AS BALTIKA ANNUAL REPORT 2016

AS BALTIKA

2016 CONSOLIDATED ANNUAL REPORT

(Translation of the Estonian original)

Commercial name	AS BALTIKA
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Internet homepage:	www.baltikagroup.com
Main activities	Design, development, production and sales arrangement of the fashion brands of clothing
Auditor	AS PricewaterhouseCoopers
Beginning and end of financial year	01.01.2016 - 31.12.2016

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BALTIKA GROUP IN BRIEF

Baltika Group, with the parent company AS Baltika, is an international fashion retailer. Baltika Group develops and operates fashion brands: Monton, Mosaic, Baltman, Bastion and Ivo Nikkolo. Baltika employs a vertically integrated business model, which means that it controls all stages of the fashion process: design, manufacturing, supply chain management, distribution/logistics, wholesale and retail. As at 31 December 2016 Group had 128 stores, including 33 franchise partners´ stores in Spain, Ukraine, Belarus and Russia. The shares of AS Baltika are listed on the Nasdaq Tallinn Stock Exchange that is part of the exchange group NASDAQ.

MISSION AND KEY STRATEGIC STRENGTHS

Baltika Group creates quality fashion that allows people to express themselves and feel great.

- Learning organisation with high targets
- Flexible, vertically integrated business model
- Centralised management with strong retail organisations in the markets
- Brand portfolio covering a broad customer base

KEY FIGURES AND RATIOS

	2016	2015[1]	2014	2013	2012
Comprehensive income data, in millions					
Revenue	47.0	48.8	57.1	58.3	56.3
Gross profit	23.5	23.1	28.9	31.2	30.7
EBITDA	2.0	0.9	0.6	2.3	3.7
Operating profit	0.7	-0.3	-0.7	0.7	2.0
Profit before income tax	0.2	-0.8	-1.1	0.3	1.1
Net profit	0.2	-0.8	-1.3	0.1	0.8
Other data					
Number of stores in retail	95	95	105	124	113
Number of stores total	128	123	128	126	113
Retail sales area in the end of period, sqm	17,161	17,046	20,232	23,852	22,210
Number of employees (31 Dec)	1,049	1,095	1,228	1,345	1,288
Sales activity key figures					
Revenue growth	-4.0%	2.0%	-2.1%	3.6%	5.5%
Retail sales growth	-7.1%	1.3%	-5.8%	3.6%	5.2%
Share of retail sales in revenue	84.4%	87.6%	90.0%	93.6%	93.5%
Share of exports in revenue	56.4%	56.6%	65.2%	66.5%	68.0%
Gross margin	50.0%	47.3%	50.8%	53.5%	54.5%
Operating margin	1.5%	-0.6%	-1.2%	1.1%	3.5%
EBT margin	0.4%	-1.6%	-2.0%	0.5%	1.9%
Net margin	0.4%	-1.7%	-2.2%	0.2%	1.4%
Inventory turnover	2.17	2.16	2.09	2.09	2.37
Financial position data, in millions[2]					
Total assets	18.9	18.1	23.1	24.3	23.5
Interest-carrying liabilities	7.0	6.3	7.3	5.3	6.3
Shareholders' equity	5.0	4.8	8.7	11.5	10.2
Current ratio	1.1	1.3	1.6	1.5	1.8
Debt to equity ratio	141.6%	131.5%	83.0%	46.1%	61.6%
Net gearing ratio	133.2%	123.2%	74.9%	38.7%	41.2%
ROE	3.8%	-92.8%	-13.4%	1.0%	8.9%
ROA	0.9%	-28.1%	-5.4%	0.4%	2.8%

	2016	2015	2014	2013	2012
Key share data, EUR[2]					
Number of shares outstanding (31 Dec)	40,794,850	40,794,850	40,794,850	40,794,850	35,794,850
Weighted average number of shares	40,794,850	40,794,850	40,794,850	38,644,165	35,794,850
Share price (31 Dec)	0.28	0.34	0.46	0.55	0.57
Market capitalisation, in millions (31 Dec)	11.5	14.0	18.8	22.3	20.5
Earnings per share (EPS)	0.00	-0.16	-0.03	0.00	0.02
Diluted earnings per share (DPS)	0.00	-0.16	-0.03	0.00	0.02
Change in EPS, %	103%	433%	-1278%	-87%	111%
P/E	65.21	-2.19	-14.9	208.2	28.7
Book value per share	0.12	0.12	0.21	0.28	0.28
P/B	2.3	2.9	2.2	1.9	2.1
Dividend per preference share	0	0	0	0	0
Interest rate	0%	0%	0%	0%	0%
Preference share dividend payout ratio	0%	0%	0%	0%	0%
Dividend per share	0*	0	0	0	0
Dividend yield	0%*	0%	0%	0%	0%
Dividend payout ratio	0%*	0%	0%	0%	0%

*Proposal to the general meeting.

[1]In connection with Baltika's exit from Russian retail business in 2015, other data and sales activity key figures for 2015 are presenting only results of continued operations.

[2]Financial position data and key share data includes impact of continued and discontinued operations.

Any reference to Baltika's "share" or "shares" is a reference to ordinary shares unless indicated otherwise.

Definitions of key figures and ratios

EBITDA= Operating profit-depreciation and amortisation - disposal of fixed assets
Gross margin = (Revenue-Cost of goods sold)/Revenue
Operating margin = Operating profit/Revenue
EBT margin = Profit before income tax/Revenue
Net margin = Net profit (attributable to parent)/Revenue
Inventory turnover = Cost of goods sold/Average inventories[3]
Current ratio = Current assets/Current liabilities
Debt to equity ratio = Interest-carrying liabilities/Equity
Net gearing ratio = (Interest-carrying liabilities-Cash and cash equivalents)/Equity
Return on equity = Net profit (attributable to parent)/Average equity[3]
Return on assets = Net profit (attributable to parent)/Average total assets[3]
Market capitalisation = Share price (31 Dec) x Number of shares outstanding (31 Dec)
EPS = Net profit (attributable to parent)/Weighted average number of shares
DPS = Diluted net profit (attributable to parent)/Weighted average number of shares
P/E = Share price (31 Dec)/EPS
Book value per share = Equity/Number of shares outstanding (31 Dec)
P/B = Share price (31 Dec)/Book value per share
Dividend yield = Dividends per share/Share price (31 Dec)
Dividend payout ratio = Paid out dividends/Net profit (attributable to parent)
[3]Based on 12-month average

MANAGEMENT BOARD'S CONFIRMATION OF MANAGEMENT REPORT

The Management Board confirms that the management report presented on pages 5 to 49 presents a true and fair view of the business developments and results, of the financial position, and includes the description of major risks and doubts for the Parent company and consolidated companies as a group.

Meelis Milder
Chairman of the Management Board
22 March 2017

Maigi Pärnik-Pernik
Member of the Management Board
22 March 2017

MANAGEMENT REPORT

CHAIRMAN'S STATEMENT

In 2016, Baltika Group completed the procedures undertaken to reduce risk and improve operational efficiency in its business model. In 2014 we exited from Ukrainian retail market, with brand stores there beginning collection sales on a franchise model basis. In 2015, Baltika Group exited from Russian retail market and Baltika fashion brand resales also continued through an experienced franchising partner. The successful executed move from our retail system to a franchise model in both Ukraine and Russia has allowed us to continue sales of Monton and Mosaic brands to customers in these markets without us losing significant sales volumes, but also returning to profitability.

Although the exits from the Ukrainian and Russian markets brought with them significant costs to the company, which were among the biggest reasons for the losses in 2014 and 2015 financial year, Baltika Group managed, with a number of other significant changes (in inventory management and collection development), to create a business model that allows for profitable growth and uses multi-channel sales by the beginning of 2017: the historically profitable Baltic retail market in combination with the fast-growing potential of wholesale, franchising and e-commerce trends.

The largest challenge in the coming years will certainly be developing the business model to be more competitive on an international level – Baltika is becoming an international brand house whose aim is to offer excellent brand-driven customer experiences in all sales channels.

One conclusion we can take from these years of changes is that the Baltika Group's brand portfolio passed the quality test. If one of the most frequently asked questions is why five brands for a company the size of Baltika, our answer is that we want to sell to as many different customer groups in the small Baltic retail market as possible and to meet their needs, sharing common operations and management costs and dispersing risk. We have created for all our fashion brands – Monton, Mosaic, Baltman, Ivo Nikkolo and Bastion – unified back office structures and processes, the result of which being that we manage our portfolio made up of different brands with optimum costs. Today, we have created an optimised and profitable network of 95 branded stores in Estonia, Latvia and Lithuania, in which we see more room for the growth of our smaller brands and ways to consolidate certain retail sales under Baltika's newest AndMore retail concept.

At the same time, competition in the Baltic retail market has grown significantly in recent years, and most of Europe's stronger clothing brands have entered the market. Online sales for international fashion brands have also grown yearly and this has in turn led to a situation where customer requirements and expectations as well as purchasing habits have changed. This also makes the Baltika Group and the teams of all our brands – Monton, Mosaic, Baltman, Ivo Nikkolo and Bastion – put in even more effort in the name of offering the best customer experience.

In 2016, we took many important steps in the interests of offering excellent customer experiences and preserving our position in the top five largest fashion product retailers in the Baltic States, like the following:

- we pay more attention to original design features and collection quality (nearly 45% of our collections are produced in Estonia by Baltika Group subsidiaries);
- better planned and managed outsourcing, which allows us to work with less inventory and lower mark downs;
- actively oriented customer communication with loyal customers of Baltika fashion brands in all three retail markets, through the AndMore customer programme;
- brand shop location planning in the best shopping centres in Estonia, Latvia and Lithuania;
- development of the e-store Andmorefashion.com;
- further development of multi-brand shops and creation of Andmore concept (e.g. Monton AndMore).

The profitable retail business in Baltika's home markets of Estonia, Latvia and Lithuania has given Baltika the opportunity to develop the franchise sale trend in new markets. The first franchise agreements with foreign partners were signed back in 2013, with agreements in Tenerife, Spain following in 2014-2015, and in 2016 we concluded the first agreement to open a Monton AndMore store in Novi Sad, Serbia This time has been spent on creating value for franchise partners and improving the franchise model, and in years to come we see great potential in franchise trends to grow Baltika Group's exports in Europe.

In wholesale, Baltika has been active in selling to prestigious department stores and retailers for more than 20 years. In order to grow design markets, we have invested effort in the last years in finding new partners and markets, of which particularly noteworthy is the stocking of the Monton collection in the exclusive German department store chain, Peek & Cloppenburg. Monton was sold as the first brand from Eastern Europe in spring 2016 in three Peek & Cloppenburg department stores, with the number reaching 25 sales points by the end of that year, and for 2017, orders have been submitted by 39 Peek & Cloppenburg department stores in central and Eastern Europe.

Sales in the online store Andmorefashion.com have also grown rapidly, which on the one hand supports Baltika's retail sales, providing information on collections and so-called pre-shopping options. Furthermore, Estonian design exports are growing through the Andmorefashion.com e-store. In 2016, e-store turnover exceeded the 1 million euro mark for the first time, with most sales growth in Latvia, Lithuania and Russia.

In addition to sales channel development and diversification, we continued with many management and business process development projects in 2016, the result of which was significant improvement in the operating cost-gross profit ratio. As 2017's challenge which meets the same objective as above, we see logistical process development, sales efficiency improvement, and the development of an integrated management system for our own production.

In 2018, Baltika will celebrate its 90th anniversary as the largest brand house in the Baltics, and we hope to celebrate it as a successful, dynamic and international company.

Meelis Milder
Chairman of the Management Board

FINANCIAL RESULTS OF 2016

Baltika Group's net profit for year 2016 was 0.2 million euros. Last year's comparative result was loss in amount of 0.8 million euros and result with discontinued operations was net loss in amount of 6.4 million euros.

In connection with Baltika Group's exit from the Russian retail business, which represented a major line of business of the Group, the 2015 results of the Russian companies' retail are presented as discontinued operation.

Baltika's revenue in 2016 was 47 million euros, decreasing 4% compared to last year. Revenue growth was largest with 21% in wholesale and franchise and was 6 million euros. The increase in revenue is mainly attributable to Russian retail market's transition to franchise partner and Monton collection entrance to German department store chain Peek & Cloppenburg. Within year the number of Monton selling Peek & Cloppenburg department stores increased from 3 to 25.

In addition to wholesale channel the franchise channel is actively being developed as well. At the beginning of October Baltika signed a franchise agreement with Serbian enterprise Victoria Elegans d.o.o., who opened Baltika's brands representing store Monton AndMore in Novi Sad Serbia on 8 of March 2017. Monton AndMore is a Baltika's new store concept to increase international sales and where in addition to Monton other Baltika's brands are represented as well. As at the end of the year there were 33 franchise stores, forming 26% of total stores portfolio.

Revenue from Baltika Group's e-store Andmorefashion.com increased 9% and was 1.1 million euros. With an increase of wholesale and franchise revenue and e-store revenue one of the objectives for 2016 – growth in other sales channel revenue was met.

Baltika's 2016 retail revenue was 39.7 million euros, which is 7% less than in the previous year. However the gross profit margin has increased.

Baltika's gross profit margin in 2016 was 50%, which means 2.7 percentage points growth compared to last year (2015: 47.3%). Gross profit margin has increased due to better intake margin and lower mark downs, thus margin has increased in all sales channels.

One of the reasons behind the improved results is the decision to leave from unprofitable high risk retail markets in Ukraine and Russia and transfer these brand stores over to franchise partner. This has allowed increase in franchise channel revenue while minimizing the risks and maintaining Baltika's brands on these complicated markets.

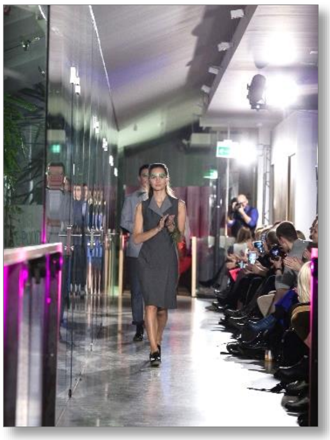
In addition, the results have improved as well due to more effective gross profit margin management and decrease in distribution and administrative expense. The year gross profit amounted 23.5 million euros, the comparative result from 2015 was 0.4 million euros less i.e. 23.1 million euros. Distribution, administrative and general expense has decreased almost 0.8 million euros.

In 2017 Baltika will continue with chosen course and strategy. Baltika's objective in home markets: in Estonia, Latvia and Lithuania is to maintain and strengthen their current position and the company's objective is also to grow outside Baltics through wholesale and franchise.

HIGHLIGHTS OF THE PERIOD UNTIL THE RELEASE OF ANNUAL REPORT

- From 1st of February 2016 Maigi Pärnik-Pernik continues working as a member of AS Baltika Management Board and is responsible for the finance functions and for the disclosure of information on the exchange.

- On 9th of February 2016 Baltika held a fashion show to launch spring-summer collection. The newest collections were shown in Baltika's headquarter and after the show collections were available in shops and in e-store.



- On 22nd of February 2016 Baltika signed an agreement with OÜ Ellipse Group to sell 100% of shares of Russia's retail operating company OOO Olivia that owns subsidiaries OOO Stelsing and OOO Plazma. OÜ Ellipse Group will continue to cooperate with Baltika as franchise partner and on 22 February cooperation agreement was signed for the next five years. The price received for the Russian entities was 463 thousand euros and payment schedule was agreed for 5 years, depending on Russian entities financial results.

- On 14th of March 2016 Lilian Nõlvak started working as a communication manager of AS Baltika. Previously Lilian worked as PR manager in Elion Ettevõtted AS (now known as Telia Eesti AS).

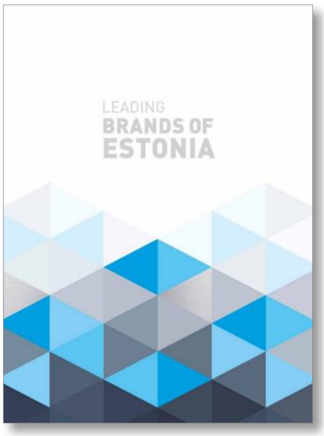
- Supervisory Board of AS Baltika decided to recall from the Management Board starting from 17th of March 2016 Management Board member Kati Kusmin.

- Baltika ended representing Blue Inc London brand in Baltics states under the franchise agreement due to low sales efficiency and closed four stores in Estonia and in Latvia at the beginning of the year. Baltman store was opened as a replacement in one of the sales areas in Tallinn Ülemiste shopping centre and in Riga Origo shopping centre, Bastion store was opened.

- On 18th of April 2016 Monton presented its Rio Olympics special collection for the first time to public in Lennusadam.

- From 2nd of May 2016 Kristel Sooaru started working as Sales and Marketing Director. Kristel has previously occupied different management positions at Baltika for 19 years, last position was the head of menswear collections and before that she was the head of Baltman brand. Before returning to Baltika Kristel was the purchase manager of TKM King, which is the holding company of Tallinna Kaubamaja Group's footwear trade store chains ABC King and SHU.

- The Annual General Meeting of AS Baltika, held on 2nd of May 2016, approved the Annual report for 2015 and covering net loss from retained earnings. Meeting also approved the amendments of the Articles of Association.



- Baltika was chosen as one of the leading brands in Estonia. The Estonian Chamber of Commerce and Industry is preparing the book "Leading Brands of Estonia", which contains 60 leading brands of Estonia. Baltika was chosen in top fifty most widely known and internationally operating companies in Estonia. In 2016 published first edition will be presented in this fall. The criterions of choosing the leading Estonian companies and brands were: created in

Estonia and recognisable Estonian heritage, widely known in Estonia, brand is positioned as Estonian brand, has an export potential or operates internationally.

- On 27th of July 2016 AS Swedbank and AS Baltika signed an agreement amendment according to which Baltika will get during one-year period investment loan in the amount of 2 million euros with a repayment period of 4 years. Agreement amendment also contains 20 month extension for the repayment of the existing loan in the amount of 1 million euros. Loan interest margin remained same.
- On 24th of August 2016 Baltika Group presented its fashion brands autumn/winter collection in the NO99 theatre. For the first time in the history of the fashion show, it was broadcasted in all Baltika Group’s home markets – Estonia, Latvia and Lithuania via Delfi.
- On 21st-25th of September 2016 a delegation of 22 Estonian design brands, including three of Baltka’s fashion brands – Baltman, Ivo Nikkolo and Monton, participated in the Washington DC Fashion Week. The aim of taking Estonian fashion and design to Washington was to introduce strong Estonian brands in the US, to create long-lasting cooperation opportunities and to develop e-commerce of the sector.
- At the beginning of October Baltika signed a franchise agreement with Serbian enterprise Victoria Elegans d.o.o., who opened the first Monton AndMore multibrand store in Novi Sad, Serbia on 8th of March 2017.
- On 22nd of October in Tallinn Kultuurikatel during Tallinna Fashion Week Baltman – the first men’s fashion brand in Estonia – presented its special collection to celebrate the 25th anniversary of Baltman.

- At the last week of October in Riga Fashion Week, which is the most influential fashion event in Baltics, Ivo Nikkolo presented its 2017 spring-summer collection, which received a warm feedback from Estonian, Latvian and Lithuanian fashion-audience. In addition, an overview of the collection was published in Vogue Russia and Elle Italy websites.
- At the beginning of November Monton marketing team won Digitegu 2016 (“*Digital deed 2016”*) award for the best e-mail marketing.

- As at 31st of December 2016 there were 95 stores in Baltika’s retail store portfolio.
- On 7th of March 2017 Monton, Mosaic, Ivo Nikkolo, Baltman and Bastion presented their 2017 spring-summer collection in Hansaplant gardening centre. Fashion show also broadcasted via Baltika’s e-store Andmorefashion.com.
- On 17th of March 2017 Monton, who is celebrating its 15th anniversary this year, presented within the Tallinn Fashion Week a special collection inspired by the magic of opposites, of which the majority of items are handmade.

MEETING THE OBJECTIVES OF 2016

- Growth in Baltic retail market sales and increase of profitability through improvement of gross profit margin

  In a situation where competition in Baltic retail market has increased significantly as most of the widely known European fashion brands have entered to the market and in turn clients' expectations on products' originality and on price and quality ratio have increased, this is one of the most challenging objectives to meet. In 2016 the retail revenue was 39.7 million euros, which is 7% less than in previous year. At the same time owing to lower mark downs and more effective purchasing price management the Baltics retail gross profit margin has increased 2.7 percentage points from 52.7% to 55.4%, which makes the year gross profit 22 million euros (2015: 22.5 million euros)

  Objective for gross profit margin has been met, but objective for growth of sales has not been met.

- Other sales channels (wholesale, franchise and e-store) development and increase in sales growth

  In 2016 wholesale and franchise revenue was 6 million euros, increasing by 1 million euros i.e. 21% compared to previous year. The increase in volume is largely attributed by Monton collection success in Peek & Cloppenburg department stores. Within year the number of Monton collection selling Peek & Cloppenburg department stores has increased from 3 to 25. In addition growth in wholesale and franchise sales revenue was supported by Russian retail market transition over to franchise partner. At the end of the year the franchise partners portfolio increased as well: at the beginning of October Baltika signed a franchise agreement with Serbian enterprise Victoria Elegans d.o.o., who at the beginning of March 2017 opened the first Baltika's brands representing store in Serbia.

  In 2016 the growth of e-store Andmorefashion.com, that covers all five if Baltika's brands, was continually fast. Over the year improvements to e-store functionality and speed were made, one new delivery system was added in a form of DPD courier, and changes in e-store photo-language were made. Also from July 2016 Monton and Mosaic products are available in Amazon.de website, which is visited by more than 30 million visitors in a month. In a year total e-store revenue was 1.1 million euros (increase of 9% compared to 2015). Thus the objective given to wholesale, franchise and e-store has been met.

- Better inventory management – higher inventory turnover

  Better inventory management has been one of the main objectives for Baltika Group in recent year. The company has created new structures and tools for collection development and for inventory planning and realising. Baltika Group's 2016 inventory turnover (cost of goods sold divided by 12 months average inventories) was 2.17, the comparative result from last year was 2.16. Thus the inventory turnover has not increased significantly. In 2015 company had additional discount pressure due to overstock, but in 2016 the inventory level was under stricter control and thus the gross profit and average stock ratio has improved from 1.94 to 2.16. The objective of better inventory management has been partially met.

- Operating efficiency improvement – decrease of head-office expense

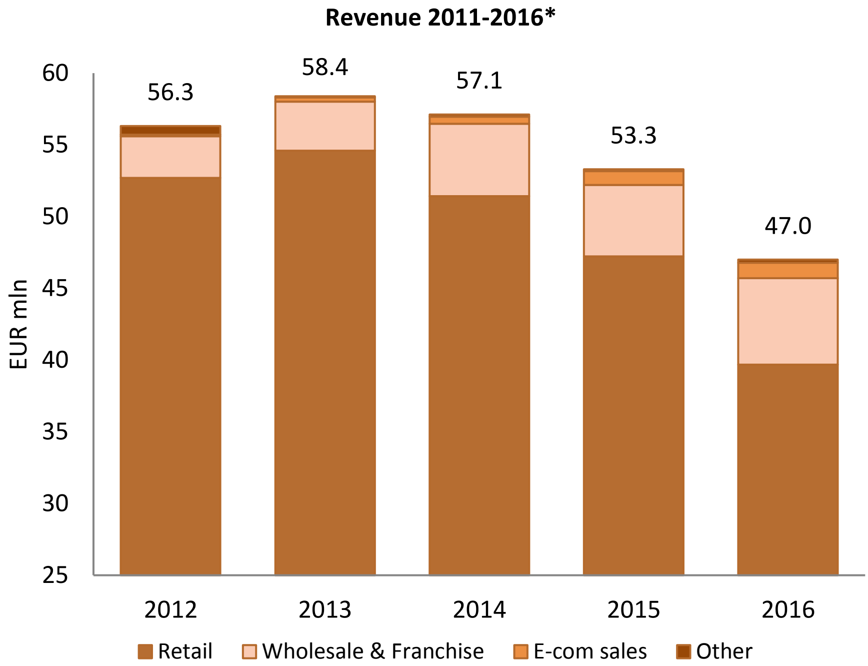
  Due to lack of qualified labour force the wage growth pressure is high on all Baltic states, thus making head-office process more effective and decrease expenses is very important to Baltika. In 2016 head-office expenses have decreased 0.5 million euros i.e. 6%. The objective has been met.

