction of equity in subsidiary	60	17,387
Proceeds from sale of property, plant and equipment	-	6
Purchase of intangible assets	(19)	(15)
Transfer of the field of real estate development	-	53,322
Interest received	0	1
Dividends received	14,467	20,165
Total cash flows from investing activities	14,669	52,665
Cash flows from financing activities		
Proceeds from borrowings	1,988	-
Loan repayments received	-	(10,974)
Repayments of lease liabilities	(79)	(29)
Dividends paid	(17,700)	(17,700)
Total cash flows from financing activities	(15,791)	(28,703)
Net increase/decrease in cash and cash equivalents	(7,874)	6,796
Cash and cash equivalents in the beginning of period	7,979	1,183
Effect of exchange rate changes	(2)	-
Cash and cash equivalents at end of the period	103	7,979

NOTE 37 EVENTS AFTER THE REPORTING PERIOD

In the beginning of 2020, the existence of a new coronavirus (SARS-CoV-2) was confirmed, which has now spread worldwide, including in Estonia, causing problems for companies and economic activities. The company assesses the viral disease outbreak (COVID-19) as a non-adjusting event after the balance sheet date. Due to the uncertain and rapidly evolving situation, the company does not consider it proper to provide a quantitative assessment of the potential impact of the outbreak on the company.

However, it must be assumed that the national measures taken to combat the spread and consequences of the virus have a serious impact on both the construction and real estate sector in all countries where the group companies are operating. The sharply risen uncertainty about the future will push the construction service customers to postpone their investment decisions and the readiness of home buyers to purchase new apartments decreases. As the national measures include restrictions on freedoms of movement and operation, these will have a negative impact on the supply chains of construction companies and the availability of workforce. Due to that delays might start to occur in construction works. The company is concentrating on monitoring and ensuring both the short and long term liquidity in cooperation with its clients and financing banks. Group's financial state is solid – equity ratio is at 46% of assets and the group has sufficient monetary reserves and unused financing limits from banks to avoid serious liquidity problems. At the same time the group as a whole and each company in the group separately will keep focus on cost management, including cutting costs that is necessary to maintain efficiency in an environment where the amount of works carried out will probably decrease.

The governmental sector will have a pivotal role in ensuring as quick a recovery of the construction sector as possible. This includes enforcing compensation mechanisms for the economic downturn, timely and proper easing of restrictions as well as procuring for construction services. In a situation where the private sector demand will have decreased, the share of the public sector in construction shall be higher than until now. It is important for the public sector to carry out investments into infrastructure and buildings, ensuring work for the construction sector as a whole. The group continues to carry out construction works for clients as well as for own developments, while complying with the restrictions set to impede the spread of the virus and ensuring the health protection of its employees as well as third parties by enforcing precautionary measures.



Independent auditor's report

To the Shareholders of AS Merko Ehitus

(Translation of the Estonian original)*

Report on the audit of the consolidated financial statements

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 2019, 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 dated 31 March 2020.

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of comprehensive income for the year ended 31 December 2019;
- the consolidated statement of financial position as at 31 December 2019;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated cash flow statement for the year then ended; and
- the notes to the consolidated financial statements, which include 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

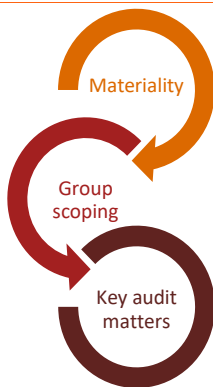
We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements of the Auditors Activities Act of the Republic of Estonia. We have fulfilled our other ethical responsibilities 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. The non-audit services that we have provided to the Group in 2019 are disclosed in the management report and note 7 to the consolidated financial statements.

Our audit approach

Overview



Overall group audit materiality is EUR 3.2 million, which represents approximately 1% of consolidated total revenue.

A full scope audit was performed by us or, under our instructions, by PwC network firms and firms outside PwC network for Group entities covering 99% of the Group's revenues and 96% 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.