2016 Consolidated Annual Report (in thousands of euros)

REVENUE

Continued operations

EUR million	**2016**	**2015**	**+/-**
Retail	39.7	42.7	*-7%*
Wholesale & Franchise	6.0	5.0	*21%*
E-com sales	1.1	1.0	*9%*
Other	0.2	0.1	*78%*
Total	**47.0**	**48.8**	***-4%***



*Revenue total discontinued and continued operations

RETAIL

In 2016 retail revenue was 39.7 million euros i.e. 7% less than last year's comparative result.

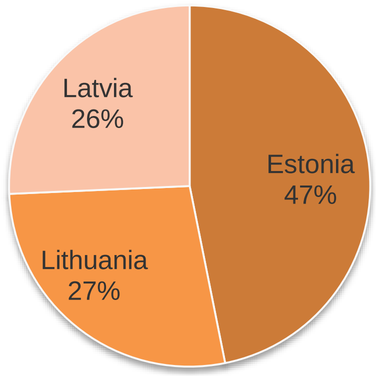
Retail sales by markets

EUR million	**2016**	**2015**	**+/-**
Estonia	18.6	19.4	*-4%*
Lithuania	10.9	12.1	*-10%*
Latvia	10.2	11.2	*-9%*
Total	**39.7**	**42.7**	***-7%***
Russia*	0.0	4.5	*-100%*

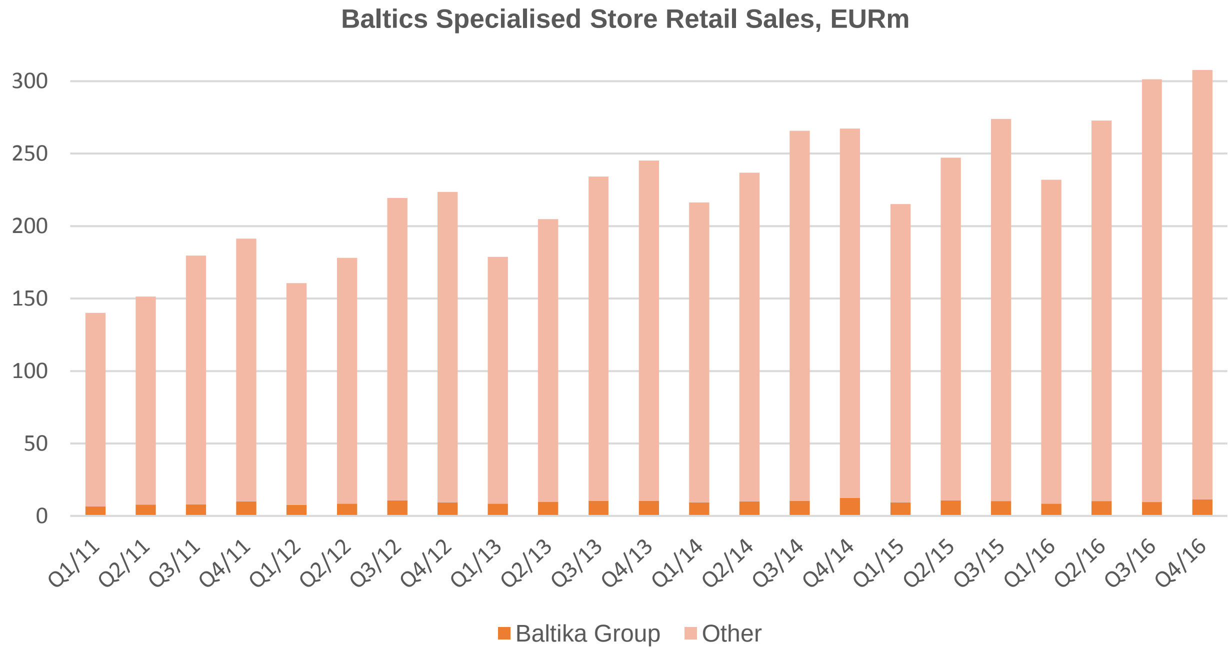
*discontinued operations

2016 Consolidated Annual Report (in thousands of euros)

Breakdown of retail sales by market – 2016



Baltika Group's biggest retail market continues to be Estonia. In a year the share of Estonian market has increased by 1.4 percentage points, from 45.5% to 46.9%.



Source: LHV, Statistics Estonia, Central Statistical Bureau of Latvia, Statistics Lithuania

Retail revenue in Estonia has decreased the least but due to increase in operating area sales efficiency has decreased the most in Estonia. One of the reasons behind the decrease in sales efficiency is the changes in stores portfolio. In addition to large shopping centres, expansions to Tallinn and other Estonian cities' smaller shopping centres, where sales efficiency is relatively lower, have been made. Lithuania's results have been influenced by the decrease in revenue and by planned store renovations to improve the customer experience.

Sales efficiency by market (sales per sqm in a month, EUR)

EUR/m²	**2016**	**2015**	**+/-**
Estonia	205	226	*-9%*
Lithuania	163	180	*-9%*
Latvia	223	234	*-5%*
Baltics	**195**	**213**	***-8%***

2016 Consolidated Annual Report (in thousands of euros)

AndMore bonus programme for loyal customers

The loyal customer programme AndMore, which covers all the stores and the e-shop, has been in use since 2014. With the AndMore bonus programme, every purchase grants the customer a bonus, which they can begin to use from their next purchase. Customers can earn 5%, 7% or 10% bonuses, depending on their customer level determined by the annual purchase volume. In addition, customers can use a one-time purchase bonus of 5, 7 or 10 euros on their birthday.

A common customer programme allows to get a good overview of our loyal customers and their preferences, which in turn enables to send them personalised messages based on customer behaviour. Every customer can also monitor their personal bonus account balance in the e-shop at Andmorefashion.com.

As of 2016, 447,000 people had joined the bonus programme. There were 203,000 joined customers in Estonia, 99,000 in Latvia and 144,000 in Lithuania. In 2016, the purchase volume of loyal customers comprised 74% of Baltika's total retail sale in the Baltic region. In total, loyal customers made over 630 thousand purchases during the year.

STORES AND SALES AREA

At the end of 2016 Baltika Group had 128 stores in seven countries with total sales area of 23,211 m^2, among which 33 franchise stores with a total sales area of 6,050 m^2. Retail network average operating area increased by 1% in a year. In 2016 Baltika ended representing Blue Inc London brand in Baltics states under the franchise agreement due to low sales efficiency and closed 4 stores in Estonia and in Latvia. On two of the shops' areas new concept stores were opened: In Tallinn Ülemiste shopping centre Baltman store and in Riga Origo shopping centre Bastion store was opened. In addition 2 new Baltika's brand stores were opened: in Tartu Kvartal shopping centre Monton and Mosaic store and in Riga Mols shopping centre Baltman store.

Stores by markets

	31 December 2016	31 December 2015	+/-
Estonia	44	44	0
Lithuania	29	29	0
Latvia	22	22	0
Russia[1]	0	10	-10
Russia[2]	12	5	7
Ukraine[3]	16	15	1
Belarus[3]	2	2	0
Spain[3]	3	6	-3
Total stores	**128**	**133**	**-5**
Total sales area, sqm	**23,211**	**24,371**	**-1,160**

[1]Russian retail is part of the discontinued operations. Eight of Russian retail stores will continue operating as franchise stores.

[2]Russian franchise stores have a total sales area of 2,424 m^2. Eight of Russian franchise stores, with a total sales area of 1,940 m^2, were in comparative period part of Russian retail which is retail segment discontinued operation.

[3]Franchise stores in Ukraine, Belarus and Spain have a total sales area of 3,626 m^2.

2016 Consolidated Annual Report (in thousands of euros)

Photos: Monton and Mosaic store in Tartu Kvartal shopping centre

In addition to retail stores two new Monton franchise stores were opened in Ukraine: one in Kiev and the other in Zaporogie. Decrease in number of stores is due to closing of low profit stores in Spain and exiting form Russian retail business – before stores transfer over to franchise partner two stores with low efficiency were closed. However at the end of 2016 the portfolio of franchise partners increased: at the beginning of October Baltika signed a franchise agreement with Serbian enterprise Victoria Elegans d.o.o., who in March 2017 opened the first Baltika's brands representing store Monton AndMore in Novi Sad, Serbia. Monton AndMore is a Baltika's new store concept to increase international sales and where in addition to Monton other Baltika's brands are represented as well. At the end of the year there were 33 franchise stores, forming 26% of total stores portfolio.

Photos: Baltman store in Ülemiste Shopping Center

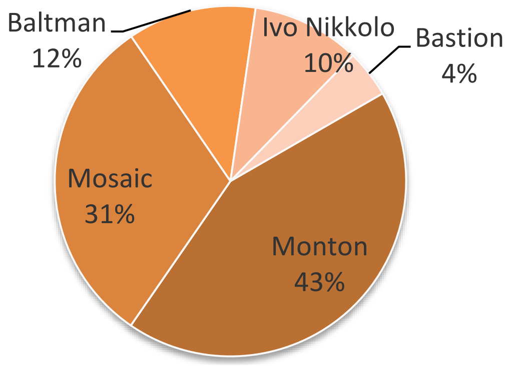
Baltika's retail network by market and brand, 31 December 2016

	Estonia	Lithuania	Latvia	Total	+/- vs 2015
Monton	9	8	6	23	0
Mixed brands	4	3	3	10	1
Mosaic	11	9	4	24	-1
Baltman	5	6	3	14	2
Ivo Nikkolo	6	3	4	13	0
Bastion	7	0	2	9	1
Blue Inc	0	0	0	0	-4
Outlet	2	0	0	2	1
Total	**44**	**29**	**22**	**95**	**0**
m^2	7,707	5,570	3,883	17,161	115

OVERVIEW OF BRANDS

In 2016 Monton brand with 45% and Mosaic brand with 31% had a largest share of Baltika Group's total revenue. Monton share of revenue increased by 4 percentage points. In retail Monton, Baltman and Ivo Nikkolo have increased their share of revenue. If in recent years Mosaic have had the largest share of wholesale and franchise revenue then in this year Monton, whose sales formed 59% of wholesale and franchise revenue, has taken the leading position in this channel as well. E-store revenue is divided more equally among brands. Monton has the largest share – 33%, followed by Mosiac with 27%. In the third place is Ivo Nikkolo brand, which deserves to be recognized, with the share of 22% of e-store sales i.e. one percentage point more than on previous year.

Breakdown of retail sales by brand – 2016



Monton

In 2016, Monton's total sales revenue amounted to 20.9 million euros, having grown 5.4% i.e. 1.1 million in a year.

Baltika's most successful and youthful brand, Monton, is represented in stores in its home market in the Baltic region: Estonia, Latvia and Lithuania, and, via a network of franchise partners, in Russia, Ukraine, Belarus and Spain. In 2016, a new Monton concept store was opened in Tartu in May, and new franchise stores in Ukraine in Kiev in July and in Zaporogie in August.

Since the beginning of 2016, Monton has strengthened its presence in one of the most well-known and oldest high-street fashion stores in Europe, Peek & Cloppenburg. While the 2016 spring-summer collection was sold in three Peek & Cloppenburg stores in Germany, since November the number of stores selling the women's collection has risen to 25 – in Germany, Austria, Czech Republic, Bulgaria, Poland, Croatia, Hungary and Romania. Monton's collections also continue to be represented at five Finnish department stores. International success has been ensured by the unique design signature, reliable quality and good fit of the collections.

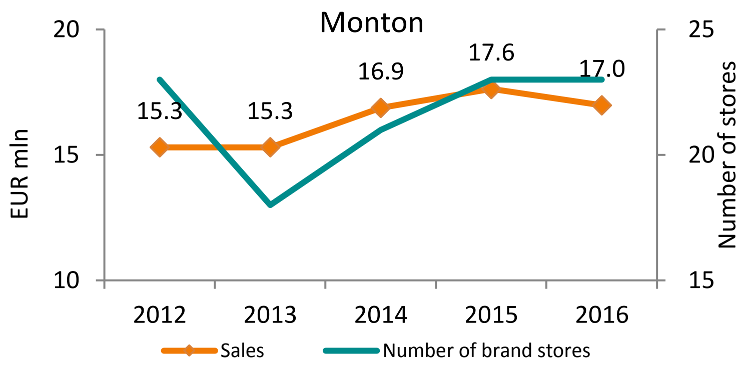
The share of wholesale and franchise sales made up 17% of Monton's 2016 sales revenue, i.e. 3.5 million euros, having increased by 1.7 million euros in a year.

The majority of Monton's sales revenue – 81% or 17 million euros – came from retail sales, which decreased by 4% in a year. In 2016, the sales of the women's collection was not as successful as expected, dropping 6%, but the strong men's collection ensured a 2% growth. Monton's biggest retail market is Estonia.

Photos: Estonian Olympic sportsmen wearing Olympic uniforms by Monton

In April 2016, Monton presented a special collection dedicated to the Rio Olympic Games. The collection intertwined elements inspired by the sea into one integral whole with chic cuts and high-quality fabrics. The Rio collection was Baltika's most successful dedicated Olympic Games collection in terms of both sales revenue and profit. The collection earned praise from Estonian athletes, Monton's retail, wholesale and e-shop customers, and international journalists. Monton has been an official supporter of the Olympic athletes for 12 years and Estonian athletes have therefore worn collections designed by Monton in Athens, Turin, Beijing, Vancouver, London, Sochi and Rio.

Monton retail sales



Revenue from continued operations

Mosaic

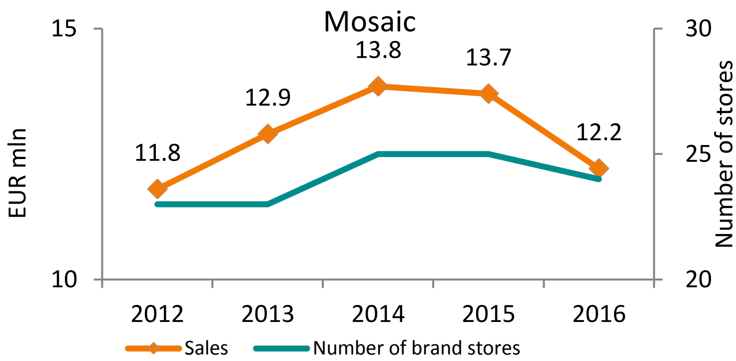
In 2016 Mosaic's sales revenue amounted to 14.4 million euros, having decreased by 10% i.e. 1.6 million euros in a year, mainly in retail and wholesale markets. Sales grew in the e-shop by 6% over the year. Tightening competition posed various challenges to Mosaic in 2016.

In Baltika Group's retail network, the Mosaic collection is represented in 24 concept stores in the Baltic countries. In addition, Mosaic is represented as a franchise store in Ukraine and Russia and in various wholesale channels: Stockmann department stores in Estonia, Latvia and Russia, and Aleksi 13 department stores in Finland. Estonia is still the biggest market for the Mosaic brand.

Mosaic's role in the Baltika Group's brand portfolio is to offer classic and practical everyday fashion for women and men. Carefully chosen tones, fabrics and details are in line with the latest fashion trends, while the timelessly elegant cuts make the clothes easy to combine with both the existing wardrobe and the collections of future seasons. The precise and representative look is complemented to perfection by the good fit of the clothes. For this reason, Mosaic continues to invest in a large selection of sizes and a good fit, so that every customer can find beautiful, elegant and well-fitting clothes regardless of body type and height.

2016 was an important year for Mosaic, as the brand celebrated its 10^{th} birthday. The anniversary year included various marketing activities, mainly in the first half of the year.

Mosaic retail sales



Revenue from continued operations

Baltman

In 2016, Baltman's total sales revenue amounted to 5 million euros, having decreased by 7% or 0.3 million euros in a year. The drop mainly came from wholesale and, to a smaller degree, retail sales. At the same time, sales in the e-shop grew 50% over the year.

There are 14 Baltman concept stores in Baltika Group's retail network, located in Estonia, Latvia and Lithuania. In addition, Baltman is sold in the men's department 'Meestemaailm' at Tallinna Kaubamaja. Estonia continues to be Baltman's biggest market.

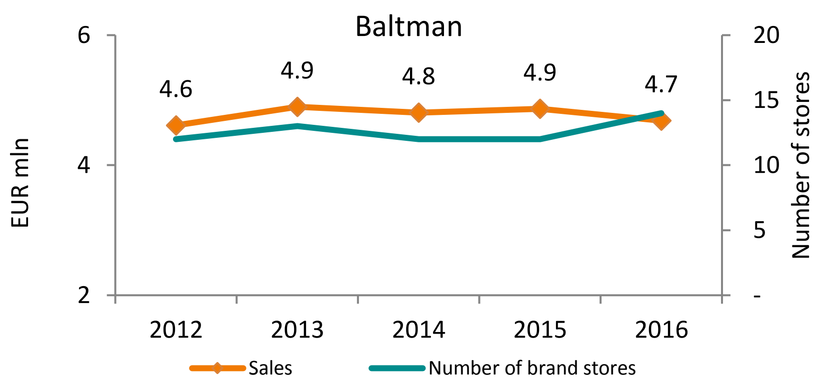
Baltman is a prestigious lifestyle brand for men, offering stylish and classic high-quality clothing, personal service and a comfortable shopping environment. Baltman is also the oldest brand of the Baltika Group – it was created in 1991 and celebrated its 25th birthday in 2016.

In celebration of Baltman's 25th anniversary, the brand's head designer Antonio created the autumn collection 'Born Fearless', which was presented at Tallinn Fashion Week. The way of thinking that inspired the 'Born Fearless' collection has in the past 25 years been characteristic of both the entrepreneurs who cast the foundation for the Estonian, Latvian and Lithuanian economy and Baltman's product development, as today's innovative materials in business clothes do not fear creases, mobile radiation or even heavy rain.

The use of premium-quality fabrics is an important cornerstone in creating the Baltman collections. Baltman cooperates with fabric producers of long-standing history and production experience from all over the world. Baltman suits, for instance, are made of fabrics made by Loro Piana, Dormeuil and Marzotto Tessuti. All Baltman suits are manufactured in Estonia, at Baltika Group's production enterprise Baltika Tailor.

One of the great successes in 2016 was the opening of Baltman's new representative shop in the former Blue Inc. store at Ülemiste Shopping Centre. The new shop was launched successfully and has exceeded expectations.

Baltman retail sales



Revenue from continued operations

Ivo Nikkolo

The total sales revenue of the Ivo Nikkolo brand amounted to EUR 4.4 million in 2016, having decreased by 6% over the year. The decrease was evident in retail sales as well as the wholesale and franchise channel. On the other hand, the Ivo Nikkolo brand has been successful in e-sales and is in third place by sales volume among the Baltika brands.

The Ivo Nikkolo brand is represented in 13 concept stores, all located in Baltika's own retail network in the Baltic region. The newest store, opened in 2016, is at the Tasku Centre in Tartu.

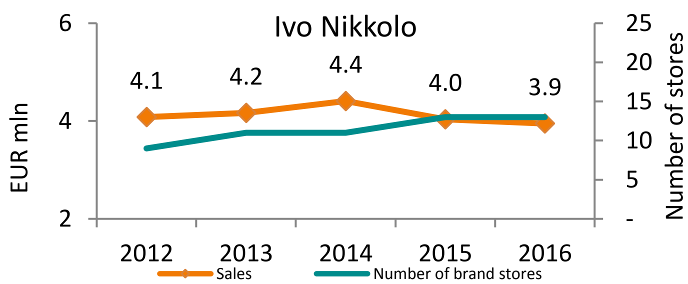
The Ivo Nikkolo collection is renowned and appreciated thanks to its original and recognisable design signature as well as for the use of high-quality and innovative fabrics. No less importance can be placed on the high fabric quality requirements of the fans of the Ivo Nikkolo brand. Ivo Nikkolo's customers are independent, value distinguished and appreciate the original design, which is playful and often includes surprising details. In 2016, a new team of designers started work at Ivo Nikkolo – Britta Laumets and Margot Vaaderpass.

Under-supply played a big role in the decrease in sales revenue in 2016, particularly in outerwear. The customers' need for warm down jackets and coats was higher than the supply. At the same time, the second quarter was successful for the brand, with linen products becoming a real hit and the sales of dresses rising to the desired level.

At the Riga Fashion Week at the end of October, Ivo Nikkolo presented its spring-summer collection for this year – 'Body lines', inspired by the female body. The success of the fashion show was measurable by various news items created by the media as well as by posts spreading in social media. A showroom for the local and international media, bloggers and stylists visiting the Fashion Week was also opened at the Galleria Riga shopping centre in the heart of Riga.

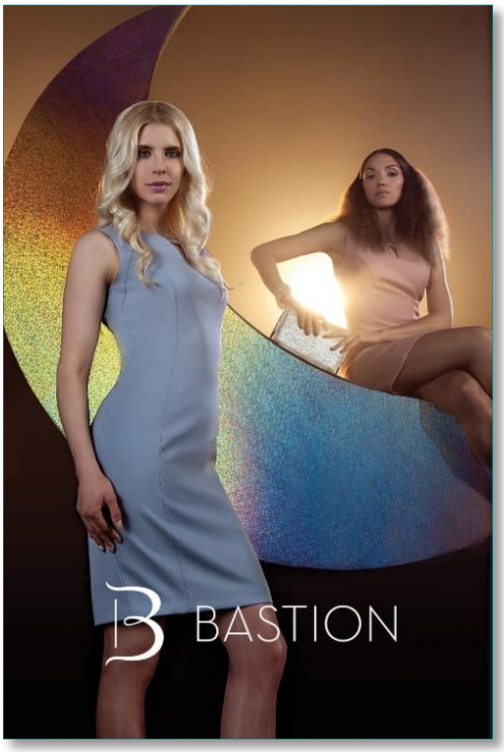
In addition, Ivo Nikkolo took part in a fashion week held in Washington at the end of September along with the best of Estonian fashion design – 22 Estonian fashion and design brands were represented. The 2016 autumn-winter collection was also presented at the Design Night held in Tallinn. The brand's aspiration to bring timeless classics and distinguished urbanism brought to the stage exclusive models, which stemmed from the principle 'less, but of higher value'.

Ivo Nikkolo retail sales



Revenue from continued operations

Bastion



The total sales revenue of the Bastion brand amounted to 2 million euros in 2016, having decreased by 6% in a year. Bastion is still the least represented and lowest volume brand in Baltika's brand portfolio.

As of the end of 2016, there were 9 Bastion concept stores, 7 in Estonia and 2 in Latvia. In the Baltic region, the Bastion brand was also represented in a multi-brand store in Lithuania. In 2016, a new store was opened at the Origo Centre in Riga and the Bastion store at Domina received a conceptual upgrade.

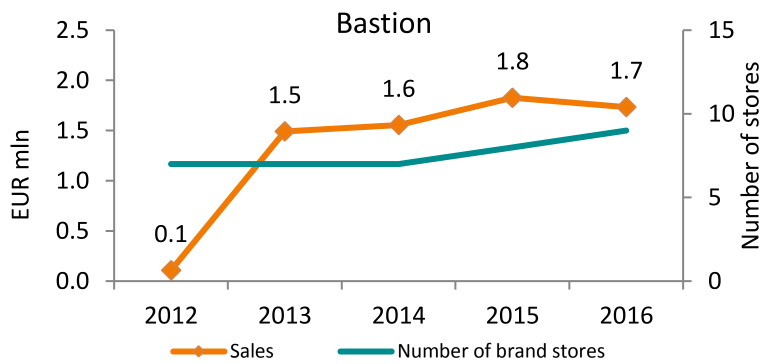
The signature of the Bastion collection continues along feminine lines, offering its customers clothing for every occasion. Quite a few products are wearable 8+5 hours – suitable for both the office and a party or other important event afterwards. Attention is also paid to the comfort of the wearer; for this reason, the collection mainly uses stretchy hosiery fabrics.

The main problems in 2016 were the following: a weak spring collection and under-supply, particularly in jackets, skirts and trousers, where purchase volumes had been intentionally cut, as well as inefficient additional premises due to which the growth of sales fell short of the growth in premises.

For the promotion faces of the 2016 autumn-winter campaign, Bastion chose members of the Estonian girl band La La Ladies, who by their essence and stage attitude represent the same values as Bastion, being extremely feminine, enchanting and celebrating every moment in life. One of the most well-known Estonian fashion bloggers Kristjaana Mere stepped in as a Lookbook model. Through such ventures, the brand salutes the beauty of Estonian women.

The special year-end collection was born in cooperation with Moët & Chandon. The collection was inspired by champagne bubbles and intended to make women feel like the true queen of a party – the bright, dazzling and shimmering fabrics would not go unnoticed in any room.

Bastion retail sales



Revenue from continued operations

WHOLESALE AND FRANCHISE

The objective for 2016 was to increase wholesale and franchise sales in existing markets, find new franchise partner and increase sales through international department stores chain Peek & Cloppenburg.

Sales objective set at the beginning of the year turned out to be rather challenging, especially due to the economic situation in Eastern-Europe markets and rouble volatility. Russian rouble related markets were in constant decline and the buyers' willingness and capability to purchase was low. Thus at the beginning of the year additional objective was set – to maintain existing clients and not to lose the market share in CIS countries. As at the end of the year the number of franchise stores in CIS countries was 30. During 2016 two new Monton stores were opened in Ukrainian market: one in Kiev and the other one in Zaporogie and one low profit store was closed. The number of Russian franchise stores has increased due to Russian retail market transition over to franchise partner: at the beginning of the year 8 of former retail stores were transitioned over franchise partner. However the other franchise partner closed one of the low efficiency stores in Moscow.

Wholesale and franchise revenue in 2016 was 6 million euros, increasing by 1 million euros i.e. 21% compared to last year. Increase in volume is mainly attributable to Russian retail market's transition over to franchise partner and increased wholesale to Peek & Cloppenburg department stores chain. As at the end of the year Monton collection was sold in 25 Peek & Cloppenburg department stores in Europe i.e. within a year the number of Monton selling department stores have increased by 22.

In addition to wholesale enlargement Baltika's franchise partners portfolio has increased as well. At the beginning of the October Baltika signed a franchise agreement with Serbian enterprise Victoria Elegans d.o.o., who opened Baltika's brands representing store Monton AndMore in Novi Sad Serbia on 8th of March 2017. Monton AndMore is a Baltika's new store concept to increase international sales and where in addition to Monton other Baltika's brands are represented as well. Serbian Monton AndMore store will initially sell Monton, Mosaic and Bastion collections. At the end of the year there were 33 franchise stores, forming 26% of total stores portfolio.

If in previous years Mosaic has had the largest volume of wholesale and franchise sales then in 2016 due to Russian retail sales transition over to franchise sales and due to successful cooperation with Peek & Cloppenburg department stores Monton has taken the leading position in wholesale and franchise sales. Monton share of wholesale and franchise sales was 59%.

The objective for 2017 is to grow with Peek & Cloppenburg chain in Europe department stores, successfully activate Serbian market with new multibrand concept and find 1 new franchise partner.

E-STORE SALES

In 2016 the growth of e-store Andmorefashion.com, that covers all five of Baltika's brands, was continually fast. E-store has an important role also in retail by supporting Baltika's brands stores as a way of pre-shopping. Over the year 1,200,000 customers from more than 70 countries visited Andmorefashion.com website. E-store was mostly visited by women (87% from visitors) in ages from 25 to 34 (37% from visitors).

Over the year improvements to e-store functionality and speed were made, one new delivery system was added in a form of DPD courier, and changes in e-store photo-language were made. Also from July 2016 Monton and Mosaic products are available in Amazon.de website, which is visited by more than 30 million visitors in a month.

In a year total e-store revenue was 1.1 million euros (increase of 9% compared to 2015), from which Monton products formed 33%, 27% Mosaic, 22% Ivo Nikkolo, 13% Bastion and 5% Baltman. Most popular product departments were cardigans and dresses, of which 6,300 and 5,200 pieces were sold respectively.

E-store is able to supply in total 44 countries. In 2016 17,211 orders were made in e-store and delivered to 35 different countries. Baltic countries formed a largest portion of sales: Estonia 56%, Latvia 16%, Lithuania 14%. 3% of sales formed Russia and 5% Finland.

In 2017 the objective is to widen the Click&Collect service to other markets and thereby continually increase integration of e-store and stores. Also the objective is to improve e-store logistics process to offer clients faster service and improve user experience on different devices.

OPERTAING EXPENSES AND PROFIT

Baltika's gross profit margin in 2016 was 50%, which is 2.7 percentage points improvement compared to previous year (2015: 47.3%). The gross profit margin has improved due to better purchasing price and lower mark down, thus margin has increased in all sales channels. Company's gross profit was 23.5 million euros i.e. 0.4 million euros more than the comparative result from last year.

Distribution expense decreased 3% i.e. 0.7 million euros compared to last year and were 20.3 million euros. Distribution expense in head-office have decreased 6% i.e. 0.4 million euros compared to last year and in Baltics retail market costs have decreased 2% i.e. 0.3 million euros. General and administrative expense were 2.5 million euros, decreasing 4% compared to last year. In 2016 distribution and general expense ratio to revenue was 48.6% (2015: 48.4%). Despite the decrease in costs the expense ratio has increased 0.2 percentage points. Increase in ratio is due to decrease in revenue. The operating profit was 0.7 million euros, which is 1 million euros better result than previous year comparative result.

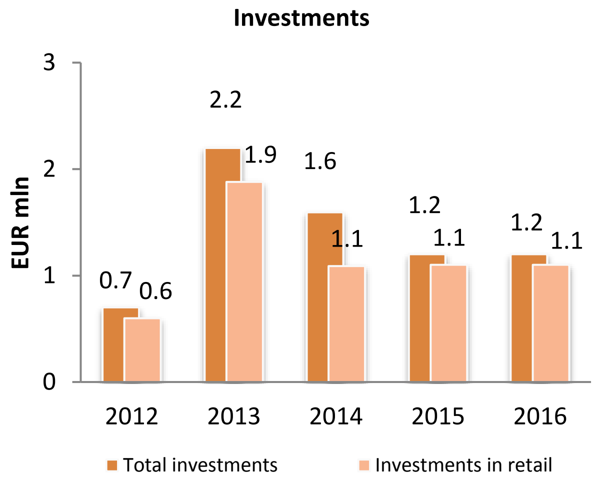
The net financial expenses in 2016 stayed on last year's level and were 0.5 million euros, which makes Baltika Group's 2016 net profit 0.2 million euros. Comparative result from last year is a loss in amount 0.8 million euros and the result with discontinued operations is a net loss 6.4 million euros.

FINANCIAL POSITION

As at 31 December 2016, Baltika Group inventories totalled 11.1 million euros, increasing 0.7 million euros compared to last year-end. Goods and goods purchased for resale inventories have increased by 3% i.e. 0.3 million euros and fabrics and accessories inventories have increased by 6% i.e. 0.1 million euros. Compared to last year the prepayments to suppliers have increased 22% i.e. 0.1 million euros.

As at 31 December 2016 Group's trades receivable were 2 million euros, which is 0.3 million euros more than at the end of last year. Trades receivable have mainly increased due to increase in wholesale and franchise sales, where there are longer payment periods.

As at 31 December 2016 the property, plant and equipment and intangible assets cost value was 4.7 million euros (31.12.2015: 4.8 million euros). Investments into material and immaterial assets were 1.2 million euros. The property, plant and equipment and intangible assets depreciation and amortization was 1.3 million euros (2015: 1.2 million euros).



As at 31 December 2016 borrowings amounted 7.0 million euros, which signifies together with the usage of overdraft facility increase of 0.7 million euros compared to the last year-end (31 December 2015: 6.3 million euros). At the end of July Baltika received investment loan in amount of 2 million euros, from which 1.5 million euros was taken into use in the third quarter, this is one of the main reasons behind the increase of borrowings.

As at 31 December 2016 Group's net debt (interest-bearing liabilities less cash and cash equivalents) was 6.6 million euros, which is 0.7 million euros more than at the end of last year. The net debt to equity ratio was 133% as at 31 December 2016 (31 December 2015: 123%). The deterioration of the ratio is driven by the increase in borrowings (loan taken at the end of July).

As at 31 December 2016 total equity attributable to equity holders of the parent was 5.0 million euros (31 December 2015: 4.8 million).

CASH FLOWS

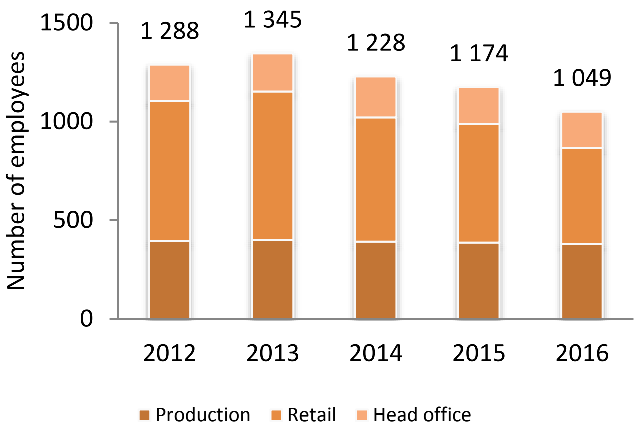
In 2016 company's cash flow from operating activities was 0.5 million euros, decreasing 1.8 million euros compared to last year. Decrease is mainly attributable to investments into working capital: increased inventory and trade receivables and decreased trade payables, resulting in cash outflow in amount of 1.2 million euros. Input to the investment activities i.e. purchase of property, plant and equipment and intangible assets were made in amount of 1.2 million euros. Bank loan repayments were made in amount of 0.8 million euros (2015: 1.0 million euros) and in third quarter investment loan in amount of 1.5 million euros was taken into use. Group cash flow amounted 0.02 million euros (2015: -0.3 million euros), which resulted in cash balance in amount of 0.4 million euros as at the end of the year.

PEOPLE

As at 31 December 2016 Baltika Group employed 1,049 people that is 125 people less than as at 31 December 2015 (1,174): 487 (31.12.2015: 601, among who 79 are Russian retail market employees) in the retail system, 380 (31.12.2015: 387) in manufacturing and 182 (31.12.2015: 186) at the head office and logistics centre. The 2016 twelve months' average number of staff in Group was 1,073 (12 months 2015 with Russian retail market staff: 1,210). The proportion of staff employed outside Estonia was 27%, i.e. 282 people (2015: 33%, 390). 2015 number of employees includes Russian market (discontinued operations) retail staff – 79 people as at 31.12.2015.

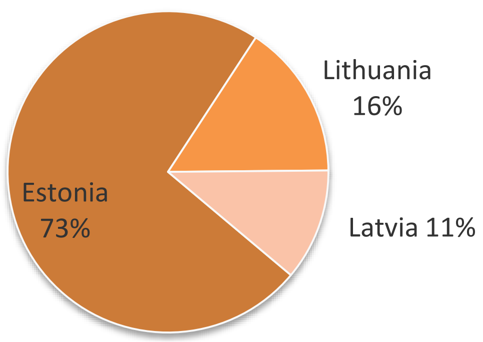
Baltika Group continued operations employees' remuneration expense in twelve months amounted to 10.5 million euros (2015: 10.8 million euros). The accrued remuneration of the member of the Supervisory Board and Management Board totalled 0.3 million euros (2015: 0.2 million euros).

Number of employees*



* Number of employees is presented including discontinued operations

Breakdown of personnel by country at 31 December 2016

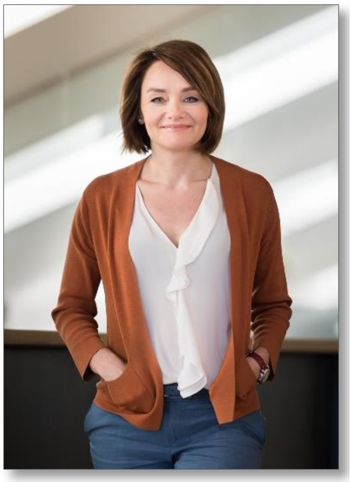


Starting from 1st of February 2016 Maigi Pärnik-Pernik continues to fulfil the tasks of Management Board member. On 30th of January 2015 the Supervisory Board of AS Baltika decided to suspend Maigi Pärnik-Pernik Management Board contract for the duration of her maternity leave and appointed Meelis Milder as the Management Board member responsible for the finance function and for the disclosure of information on the exchange. From 1st of February 2016 Management Board member responsible for the finance function and for the disclosure of information on the exchange is again Maigi Pärnik-Pernik.

On 14th of March 2016 Lilian Nõlvak started working as a communication manager of AS Baltika. Previously Lilian worked as PR manager in Elion Ettevõtted AS (now known as Telia Eesti AS).

Supervisory Board of AS Baltika decided to recall from the Management Board starting from 17th of March 2016 Management Board member Kati Kusmin.

From 2nd of May 2016 Kristel Sooaru started working as Sales and Marketing Director. Kristel has previously occupied different management positions at Baltika for 19 years, last position was the head of menswear collections and before that she was the head of Baltman brand. Before returning to Baltika Kristel was the purchase manager of TKM King, which is the holding company of Tallinna Kaubamaja Group's footwear trade store chains ABC King and SHU.



Maigi Pärnik-Pernik

Lilian Nõlvak

Kristel Sooaru

OUTLOOK AND OBJECTIVES FOR 2017

Economic environment

In the economic environment, the current situation can generally be expected to continue. Political risks in the world economy remain great: the impact of Brexit and the US president Donald Trump, the upcoming elections in Europe, geopolitical tensions and other such factors mean the continuation of uncertainty. At the same time, the economies of our neighbouring countries as well as Europe and the USA have held strong, and the majority of analysts expect the stable economic growth to continue in 2017.

Expectations for 2017 are similar for Estonia, Latvia and Lithuania: economic growth will be around 2-3%, mainly supported by an increase in public sector investments. The acceleration of Estonia's economic growth is also boosted by Estonia's presidency of the European Union. The increase in prices is estimated to accelerate sharply in 2017, mainly due to an increase in the price of raw materials. The price increase combined with a certain deceleration in the nominal growth of salaries should have an adverse effect on the growth of consumption.

The aforementioned events may have an important effect on the future activities and financial standing of Baltika Group, but the extent of their possible impact is still hard to forecast. The future economic situation and the effect thereof on the activities of Baltika Group may differ from the management's expectations.

Baltika Group

Baltika is growing from a vertical retail business into an international brand house that is aimed at ensuring a high-quality customer experience through all its different sales channels. Baltika's largest business segment by sales volumes, profit and integral customer experience management is its retail business in the Baltic countries where competition has tightened considerably in recent years. The majority of strong European clothes brands have entered the market, which has created a situation where the customers' expectations for the originality of products and the price and quality ratio have sharply increased.

One of the essential objectives in 2017 is still to maintain and increase sales volumes and profitability in the Baltic retail market through offering customers a better shopping experience. For that purpose, certain product development and retail business operation principles have been changed. More attention is paid to the original design signature and a larger proportion of high-quality products made in the factories of Estonia or nearby Lithuania. Active and well-targeted communication with loyal customers via the AndMore customer programme, as well as the development of Andmorefashion.com e-shop possibilities for improving the dissemination of information to customers (preliminary product selection), well-planned and managed outsourcing – which allows the brand to work with a smaller permanent stock and lower discounts – and the further development of the concept of multi-brand stores under the AndMore branding (Monton AndMore, etc.).

Besides the profitable Baltic segment, Baltika places great importance on developing and increasing sales in the wholesale, franchise and e-commerce area, which has strong sales potential. The branded and domestically profitable retail concepts have given Baltika the chance to develop a new sales direction for new markets – franchise. The first franchise agreements with foreign partners were concluded in 2013 in Belarus, followed by agreements in Tenerife, Spain, in 2014-2015, and the first Monton AndMore store was opened in March 2017 in Novi Sadi, Serbia. Together with the changes in the Ukrainian and Russian operating model, i.e. the exit from the retail market and transfer to the franchise model, Baltika had 33 franchise shops as at the end of the year. Baltika aims to improve and develop the franchise model further and actively seek new partners in new markets.

Also in wholesale the objective is to increase sales to existing partners and find new partners and markets. E-store constant development continues as well.

The Management board has divided the objectives into three groups:

- Successful company: increase profitability and improving gross profit and operating expense ratio;
- Content customer: increase in all sales channels through offering better customer experience;
- Motivated employee: to increase profitability it is important to maintain employees' motivation and dedication.

No major investments are planned for 2017, regular amounts will be invested into own retail network.

BALTMAN
monton
MOSAIC
Ivo Nikkolo
BASTION

SOCIAL RESPONSIBILITY REPORT

The foundation of the activities of Baltika Group are transparent. The Group regards social responsibility and environmental impact management as being important in its everyday activity. More detailed coverage of the natural environment (production, supply, material and resource handling) and social aspects (employees, human rights, transparent management) related to the Group's activities confirm its will to make an increasing substantive contribution in those areas.

Baltika contributes to the development of socially important areas through various projects. The environmental parameter has been integrated into the Group's management system and the everyday work of individual units is organised in as environmentally friendly manner as possible.

The Company cares for its employees and has established the valuation of employees as a strategically important subject. Baltika Group aims to ensure that the entire supply chain observes the social and environmental principles and requirements established by Baltika.

EMPLOYEES

Baltika Group is an international organisation that supports diversity, different cultures and nationalities.

As at 31 December 2016, Baltika employed 1,049 people, which is 125 people fewer than on 31 December 2015 (1,174). In total, 487 people worked in retail (31 December 2015: 601), 380 in production (31 December 2015: 387) and 182 at the headquarters and the logistics centre (31 December 2015: 186).

The personnel of Baltika Group in 2016:

- 4.9% men and 95.1% women;
- 39 years is the average age in Baltika Group, 50 years in the production units;
- The average length of service in Baltika Group is 9.1 years. The employees of the production units have the greatest length of service – 18 on the average. The employees of the Latvia retail organisation have the shortest average length of service – 5.1 years;
- People of 10 different nationalities work at Baltika's headquarters.

Photo: "People of Baltika" different team members from design to sales, August 2017

2016 Consolidated Annual Report (in thousands of euros)

Table 1. Baltika Group's personnel by units

	Personnel 31 Dec 2016	%	Men (%)	Women (%)	Start working during 2016	Left during 2016
Baltika AS	182	17.4%	2.6%	14.7%	44	42
Baltika Tailor OÜ	380	36.2%	1.0%	35.2%	45	55
Retail	487	46.4%	1.3%	45.2%	341	371
Estonia	205	19.5%	0.6%	19.0%	114	116
Latvia	164	15.6%	0.3%	15.3%	113	129
Lithuania	118	11.2%	0.4%	10.9%	114	126
BALTIKA GROUP	**1,049**	**100%**	**4.9%**	**95.1%**	**430**	**468**

Table 2. Baltika Group's personnel by markets

	Personnel 31 Dec 2016	%	Men (%)	Women (%)	Start working during 2016	Left during 2016
Estonia	767	73.1%	4.2%	68.9%	203	213
Lithuania	164	15.6%	0.3%	15.3%	113	129
Latvia	118	11.3%	0.4%	10.9%	114	126
BALTIKA GROUP	**1,049**	**100%**	**4.9%**	**95.1%**	**430**	**468**

Baltika Group considers employee satisfaction and motivation as well as the image of the employer to be important areas. In 2016, the company took rigorous steps to place the management of people into an even more central focus of Baltika Group. For example the process of renewal of the corporate values and developing the employees' value proposition was started, in addition Baltika Group focuses on aspects required for the creation of a developing and satisfying working environment.

Baltika Group's personnel rules and principles are stated in the rules of procedure that determine the mutual obligations and rights of the employee and the employer, the procedure for recruitment and remuneration, occupational health and safety issues, holidays, maintenance of trade secrets and the principles of prevention of conflicts of interest and corruption. Regulations implementing the rules of procedure have been established in all the Group entities.

In addition, several processes important from the viewpoint of employee development and motivation were reviewed in 2016 – for instance, the new employee inception programme, training and development need principles, recruitment and selection procedure and performance pay principles. Baltika Group has clear remuneration principles that apply to all the units.

Risks and risk management

Baltika Group has mapped employee-related risks in all the markets and taken those risks into account in the development of its strategic directions of activity. The latter is focused on risks related to the recruitment and training of employees, the improvement of motivation and satisfaction, and the strengthening of the Baltika Group brand as an employer. In 2017, the objective is to create an activity plan for strengthening the image as an employer, to map the labour market in all the retail markets and to plan activities that would facilitate finding and maintaining employees (e.g. the development of the working environment inside the organisation via offering more flexible working hours).

Occupational health and safety

Due to the specific nature of the production and retail trade areas, occupational health and safety risks are very important for the company. Baltika acknowledges and takes those risks into consideration in its everyday activities, as evidenced by the small number of work accidents.

Every Baltika unit has specialists who are responsible for matters related to occupational health and safety. Their task is to introduce all new employees to the relevant processes and guidelines and to plan changes in the area of occupational health and safety.

- **In 2016 there were 4 industrial accidents registered in Baltika Group. There were no fatal accidents.**

Involvement and development of employees

Baltika Group supports gathering open feedback and values the diversity of opinions. In addition to communication supporting working environment and active e-mail communication, there are organized employee satisfaction surveys with open-ended answers, regular development interviews, developed an intranet newsroom with commenting option etc.

Baltika values its people and places great importance on the training and development of employees. In 2016, the company launched the Fashion Academy training programme in the course of which employees learnt about retail trade management and holding negotiations as well as the general economic and management areas. The employee exchange projects Shop Day and Office Day also continued in 2016, with employees from the headquarters working in stores and experiencing the everyday store activities, and vice versa. Twice a year, before the release of a new collection, the retail employees of all Baltika's three home markets (Estonia, Latvia, Lithuania) receive thorough training related to the new collection. Baltika Group maps training and development needs once a year.

- **In 2016 75% of Baltika Group's employees took part from training and development activities (incl. new collection introduction).**



Photos: Head Office and Lithuanian Market cooperation during Model Store Project: redrawing store plans

In addition to improving professional skills, Baltika Group pays special attention to increasing the health awareness of its employees. In 2016 the Estonian unit of Baltika Group held a Health Week, which will be expanded to cover the entire Group in 2017. The Health Week included various events aimed at increasing the health awareness of employees.

How does Baltika Group care for its employees?

- Remembers long-standing employees and recognises them at corporate events;

- recognises employees who are successful in their work, good team players and creators and maintainers of a positive internal environment (annual recognition of the Employees of the Year);
- places importance on time spent together outside of work and organises fun joint events for its employees;
- considers it important to involve employees in organising and carrying out various events, e.g. organising fashion shows at the beginning of seasons and participating in such shows as models;
- in anniversary years, Baltika organises a great joint get-together for its former long-standing employees.
- Baltika Group encourages employees' studies and growth by giving out scholarships to Baltika's employees, who are continuing their professional studies. The aim of the scholarship is to support Baltika's employees' skills and knowledge improvement, which in turn adds value to company, helps company to achieve its business goals and gives employees an opportunity to educate themselves.

The introduction of a feedback system among employees was one of the most important activities in 2016. In 2016 employee satisfaction survey was organized with a aim to involve employees in the new corporate value process and to take today's feedback into account in making strategic corporate decisions.

In total, a third of the employees of the Group responded to the survey. The survey covered activities related to reputation and working environment, the management of the company and its units as well as satisfaction with those activities. The survey results showed that the employees' awareness of their work-related goals was rated the highest (5.2 to 5.4 out of 6). It is also worth noting that the employees are of the opinion that attention is paid in their unit to customer satisfaction (5.1 to 5.3 out of 6). The company will conduct similar surveys every other year, which means that the next survey will be held in 2018.

CUSTOMER EXPERIENCE MANAGMENT

A satisfied customer is one of Baltika's objectives. One of the main topics in 2016 was the development of an integral view to customer experience in all the sales channels (retail organisations, franchise stores, wholesale partners, e-shop). In 2016, the focus was more on retail organisations, with the following major activities and changes:

- Service standards were upgraded;
- the company updated the AndMore loyal customer bonus programme and linked participation in the programme with the ID card for improved data security (in Estonia);
- security is considered very important in gathering and storing customer data in Baltika Group. As at the end of 2016, more than 450,000 customers had joined the AndMore customer programme. Procedures have been established for gathering and storing data in accordance with legal acts, customer data are stored in a physical external server to which only relevant employees and developers have access.
- Baltika analysed the role and value of customer experience for the company and made preparations for launching a customer experience management programme in 2017. That includes the creation of a customer experience process, the development of indicators and the introduction of the necessary technical developments.

In Baltika Group, the following regulations control sales activities aimed at retail customers, the store operating practices and customer communications:

- Customer communication and marketing and advertising activities are based on the internal activity guidelines agreed in the Group. In addition, Baltika also complies with all the norms established by law in its home markets.
- Retail Operations Manual. The document contains complete information about the company, brands,

customer programme, customer communication and customer service standards, customer complaint handling procedure, consumer protection, work safety, products and product handling and display, retail trade indicators, employee motivation systems, etc. The document is updated every year. A similar manual has also been developed for Baltika Group's franchise partners. The aim of the manual is to ensure that the customer experience in stores operating under the Baltika brand is the same as in Baltika's own retail stores.