- 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 3,2 million
How we determined it	Approximately 1% of consolidated total revenues
Rationale for the materiality benchmark applied	We have applied this benchmark, as revenue 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
<p><i>Revenue recognition on construction contracts</i> (refer to Note 1 'Summary of significant accounting policies – subsections 1.20 'Revenue' and Note 4 'Operating Segments' for further details).</p> <p>In 2019 the Group has recognised revenue of EUR 327 million, EUR 257 million of which is related to construction services.</p> <p>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.</p> <p>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.</p> <p>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.</p>	<p>We audited revenue recognition on construction contracts through a combination of controls testing and substantive testing.</p> <p>We assessed if Group had appropriately applied the guidance in the revenue standard, IFRS 15 regarding accounting for revenue, including for revenue recognised over time.</p> <p>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.</p> <p>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:</p> <ul style="list-style-type: none">• 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. <p>We also evaluated the correctness of disclosures in relation to the construction contracts.</p>
<p><i>Valuation of inventory relating to property developments</i> (refer to Note 1 'Summary of</p>	<p>We assessed the management's expertise to perform valuation of property. The management is experienced in property valuation and the</p>



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 2019 the Group’s statement of financial position sheet includes inventory in the amount of EUR 164 million, of which EUR 28 million were finished apartments, EUR 66 million unfinished apartments and EUR 70 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.

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 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.

How we tailored our Group 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 and firms outside PwC network for entities covering 96% of the Group’s assets and 99% 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 or firms outside PwC network, 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. The other information comprises of Main facts, Statement of the chairman of the management board, Merko Group, Management report, Management declaration, Profit allocation proposal, Other notes to the annual report (but does not include 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 12 years. In accordance with the Auditors Activities Act of the Republic of Estonia and the Regulation (EU) No 537/2014, our appointment as the auditor of AS Merko Ehitus can be extended for up to the financial year ending 31 December 2027.

AS PricewaterhouseCoopers

/ digitally signed /

Tiit Raimla
Certified auditor in charge, auditor's certificate no.287

/ digitally signed /

Janno Hermanson
Auditor's certificate no.570

31 March 2020

** 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 31.12.2019	122,325,819
incl. net profit for 2019	16,269,700
The Management Board proposes profit allocation as follows:	
To allocate the net profit of the year ended at 31 December 2019 to retained earnings	16,269,700
Retained earnings after profit allocation	122,325,819

Andres Trink Chairman of the Management Board / digitally signed / 31.03.2020

Tõnu Toomik Member of the Management Board / digitally signed / 31.03.2020

OTHER NOTES TO THE ANNUAL REPORT

KEY FINANCIAL INDICATORS IN 2015-2019	109
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KEY FINANCIAL INDICATORS IN 2015-2019

CONSOLIDATED INCOME STATEMENT

in thousands of euros

	2019	2018	2017	2016	2015
Revenue	326,779	418,011	317,598	251,970	251,012
Cost of goods sold	(291,958)	(384,962)	(286,747)	(232,961)	(228,044)
Gross profit (loss)	34,821	33,049	30,851	19,009	22,968
% of revenue	10.7%	7.9%	9.7%	7.5%	9.1%
Marketing expenses	(4,260)	(3,285)	(3,215)	(3,281)	(3,230)
General and administrative expenses	(12,988)	(12,304)	(11,289)	(10,076)	(8,907)
Other operating income	2,983	3,527	3,793	2,466	1,943
Other operating expenses	(1,318)	(1,115)	(601)	(399)	(278)
Operating profit (loss)	19,238	19,872	19,539	7,719	12,496
% of revenue	5.9%	4.8%	6.2%	3.1%	5.0%
Finance income	3	8	4	46	120
Finance costs	(684)	(696)	(849)	(649)	(786)
Profit (loss) from joint ventures	1,766	591	78	163	(138)
Profit (loss) before tax	20,323	19,775	18,772	7,279	11,692
% of revenue	6.2%	4.7%	5.9%	2.9%	4.7%
Corporate income tax expense	(3,833)	(375)	(3,020)	(1,275)	(1,857)
Net profit (loss) for the financial year	16,490	19,400	15,752	6,004	9,835
incl. attributable to equity holders of the parent	16,270	19,343	14,694	6,122	10,000
% of revenue	5.0%	4.6%	4.6%	2.4%	4.0%
Attributable to non-controlling interests	220	57	1,058	(118)	(165)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

in thousands of euros

	31.12.2019	31.12.2018	31.12.2017	31.12.2016	31.12.2015
ASSETS					
Current assets					
Cash and cash equivalents	24,749	39,978	39,210	33,544	39,905
Trade and other receivable	50,413	76,183	75,844	45,566	24,854
Prepaid corporate income tax	104	224	492	617	421
Inventories	166,226	117,992	118,421	123,364	109,090
	241,492	234,377	233,967	203,091	174,270
Non-current assets					
Investments in joint ventures	2,498	732	79	434	284
Other long-term loans and receivables	11,094	10,391	17,163	15,371	16,419
Deferred income tax assets	-	-	5	1,325	1,423
Investment properties	14,047	13,771	15,719	4,108	4,371
Property, plant and equipment	11,919	9,715	9,665	12,838	13,442
Intangible assets	777	671	497	673	879
	40,335	35,280	43,128	34,749	36,818
TOTAL ASSETS	281,827	269,657	277,095	237,840	211,088
LIABILITIES					
Current liabilities					
Borrowings	20,725	19,900	24,218	21,485	5,525
Payables and prepayments	69,585	77,016	74,972	56,259	43,266
Corporate income tax liability	812	381	413	278	711
Short-term provisions	7,976	8,100	4,569	5,637	5,013
	99,098	105,397	104,172	83,659	54,515
Non-current liabilities					
Long-term borrowings	43,001	24,266	35,138	24,516	25,660
Deferred income tax liability	1,682	1,481	1,259	1,122	788
Other long-term payables	3,491	2,179	1,789	2,061	1,159
	48,174	27,926	38,186	27,699	27,607
TOTAL LIABILITIES	147,272	133,323	142,358	111,358	82,122
EQUITY					
Non-controlling interests	4,217	4,577	4,567	3,692	3,268
Equity attributable to equity holders of the parent					
Share capital	7,929	7,929	7,929	7,929	7,929
Statutory reserve capital	793	793	793	793	1,200
Currency translation differences	(710)	(721)	(702)	(645)	(663)
Retained earnings	122,326	123,756	122,150	114,713	117,232
	130,338	131,757	130,170	122,790	125,698
TOTAL EQUITY	134,555	136,334	134,737	126,482	128,966
TOTAL LIABILITIES AND EQUITY	281,827	269,657	277,095	237,840	211,088

OTHER KEY FIGURES

attributable to equity holders of the parent

		2019	2018	2017	2016	2015
EBITDA	million EUR	21.9	21.9	22.2	11.2	15.5
EBITDA margin	%	6.7	5.2	7.0	4.4	6.2
General expense ratio	%	5.3	3.7	4.6	5.3	4.8
Staff costs ratio	%	11.4	8.2	10.1	11.7	12.2
Revenue per employee	thousand EUR	461	563	434	325	322
ROE	%	12.9	15.3	11.9	5.0	8.0
ROA	%	5.6	6.9	5.8	2.8	4.4
ROIC	%	11.1	11.5	11.4	5.1	7.9
Equity ratio	%	46.2	48.9	47.0	51.6	59.5
Debt ratio	%	22.6	16.4	21.4	19.3	14.8
Current ratio	times	2.4	2.2	2.2	2.9*	3.2
Quick ratio	times	0.8	1.1	1.1	1.1*	1.2
Accounts receivable turnover	days	45	40	40	37	39
Accounts payable turnover	days	53	41	40	38	39
Number of employees as at 31.12	people	694	764	757	797	791
Average number of employees	people	709	743	732	776	779
Secured order book as at 31.12	million EUR	141	229	344	270	247
New contracts signed	million EUR	170	246	335	202	247

* 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

		2019	2018	2017	2016	2015
Earnings per share (EPS)	EUR	0.92	1.09	0.83	0.35	0.56
Equity per share	EUR	7.13	7.16	6.99	6.90	7.02
Dividend per share	EUR	*	1.00	1.00	0.41	0.51
Dividend rate	%	*	92	120	119	90
Dividend yield	%	*	10.9	11.4	4.5	6.0
P/E ratio	times	10.20	8.42	10.61	26.17	15.01
P/B ratio	times	1.32	1.28	1.26	1.31	1.21
Share price trend						
Average	EUR	9.55	10.02	9.27	8.44	8.47
Highest	EUR	10.30	11.80	9.69	9.22	10.50
Lowest	EUR	8.74	8.70	8.75	7.60	7.06
Share price as at 31.12	EUR	9.38	9.20	8.81	9.05	8.48
Market value as at 31.12	million EUR	166.0	162.8	155.9	160.2	150.1
Share turnover trend						
Share turnover	million EUR	21.31	12.16	4.69	5.35	7.71
Transactions	pcs	8,558	4,299	2,203	2,312	2,829
Shares traded	million pcs	2.23	1.18	0.51	0.63	0.90
Ratio of shares traded	%	12.6	6.7	2.9	3.6	5.1
Number of shares	million pcs	17.70	17.70	17.70	17.70	17.70
Number of shareholders as at 31.12	pcs	3,924	2,664	2,040	1,813	1,624

* Ratios related to dividends for 2019 will depend on the decision of the general meeting of shareholders to pay dividends.