- In 2016, the company created a new cooperation format, Retail Council, which includes the heads of Baltika Group's three retail markets, the Group's Marketing and Sales Director, and the Group's Chief Executive Officer. The objective of the Retail Council is to increase the efficiency of retail trade processes and thereby improve the efficiency of work organisation and customer satisfaction.

During 2016 Baltika Group did not conduct a customer satisfaction survey that covers full customer base, however almost every year there is a smaller survey among the sections of loyal customers (around 500 - 2,000 respondenta). In 2016 the focus was on Ivo Nikkolo and Monton brand: sample covered all the retail markets and different age groups and feedback covered information about customers' buying behaviour as well as about product price, quality, fit etc.

Everyday feedback on products and collections given by customers regarding Baltika's customer service personnel reaches the headquarter of Baltika Group via regular reports. Customers can also provide feedback via Customer Support e-mail or Customer Support hotline – those channels give us valuable feedback on both products and the service level in Baltika stores.

The customer complaints process (including returns and replacements) is in the retail frontline competence. In 2016, customer complaints were received in all the retail markets. A separate process and information system has been created for product quality related feedback from customers, through which information is gathered from the customers of retail organisations and forwarded to the quality department of Baltika Group. The history of complaints forwarded by e-mail and telephone is recorded automatically. Complaints are solved in the company on a case-specific basis. If complaints become more frequent in an area, this is pointed out to the head of the relevant area.

- **In 2016 there were no violation of marketing ethics, also no registered violation in consumer protection.**

HUMAN RIGHTS

Baltika Group is dedicated to ensuring that the conduct of all the parts of the production and supply chain is ethical and responsible. In its work, Baltika Group complies with the International Labour Organisation's convention on the basis of which the Ethical Trading Initiative used in Baltika Group has been prepared.

In its processes, Baltika Group observes the Supplier Manual, which describes how to ensure proper working conditions and the protection of all human rights for all employees throughout the supply chain. Thus, the Supplier Manual stipulates how to ensure safe and hygienic working conditions, fair pay and holidays and other such aspects for the employees.

In order to ensure compliance with human rights, Baltika's employees conduct audits among the existing and potential new suppliers at least once every year, checking, among other things, that no child labour is used, work is paid for, working conditions are humane, work safety is ensured, etc.

- **In 2016, while evaluating potential suppliers in Bangladesh, Baltika Group decided relinquish cooperation with three production companies because they did not fulfil all the necessary requirements regarding employees safety.**

Audits are also conducted at the Estonian production unit of Baltika Group. As uniform requirements must apply to all producers, the ones established in Estonian production also set a standard for cooperation partners.

- **In 2016 there weren't any environmental, working environment, human rights or fair trade violations registered in Baltika Group's production or supply chain.**

COMMUNITY ACTIVITIES AND SPONSORSHIP

Community activities of Baltika Group

In order to support a positive image and achieve the common goals of Baltika Group, the company has for years engaged in the development of the fashion and clothes industry and the creative industry community. Baltika Group supports the fashion design department of the Estonian Academy of Arts and the areas of specialisation related to the clothes industry at the Tallinn University of Applied Sciences, supporting the education of young fashion design students with a monetary grant under a cooperation agreement and involving students in various high-level training courses offered to the employees of the Baltika Group. In addition, the chief specialists and department heads of Baltika Group gave lectures and conducted training events for the students of the Estonian Academy of Arts, and engaged students in the creation of collections. Baltika Group and the Estonian Academy of Arts, the Tallinn Industrial Education Centre, the Tallinn University of Applied Sciences and Tallinn University of Technology have established a well-functioning practice placement system in the framework of which design and clothes industry students can obtain practical knowledge at Baltika Group. In addition, all the students of clothes design and technology areas in Estonia are taken on excursions to Baltika Group's production and logistics units as well as to the headquarters in order to give the students a good overview of the functioning of a clothes industry enterprise.

Baltika Group is also involved in activities related to supporting and developing the creative industry business. To this end, the members of Baltika Group's management belong to the management board of the Estonian Service Industry Association, the supervisory board of the Estonian Design Centre, the management board of the Estonian Fashion Brands Association, the Estonian Clothing and Textile Association and the management board of the Estonian Traders' Association, working in those professional associations and non-profit organisations outside their everyday work to promote the creative and clothes industry in Estonia.

With regard to sponsorship, charity and community activities, Baltika Group relies on Baltika's values and sponsorship principles. Baltika Group strives to be a responsibly operating member of society and contribute towards preserving/developing the heritage of Estonian fashion design and clothes industry as well as towards encouraging design approaches.

Areas that we support:

- Development of the fashion design and clothing industry areas;
- Design and clothing industry education;
- Encouraging the creative industry.

Baltika Group therefore supported various activities in 2016 to inspire and recognise a new generation of fashion designers. Those fashion events included Fashion Plane, the ERKI Fashion Show of the Estonian Academy of Arts, the MPT Fashion show of the Tartu Art College, the fashion show 'Pink Scissors' of Rocca Al Mare School, etc.

In addition, Baltika Group was a major supporter of the Estonian Design Awards in 2016, and it presented its own special award for the designer/design brand with the highest export capability – Estonian fashion artist Roberta Einer who resides in London. The award also included the opportunity to substantively cooperate with Baltika Group for the purposes of design export.

Sponsorship on Baltika Group's retail markets

Monton

Monton has been sponsoring the Estonian Olympic Committee since 2004, during which time the designers at Monton have created ceremonial outfits for the Estonian Olympic athletes. The athletes have worn collections designed especially for the Olympic Games in Athens, Turin, Beijing, Vancouver, London, as well as in Sochi.

The special collection created for the 2016 Rio Olympic Games tells the story of Estonians as a sea-loving nation. Estonia is a maritime country and for us, the sea means history, work, food, culture, education, traditions and beliefs. In one way or another, the sea is a part of every Estonian's life, and its power and beauty, unpredictability and force are keywords that also describe the world of sports. The summery, comfortable and trendy clothes adorned the athletes of the Estonian Olympics delegation in Rio Summer Olympics, and all sports enthusiasts had the opportunity to cheer for their favourite athletes while being dressed in the same clothes. These clothes are also perfectly suitable for everyday wear.

The Rio special collection by Monton became highly popular among athletes as well as people in Estonia.

Photo: Baltika Group employees showing their support to Estonian athletes on the opening day of Rio Olympic Games in front of the Baltika headquarter

In addition to long-term collaboration with the Estonian Olympic Committee, Monton has also been supporting Estonia's most successful student company for several years now. In 2016, this company was Spoony that produces edible spoon-shaped sweets. By today, the young entrepreneurs' success has grown to such extent that their products are sold in Estonia and abroad in a number of retail chains as well as cafés.

In Lithuania, Monton's collaboration with the Lithuanian Beach Volleyball Federation is going strong – the Lithuanian retail organisation sponsored the beach volleyball player Ieva Dumbauskaitė, who represents Lithuania in both national and international competitions. As part of the sponsorship, the company helps to set up new beach volleyball courts in order to popularize sports among not only professional athletes but also ordinary people interested in a healthy lifestyle. With the company's support, new beach volleyball courts were set up at the main beach in the city of Klaipeda.

Photo: Hurdler Jaak-Heinrich Jagor and long jumper Ksenja Balta in Monton Rio collection show

Baltman

Baltman has been creating world class business attire in the Baltic States for a quarter of a century. The brand's aim is to recognize and praise fearless people in Estonia, Latvia and Lithuania – people whose courage to initiate change, sense of responsibility and entrepreneurial spirit have moved our life forward.

For example, in 2016 Baltman sponsored the winner of Eesti Laul, the Estonian national selection for the Eurovision Song Contest, Jüri Pootsman, and the Estonian delegation's visit to the final competition of the Eurovision Song Contest.

On its 25th birthday, Baltman also specially recognised 13 fearless socially active people, business men and creative minds, and one country. During the formal birthday reception at Tallinn Creative Hub, three of them received recognition: head of the Estonian Anti-Doping Agency Kristjan Port, photographer Herkki Erich Merila and singer Tanel Padar. The same fearless way of thinking, which characterises Baltman's product development team as well as its founders, has been characteristic of many Estonian entrepreneurs and public figures who have helped to lay the country's foundation during the past 25 years, and who received Baltman's recognition and the "Dragonfly" badge at that night as a symbol of their courage. With this gesture, Baltman wished to give recognition to people whose courage to initiate things, sense of responsibility and entrepreneurial spirit have moved our life in Estonia forward in the past 25 years. Born fearless – this includes all great minds who could serve as role models or a source of inspiration for all of us with their actions, ideas and decisions.

Photo: Head of Baltman brand Kaja Milder hands over "Fearless" recognition to singer Tanel Padar

In Latvia, Baltman primarily supports the country's most influential fields of sport, which greatly impact the society and inspire youth – bobsledding, ice hockey, basketball and football. In 2016 the company began collaboration with Kaspars Daugaviņš, captain of the Latvian national ice hockey team, to support his dedication, work ethic and passion for ice hockey. In addition, Baltman sponsored the entire Latvian national ice hockey team by providing them with high-quality formal suits, including the team's management as well as every player on the field. Furthermore, Baltman supports the Latvian national symphony orchestra by providing the 100-member orchestra with Baltman dress coats. The Latvian national symphony orchestra was founded in 1926, and its 100-member team of top musicians is held in high regard within the country as well as abroad – with their 250 performances per year they brilliantly represent Latvia and the entire Baltic region.

Photo: Captain of Latvian hockey association Kaspars Daugaviņš wearing Baltman suit

In Lithuania, in 2016 Baltman continued to support Lithuania's most successful basketball club Kaunas Žalgiris, whose coaches are wearing Baltman Travel suits this season. These suits truly correspond to their wearers' needs – the garments are made from nano-processed fabrics, which makes the Estonian-made suits liquid proof and crease free but also comfortable, as they need no care during the intense competition period.

Photo: Kaunas Žalgiris head coach Šarūnas Jasikevičius

Mosaic

In Estonia, just before the Mothers' Day, Mosaic in collaboration with the news portal Delfi supported mothers who are not able to afford a sophisticated outfit in their everyday lives. A set of items from the Mosaic collection, stylised by the head designer of Mosaic women's collection Merle Lõhmus, was given as a gift to five hardworking mothers.

In Latvia, in 2016 Mosaic supported the annual Latvian teachers' conference, awarding four Latvia's best teachers with valuable gifts.

Photo: Latvian teachers' conference, The teacher of the year with a Mosaic gift certificate

Ivo Nikkolo

Ivo Nikkolo is a brand that supports and motivates young talented artists. During the Riga Fashion Week, Ivo Nikkolo presented the young talented artist Triin Kukk's jewellery collection "Knot Lines" next to the brand's own collection, with the aim of helping the young talented artist to showcase her creative output on the international arena. Triin Kukk's jewellery collection was also brought to the limelight in the showroom event during the Riga Fashion Week, where Ivo Nikkolo designers introduced the designer's work to Latvian fashion and art journalists.

In addition, in 2016 Ivo Nikkolo supported the local Latvian artists' project "Meet Art", which temporarily transformed the Ivo Nikkolo brand stores in Riga into an exhibition hall and thereby brought young artists' creations closer to people. The talented Latvian ceramicist Andris Vēzis's works were also displayed in the brand stores as part of the project.

Photo: Ivo Nikkolo autumn/summer 2017 collection show in Riga Fashion Week, where a jewellery collection of young and talented jewellery designer Triin Kuke was included

MANAGEMENT OF ENVIRONMENTAL IMPACTS

General management of environmental aspects

Baltika Group pays attention to environmental impacts related to the fashion industry and production (e.g. use of resources, chemicals and waste) in supply chain management, in the head office, as well as in the Estonian production units in Tallinn and at Ahtme in Ida-Viru County. Environmental impact management is also directed by our European retail and wholesale trade partners, who have established strict requirements for the quality and environmental aspects related to the products.

For Baltika, the management of environmental impacts, transparency and traceability are the cornerstones of the supply chain. As a result, one of the primary documents regulating collaboration between Baltika Group and its suppliers is the Supplier Manual. This document sets out the principles of ethical and responsible procurement, establishing requirements for quality, environmental issues as well as labour aspects related to the issue of ethics. The development and annual updating of the Supplier Manual involves the management board and all departments in Baltika Group.

The main environment-related aspects regulated by the Supplier Manual are as follows:

- Waste reduction and environmentally-friendly waste management
- Optimisation of the use of energy and natural resources by suppliers
- Consideration of air, noise and smell levels in production units
- Reduction of the use of chemicals and consideration of international, national and sector-based practices
- Reduction of the use of water and environmentally-friendly management of wastewater

In 2016, Tallinn University of Technology, who is an important cooperation partner for Baltika Group, helped to update the Supplier Manual. The project included updating the part that defines requirements for products, chemicals and quality, and these requirements in turn are based on conditions set out by the EU with regard to chemicals used in textile products. In 2017 the collaboration project concentrates on implementing the updated Supplier Manual in the entire supply chain.

PRODUCTION AND SUPPLY CHAIN MANAGEMENT

Baltika regards it as the company's mission to maintain the heritage of the Estonian clothing industry and contribute to its development. Approximately 45% of Baltika's production takes place in Estonia, thus ensuring complete transparency of half of the supply chain. Local production is a growing trend in the world's fashion industry, because in addition to the flexibility and speed of production, it also enables to directly manage social and environmental impacts. The rest of production takes place in the Far East, Turkey and Europe (Latvia, Lithuania, Italy).

Photo: Baltika production and logistics cemters in Tallinn, Estonia

Baltika is demanding when it comes to suppliers – the company values accountability, personal feedback, strategic and long-term cooperation. In order to ensure responsible production, employees at Baltika conduct audits at least once a year among all existing and potential new cooperation partners. The company has created detailed questionnaires for evaluating the partner's conformity. For example, it enquires about the management of liquid waste and wastewater, and whether the management of other production waste is arranged in a secure and accountable manner. In addition to the audit carried out by Baltika, many partners have implemented environment management systems and/or quality certificates (e.g. Oekotex).

Today, Baltika has 15 manufacturers in Asia, and cooperation with most of them has lasted for years. For example, cooperation with the company Li&Fung started back in 2007, and at the same time Baltika began collaboration with the company on developing the Supplier Manual.

PRODUCTS AND QUALITY

The quality of products is very important for Baltika. A high-quality garment has a longer life span and allows for re-use, which is a crucial environmental factor in the clothes industry. Baltika has a separate quality department, and the company has developed a thorough quality control process. For example, a part of this process is test-wearing of the products to analyse their fit and durability. Quality control is performed on new fabrics as well as products arriving at stores. Thus, the amount of defective products is measured at three levels:

1. At Baltika warehouse by the quality department.
2. At Baltika stores by employees (defects sustained during transport or handling in the store).
3. Amount returned by clients.

Baltika Group is constantly working towards ensuring that clients find their clothes a great fit and of high quality. Therefore, the company has established specific indicators to measure the level of quality, and the amount of defective products.

One of such quality indicators is, for example, the percentage of customer returns out of the retails sales volume – this figure should remain below 0.2%. In 2015 and in 2016 the figure remained within given range. The amount of returns in the e-channel is higher, as products cannot be tried on before making the purchase, reaching 14.6% in 2016. With the help of a number of enhancement projects, including technical development of visual images in the e-store Andmorefashion.com, the same figure was successfully brought down to 13% in 2016. Considering the specific nature of e-stores, where customers cannot try on the products before making the purchase, this figure is at an expected level.

The choice of fabrics for clothes collections is made primarily based on the price, appearance and functionality of the product. There is currently no specific strategy for using environmentally-friendly materials in collections; however, the group has created specific collections with the aim of educating the consumers and guiding them towards making environmentally-friendlier choices. In creating clothes collections, the focus is also on ensuring that the products are safe for the wearers' health, and therefore AZO tests are performed to analyse chemical composition of the products.

Eco-innovative solutions used by the group include usage of digital prints, which saves water and reduces pollution. With premium brands, the group has tested a number of innovative fabrics and solutions. For instance, Baltman uses a specific radiation proof fabric in order to reduce the negative impact of mobile phones carried in the breast pocket.

Since materials of animal origin are also used in collections, the Supplier Manual regulates the issue of treatment of animals. The main principles are:

- cruel treatment of animals is forbidden;
- skin must not be removed from a live animal;
- feathers must not be plucked from live birds;
- wool or fur is sheared, not plucked from a live animal together with skin;
- no products must be sourced from endangered species.

USE OF MATERIALS AND RESOURCES

Baltika Group values managing environmental impacts and is guided by the sustainable manners in its activities.

Baltika Group follows a sustainable way of thinking and recycling trends in developing its store concepts and setting up stores. Therefore, reuse of different materials and furniture items carries an important role in retail concepts. Technical and lighting solutions are designed following the principle of energy efficiency. In this area, the group cooperates with industry leaders and includes their expertise in new developments.

Baltika Group uses a considerable amount of old furniture in developing store concepts and creating store environments, and contributes to its renovation and restoration. Several stores feature pieces of furniture found in a poor state and then restored, for example turning machines and chairs from the 19th century Estonian households and soft furniture from the 20th century, which has been used in creating new store concepts and through that given a new life and function.

To reduce negative environmental impact during the stores renovation and choosing materials before the renovation of each store, a renovation audit is conducted. During the audit the investment needs in new furniture and technical equipment are determined, also, an inventory is conducted to determine the opportunities for using existing technical equipment or furniture.

A sustainable mindset is also maintained in the areas of product transport and choice of packaging materials for client purchases. For example:

- Baltika Group does not usually purchase transport packages itself, but reuses packing cases brought to the company by suppliers instead. For suppliers, the guidelines regarding packages are described in the Supplier Manual;
- Cardboard packages are returned to the central warehouse from Baltika Group stores, where they are reused for packaging and transporting products. Film materials used for product transport are collected and utilised by department stores;
- Products purchased by clients are packaged in both paper and plastic bags. In 2016, two out of five brands used paper bags. The goal in 2017 is to start using recycled paper bags in the stores of the Monton brand, which is the largest brand in the group;
- To reduce negative environmental impact from marketing materials the goal in 2017 is to introduce a change in large advertising campaigns and switch from plastic materials to digital solutions.

In addition to furniture and package material reuse the efficient usage of stock excess and existing materials is important as well. Thus, Group has a precise material computation and overview of inventories: when possible, the usage of existing materials is preferred to purchasing new fabrics and the group also actively cooperates with small enterprises, schools, kindergartens and craftsmen to ensure that textile waste and surplus clothes are efficiently re-used. For example:

- Surplus ready-made clothes (final remaining items of collections) are donated;
- Clothes produced by Baltika Group and returned by customers to the Fashion Street are donated to young Estonian designers who will reprocess them;
- Fabric samples are distributed to art schools and kindergartens.

CORRUPTION

In Baltika Group, the topic of corruption is regulated by Baltika Group's Rules of Procedure. The Rules of Procedure regulate areas such as misuse of internal information, the concept of insiders and obligations extended to them, questions related to maintaining and managing business, service and production secrets.

- **In 2016 there were no registered corruption cases, fair trade or ethics or any other similar violation in Baltika Group.**

BALTIKA SHARE

Baltika's share has been listed on the Nasdaq Tallinn Stock Exchange since 5 June 1997. Nasdaq Tallinn Stock Exchange is a member of the world's largest exchange company NASDAQ. NASDAQ was established at the beginning of 2008 when NASDAQ Stock Market completed its merger with the Baltic and Nordic exchange company OMX. Stock Exchange Company delivers trading, exchange technology and public company services in 50 countries and to over 3,500 companies.

Baltika's share does not have an official market maker. The rules enforced in 2005 require newly listed companies to sign a relevant agreement for a certain period. For shares that have been listed for a longer time, it has not been necessary to enter into or extend such agreements

SHARES

AS Baltika has 40,794,850 ordinary shares. Nominal value of share is 0.2 euros per share and no changes to nominal value per share took place in 2016.

Ordinary shares

Baltika's ordinary shares are listed on the NASDAQ Tallinn Stock Exchange and carry equal voting and dividend rights. In the text below (the key share data, share price and trading figures, shareholder structure), any reference to AS Baltika's "share" or "shares" is a reference to ordinary shares unless indicated otherwise.

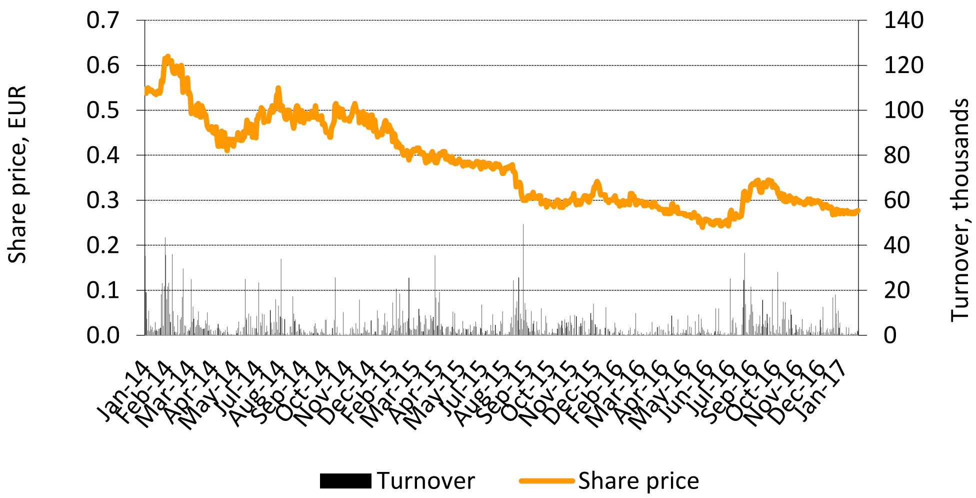
Information on listed ordinary shares

NASDAQ symbol: BLT1T
ISIN number: EE3100003609
Minimum number of shares to trade: 1
Number of shares: 40,794,850
Nominal value of a share: 0.2 euros
Votes per share: 1

SHARE PRICE AND TRADING

In 2016 the price of the Baltika share decreased by 17% to 0.283 euros, the Group's year-end market capitalisation was 11.5 million euros. During the same period, the OMX Tallinn All-Share Index increased by 20%.

Share price and turnover



Share trading history

EUR	2012	2013	2014	2015	2016
High	0.65	0.95	0.63	0.49	0.35
Low	0.28	0.52	0.41	0.29	0.24
Average	0.43	0.74	0.49	0.36	0.29
Year-end price	0.57	0.55	0.46	0.34	0.28
Change, %	91%	-5%	-16%	-26%	-18%
Traded volume	4,067,574	4,569,595	2,249,732	3,153,469	2,580,854
Turnover, in millions	1.75	3.38	1.16	1.12	0.77

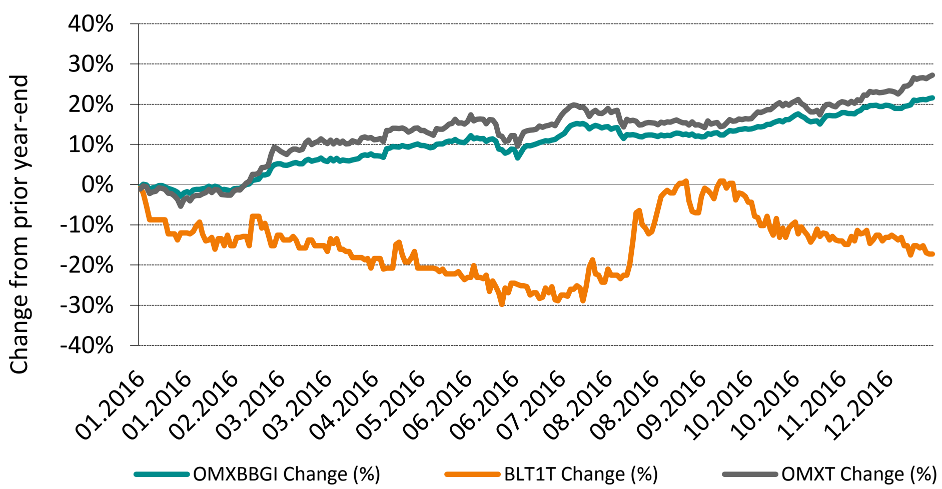
INDICES

The Nordic and Baltic exchanges of NASDAQ use the same index structure. The NASDAQ OMX Baltic index family comprises the All Share Index, the Tradable Index, the Benchmark Index, and sector indices. The indices are calculated in euros as price (PI) and/or gross (GI) indices. All indices are chain-linked, meaning that they are calculated based on the price level of the previous trading day. All Baltic equity indices, except sector indices, have a base value of 100 and a base date of 31 December 1999. The sector indices have base value of 1000 and base date of 30 June 2011. The base date for OMX Tallinn is 3 June 1996.

As of March 2017 Baltika share was part of the following all share indexes:

Index	Description	Type	Short name
OMX Tallinn GI	OMX Tallinn all share index	Gross index	OMXT
OMX Baltic GI	Baltic all share index	Gross index	OMXBGI

Yearly changes of Baltika share and gross indexes



SHAREHOLDER STRUCTURE

At the end of 2016, AS Baltika had 1,755 shareholders. The number of shareholders decreased over the year by 3%.

The largest shareholder of AS Baltika is KJK Fund Sicav-SIF (shares on ING Luxembourg S.A. account), which owned 30.86% of ordinary shares as at the end of 2016. The full list of shareholders is available on the website of the Estonian Central Securities Depository (www.e-register.ee).

2016 Consolidated Annual Report (in thousands of euros)

Largest shareholders as at 31 December 2016

	Number of shares	Holding
ING Luxembourg S.A. client	12,590,914	30.86%
Clearstream Banking Luxembourg S.A. clients	5,726,142	14.04%
BMIG OÜ	4,750,033	11.64%
Skandinaviska Enskilda Banken Ab clients	3,407,305	8.35%
Svenska Handelsbanken clients	1,320,000	3.24%
Meelis Milder	1,013,735	2.48%
AS Genteel	977,837	2.40%
Luksusjaht AS	900,237	2.21%
Central Securities Depository of Lithuania	750,136	1.84%
Others	9,358,511	22.94%
Total	**40,794,850**	**100%**

Largest shareholders are international investment funds and other legal entities who own approximately 81% of the shares. Individuals hold approximately 19% of the shares.

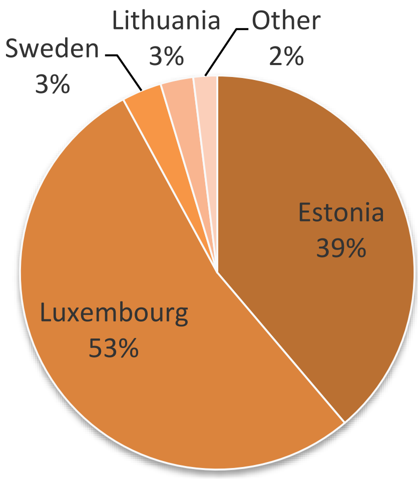
Shareholder structure by shareholder type as at 31 December 2016

	Number of shares	Holding
Management Board members, immediate family members and entities under their control	6,097,951	14.95%
Legal persons	28,241,778	69.23%
Individuals	6,455,121	15.82%
Total	**40,794,850**	**100%**

Shareholder structure by size of holding as at 31 December 2016

Holding	Number of shareholders	Percentage of shares	Number of shares	Percentage of voting rights
> 10%	3	0.17%	23,067,089	56.54%
1.0 – 10.0%	7	0.40%	8,807,753	21.60%
0.1 – 1.0%	34	1.94%	3,937,771	9.65%
< 0.1%	1,711	97.49%	4,982,237	12.21%
Total	**1,755**	**100%**	**40,794,850**	**100%**

Shareholder structure by country at 31 December 2016



2016 Consolidated Annual Report (in thousands of euros)

SHARE CAPITAL

As at 31 December 2016 Baltika had 40,794,850 shares with nominal value of 0.2 euros per share.

According to the Articles of Association, AS Baltika maximum share capital is 20 million euros.

Changes in share capital

Date	Issue type	Issue price, EUR	Number of shares issued	Total number of shares	Share capital at par value EUR '000	Share premium EUR '000
31/12/2009				**22,644,850**	**14,473**	**67**
21/06/2010	Issue of ordinary shares	0.77	8,850,000	**31,494,850**	20,129	1,131
31/12/2010				**31,494,850**	**20,129**	**1,198**
30/05/2011	Share nominal conversion to euros				1,918	-1,377
31/05/2011	Cancellation of preference shares		-4,000,000	**27,494,850**	-2,556	**0**
31/05/2011	Issue of ordinary shares		4,000,000	**31,494,850**	2,556	**0**
03/08/2011	Issue of ordinary shares	0.7	4,300,000	**35,794,850**	3,010	0
31/12/2011				**35,794,850**	**25,057**	**89**
11.05.0212	Decrease of share nominal value				-17,898	-89
31/12/2012				**35,794,850**	**7,159**	**63**
16/07/2013	Conversion of H-bonds to shares	0.3	5,000,000	**40,794,850**	1,000	496
31/12/2013				**40,794,850**	**8,159**	**684**
31/12/2014				**40,794,850**	**8,159**	**809**
31/12/2015				**40,794,850**	**8,159**	**496**
31/12/2016				**40,794,850**	**8,159**	**496**

DIVIDENDS

According to Baltika Group dividend policy no dividends will be paid until Group has a strong financial position and adequate investment ability. One indicator of strong financial position is when the capital to net gearing ratio is under 50% and availability of sufficient funds (cash and cash equivalents minus overdraft and short term borrowings is over 1% of total number of shares). In addition the actual dividend pay-out ratio will be determined based on the Group's cash flows, development prospects and funding needs.

When the aforementioned financial position is achieved, the Group will determine specific ratio what amount of profit will be paid out as dividends.

The Group ended 2016 with a consolidated net profit of 0.2 million euros. The Management Board of Baltika proposes that this year no dividends be distributed to the holders of ordinary shares. In previous year, the company did not distribute any dividends either.

For dividend history and ratios, please refer to the Key share data table.

CORPORATE GOVERNANCE REPORT

The Corporate Governance Code (CGC) of Nasdaq Tallinn Stock Exchange is a set of rules and principles, which is designed mainly for listed companies. Since the provisions of CGC are recommendations by nature, the company need not follow all of them. However, where the company does not comply, it has to provide an explanation in its corporate governance report. The "comply or explain" approach has been mandatory for listed companies since 1 January 2006.

Baltika adheres to all applicable laws and regulations. As a public company, Baltika also observes the rules of Nasdaq Tallinn Stock Exchange and the requirement to treat investors and shareholders equally. Accordingly, Baltika complies, in all material respects, with the provisions of CGC. Explanations for departures from CGC are provided below. In addition, corporate governance report contains information on the annual General Meeting taken place in 2016, the Supervisory Board, the Management Board and explains Baltika's governance structure and processes.

CGC Article 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 General Meeting took place on May 2, 2016, which was attended by Meelis Milder, Chairman of the Management Board, Maigi Pärnik-Pernik, member of the Management Board and AS Baltika's auditors Heili Uustalu and Tiit Raimla from AS PricewaterhouseCoopers. Jaakko Sakari Mikael Salmelin, Chairman of the Supervisory Board did not take part of the meeting, however Reet Saks, member of the Supervisory Board attended and led the meeting.

CGC Article 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.

Since Baltika does not have the required technical equipment that would allow secure identification of the shareholders, observation of the General Meeting and participation thereof is not possible by means of communication equipment. Since the majority of the shareholders are overseas' residents, providing secure identification of the participants would be too cost prohibitive.

CGC Article 1.3.4.

Profit distribution shall be considered in General Meeting as a separate agenda item and a separate resolution shall be passed regarding it

So far, the profit distribution decision has been approved together with the approval of the Annual Report. Starting from the next General Meeting, Baltika plans to consider the profit distribution as a separate item on the agenda.

CGC Article 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.

The remuneration and other benefits provided to members of the Management Board are set out in their employment contracts. Owing to the confidentiality of the contracts, Baltika does not disclose the remuneration and benefits provided to each member of the Management Board. However, Baltika discloses the total amount of remuneration expense to members of the Supervisory Board and Management Board in the management report section of its interim and annual reports. In 2016, the figure amounted to 0.3 million euros. The contractual severance benefits of members of the Management Board range from 3- to 18-fold monthly remuneration depending on the period of service.

Baltika's employees are eligible to performance pay, which in case of markets is based on the fulfilment of profit target of profit centres, in case of Baltika head-office employees, it is based on the fulfilment of Baltika Group profit targets. From 2016 the chairman´s and members´ of the Management Board performance pay is based on the fulfilment or exceeding of EBITDA target and can be 0-10 months monthly salary accordingly. Baltika can pay up to 50% of the expected bonus amounts in advance during the year; the final amount is calculated and paid out after the financial statements have been audited. The bonus of the chairman of the Management Board/CEO is determined by the Supervisory Board. The bonuses of members of the Management Board are determined by the chairman of the Supervisory Board based on the proposal made by the chairman of the Management Board. Baltika discloses the total amount of remuneration expense to the members of the Management Board in Note 26 of the Annual Report.

Members of the Management Board can receive one funded pension contribution of up to one month's salary per year, provided after they have worked in the director's position for at least three years. Members of the Management Board may use a company car and are eligible to other benefits provided for in the company's internal rules. Share option program that was approved on 27 April 2015 Annual General Meeting of Shareholders was issued to members of the Management Board.

CGC Article 3.2.5.

The amount of remuneration of a member of the Supervisory Board shall be published in the Corporate Governance Recommendations Report, indicating separately basic and additional payment (incl. compensation for termination of contract and other payable benefits).

Annual General Meeting of shareholders decided on 27 April 2015 the emoluments of the members of the Supervisory Board. The remuneration of the chairman of the Supervisory Board amounts to 650 euros per month and the remuneration of a member of the Supervisory Board to 400 euros per month. A member of the Supervisory Board is not eligible to severance compensation or any other monetary benefits.

CGC Article 3.3.2.

Members of the Supervisory Board shall promptly inform the Chairman of the Supervisory Board and Management Board regarding any business offer related to the business activity of the Issuer made to him, a person close to him or a person connected with him. All conflicts of interests that have arisen in preceding year shall be indicated in the Corporate Governance Recommendations Report along with their resolutions.

In 2016 nor 2015 no conflicts of interests occurred.

CGC Article 5.6.

The issuer shall disclose the dates and places of meetings with analysts, and presentations and press conferences organized for analysts, investors or institutional investors on its website. The issuer shall enable shareholders to attend the above meetings and shall make the texts of the presentations available on its website.

In accordance with the rules of the Nasdaq Tallinn Stock Exchange, Baltika first discloses all material and price sensitive information through the stock exchange system. The information disseminated at meetings and press conferences is limited to previously disclosed data. All information that has been made public, including presentations made at meetings, is available on the Group's website (www.baltikagroup.com), which lists the contacts of persons who can provide further information. Presenting a schedule of meetings on the corporate website is currently not relevant.

As a rule, the issuer cannot enable other shareholders to attend the meetings held with institutional investors and analysts. To ensure the objectivity and unbiased nature of the meetings, institutional investors observe internal rules which do not allow third parties to attend such meetings.

CGC Article 6.2.

Election of the auditor and auditing of the annual accounts

In accordance with Baltika's Articles of Association, the auditor(s) is (are) appointed by the General Meeting of shareholders for the performance of a single audit or for a specific term. The Annual General Meeting which convened on 28 April 2014, appointed AS PricewaterhouseCoopers as the auditor of the annual financial statements for 2014-2016. Independent Auditor's Report of 2016 will be signed by certified auditor in charge Tiit Raimla. The audit firm is chosen based on the received offer with the best quality-price ratio – AS Baltika ensures the auditor's independence by following rotation rules applicable to listed entities in EU.

The audit fee is fixed in an agreement which is concluded by the Management Board. In the notice of the Annual General Meeting, Baltika publishes the information required by the Commercial Code (Section 294 Subsection 4) that does not include the auditor's fee. Baltika does not disclose the auditor's fee because the disclosure of such sensitive information would impair the competitive position of the audit firm (CGC Article 6.2.1.).

Under the law, the agreement entered into by an audit firm is governed by International Standards on Auditing, the Auditors Activities Act and the risk management policies of the audit firm that do not require the auditor to submit a memorandum on the issuer's non-compliance with the Corporate Governance Code. Accordingly, the agreement signed between AS Baltika and its audit firm does not include a corresponding article and the auditor does not submit such a memorandum (CGC Article 6.2.4.).

Subsection §24^2 (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.

AS Baltika has not deemed it necessary to implement a diversity policy, as AS Baltika always considers the best interest of Baltika in the recruitment of staff and management members and therefore makes the decisions based on the education, skills and previous experience of the person on a gender neutral and non-discriminatoty basis.

GOVERNANCE PRINCIPLES AND ADDITIONAL INFORMATION

AS Baltika is a public limited company whose governing bodies are the shareholders' General Meeting, the Supervisory Board and the Management Board.

General meeting

The general meeting is Baltika's highest governing body. General meetings may be annual or extraordinary. The Annual General Meeting convenes once a year within six months after the end of the Baltika's financial year. An extraordinary General Meeting is called by the Management Board when the Baltika's net assets based on audited results have declined below the level required by the law and there is over 2 months to annual General Meeting of shareholders or when calling of a meeting is demanded by the Supervisory Board, the auditor, or shareholders whose voting power represents at least one tenth of the Baltika's share capital. A General Meeting may adopt resolutions when more than half of the votes represented by shares are present. The set of shareholders entitled to participate in a General Meeting is determined at 8 a.m. at the date of the General Meeting.

The Annual General meeting of 2016 was held on 2 May at 24 Veerenni in Tallinn, Estonia. A total of 24,375,743 shares were represented i.e. 59.75% of the voting stock. In accordance with good practise the shareholders had the possibility to ask questions in addition to Management Board members also from the auditor. The meeting approved the company's annual report, loss allocation proposal for 2015 and the amendments to the Articles of Association.

Shareholders with significant share of Baltika's ordinary shares at the end of 2016 were KJK Fund Sicav-SIF (shares on ING Luxembourg S.A. account) (30.86%), Clearstream Banking Luxembourg S.A clients (14,04%) and Meelis Milder together with his immediate family members and entities under his control (14,95%).

No shareholders have shares that grant them a right for specific control. AS Baltika is unaware of any shareholders having concluded any voting agreements.

Supervisory Board

The Supervisory Board plans the activities of AS Baltika, organises the management and supervises the activities of the Management Board. The Supervisory Board meets according to the need but not less frequently than once every three months. A meeting of the Supervisory Board has a quorum when more than half of the members participate. A resolution of the Supervisory Board is adopted when more than half of the members of the Supervisory Board who participate in the meeting vote in favour. Each member of the Supervisory Board has one vote. There were 5 meetings of the Supervisory Board and Supervisory Board members attended most of the meetings in 2016.

According to the Articles of Association, Baltika's Supervisory Board has three to seven members. The members are elected by the general meeting for a period of three years.

Annual General Meeting of shareholders on 27 April 2015 elected Supervisory Board composition: Tiina Mõis, Reet Saks, Lauri Kustaa Äimä, Jaakko Sakari Mikael Salmelin, Valdo Kalm. The Supervisory Board meeting on 13 May 2015 elected Jaakko Sakari Mikael Salmelin as the chairman of the Supervisory Board.

Jaakko Sakari Mikael Salmelin is a partner of KJK Capital Oy; he has managed various Eastern European funds focusing mainly on the Baltic and Balkan markets. Tiina Mõis is the director of the investment firm AS Genteel and a member of the councils of AS LHV Pank and AS LHV Group. Reet Saks is an attorney with Law Office Raidla Ellex, a long-term partner of Baltika. Reet Saks has been a member of Baltika's Supervisory Board since 1997. Lauri Kustaa Äimä is a managing director of Kaima Capital Oy and a chairman or member of the Supervisory Boards of several Baltic and Finnish companies and he has long-term experience in advising potential investors on matters related to investing in the companies of the Baltic countries. Valdo Kalm is the chairman of AS Tallinna Sadam Management Board and has from previous long-term work experience specialised knowledge in technology and telecommunications industry.

Two Boards members own Baltika's shares: Tiina Mõis owns 977,837 ordinary shares i.e. 2.4% of share capital through the company under her control and Lauri Kustaa Äimä 24,590 ordinary shares i.e. 0.1% as at the end of 2016.

In addition to those indicated in related party disclosure in the financial statements, Supervisory Board members did not have any investments above 5% that is a business partner of Baltika Group.

Three out of the five members of Baltika's Supervisory Board were independent. The dependent members are Reet Saks and Tiina Mõis who hasve been the members of Baltika's Supervisory Board for more than ten years.

Audit Committee

AS Baltika has an audit committee, with rules of procedure approved by Supervisory Board. The audit committee is responsible for monitoring and analysing the processing of financial information, the effectiveness of risk management and internal controls, and the external audit of the consolidated financial statements. The committee is also responsible for making recommendations in relation to the above issues to prevent or eliminate problems and inefficiencies.

The audit committee reports to the Supervisory Board and its members are appointed and removed by the Supervisory Board. The committee has two to five members whose term of office is three years. The members of the audit committee are not remunerated for serving on the committee. Baltika's audit committee is chaired by Reet Saks. Members of the committee are Tiina Mõis and Jaakko Sakari Mikael Salmelin.

In 2016 the audit committee gathered one time. The committee met in December with the representatives of the audit firm AS PricewaterhouseCoopers to obtain overview of the observations made during 2016 audit interim work.

Management Board

The Management Board is a governing body which represents and manages Baltika in its daily activities in accordance with the law and the Articles of Association. The Management Board has to act in the best economic interests of the company. The members of the Management Board elect a chairman from among themselves who organises the activities of the Management Board. Every member of the Management Board may represent the company in all legal acts.

To ensure effective and efficient risk management and internal control, the Management Board:

- analyses the risks related to its business and financial targets;
- prepares relevant internal rules and regulations;
- develops forms and instructions for the preparation of financial statements required for making management decisions;
- ensures operation of the control and reporting systems.

The Management Board does its best to ensure that the Group's parent company and all entities belonging to the Group comply with governing laws and regulations.

According to the Articles of Association, Baltika's Management Board may have two to five members who are elected by the Supervisory Board for a period of three years. The supervisory Board may also remove a member of the Management Board.

2016 Consolidated Annual Report (in thousands of euros)

Baltika's management board has two members: Chairman Meelis Milder and Maigi Pärnik-Pernik.

The Chairman of the Management Board Meelis Milder is the company's CEO, Maigi Pärnik-Pernik is the CFO.

On 30 January 2015 the Supervisory Board of AS Baltika decided to suspend Maigi Pärnik-Pernik Management Board contract for the duration of her maternity leave and appointed Meelis Milder as the Management Board member responsible for the finance function and for the disclosure of information on the exchange. From 1 February 2016 Management Board member responsible for the finance function and for the disclosure of information on the exchange is again Maigi Pärnik-Pernik.

Supervisory Board of AS Baltika decided to recall Kati Kusmin from the Management Board starting from 17 March 2016.

Management board member Meelis Milder and his immediate family member own Baltika's shares also through the holding company OÜ BMIG, which at the end of 2016 held 11.64% of Baltika's share capital. Latter member of the Management Board and his immediate family member hold 80.1% of OÜ BMIG shares. In addition, Chairman of the Management Board has individual shareholdings. Consequently, through their direct and indirect holdings, at the end of 2016 Chairman of the Management Board, his immediate family members and entities under their control owned 14.95% of AS Baltika share capital.

Management Board members did not have in addition to those indicated in related party disclosure in the financial statements any investments above 5% that is a business partner of Baltika Group.

Shareholdings of members of the Management Board at 31 December 2016

	No of shares	Holding
OÜ BMIG	4,750,033	11.64%
Meelis Milder	1,013,735	2.48%
Immediate family members of Management Board members	334,183	0.82%
Total OÜ BMIG and Management Board members	**6,097,951**	**14.95%**
Baltika share capital	**40,794,850**	**100%**

CONSOLIDATED FINANCIAL STATEMENTS

MANAGEMENT BOARD'S CONFIRMATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

The Management Board confirms the correctness and completeness of AS Baltika's 2016 consolidated financial statements as presented on pages 50 to 97.

The Management Board confirms that:

1. the accounting policies and presentation of information is in compliance with International Financial Reporting Standards as adopted by the European Union;

2. the financial statements present a true and fair view of the financial position, the results of the operations and the cash flows of the Group;

3. the Group is going concern.

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Meelis Milder
Chairman of the Management Board
22 March 2017

____
Maigi Pärnik-Pernik
Member of the Management Board
22 March 2017

2016 Consolidated Annual Report (in thousands of euros)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note	31 December 2016	31 December 2015
ASSETS			
Current assets			
Cash and cash equivalents	4	419	398
Trade and other receivables	5	1,956	1,607
Inventories	6	11,096	10,424
Total current assets		**13,471**	**12,429**
Non-current assets			
Deferred income tax asset	7	228	234
Other non-current assets	8	522	584
Property, plant and equipment	9	3,022	2,910
Intangible assets	10	1,676	1,944
Total non-current assets		**5,448**	**5,672**
TOTAL ASSETS		**18,919**	**18,101**
LIABILITIES AND EQUITY			
Current liabilities			
Borrowings	12	5,835	3,009
Trade and other payables	13,14	6,923	6,709
Total current liabilities		**12,758**	**9,718**
Non-current liabilities			
Borrowings	12	1,196	3,312
Other liabilities	13	0	283
Total non-current liabilities		**1,196**	**3,595**
TOTAL LIABILITIES		**13,954**	**13,313**
EQUITY			
Share capital at par value	15	8,159	8,159
Share premium		496	496
Reserves	15	1,182	1,182
Retained earnings		-5,049	1,310
Net profit (loss) for the period		177	-6,359
TOTAL EQUITY		**4,965**	**4,788**
TOTAL LIABILITIES AND EQUITY		**18,919**	**18,101**

The Notes presented on pages 56-97 are an integral part of these consolidated Financial Statements.

2016 Consolidated Annual Report (in thousands of euros)

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

	Note	2016	2015
Continuing operations			
Revenue	16,17	46,993	48,806
Client bonus reserve	17	23	-70
Revenue after client bonus provision		47,016	48,736
Cost of goods sold	18	-23,519	-25,660
Gross profit		**23,497**	**23,076**
Distribution costs	19	-20,336	-21,010
Administrative and general expenses	20	-2,504	-2,603
Other operating income (-expense)	22	44	242
Operating profit (loss)		**701**	**-295**
Finance costs	23	-519	-508
Profit (loss) before income tax		**182**	**-803**
Income tax expense		-5	-41
Net profit (loss) from continuing operations		**177**	**-844**
Net loss for the period from discontinued operations	28	**0**	**-5,515**
Net profit (loss) for the period		**177**	**-6,359**

Basic earnings per share from net profit (loss) for the period, EUR	25	0.00	-0.16
From continuing operations		0.00	-0.02
From discontinued operations		0.00	-0.14
Diluted earnings per share from net profit (loss) for the period, EUR	25	0.00	-0.16
From continuing operations		0.00	-0.02
From discontinued operations		0.00	-0.14

The Notes presented on pages 56-97 are an integral part of these consolidated Financial Statements.

2016 Consolidated Annual Report (in thousands of euros)

CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

	2016	2015
Net profit (loss) for the period	**177**	**-6,359**
Other comprehensive income		
Items that subsequently may be reclassified to profit or loss		
Currency translation differences	0	2,723
Other comprehensive income (loss) for the period	**0**	**2,723**
Total comprehensive profit (loss) for the period	**177**	**-3,636**
Total comprehensive income (loss) loss arises from:		
Continuing operations	177	-844
Discontinued operations	0	-2,792

The Notes presented on pages 56-97 are an integral part of these consolidated Financial Statements.

2016 Consolidated Annual Report (in thousands of euros)

CONSOLIDATED CASH FLOW STATEMENT

	Note	2016	2015
Cash flows from operating activities			
Continuing operations:			
Operating profit (-loss)		701	-295
Adjustments:			
Depreciation, amortisation and impairment of PPE and intangibles	18,19,20	1,288	1,234
Profit/loss from disposals of PPE		15	-14
Other non-monetary expenses		2	-327
Changes in working capital:			
Change in trade and other receivables	5,7,8	-293	29
Change in inventories	6	-672	2,042
Change in trade and other payables	13	-283	-19
Interest paid and other financial expenses		-305	-300
Interest received		7	0
Income tax paid		0	-12
Discontinued operations		0	-77
Net cash generated from operating activities		**460**	**2,261**
Cash flows from investing activities			
Continuing operations			
Acquisition of property, plant and equipment, intangibles	9,10	-1,207	-1,208
Proceeds from disposal of property, plant and equipment		50	6
Discontinued operations		0	-7
Net cash used in investing activities		**-1,157**	**-1,209**
Cash flows from financing activities			
Continuing operations:			
Proceeds from borrowings	12	1,500	0
Repayments of borrowings	12	-807	-985
Change in overdraft balance	12	194	-226
Repayments of finance lease	12	-145	-153
Repayment of convertible bonds	12	-24	0
Net cash generated from (used in) financing activities		**718**	**-1,364**
Total cash flows		**21**	**-312**
Cash and cash equivalents at the beginning of the period	4	398	710
Cash and cash equivalents at the end of the period	4	419	398
Net change in cash and cash equivalents		**21**	**-312**

The Notes presented on pages 56-97 are an integral part of these consolidated Financial Statements.