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 (%)	=	$\frac{(\text{Profit before tax} + \text{interest expense} - \text{foreign exchange gain (loss)} + \text{other financial income}) \text{ of the current 4 quarters}}{(\text{Shareholders equity (average)} + \text{interest-bearing liabilities (average)}) \text{ of the current 4 quarters}}$
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	=	$\frac{\text{Current assets} - \text{inventories}}{\text{Current liabilities}}$
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 (%)	=	$\frac{\text{Operating profit} + \text{depreciation}}{\text{Revenue}}$
General expense ratio (%)	=	$\frac{\text{Marketing expenses} + \text{General and administrative expenses}}{\text{Revenue}}$
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 2019 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	2019	2018
Real estate activities		
6810 sales of own real estate	282	4,735
6820 renting and operating of own or leased real estate	54	62
Total revenue	336	4,797

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.

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

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, 7-8, 16, note 4	
102-3	Location of headquarters	p. 2	
102-4	Location of operations	p. 4, 16, note 19	
102-5	Ownership and legal form	p. 4, 35-37, 39-44	
102-6	Markets served	p. 4, 16, note 4	
102-7	Scale of the organisation	p. 4, 10, 25	
102-8	Basic information on employees	p. 25	
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. 23-25, 30	
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, 29-30	In addition to Merko Ehitus values, mission and vision, our operations are guided by responsible management system and business principles, including code of business ethics. 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. 39-44	
STAKEHOLDER ENGAGEMENT			
102-40	List of stakeholders	p. 114	
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. 114	
102-43	Approach to stakeholder engagement	p. 114	

102-44	Key topics and concerns raised	p. 21, 26	Customers and employee satisfaction surveys, grievances about labour practices
REPORTING PRACTICE			
102-45	Entities included in the consolidated financial statements		The report covers all of Merko Ehitus group's functions, unless otherwise mentioned.
102-46	Defining report content and topic Boundaries	p. 114	
102-47	List of material topics	p. 114	
102-48	Restatements of information		-
102-49	Changes in reporting		-
102-50	Reporting period		The reporting period is the calendar year, January 1, 2019 – December 31, 2019
102-51	Date of most recent previous report		The most recent previous integrated annual report was published on April 10, 2019.
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. 115-119	
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. 25	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.
Direct economic value generated and distributed for stakeholders 2019 (2018)			
Customers Revenue EUR 326.8 million (418.0)	Suppliers Materials and goods, EUR 58.0 million (70.3) External services EUR 185.1 million (262.2)		Employees 694 employees (764) Labour costs EUR 37.4 million (34.4)
	Investors Dividends EUR 17.7 million (17.7)		Public sector Corporate income tax expense EUR 3.8 million (0.4)
201-1	Direct economic value generated and distributed		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

	2019	2018
Estonia	22,100	17,999
Latvia	2,123	2,559
Lithuania	-226	4,706
Norway	1,434	1,234
Total	25,431	26,498

* Actually paid and not calculated tax amounts.

PAID* TAXES BY TAX TYPES

in thousands of euros

	2019	2018
Value added tax	5,297	12,108
Taxes on employee wages and fringe benefits	15,395	12,894
Other taxes	1,287	1,107
Corporate income tax	3,452	389
Total	25,431	26,498

* 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 40-43	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 Baltic region, our economic activity has a significant impact on the local economic environment. We build new building: homes for hundreds of families and large public buildings, educational establishments, defence facilities, office buildings and shopping centres among others. In addition, we build and maintain public roads, ensure better energy supply, and work 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. 17, 21, 30-31	
203-2	Significant indirect economic impacts	p. 17-19, 30-33	
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, 68-69	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. 29-30	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 2019. 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 Merko group follow the principles of ensuring the requirements of European Parliament and of the Council regulation 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		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) and the local legislation that requires Merko to comply with its large company energy audit obligation. The regular energy audits of Merko group companies have been regularly submitted and declared to be in conformity.
301-2	Energy consumption outside of the organisation		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 energy consumption, fuel consumption and CO ² emissions. From 2019 onwards, 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 implementation of energy-efficient building solutions.
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 and the principles of legislation. Merko maintains in-house 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. 30	
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.25-29	
401-1	New employee hires and employee turnover	p. 25	The age groups are not gathered at group level.
401-2	Benefits provided to full time employees	p. 29	
GRI 403: Occupational Health and Safety 2016			
GRI 103-1 to GRI 103-3	Management approach	p. 27-28	
403-2	Rates of injury, fatalities and absenteeism	p. 28	
GRI 404: Training and Education 2016			

GRI 103-1 to GRI 103-3	Management approach	p. 26, 28-29	
404-2	Programs for skills management and lifelong learning that support the continued employability of employees and assist them in managing career endings	p. 28-29	
404-3	Employees receiving regular performance and career development reviews	p. 26	
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. 7-8, 30-31, 114	
413-2	Operations with significant actual and potential negative impacts on local communities		-
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.