2016 Consolidated Annual Report (in thousands of euros)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital	Share premium	Reserves	Retained earnings	Currency translation reserve	Total
Balance as at 31 December 2014	**8,159**	**809**	**1,182**	**1,310**	**-2,723**	**8,737**
Net loss for the period	0	0	0	-6,359	0	-6,359
Other comprehensive income for the period	0	0	0	0	2,723	2,723
Total comprehensive income (loss) for the period	**0**	**0**	**0**	**-6,359**	**2,723**	**-3,636**
Equity-settled share-based transactions	0	-313	0	0	0	-313
Total transactions with owners, recognised directly in equity	**0**	**-313**	**0**	**0**	**0**	**-313**
Balance as at 31 December 2015	**8,159**	**496**	**1,182**	**-5,049**	**0**	**4,788**
Net profit for the period	0	0	0	177	0	177
Total comprehensive income for the period	**0**	**0**	**0**	**177**	**0**	**177**
Balance as at 31 December 2016	**8,159**	**496**	**1,182**	**-4,872**	**0**	**4,965**

Additional information on share capital and changes in equity is provided in Note 15.

The Notes presented on pages 56-97 are an integral part of these consolidated Financial Statements.

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PricewaterhouseCoopers, Tallinn

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 General information and summary of significant accounting policies

General information

Baltika Group, with the parent company AS Baltika, is an international fashion retailer. Baltika Group develops and operates fashion brands: Monton, Mosaic, Baltman, Bastion and Ivo Nikkolo. Baltika employs a vertically integrated business model, which means that it controls all stages of the fashion process: design, manufacturing, supply chain management, distribution/logistics, wholesale and retail. As at 31 December 2016, Group had 95 Baltika's retail-stores in three markets in the Baltics and 33 franchise partners´ stores in Spain, Ukraine, Belarus and Russia. As at 31 December 2016 Baltika Group employed 1,049 people (31 December 2015: 1,174).

The shares of AS Baltika are listed on the Nasdaq Tallinn Stock Exchange that is part of the exchange group NASDAQ. The largest and the only shareholder holding above 20% of shares (Note 15) of AS Baltika is KJK Fund Sicav-SIF (on ING Luxembourg S.A. account).

AS Baltika (the Parent company) (registration number: 10144415, address: Veerenni 24, Tallinn, Estonia) is a company registered in the Republic of Estonia and during 2016 was operating in Estonia, Latvia and Lithuania in retail markets and as a franchisor in Belarus, Spain, Ukraine and Russia.

The consolidated financial statements prepared for the financial year ended at 31 December 2016 include the consolidated financial information of the Parent company and its subsidiaries (together referred to as the Group): OY Baltinia AB, Baltika Sweden AB, OÜ Baltika Tailor, OÜ Baltika Retail, OÜ Baltman, SIA Baltika Latvija, UAB Baltika Lietuva (see Note 27 for group structure).

The Management Board of AS Baltika authorised these consolidated financial statements on 22 March 2017. Pursuant to the Commercial Code of the Republic of Estonia, the financial statements are subject to approval by the Supervisory Board of the Parent company and the Annual General Meeting of shareholders.

Discontinued operations

As of 31 December 2015 Russian retail market segment met the conditions of a disposal group as held for sale and was classified accordingly. On 22 February 2016, the Group exited Russian retail market. As Russian market represented a major line of business in Group´s activities, and its operations and cash flows were clearly distinguished from other Group´s operations and cash flows, it´s results were reported as discontinued operations. All financial statements and accompanying notes reflect information about continuing operations unless stated otherwise. See more information in Note 28.

Basis of preparation

The Group's 2016 consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS). The financial statements have been prepared under the historical cost convention. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

New International Financial Reporting Standards, amendments to published standards and interpretations by the International Financial Reporting Interpretations Committee

There are no new or revised standards or interpretations that came effective for the first time for the financial year beginning on 1 January 2016 that had a material impact to the Group.

New Accounting Pronouncements

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 2017, and which the Group has not early adopted.

IFRS 9, Financial Instruments: Classification and Measurement (effective for annual periods beginning on or after 1 January 2018). Key features of the new standard are:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity's business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets' cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.·
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
- IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a 'three stage' approach which is based on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.
- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

The Group is currently assessing the impact of the new standard on its financial statements.

IFRS 15, Revenue from Contracts with Customers (effective for annual periods beginning on or after 1 January 2018). The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed. The Group is currently assessing the impact of the new standard on its financial statements

IFRS 16, Leases (effective for annual periods beginning on or after 1 January 2019; not yet adopted by the EU). The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Group is currently assessing the impact of the new standard on its financial statements.

Disclosure Initiative - Amendments to IAS 7 (effective for annual periods beginning on or after 1 January 2017). The amended IAS 7 will require disclosure of a reconciliation of movements in liabilities arising from financing activities. The Group is currently assessing the impact of the new standard on its financial statements.

IFRIC 22 Foreign Currency Transactions and Advance Consideration (effective for annual periods beginning on or after 1 January 2018; not yet adopted by the EU). The interpretation applies where an entity either pays or receives consideration in advance for foreign currency-denominated contracts. The interpretation clarifies that the date of transaction, i.e the date when the exchange rate is determined, is the date on which the entity initially recognises the non-monetary asset or liability from advance consideration. However, the entity needs to apply judgement in determining whether the prepayment is monetary or non-monetary asset or liability based on guidance in IAS 21, IAS 32 and the Conceptual Framework. The Group is currently assessing the impact of the interpretation on its financial statements.

Principles of consolidation, accounting for business combinations and subsidiaries

Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. All subsidiaries have been consolidated in the Group's financial statements.

A subsidiary is consolidated from the date on which control is transferred to the Group and is no longer consolidated from the date on which control ceases. 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 measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

The excess of the consideration transferred, the amount of any non-controlling interest 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 profit or loss.

In the consolidated financial statements, the financial statements of the subsidiaries under the control of the Parent company are combined on a line-by-line basis. Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Group and all of its subsidiaries use uniform accounting policies consistent with the Group's policies. Where necessary, the accounting policies of the subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Investments into subsidiaries are reported at cost (less any impairment losses) in the separate primary financial statements of the Parent company.

Discontinued operations

A discontinued operation is a component of the Group that either has been disposed of, or that is classified as held for sale, and: (a) represents a separate major line of business or geographical area of operations; (b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or (c) is a subsidiary acquired exclusively with a view to resale.

A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial purposes, from the rest of the entity. The Group has disclosed the results of discontinued operation as a single amount in the statement of comprehensive income and presented the analysis of this amount in a separate note “Discontinued operations” (Note 28). The description of the facts and circumstances of the sale of the discontinued operations have been described in the same note.

Intra-Group transactions between discontinued and continuing operations are eliminated based on whether the arrangement between the continuing and discontinuing operations will continue subsequent to the disposal. The results of the discontinued operation include only those costs and revenues that will be eliminated from the Group on disposal.

Foreign currency

Functional and presentation currency

Items included in the financial statements of each of the Group’s entities are measured using the currency of the primary economic environment in which the entity operates (“the functional currency”) which is the local currency. The functional currency of the Parent company and subsidiaries located in Baltics is euro. The consolidated financial statements have been prepared in euros.

Financial statements of foreign operations

The results and financial position of the foreign subsidiaries of the Group are translated into presentation currency as follows:

- assets and liabilities are translated into euros at the closing rate at the date of the balance sheet;
- income and expenses for statement of profit and loss are translated at monthly average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions);
- all resulting exchange differences are recognised as a separate component of equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate of the balance sheet date.

When a subsidiary is partially or wholly disposed through sale, liquidation, repayment of share capital or abandonment, the exchange differences deferred in equity are reclassified to profit or loss.

Foreign currency transactions and balances

During the year, all foreign currency transactions of the Group have been translated to functional currencies based on the foreign currency exchange rates of the applicable Central Bank prevailing on the transaction date. Monetary assets and liabilities denominated in a foreign currency have been translated into functional currency based on the foreign currency exchange rates of the applicable Central Bank prevailing on the balance sheet date. Foreign exchange gains and losses, including arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition, are recognised in the statement of profit and loss as income or expenses of that period.

Gains and losses arising from trade receivables and payables denominated in foreign currencies are recognised net under “Other operating income (-expense)” (Note 22). Gains and losses arising from cash, cash equivalents and borrowings are recognised net method in “Financial Costs” (Note 23).

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand as well as bank account balances, and term deposits with original maturities of three months or less. Bank overdrafts are shown under current or non-current borrowings (depending on the nature and term of the contract) in the statement of financial position. Cash and cash equivalents are measured at amortised cost.

Financial assets

The purchases and sales of financial assets are recognised at the 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 investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership.

Depending on the purpose for which financial assets were acquired as well as management’s intentions, financial assets are classified into the following categories at initial recognition:

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

As at 31 December 2016 and 31 December 2015, the Group had no other classes of financial assets than those classified under the category of loans and receivables.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Receivables are initially recognised at fair value plus transaction costs. After initial recognition, loans and receivables are accounted for at amortised cost using the effective interest rate method. This method is used for calculating interest income on the receivable in the following periods.

When it is probable that the Group is unable to collect all amounts due according to the original terms of receivables, an allowance is set up for the impairment of these receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the allowance is the difference between the carrying amount and the recoverable amount. The recoverable amount is the expected future cash flows discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the impairment loss is recognised in the statement of profit and loss within “Other operating expenses”. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables.

Other receivables are assessed based on their collectible amounts. The collection of each receivable is assessed separately, taking into consideration all known information on the solvency of the debtor. Doubtful receivables are written down in the statement of financial position to the collectible amount. Irrecoverable receivables are derecognised.

Receivables are generally included in current assets when they are due within 12 months after the balance sheet date. Such receivables whose due date is later than 12 months after the balance sheet date are reported as non-current assets.

Inventories

Inventories are recorded on the statement of financial position at cost, consisting of the purchase costs, direct and indirect production costs and other costs incurred in bringing the inventories to their present location and condition.

Purchase costs include the purchase price, customs duties and other non-refundable taxes and direct transportation costs related to the purchase, less discounts and subsidies. The production costs of inventories include costs directly related to the units of production (such as direct materials and packing material costs, unavoidable storage costs related to work in progress, direct labour) and also a systematic allocation of fixed and variable production overheads (such as depreciation and maintenance of factory buildings and equipment, overhaul costs, and the labour cost of factory management).

The FIFO method is used to account for the cost of inventories. Inventories are measured in the statement of financial position at the lower of acquisition/production cost or net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

Property, plant and equipment

Property, plant and equipment are non-current assets used in the operating activities of the Group with a useful life of over one year. An item of property, plant and equipment is initially recognised at its acquisition cost which consists of the purchase price (including customs duties and other non-refundable taxes) and other expenditures directly related to the acquisition that are necessary for bringing the asset to its operating condition and location.

An item of property, plant and equipment is subsequently stated at cost less any accumulated depreciation and any impairment losses. Subsequent expenditure incurred for an item of property, plant and equipment is recognised as a non-current asset when it is probable that the Group will derive future economic benefits from it and its cost can be measured reliably. The cost of reconstruction carried out on leased premises is depreciated over the shorter of the useful life of the asset and the lease term. Other maintenance and repair costs are expensed when incurred.

Depreciation of other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

buildings and structures		
-rental space-related assets	5-7	years;
-buildings	60	years;
machinery and equipment	2-7	years;
other fixtures	2-10	years.

At each balance sheet date, the appropriateness of depreciation rates, methods and the residual value is assessed. When the residual value of the asset exceeds its carrying amount, the depreciation of the asset is ceased.

At each reporting date the management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, the management estimates the recoverable amount, which is determined as the higher of an asset’s fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in the statement of profit and loss within “Other operating expenses”. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset’s value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in statement of profit or loss under “Other operating income (expenses)”.

Intangible assets (excluding goodwill)

An intangible asset is initially recognised at its acquisition cost, comprising its purchase price, any directly attributable expenditure on preparing the asset for its intended use and borrowing costs that relate to assets that take a substantial period of time to get ready for use. After initial recognition, an intangible asset is carried at its acquisition cost less any accumulated amortisation and impairment losses.

Trademarks and licenses

Acquired trademarks and licenses are shown at historical cost. Trademarks and licenses have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of trademarks and licenses over their estimated useful lives (5-50 years).

Computer software

Costs associated with developing or maintaining computer software programmes are recognised as an expense as incurred. Costs that are directly associated with the development of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognised as intangible assets. Costs include the employee costs incurred as a result of developing software and an appropriate portion of relevant overheads.

Computer software development costs recognised as assets are amortised over their estimated useful lives (3-10 years).

Goodwill

Goodwill represents the excess of the consideration transferred over the fair value of the Group's share in net fair value of the net identifiable assets, liabilities and contingent liabilities of the acquire and the fair value of non-controlling interest in the acquiree. Goodwill which arose in the acquisition of a business is recognised as an intangible asset in the consolidated financial statements. The excess of the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost ("negative goodwill") is immediately recognised under "Other operating income".

At the transaction date, goodwill is recognised in the statement of financial position at its acquisition cost. Goodwill is subsequently carried at its cost less any impairment losses. Goodwill is not amortised. Goodwill is allocated to CGUs (cash generating units) for the purpose of impairment testing.

At each balance sheet date (or more frequently when an event or change in circumstances indicates that the fair value of goodwill may have become impaired), an impairment test is performed and if necessary, goodwill is written down to its recoverable value (if it is lower than its carrying amount).

Impairment of non-current assets

Intangible assets with indefinite useful lives (goodwill) are not subject to amortisation but are tested annually for impairment, by comparing their carrying amount with the recoverable amount.

Assets that are subject to amortisation and depreciation and assets with infinite useful life (land) are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If such circumstances exist, the recoverable amount is compared with the carrying amount.

An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (CGU).

Assets which were written down are reviewed on each balance sheet date to determine whether their recoverable value has arisen. The reversal of the impairment loss is recorded in the statement of profit and loss of the financial year as a reduction of the impairment losses. Impairment loss recognised for goodwill is not reversed.

Finance and operating leases

Leases, in the case, of which the lessor retains substantially all the risks and rewards of ownership, are classified as operating leases. Other leases are classified as finance leases.

The Group as the lessee

Finance leases are capitalised at the inception of the lease at the lower of the fair value of the leased property or the present value of minimum lease payments. Each lease payment is allocated between the liability and finance charges (interest expense) so as to achieve a constant rate on the finance balance outstanding. The interest element of the finance cost is charged to the statement of profit and loss over the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. Assets leased under finance leases are depreciated similarly to acquired non-current assets whereas the depreciation period is the lower of the asset's expected useful life or the duration of the lease term (when the transfer of ownership is not sufficiently certain).

Payments made under operating leases are charged to the statement of profit and loss on a straight-line basis over the lease term.

The future minimum lease payments under non-cancellable operating leases are calculated based on the non-cancellable periods of the leases taking into account the following criteria:

- should the termination of the agreement require a mutual agreement, lease payments for the three-month period are taken into consideration;
- should the termination of the agreement require an advance notice, lease payments due within the advance notice period are taken into consideration.

Transferred receivables

A factoring contract is the sale of receivables whereby depending on the type of the factoring contract the buyer has the right to sell back the transferred receivable to the seller within a certain time period (factoring with recourse) or there is no sell back right and all the risks and rewards of ownership of a receivable are transferred from the seller to the buyer (factoring without recourse).

Payables to employees

Payables to employees contain the contractual right arising from employment contracts with regard to performance-based pay which is calculated on the basis of the Group's financial results and meeting of objectives set for the employees. Performance-based pay is included in period expenses and as a liability if it is to be paid in the next financial year. In addition to the performance-based pay, this liability also includes accrued social and unemployment taxes calculated on it.

Pursuant to employment contracts and current legislation, payables to employees also include an accrued holiday pay liability at the balance sheet date. In addition to the holiday pay, this liability also includes accrued social and unemployment taxes.

Provisions and contingent liabilities

Provisions for liabilities and charges resulting from restructuring costs and legal claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

Other obligations whose settlement is not probable or the amount of accompanying expenditure of which cannot be measured with sufficient reliability, but that in certain circumstances may become obligations, are disclosed as contingent liabilities in the notes to the financial statements.

Financial liabilities

All financial liabilities (trade payables, borrowings, bonds and other current and non-current borrowings) are initially recorded at the proceeds received, net of transaction costs incurred on trade date. The amortised cost of current liabilities normally equals their nominal value; therefore current liabilities are stated in the statement of financial position in their redemption value. Non-current liabilities are initially recognised at the fair value of the consideration receivable (less transaction costs) and are subsequently measured at amortised cost using the effective interest rate method.

A financial liability is classified as current when it is due within 12 months after the balance sheet date or the Group does not have an unconditional right to defer the payment for longer than 12 months after the balance sheet date. Borrowings with a due date of 12 months or less after the balance sheet date that are refinanced into non-current borrowings after the balance sheet date but before the approval of the annual report, are classified as current. Borrowings that the lender has the right to recall due to the violation of terms specified in the contract are also classified as current liabilities.

Offsetting

Financial assets and financial liabilities are offset only when there exists a legally enforceable right and these amounts are intended to be settled simultaneously or on a net basis.

Share capital

Ordinary shares are classified in equity. The costs directly related to the issuance of shares are recognised as a reduction of the equity item “Share premium” or in case of absence of share premium as a reduction of the equity item “Retained earnings”. Preference shares are classified in equity in case they meet the definition of equity instrument or if they form a compound financial instrument which includes a component that meets the definition of equity. The costs directly related to the issuance of shares are recognised as a reduction of the equity by the equity instrument and as a reduction of the liability and equity in proportion by the compound financial instrument.

Compound financial instruments

Compound financial instruments issued by the Group can comprise of (i) convertible notes that can be converted to share capital at the option of the holder, and the number of shares to be issued does not vary with changes in their fair value and (ii) preference shares which entitle the holder a guaranteed interest and subsequent conversion of the instrument into ordinary shares. The liability component of a compound financial instrument is recognised initially at the fair value of a similar liability that does not have an equity conversion option. The equity component is recognised initially at the difference between the fair value of the compound financial instrument as a whole and the fair value of the liability component. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Other reserves

Reserves are set up in accordance with the resolution of the general meeting of shareholders and they can be used to offset losses from prior periods as well as to increase share capital. Payments shall not be made to shareholders from reserves.

Statutory reserve

In accordance with the Commercial Code, statutory reserve has been set up from annual net profit allocations. During each financial year, at least one-twentieth of the net profit should be transferred to 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.

Share-based payments

The fair value of services (work contribution) supplied by the employees to the Group in exchange for the shares is recognised as an expense in the statement of profit and loss and in share premium in equity during the vesting period (from the grant date of convertible bonds until the vesting date). The fair value of the services received is determined by reference to the fair value (market value) of equity instruments granted to the employees at the grant date. For the employee to receive the right to be able to convert the convertible bond into shares under the share-based payment agreement, there must be an existing employment relationship and therefore at each balance sheet date, the number of estimated convertible bonds expected to be vested is assessed and personnel expenses as well as share premium items are adjusted to reflect the change in the number of bonds expected to be converted. The amounts received for shares upon the conversion of a convertible bond less direct transaction costs is recognised in the items “Share capital” and “Share premium” in equity.

Revenue recognition

Revenue is recognised at the fair value of the consideration received or receivable, taking into consideration all discounts and concessions made. Revenue from the sale of goods is recognised when significant risks and rewards of ownership of the goods are transferred to the buyer and the amount of revenue and costs incurred in respect of the transaction can be measured reliably.

Retail sales

Revenue from the sale of goods is recognised at the time of selling the goods to the customer at the retail store, generally for cash or by card payment. The sales price also includes fees for card transactions recognised as distribution costs. Past experience is used to estimate and provide for sales returns at the time of sale.

Wholesale, franchise and e-commerce

Revenue from the sale of goods is recognised when the risks and returns have been passed to the customer according to delivery terms. Past experience is used to estimate and provide for sales returns at the time of sale.

Other

Revenue from the rendering of services is recorded in the accounting period in which the services are rendered. If a service is rendered over a longer period of time, revenue from the rendering of a service is recorded using the stage of completion method. Interest income is recognised when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of revenue can be measured reliably. For further information see section “Interest income and expenses”. Dividend income is recognised when the right to receive payment is established.

Revenue from the sale of goods and services is included in the statement of profit and loss on line “Revenue”.

Client bonus provision

The Group operates a client loyalty programme: customers accumulate bonus-points from purchases made, which entitle them to discounts on future purchases. The provision for bonus-points is recognized on the moment of the initial sales transaction as a reduction of revenue and by recognizing related provision in the statement of financial position using estimates for probable redemption of bonus-points. Bonus-points expire after six months from the customer´s last purchase.

Interest income and expenses

Interest income/expenses have been recognised in the statement of profit and loss for all financial instruments that are measured at amortised cost using the effective interest rate method. The effective interest rate is a method for calculating the amortised cost of a financial asset or a financial liability or the method for allocating interest income/expenses to the respective period. The effective interest rate is the rate that discounts the expected future cash receipts/payments over the expected useful life of the financial asset or the financial liability to its carrying amount. In calculating the effective interest rate, the Group assesses all contractual terms of the financial instrument but does not consider future credit losses. All contractual major service fees paid or received between the parties that are an integral part of the effective interest rate, transaction costs and other additional taxes or deductions are used in the calculation. If a financial asset or a group of similar financial assets has been written down due to impairment, interest income is calculated on them using the same interest rate as was used for discounting the future estimated cash receipts in order to determine the impairment loss.

Interest income is recognised when it is probable that the economic benefits associated with the transaction will flow to the group and the amount of income can be measured reliably. When the receipt of interest is uncertain, interest income is recognised on a cash basis. Interest income is recognised in the line “Finance income”.

Segment reporting

Business segments are components of the Group that engage in business activities from which it may earn revenues and incur expenses, for which discrete financial information is available and whose operating results are regularly reviewed by the entity’s chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance. Operating segments are reported in a manner consistent with the internal reporting provided to the Group’s chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing the performance of the operating segments, has been identified as the Management Board of the Parent company AS Baltika.

Segment results include revenues and expenses directly attributable to the segment and the relevant part that can be allocated to the particular segment either from external or internal transactions. Segment assets and liabilities include those operating assets and liabilities directly attributable to the segment or those that can be allocated to the particular segment.

Current and deferred income tax

Corporate income tax in Estonia

According to the Income Tax Act, the annual profit earned by Estonian entities is not taxed in Estonia and thus there are no temporary differences between the tax bases and carrying values of assets and liabilities and no deferred tax assets or liabilities arise. Instead of taxing the net profit, the distribution of retained earnings is subject to income tax of 20/80 of the amount paid out as dividends. The corporate income tax arising from the payment of dividends is accounted for as an expense in the period when dividends are declared, regardless of the actual payment date or the period for which dividends are paid.

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Corporate income tax in other countries

In accordance with the local income tax laws, the net profit of companies located in Latvia and Lithuania that has been adjusted for the permanent and temporary differences as stipulated by law is subject to corporate income tax.

Corporate income tax rates

	2016	2015
Latvia	15%	15%
Lithuania	15%	15%

Deferred income tax is provided using the liability method. Deferred income tax is calculated on all significant temporary differences between the tax bases of assets and liabilities and their carrying values in the consolidated balance sheet. The main temporary differences arise from depreciation and tax loss carry-forwards. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry-forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry-forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Earnings per share

Basic earnings per share are determined by dividing the net profit for the financial year by the period's weighted average number of shares outstanding. Diluted earnings per share are determined by dividing the net profit for the financial year by the weighted average number of shares taking also into consideration the number of dilutive potential shares.

NOTE 2 Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on Management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In addition to estimates, Management uses certain judgements in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include: assessment of net realizable value of inventories (Note 6, 18) and impairment testing of goodwill (Note 10).

Assessment of net realizable value of inventories (Note 6)

Upon valuation of inventories, the Management relies on its best knowledge taking into consideration historical experience, general background information and potential assumptions and conditions of future events. In determining the impairment of inventories, the sales potential as well as the net realisable value of finished goods is considered (carrying amount net of allowances of 8,545 thousand euros as at 31 December 2016 and 8,088 thousand euros as at 31 December 2015). Upon assessment of net realizable value of raw materials, their potential as a source of finished goods and generating income is considered (carrying amount net of allowances of 1,906 thousand euros as at 31 December 2016 and 1,790 thousand euros as at 31 December 2015). Upon valuation of work in progress, their stage of completion that can reliably be measured is considered (carrying amount of 78 thousand euros as at 31 December 2016 and 82 thousand euros as at 31 December 2015).

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Impairment testing of goodwill (Note 10)

The Management has performed an impairment test for goodwill that arose on the acquisition of the subsidiary SIA Baltika Latvija and the subsidiary OÜ Baltika Tailor. Goodwill of Russian activities was written off in December 2015 (Note 28). Future expected cash flows based on the budgeted sales and production volumes respectively have been taken into consideration in determining the recoverable amount of the cash generating units (CGU). The future expected cash flows have been discounted using the expected rate of return in the particular market within the similar industry. If the recoverable amount of cash generating unit is lower than its carrying amount, an impairment loss is recognised. Impairment testing of goodwill refer to Note 10.

NOTE 3 Financial risks

In its daily activities, the Group is exposed to different types of risks. Risk management is an important and integral part of the business activities of the Group. The Group's ability to identify, measure and control different risks is a key variable for the Group's profitability. The Group's management defines risk as a potential negative deviation from the expected financial results. The main risk factors are market (including currency risk, interest rate risk and price risk), credit, liquidity and operational risks. Management of the Group's Parent company considers all the risks as significant risks for the Group. The Group uses the ability to regulate retail prices, reduces expenses and if necessary restructures the Group's internal transactions to hedge certain risk exposures.

The basis for risk management for the Group are the requirements set by the Nasdaq Tallinn, the Financial Supervision Authority and other regulatory bodies, adherence to generally accepted accounting principles, as well as the company's internal regulations and risk policies. Overall risk management includes identification, measurement and control of risks. The management of the Parent company plays a major role in managing risks and approving risk procedures. The Supervisory Board of the Group's Parent company monitors the management's risk management activities.

Market risk

Foreign exchange risk

In 2016 and 2015 all sales from continuing operations were made in euros. In 2015 sales were conducted in RUB only in the discontinued Russian market. The Group's foreign exchange risk is related to purchases done and amounts owed in foreign currencies. The majority of raw materials used in production are acquired from the European Union and goods purchased for resale are acquired outside of the European Union. The main currencies used for purchases are EUR (euro) and USD (US dollar).

The Group's results are affected by the fluctuations in foreign currency rates. The changes in average foreign currency rates against the euro in the reporting period were the following:

Average rates	2016	2015
USD (US dollar)	-0,23%	24.54%

The changes in foreign currency rates against euro between balance-sheet dates were following:

Balance-sheet date rates	
USD (US dollar)	-3,18%

Foreign exchange risk arises only from trade payables (Note 13), as cash and cash equivalents (Note 4), trade receivables (Note 5), borrowings (Note 12) are in euro and thereof not open to foreign exchange risk.

If the foreign exchange rates (USD) in relation to the euro as at 31 December 2016 had been up to 7% higher (lower), the impact on the net profit for the year would have been +/-81 thousand euros (2015 up to 8% higher (lower).

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The assessment of foreign exchange rate sensitivity to the 2016 result is based on the assumptions that the reasonably possible fluctuations in USD/EUR exchange rate does not exceed +/-7%.

The assessment of foreign exchange rate sensitivity to the 2015 result is based on the assumptions that the reasonably possible fluctuations in USD/EUR does not exceed +/-8%.

Impact of the potential change in the currency exchange rates on the net profit/loss arising from the translation of monetary assets and liabilities

	Impact 2016	Impact 2015
Trade and other payables	-81	-2
Total	**-81**	**-2**

The Management monitors changes of foreign currency constantly and assesses if the changes exceed the risk tolerance determined by the Group. If feasible, foreign currencies collected are used for the settling of liabilities denominated in the same currency.

Interest rate risk

As the Group's cash and cash equivalents carry fixed interest rate and the Group has no other significant interest-carrying assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest rate risk arises mainly from current and non-current borrowings issued at floating interest rate and thus exposing the Group to cash flow interest rate risk. Interest rate risk is primarily caused by the potential fluctuations of Euribor and Eonia and the changing of the average interest rates of banks. The Group's risk margins have not changed significantly and correspond to market conditions.

Non-current borrowings in the amount of 1,196 thousand euros at 31 December 2016 and 312 thousand euros 31 December 2015 were subject to a floating 6 month interest rate based on Euribor (Note 12). There were no non-current borrowings at 31 December 2016 that were subject to a fixed interest rate (31 December 2015: 3,000 thousand euros). The Group analyses its interest rate exposure on a regular basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and alternative financing.

In 2016, the 6-month Euribor decreased from -0.041% at the beginning of the year to the year end -0.221%. In the beginning of 2017, Euribor has been continuing a small decline. Business analysts estimate that Euribor will not rise in 2017 enough to significantly affect the Group´s financial performance results.

If floating interest rates on the borrowings had been one percentage point higher in the reporting period with all other variables held constant, the post-tax profit for the year would have been 43 thousand euros (2015: 47 thousand euros post-tax profit lower) lower. If the floating interest rates had been 0.1 percentage point lower, the post-tax profit for the year would have been 4 thousand euros higher (2015: 1 thousand euros post-tax profit higher).

During the financial year and the previous financial year, the Group´s management evaluated and recognised the extent of the interest rate risk. However, the Group uses no hedging instruments to manage the risks arising from fluctuations in interest rates, as it finds the extent of the interest-rate risk to be insignificant.

Price risk

The Group is not exposed to the price risk with respect to financial instruments, as it does not hold any equity securities.

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Credit risk

Credit risk arises from cash and cash equivalents, deposits with banks and financial institutions as well as outstanding trade receivables.

Cash and cash equivalents

For banks and financial institutions, mostly independently rated parties with a minimum rating of "A" are accepted as long-term counterparties in Baltic states. For banks in Eastern Europe, other ratings were also considered acceptable.

Cash and cash equivalents at bank classified by credit rating[1]

	31 Dec 2016	31 Dec 2015
A	306	293
B	3	3
C	0	0
Total (Note 4)	**309**	**296**

[1]The credit rating applies on long-term deposits as published by Moody's Investor Service website.

Receivables

As at 31 December 2016 the maximum exposure to credit risk from trade receivables (Note 5) and other non-current assets (Note 8) amounted to 1,713 thousand euros (31 December 2015: 1,455 thousand euros) on a net basis after allowances.

Sales to retail customers are settled in cash or using major credit cards, thus no credit risk is involved except the risk arising from financial institutions selected as approved counterparties.

Liquidity risk

Liquidity risk is the potential risk that the Group has limited or insufficient financial (cash) resources to meet the obligations arising from the Group's activities. Management monitors the sufficiency of cash and cash equivalents to settle the liabilities and finance the Group's strategic goals on a regular basis using rolling cash forecasts.

To manage liquidity risks, the Group uses different financing instruments such as bank loans, overdrafts, commercial bond issues, issuance of additional shares and monitors receivables and purchase contracts. The unused limit of Group´s overdraft facilities as at 31 December 2016 was 2,380 thousand euros (31 December 2015: 2,574 thousand euros).

Financial liabilities by maturity as at 31 December 2016

		Undiscounted cash flows[1]			
	Carrying amount	1-3 months	3-12 months	1-5 years	Total
Loans (Note 12)[2]	3,685	303	2,504	1,110	3,917
Finance lease liabilities (Note 12)	346	51	151	155	357
Convertible bonds (Note 12, 15)	3,000	0	3,624	0	3,624
Trade payables (Note 13)	3,259	3,227	32	0	3,259
Other financial liabilities (Note 13)	30	30	0	0	30
Total	**10,320**	**3,611**	**6,311**	**1,265**	**11,187**

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Financial liabilities by maturity as at 31 December 2015

	Carrying amount	Undiscounted cash flows[1] 1-3 months	3-12 months	1-5 years	Total
Loans (Note 12)[2]	2,806	196	2,684	0	2,880
Finance lease liabilities (Note 12)	491	47	141	328	517
Convertible bonds (Note 12, 15)	3,024	0	24	3,624	3,648
Trade payables (Note 13)	3,640	7	3,633	0	3,640
Other financial liabilities (Note 13)	2	2	0	0	2
Total	**9,963**	**252**	**6,482**	**3,952**	**10,687**

[1]For interest bearing borrowings carrying floating interest rate based on Euribor, the last applied spot rate to loans has been used.

[2]Used overdraft facilities are shown under loans based on the contractual date of payment.

As at 31 December 2016, 89% of Group's financial liabilities will mature in the next 12-month period (31 December 2015: 63%), which is higher than last year mainly due to convertible notes of 3,000 thousand euros. The convertible notes have a maturity date of 30 July 2017; however, the Group plans to at least partly refinance the convertible notes by issuing new financial instruments e.g. commercial bonds in the next year. The Group has access to sufficient variety of sources of funding to meet the obligations arising from the Group's activities.

Operational risk

The Group's operations are mostly affected by the cyclical nature of economies in target markets and changes in competitive positions, as well as risks related to specific markets (especially non-European Union market – Russia, Ukraine, Belarus).

To manage the risks, the Group attempts to increase the flexibility of its operations: the sales volumes and the activities of competitors are also being monitored and if necessary, the Group makes adjustments in price levels, marketing activities and collections offered. In addition to central gathering and assessment of information, an important role in analysing and planning actions is played by a market organisation in each target market enabling the Group to obtain fast and direct feedback on market developments on one hand and adequately consider local conditions on the other.

Improvement of flexibility plays an important role in increasing the Group's competitiveness. Continuous efforts are being made to shorten the cycles of business processes and minimise potential deviations. This also helps to improve the relative level and structure of inventories and the fashion collections' meeting consumer expectations.

The most important operating risk arises from the Group's inability to produce collections which would meet customer expectations and the goods that cannot be sold when expected and as budgeted.

To ensure good collections, the Group employs a strong team of designers who monitor and are aware of fashion trends by using internationally acclaimed channels. Such a structure, procedures and information systems have been set up at the Group which help daily monitoring of sales and balance of inventories and using the information in subsequent activities. In order to avoid supply problems, cooperation with the world's leading procurement intermediaries as well as fabric manufacturers has been expanded.

The unavoidable risk factor in selling clothes is the weather. Collections are created and sales volumes as well as timing of sales is planned under the assumption that regular weather conditions prevail in the target markets – in case weather conditions differ significantly from normal conditions, the actual sales results may significantly differ from the budget.

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Debtors of the Group may be adversely affected by the financial and economic environment which could in turn impact their ability to repay the amounts owed. Deteriorating operating and economic conditions for customers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has properly reflected revised estimates of expected future cash flows in its impairment assessments, however management is unable to reliably estimate the effects on the Group's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and development of the Group's business in the current circumstances.

Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

Loan agreements with the banks include certain restrictions and obligations to provide information to the bank concerning payments of dividends, changes in share capital and in cases of supplementing additional capital.

Commercial Code sets requirement to equity level – the required level of equity has to be minimum 50% of share capital.

The Group monitors capital on the basis of net gearing ratio. This ratio is calculated as net debt divided by equity. Net debt is calculated as interest carrying borrowings less cash and cash equivalents.

The Group's long-term goal is to maintain the net gearing ratio under 50%. At the end of the reporting period the ratio was 133%. In the end of 2015 the ratio was 123%. The deterioration of the ratio is driven by the loss earned in 2015 due to one time write-offs related to the sale of Russian subsidiaries (Note 28) and by the increase in borrowings (loan taken and increase in usage of overdraft). The Group also monitors other ratios e.g. net debt to EBITDA and net debt to share capital. Based on the above the Group deems the capital structure to be in an acceptable range.

Net gearing ratio

	31 Dec 2016	31 Dec 2015
Total borrowings (Note 12)	7,031	6,297
Cash and cash equivalents (Note 4)	-419	-398
Net debt	6,612	5,899
Total equity	4,965	4,788
Net gearing ratio	**133%**	**123%**

Fair value

The Group estimates that the fair values of the financial assets (Notes 4-5, 8) and liabilities (Notes 12-14) denominated in the statement of financial position at amortised cost do not differ significantly from their carrying amounts presented in the Group's consolidated statement of financial position at 31 December 2016 and 31 December 2015.

The carrying amount less an impairment provision of trade receivables and payables is estimated by management to approximate their fair values as trade receivables and payables are short-term.

Most of the Group`s long-term borrowings are based on floating interest rates. Regarding to the Group's long-term borrowings that have a floating interest rate that changes along with the changes in market interest rates, the discount rates used in the discounted cash flow model are applied to calculate the fair value of borrowings. The Group's risk margins have not changed considerably and are reflecting the market conditions. Regarding to the Group´s long-term borrowings that have a fixed interest rate, the interest rate does not differ from the market rate. Based on that, the Management estimates that the fair value of long-term borrowings does not significantly differ from their carrying amounts. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

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The Group divides financial instruments into three levels depending on their revaluation:

- Level 1: Financial instruments that are valued using unadjusted price from the stock exchange or some other active regulated market.

- Level 2: Financial instruments that are evaluated by assessment methods based on monitored inputs. This level includes, for instance, financial instruments that are assessed by using prices of similar instruments in an active regulated market or financial instruments that are re-assessed by using the price on the regulated market, which have low market liquidity.

- Level 3: Financial instruments that are valued by assessment methods based on non-monitored inputs.

See more information about the carrying values of borrowings and about interest rates in Note 12.

NOTE 4 Cash and cash equivalents

	31 Dec 2016	31 Dec 2015
Cash at hand	110	102
Cash at bank and overnight deposits	309	296
Total	**419**	**398**

All cash and cash equivalents are denominated in euros.

For additional information, see also Note 3.

NOTE 5 Trade and other receivables

	31 Dec 2016	31 Dec 2015
Trade receivables, net	1,467	1,186
Other prepaid expenses[1]	195	189
Tax prepayments and tax reclaims, thereof	280	213
Value added tax	280	209
Other taxes	0	4
Other prepayments	14	19
Total	**1,956**	**1,607**

[1]Other prepaid expenses include prepaid lease expense of the stores and insurance expenses, prepayment for information technology services and other expenses of similar nature.

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Trade receivables by region (client location) and by due date

31 December 2016	Baltic region	Eastern European region	Other regions	Total
Not due	459	784	22	1,265
Up to 1 month past due	16	1	75	92
1-3 months past due	3	0	38	41
3-6 months past due	15	0	37	52
Over 6 months past due	17	0	0	17
Total	**510**	**785**	**172**	**1,467**

31 December 2015	Baltic region	Eastern European region	Other regions	Total
Not due	362	444	71	877
Up to 1 month past due	78	9	22	109
1-3 months past due	4	0	39	43
3-6 months past due	1	0	140	141
Over 6 months past due	0	0	16	16
Total	**445**	**453**	**288**	**1,186**

For the wholesale customers' credit policy is based on next actions: monitoring credit amounts, past experience and other factors are taken into consideration. For some wholesale clients prepayments or payment guarantees through credit institutions are required. For some contractual clients no collaterals to secure the trade receivables are required but instead, deliveries, outstanding credit amount and adherence to agreed dates are monitored continuously.

As at 31 December 2016, the Group has recorded an allowance for doubtful receivables of 332 thousand euros (31 December 2015: 736 thousand euros). The allowance is recorded for individual receivables that are estimated to be uncollectible. As at 31 December 2016, 314 thousand euros (31 December 2015: 736 thousand euros) of the allowance reserve is related to not due balances from Eastern European region and 18 thousand euros (31 December 2015: 0) is related to overdue balances from other regions. The Group expects that the rest of the unimpaired not due and overdue balances will be recovered. Trade receivables allowance expense in 2016 was 18 thousand euros (2015: 16 thousand euros).

All trade and other receivables are denominated in euros.

For additional information, see also Note 3.

NOTE 6 Inventories

	31 Dec 2016	31 Dec 2015
Fabrics and accessories	1,906	1,790
Work-in-progress	78	82
Finished goods and goods purchased for resale	8,885	8,588
Allowance for impairment of finished goods and goods purchased for resale (Note 18)	-340	-500
Prepayments to suppliers	567	464
Total	**11,096**	**10,424**

In addition to the write-down of 340 thousand euros (2015: 500 thousand euros) to reduce inventories to net realizable value as seen above, the Group recognised 162 thousand euros during 2016 (2015: 269 thousand euros) as an expense for stock-take variances and inventory write offs. This was recognised in statement of profit and loss on line "Cost of goods sold".

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For additional information, see also Note 2.

NOTE 7 Deferred income tax

Deferred income tax as at 31 December 2016

	Total
Deferred income tax asset	
On PPE and other tax base differences[1]	-100
On tax loss carry-forwards	328
Total	**228**
Deferred income tax asset, net, thereof	**228**
Non-current portion	228
Deferred income tax expense (Note 24)	**-5**

Deferred income tax as at 31 December 2015

	Total
Deferred income tax asset	
On tax loss carry-forwards	234
Total	**234**
Deferred income tax asset, net, thereof	**234**
Non-current portion	234
Deferred income tax expense (Note 24)	**-40**

[1]Income tax liability can be settled against deferred tax assets in one country/company, therefore a deferred tax asset is recognised.

The recovery of the deferred income tax asset arising from tax loss carry-forwards is dependent on future taxable profits of subsidiaries that have to exceed the existing losses to be carried forward. An analysis of expected future profits was carried out when preparing the financial statements. The presumption of profit is dependable on attainment of each respective company strategic goals. The deferred tax asset resulting from losses carried forward is recognised to the extent that the realisation of the related tax benefit through the future profits is probable.

The Group recognised all deferred income tax assets in the statement of financial position as at 31 December 2016 and 31 December 2015 in respect of losses and other tax base differences that can be carried forward against future taxable income. Losses and other tax base differences can be used for unlimited period.

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NOTE 8 Other non-current assets

	31 Dec 2016	31 Dec 2015
Non-current portion of lease prepayments[1]	276	278
Other long-term receivables[2]	246	306
Total other non-current assets	**522**	**584**

[1]Non-current portion of lease prepayments arise from lease agreements of the Group's retail subsidiaries.

[2]Other long term receivables are for the sale of property and assets and trademark MasCara.

Credit risk arises from other long-term receivables (Note 3). The Group monitors continuously outstanding credit amount and the adherence to agreed dates. The payment schedules and interest rates related to the receivable from the sale of Mascara trademark were renegotiated and amendment to previous agreement was signed in 2015. All payments have been made according to the contractual schedule.

NOTE 9 Property, plant and equipment

	Buildings and structures	Machinery and equipment	Other fixtures	Pre-payments	Total
31 December 2014					
Acquisition cost	**2,330**	**5,143**	**5,253**	**0**	**12,726**
Accumulated depreciation	-1,547	-4,535	-3,749	0	-9,831
Net book amount	**783**	**608**	**1,504**	**0**	**2,895**
Additions	491	105	559	1	1,156
Disposals, impairments	-2	1	0	0	-1
Depreciation (Note 18-20)	-280	-198	-467	0	-945
Reclassification to held for sale	-85	-49	-61	0	-195
31 December 2015					
Acquisition cost	**2,452**	**4,736**	**4,491**	**1**	**11,680**
Accumulated depreciation	-1,545	-4,269	-2,956	0	-8,770
Net book amount	**907**	**467**	**1,535**	**1**	**2,910**
Additions	544	91	589	0	1,224
Disposals, impairments	-20	0	-87	0	-107
Depreciation (Note 18-20)	-339	-151	-514	0	-1,004
Reclassifications	0	1	-1	-1	-1
31 December 2016					
Acquisition cost	**2,838**	**4,718**	**4,813**	**0**	**12,369**
Accumulated depreciation	-1,746	-4,310	-3,291	0	-9,347
Net book amount	**1,092**	**408**	**1,522**	**0**	**3,022**

Details of assets acquired under finance lease terms are shown in Note 11.

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NOTE 10 Intangible assets

	Licenses, software and other	Trade-marks	Prepayments	Goodwill	Total
31 December 2014					
Acquisition cost	**2,132**	**1,243**	**28**	**1,495**	**4,898**
Accumulated amortisation	-1,425	-293	0	0	-1,718
Net book amount	**707**	**950**	**28**	**1,495**	**3,180**
Additions	80	0	-28	0	52
Impairment (Note 28)	-8	0	0	-885	-893
Amortisation (Note 18-20)	-250	-44	0	0	-294
Currency translation differences	0	0	0	-101	-101
31 December 2015					
Acquisition cost	**2,261**	**1,243**	**0**	**509**	**4,013**
Accumulated amortisation	-1,732	-337	0	0	-2,069
Net book amount	**529**	**906**	**0**	**509**	**1,944**
Additions	23	0	0	0	23
Disposals	-1	0	0	0	-1
Amortisation (Note 18-20)	-246	-44	0	0	-290
31 December 2016					
Acquisition cost	**2,092**	**1,243**	**0**	**509**	**3,844**
Accumulated amortisation	-1,787	-381	0	0	-2,168
Net book amount	**305**	**862**	**0**	**509**	**1,676**

Trademarks with a net book value of 862 thousand euros (31 December 2015: 906 thousand euros) include acquired trademarks – Bastion and Ivo Nikkolo. The remaining amortization periods for these trademarks are 46 and 10 years respectively.

Impairment tests for goodwill

The carrying value of goodwill as at 31 December 2016 in the amount of 509 thousand euros (31 December 2015: 509 thousand euros) is tested for impairment at each balance sheet date.

The goodwill of Russian Group entities was written-off in 2015 in the amount of 885 thousand euros. The write-off decision was made based on the decision to discontinue retail operations in Russia.

The carrying amount of goodwill applicable to CGUs (cash generating units) of Baltika Tailor OÜ and SIA Baltika Latvija was tested for impairment at 31 December 2016. The recoverable amount of CGU is determined based on value-in-use calculations. The value-in-use calculations use detailed pre-tax cash flow projections covering a five-year period. Cash flows beyond the five-year period are extrapolated using the estimated growth rates.

Key assumptions used for value-in-use calculations

	Baltika Tailor CGU		Baltika Latvija CGU	
Balance at 31 December	**2016**	**2015**	**2016**	**2015**
Carrying amount of goodwill	355	355	154	154
Growth in revenue[1]	3.3%	4.1%	3.2%	4.8%
Terminal growth rate[2]	2.0%	2.0%	2.0%	2.0%
Budgeted Gross margin[3]	3.9%	4.0%	57.0%	56.8%
Discount rate[4]	11.7%	13.0%	10.9%	11.9%
Difference between recoverable and carrying amount	174	146	22,606	25,946

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[1]Management determined average annual growth in revenue for Baltika Tailor and sales efficiency per square metre and for Baltika Latvija for the five-year period.
[2]Terminal growth rate used to extrapolate cash flows beyond the year 2021.
[3]Management determined the average gross margin based on the past performance and management's expectations for the future.
[4]Pre-tax discount rate applied to the cash flow projections (WACC). The change in discount rates results from changes in industry indicators for the specific region.

The growth rates used for projections have been derived from the past experience of the growth in respective industry and the management's expectations of the respective growth rates in the projected future years in the respective region. The weighted average cost of capital (WACC) used was pre-tax and reflects specific risks applicable to the specific market and industry sector.

The tests resulted in recoverable value exceeding the carrying amount of the cash generating unit and consequently no impairment losses have been recognised.

If the average annual growth in sales efficiency (sales per m^2) were -6.0% for SIA Baltika Latvija the recoverable amount would have been equal to the carrying amount (31 December 2015: -5.6%). If the average annual growth in sales for Baltika Tailor were 3.2% (31 December 2015: 2.7%) the recoverable amount would have been equal to the carrying amount.

If the average annual gross profit margin was 39% and 3.6% for SIA Baltika Latvija and Baltika Tailor respectively the recoverable amount would have been equal to the carrying amount (31 December 2015: 34.8% and 0.0% respectively).

NOTE 11 Accounting for leases

Operating lease – the Group as the lessee

Future minimum lease payments under non-cancellable operating leases

	31 Dec 2016	31 Dec 2015
Up to 1 year	5,472	4,068
1-5 years	10,622	8,491
Over 5 years	0	920
Total	**16,094**	**13,479**

Operating lease expenses arise from lease of stores, production facility and head-office. The lease agreements for stores are predominantly not binding for long-term and can be terminated mostly less than 12-months' notice.

The lease agreements concluded with a term are subject to renewal on market conditions. The Group has signed a number of contingent lease agreements which stipulate the increase in lease payments within the lease term based on changes in consumer price index or inflation. In 2016, operating lease costs amounted to 7,465 thousand euros (2015: 7,339 thousand euros) (Note 18-20).

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Finance lease – the Group as the lessee

	Machinery and equipment	Other fixtures	Total
At 31 December 2014			
Acquisition cost	**1,384**	**273**	**1,657**
Accumulated depreciation	-955	-148	-1,103
Net book amount	**429**	**125**	**554**
Additions	69	475	544
Depreciation	-119	-132	-250
At 31 December 2015			
Acquisition cost	**1,451**	**723**	**2,175**
Accumulated depreciation	-1,072	-256	-1,327
Net book amount	**380**	**567**	**847**
Additions	60	0	60
Disposals	0	-6	-6
Depreciation	-98	-107	-205
At 31 December 2016			
Acquisition cost	**1,509**	**603**	**2,111**
Accumulated depreciation	-1,167	-248	-1,415
Net book amount	**341**	**355**	**696**

Detailed information on minimum finance lease payments by maturity is disclosed in Note 3. The carrying amounts of finance lease liabilities at the balance sheet date are disclosed in Note 12.

In 2016, the Group settled finance lease payments in the amount of 145 thousand euros (2015: 153 thousand euros).

NOTE 12 Borrowings

	31 Dec 2016	31 Dec 2015
Current borrowings		
Current portion of long-term bank loan (Note 3)	1,019	1,380
Bank overdrafts (Note 3)	1,620	1,426
Current finance lease liabilities (Note 3)	196	179
Convertible bonds (Note 15, 3)	3,000	0
Other current loans (Note 3)	0	24
Total	**5,835**	**3,009**
Non-current borrowings		
Non-current bank loan (Note 3)	1,046	0
Non-current finance lease liabilities (Note 3)	150	312
Convertible bonds (Note 15, 3)	0	3,000
Total	**1,196**	**3,312**
Total borrowings	**7,031**	**6,321**

Borrowings are denominated in euros. Management estimates that the carrying amount of the Group´s financial liabilities does not significantly differ from their fair value (Note 3). During the reporting period, the Group made loan repayments for 807 thousand euros (2015: 985 thousand euros). Interest expense of the loans and other interest carrying borrowings of the reporting period amounted to 472 thousand euros (2015: 475 thousand euros), including interest expense from borrowings or convertible bonds to related party (Note 15). Unused part of overdrafts was 2,380 thousand euros as at 31 December 2016 (31 December 2015: 2,574 thousand euros).

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Finance lease is used for acquisition of cars, furniture and equipment for shops.

Changes in 2016

In June the repayment date of the overdraft agreement (in the amount of 1,000 thousand euros) was extended until June 2017.

In July an annex under the existing facility agreement was signed, which extended the other overdraft´s repayment date until July 2017 (in the amount of 3,000 thousand euros). With the same annex the existing loan repayment period was extended by 20 months and an additional investment loan in the amount of 2,000 thousand euros was taken, which will be repaid during the next 4 years. In the third quarter 1,500 thousand euros from the new loan was taken into use.

Changes in 2015

In April an annex under an existing facility agreement was signed, which prolonged overdrafts´s repayment date until July 2016 (in the amount of 3,000 thousand euros). The annex removed the option to increase and decrease overdraft limit according to seasonality. In December a separate overdraft facility agreement´s repayment date was prolonged until June 2016 in the amount of 1,000 thousand euros.

Interest carrying loans of the Group as at 31 December 2016

	Balance	Average risk premium
Borrowings at floating interest rate (based on 6-month Euribor or 1-month Eonia)	4,031	EURIBOR or EONIA +4.60%
J-Bonds (Note 26)	3,000	6.50%
Total	**7,031**	

Interest carrying loans of the Group as at 31 December 2015

	Balance	Average risk premium
Borrowings at floating interest rate (based on 6-month Euribor or 1-month Eonia)	3,297	EURIBOR or EONIA +4.60%
J-Bonds (Note 26)	3,000	6.50%
Total	**6,297**	

The loan contracts of the Group include several covenants that may require early repayment of loans if the borrower does not fulfil the terms specified in the contract including:

- limited disposal of assets;
- limited rights for incurring additional liabilities;
- limited rights for paying dividends and deciding to issue share capital.

The Group's collaterals for bank borrowings

As at 31 December 2016 and 31 December 2015 the bank borrowings were secured with following asset types:

- commercial pledge to movables;
- trademarks;
- shares of the subsidiaries;
- cash equivalents on the bank accounts.

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As at 31 December 2016 carrying amount of assets pledged was 15,143 thousand euros, including inventories in amount of 11,096 thousand euros, property, plant and equipment in amount of 3,022 thousand euros, intangible assets in amount of 606 thousand euros and cash on the bank accounts 419 thousand euros.

As at 31 December 2015 carrying amount of assets pledged was 15,574 thousand euros, including inventories in amount of 10,424 thousand euros, property, plant and equipment in amount of 2,910 thousand euros, intangible assets in amount of 1,944 thousand euros and cash on the bank accounts 296 thousand euros.

As at 31 December 2016, AS Baltika complied with the terms and conditions of the bank loan agreements. As at 31 December 2015 AS Baltika, was not in compliance with some of the terms and conditions of the bank loan agreement. Although the bank had confirmed that the loan would not become due and payable prematurely, this loan was classified as short-term as at 31 December 2015 as the contractual payment date was in year 2016.

For additional information, see also Note 3.

NOTE 13 Trade and other payables

	31 Dec 2016	31 Dec 2015
Current liabilities		
Trade payables (Note 3)	3,259	3,640
Tax liabilities, thereof	1,603	1,570
Personal income tax	220	229
Social security taxes and unemployment insurance premium	536	559
Value added tax	770	744
Other taxes	77	38
Payables to employees[1]	991	995
Other accrued expenses	527	49
Customer prepayments	166	71
Other current payables	30	2
Total	**6,576**	**6,327**
Non-current liabilities		
Other liabilities	0	283

[1]Payables to employees consist of accrued wages, salaries and vacation accrual.

Tax authorities are entitled to check the Group’s tax accounting up to within 5 years after the term for the submission of tax declaration and when mistakes are detected to impose an additional amount of tax, interests and fines. The tax legislation of the countries the Group is operating which was enacted or substantively enacted at the end of the reporting period may be subject to varying interpretations. Consequently, tax positions taken by management and the formal documentation supporting the tax positions may be successfully challenged by relevant authorities. According to the Group’s Management Board there are no circumstances as a result of which tax authority could impose a significant additional amount of tax to the Group.

Trade payables and other accrued expenses in denominated currency

	31 Dec 2016	31 Dec 2015
EUR (euro)	2,630	2,382
USD (US dollar)	1,156	1,258
Total	**3,786**	**3,640**

For additional information, see also Note 3.

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NOTE 14 Provisions

Current provisions	31 Dec 2016	31 Dec 2015
Client bonus provision	347	370
Other provisions	0	12
Total	**347**	**382**

Short description of the client bonus provision

The Group offers a customer loyalty programme "AndMore" to its retail (including web-shop) clients in the Baltic states.

"AndMore" motivates clients by allowing them to earn a future discount on purchases made today (bonus euros). Accumulated bonuses are valid for six months from the customer´s last purchase. The program's conditions are described in detail on the company´s website.

Used assumptions

In 2016 the Group reduced the client bonus provision by 23 thousand euros (2015: increased by 70 thousand euros). The Group has used existing statistics that enable to characterize customers' usage of the bonus: earnings, usage and expiration.

The provision has been formed based on the earned, but not yet used bonuses and adjusted by the probability of expiration. Probability has been assessed based on existing customer behaviour statistics.

See also Note 17.

NOTE 15 Equity

Share capital

	31 Dec 2016	31 Dec 2015
Share capital	8,159	8,159
Number of shares (pcs)	40,794,850	40,794,850
Nominal value of share (EUR)	0.20	0.20

As at 31 December 2016 and 31 December 2015 shares comprise only ordinary shares, which are listed on the Nasdaq Tallinn.

Change in the number of shares

	Number of shares
Number of shares 31 December 2015	**40,794,850**
Number of shares 31 December 2016	**40,794,850**

As at 31 December 2016 and 31 December 2015, under the Articles of Association, the company's minimum share capital is 5,000 thousand euros and the maximum share capital is 20,000 thousand euros. All shares have been paid for.

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Changes in share capital

Convertible bonds and share options

	Issue date	Bond conversion period	Number of convertible bonds 31 Dec 2016	Number of convertible bonds 31 Dec 2015
J-Bond	28 July 2014	15 July 2017 - 30 July 2017	600	600

J-bonds

On 28 April 2014 the annual general meeting of shareholders decided to issue convertible bonds with bondholder option in the total amount of 3 million euros. Decision was to issue 600 convertible bonds with the issuance price of 5,000 euros. The three-year convertible bonds carry an annual interest rate of 6.5% and give its owner the right to subscribe for 10,000 AS Baltika shares at 0.5 euros subscription price.

Bonds (510 bonds in the amount of 2,550 thousand euros) were partly issued to a related party.

Share option program

On 27 April 2015 the Annual General Meeting of shareholders decided to conditionally increase share capital up to 1,000,000 registered shares with nominal value of 0.20 euro subscription price of 0.20 euro related to share option program. If the Baltika share price increase conditions are fulfilled, AS Baltika members of the Management Board may mark the shares three years from the date when the share option agreement has been signed.

Reserves

	31 Dec 2016	31 Dec 2015
Statutory reserve	1,182	1,182

Shareholders as at 31 December 2016

	Number of shares	Holding
1. ING Luxembourg S.A.	12,590,914	30.86%
2. Clearstream Banking Luxembourg S.A. clients	5,726,142	14.04%
3. BMIG OÜ*	4,750,033	11.64%
4. SKANDINAVISKA ENSKILDA BANKEN S.A.	3,407,305	8.35%
5. Svenska Handelsbanken clients	1,320,000	3.24%
6. Members of Management and Supervisory Boards and their immediate family members		
Meelis Milder	1,013,735	2.48%
Persons related to members of Management Board	334,183	0.82%
Entities related to Supervisory Board members not mentioned above	1,002,427	2.46%
7. Other shareholders	10,650,111	26.11%
Total	**40,794,850**	**100.00%**

Shareholders as at 31 December 2015

	Number of shares	Holding
1. ING Luxembourg S.A.	12,590,914	30.86%
2. Clearstream Banking Luxembourg S.A. clients	5,724,872	14.03%
3. BMIG OÜ*	4,750,033	11.64%
4. Skandinaviska Enskilda Banken Ab clients	3,414,700	8.37%
5. Svenska Handelsbanken clients	1,458,000	3.57%
6. Members of Management and Supervisory Board and their immediate family members		
Meelis Milder	1,000,000	2.45%
Persons related to members of Management Board	331,183	0.81%

Entities related to Supervisory Board not mentioned above	1,002,427	2.46%
7. Other shareholders	10,522,721	25.81%
Total	**40,794,850**	**100.00%**

*The investment company OÜ BMIG is under the control of the Management Board members of the Parent company

The shares of the Parent company are listed on the Nasdaq Tallinn. The Parent company does not have a controlling shareholder or any shareholders jointly controlling the entity.

NOTE 16 Segments

The Group's chief operating decision maker is the Management Board of the Parent company AS Baltika. The Parent company's Management Board reviews the Group's internal reporting in order to assess performance and allocate resources. Management Board has determined the operating segments based on these reports.

The Parent company's Management Board assesses the performance of the business by distribution channel: retail channel and other sales channels (including wholsesale, franchise and e-commerce). The retail segments are countries which have been aggregated to reportable segments by regions which share similar economic characteristics and meet other aggregation criteria provided in IFRS 8.

Description of segments and principal activities:

- Retail segment - consists of retail operations in Estonia, Latvia and Lithuania. While the Management Board reviews separate reports for each region, the countries have been aggregated into one reportable segment as they share similar economic characteristics. Each region sells the same products to similar classes of customers and use the same production process and the method to distribute their products.
- All other segments – consists of sale of goods to wholesale and franchise clients, materials and sewing services and e-commerce sales. None of these segments meet the reportable segments quantitative thresholds set out by IFRS 8 and are therefore aggregated into the All other segments category.

The Parent company's Management Board measures the performance of the operating segments based on external revenue and profit (loss). External revenue amounts provided to the Management Board are measured in a manner consistent with that of the financial statements. The segment profit (loss) is an internal measure used in the internally generated reports to assess the performance of the segments and comprises the segment's gross profit (loss) less operating expenses directly attributable to the segment, except for other operating income and expenses. The amounts provided to the Management Board with respect to inventories are measured in a manner consistent with that of the financial statements. The segment inventories include those operating inventories directly attributable to the segment or those that can be allocated to the particular segment based on the operations of the segment and the physical location of the inventories.

The Management Board monitors the Group´s results also by shops and brands. The Group makes decisions on a shop-by-shop basis, using aggregated information for decision making. For segment reporting the Management Board has decided to disclose the information by distribution channel. Most of the Management Board's decisions related to investments and resource allocation are based on the segment information disclosed in this Note.

The Management Board primarily uses a measure of revenue from external customers, segment profit, depreciation and amortisation and inventories to assess the performance of the operating segments. Information for the segments is disclosed below:

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The segment information provided to the Management Board for the reportable segments

	Retail segment	All other segments[1]	Total
2016			
Revenue (from external customers)	39,678	7,315	46,993
Segment profit[2]	7,126	1,108	8,234
Incl. depreciation and amortisation	-859	-75	-934
Inventories of segments	4,392	0	4,392
2015			
Revenue (from external customers)	42,730	6,076	48,806
Segment profit[2]	7,264	696	7,960
Incl. depreciation and amortisation	-758	-97	-855
Inventories of segments	4,465	0	4,465

[1]All other segments include sale of goods to wholesale and franchise clients, materials and sewing services and the sales from e-commerce.

[2]The segment profit is the segment operating profit, excluding other operating expenses and income.

Reconciliation of segment operating profit to consolidated operating profit

	2016	2015
Total segment profit	8,234	7,960
Unallocated expenses:[1]		
Costs of goods sold and distribution costs	-5,073	-5,970
Administrative and general expenses	-2,504	-2,585
Other operating income (expenses), net	44	300
Operating profit (loss)	**701**	**-295**

[1]Unallocated expenses include the expenses of the parent company and production companies that are not allocated to the reportable segments in internal reporting.

Reconciliation of segment inventories to inventories on consolidated statement of financial position

	31 Dec 2016	31 Dec 2015
Total inventories of segments	4,392	4,465
Inventories in Parent company and production company	6,704	5,959
Inventories on statement of financial position	**11,096**	**10,424**

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

	31 Dec 2016	31 Dec 2015
Retail	2,690	2,524
Wholesale	62	136
Assets in parent company and production company	1,946	2,194
Total	**4,698**	**4,854**

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NOTE 17 Revenue and client bonus reserve

	2016	2015
Sale of goods in retail channel	39,678	42,730
Sale of goods in wholesale and franchise channel	6,029	4,976
Sale of goods in e-commerce channel	1,063	975
Other sales	223	125
Total	**46,993**	**48,806**

Sales by geographical (client location) areas

	2016	2015
Estonia	20,487	21,199
Lithuania	11,086	12,241
Latvia	10,658	11,700
Russia	1,812	1,039
Ukraine	1,179	978
Finland	602	679
Germany	403	92
Spain	403	541
Belarus	188	248
Other countries	175	89
Total	**46,993**	**48,806**

Client bonus provision

The Group accrues for bonuses earned through the customer loyalty programme. To calculate the reserve, the Group estimated the potential amount of bonuses that will be used in the next reporting period out of the total earned but not yet used bonuses at year end.

The provision as of 31 December 2016 decreased by 23 thousand euros. For further information about the assumptions used to form a provision, see Note 14.

NOTE 18 Cost of goods sold

	2016	2015
Materials and supplies	19,012	20,843
Payroll costs in production	3,493	3,385
Operating lease expenses (Note 11)	677	661
Other production costs	405	393
Change in allowance for inventories (Note 6)	-160	251
Depreciation of assets used in production (Note 9)	92	127
Total	**23,519**	**25,660**

NOTE 19 Distribution costs

	2016	2015
Payroll costs	9,165	9,669
Operating lease expenses (Note 11)	6,348	6,235
Advertising expenses	1,319	1,396
Depreciation and amortisation (Note 9, 10)	1,071	996
Fuel, heating and electricity costs	506	523
Municipal services and security expenses	344	329
Fees for card payments	241	333

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Information technology expenses	180	162
Travel expenses	163	179
Consultation and management fees	121	242
Communication expenses	104	109
Other sales expenses[1]	774	837
Total	**20,336**	**21,010**

[1]Other sales expenses mostly consist of insurance and customs expenses, bank fees, expenses for uniforms, packaging, transportation and renovation expenses of stores, agency and service fees connected to administration of market organizations.

NOTE 20 Administrative and general expenses

	2016	**2015**
Payroll costs	1,208	1,145
Operating lease expenses (Note 11)	440	443
Information technology expenses	216	246
Bank fees	153	180
Depreciation and amortisation (Note 9, 10)	125	111
Fuel, heating and electricity expenses	68	83
Management, juridical-, auditor´s and other consulting fees	58	117
Other administrative expenses[1]	236	278
Total	**2,504**	**2,603**

[1]Other administrative expenses consist of insurance, communication, travel, training, municipal and security expenses and other services.

NOTE 21 Wages and salaries

	2016	**2015**
Payroll costs	10,540	10,754
Social security costs	3,325	3,445
Total	**13,866**	**14,199**

In 2016, the average number of employees in Baltika Group was 1,073 (2015: 1,119).

NOTE 22 Other operating income (-expense)

	2016	**2015**
Gain (loss) from sale, impairment of PPE and immaterial assets	-15	4
Other operating income	90	347
Foreign exchange losses	-35	-36
Fines, penalties and tax interest	15	-3
Other operating expenses	-11	-70
Total	**44**	**242**

For additional information, see also Note 9, 10.

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NOTE 23 Finance costs

	2016	2015
Interest costs	-472	-475
Other finance costs	-47	-33
Total	**-519**	**-508**

NOTE 24 Income tax

	2016	2015
Income tax expense	0	1
Deferred income tax expense (Note 7)	5	40
Total income tax expense	**5**	**41**

Income tax calculated on the profits of the Group's subsidiaries based on the nominal tax rate differs from effective income tax expense for the reasons presented below.

Income tax for the year ended at 31 December 2016

	Total
Profit (loss) before tax	182
Average nominal tax rate	0-15%
Tax calculated from profit (loss) at the nominal tax rate	5
The effect of income/expenses not deductible for tax purposes	-3
Utilisation of tax losses carried forward/additions of tax profits	-2
Changes in recognised balance sheet deferred tax assets	5
Income tax expense	**0**
Deferred income tax expense (income) (Note 7)	**5**

Income tax for the year ended at 31 December 2015

	Total
Profit (loss) before tax	-803
Average nominal tax rate	0-15%
Tax calculated from profit (loss) at the nominal tax rate	40
The effect of income/expenses not deductible for tax purposes	-23
Utilisation of tax losses carried forward/additions of tax profits	-34
Changes in recognised balance sheet deferred tax assets	40
Income tax expense	**1**
Deferred income tax expense (income) (Note 7)	**40**

NOTE 25 Earnings per share

Basic earnings per share

		2016	2015
Weighted average number of shares (thousand)	pcs	40,795	40,795
Net profit (loss) from continuing operations	EUR	177	-844
Net profit (loss) from discontinued operations	EUR	0	-5,515
Basic earnings per share	**EUR**	**0,00**	**-0.16**
Basic earnings per share (continuing operations)	EUR	0,00	-0.02
Basic earnings per share (discontinued operations)	EUR	0,00	-0.14

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Diluted earnings per share

		2016	2015
Weighted average number of shares (thousand)	pcs	40,795	40,795
Adjustments:			
- weighted average of J-bonds that are dilutive (thousand)	pcs	0	0
- weighted average number of share options that are dilutive (thousand)	pcs	0	230
Weighted average number of ordinary shares for diluted earnings per share (thousand)	**pcs**	**40,795**	**41,025**
Net profit (loss) from continuing operations	EUR	177	-844
Net profit (loss) from discontinued operations	EUR	0	-5,515
Interest expense (convertible bonds)	EUR	0	0
Profit (loss) used to determine diluted earnings per share	**EUR**	**177**	**-6,359**
Diluted earnings per share	EUR	**0.00**	**-0.16**
Diluted earnings per share (continuing operations)	EUR	0.00	-0.02
Diluted earnings per share (discontinued operations)	EUR	0.00	-0.14

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential shares. The company had three types of potential ordinary shares (Note 15):

- I-bonds in 2015
- J-bonds in 2015 and 2016
- Share option program in 2015 and 2016

As of 31 December 2015, no applications were received to mark the shares (I-bonds) and at the beginning on 2016 all the payments for the shares were paid back. In 2015, a calculation was done to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the company´s share) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares, calculated as described above, was compared with the number of shares that would have been issued assuming the exercise of the share options. In 2015, I-bonds were not dilutive.

The dilutive effect of the J-bonds is contingent on the share price. In 2015 and 2016, the Group assumed the J-bonds would not be converted into ordinary shares based on the average share price on Nasdaq Tallinn Stock exchange.

For the share option program, a calculation was done to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the company´s share) based on the monetary value of the subscription rights attached to outstanding share options. The number of shares, calculated as described above, was compared with the number of shares that would have been issued assuming the exercise of the share options. As the dilutive effect is contingent on the share price, the share option program did not have a dilutive effect in 2016. In 2015, it was assumed that the Share option program would be converted into ordinary shares and the weighted average number of share options that are dilutive was 230 thousand.

The average price (arithmetic average based on daily closing prices) of AS Baltika share on the Nasdaq Tallinn Stock Exchange in 2016 was 0.29 euros (2015: 0.37 euros).

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NOTE 26 Related parties

For the purpose of these financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the financial and management decisions of the other one in accordance with IAS 24, Related Party Disclosures. Not only the legal form of the transactions and mutual relationships, but also their actual substance has been taken into consideration when defining related parties.

For the reporting purposes in consolidated annual statements of the Group, the following entities have been considered related parties:

- owners, that have significant influence, generally implying an ownership interest of 20% or more; and entities under their control (Note 15);
- members of the Management Board and the Supervisory Board[1];
- immediate family members of the persons stated above;
- entities under the control or significant influence of the members of the Management Board and Supervisory Board and immediate family members;

[1]Only members of the Parent company Management Board and Supervisory Board are considered as key management personnel, as only they have responsibility for planning, directing and controlling Group activities.

Transactions with related parties

Purchases	2016	2015
Services from entities under the control or significant influence of the members of the Management Board and Supervisory Board	24	355
Total	**24**	**355**

Sales	2016	2015
Goods to the members of the Management Board and Supervisory Board	0	7
Total	**0**	**7**

In 2016, AS Baltika bought mostly management services from the related parties. In 2015, AS Baltika bought mostly management, communication and other services from the related parties.

Balances with related parties

	31 Dec 2016	31 Dec 2015
Other current loans (Note 12, 13)	2,973	2,804
Trade payables (Note 13)	0	17
Total	**2,973**	**2,821**

All transactions in 2016 as well as in 2015 and balances with related parties as at 31 December 2016 and 31 December 2015 were with entities under the control or significant influence of the members of the Management Board and Supervisory Board.

Compensation for the members of the Management Board and Supervisory Board

	2016	2015
Salaries of the members of the Management Board	253	224
Remuneration of the members of the Supervisory Board	14	14
Total	**267**	**238**

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As at 31 December 2016, there were two Management Board Members and as at 31 December 2015 there were three Management Board Members. As at 31 December 2016 and 31 December 2015, there were five Supervisory Board Members.

Changes in the Management Board in 2016

On 30 January 2015, the Supervisory Board of AS Baltika suspended Maigi Pärnik-Pernik Management Board contract for the duration of her maternity leave. From 1 February 2016 Management Board member responsible for the finance function and for the disclosure of information on the stock exchange is again Maigi Pärnik-Pernik.

From March 17, 2016, the Supervisory Board of AS Baltika decided to recall Kati Kusmin from the Management Board, who was entitled to a termination compensation in accordance with agreement, which was disbursed in 2016.

Changes in the Management Board in 2015

In April 2015, the Supervisory Board recalled Andrew James David Paterson from the Management Board, who was entitled to a termination compensation in accordance with agreement, which was disbursed in 2015.

From 8 September 2015, Maire Milder is no longer member of Management Board. Maire Milder continues in the Group as the director of Branding and Retail Development.

The termination benefits for the members of the Management Board are limited to 3-18 month's salary expense (no taxes included) in the total amount that is approximately 234 thousand euros (2015: 234 thousand euros) in case of premature termination. During 2016, the Group paid termination benefits of 36 thousand euros.

During 2015 – 2016 no changes took place in the composition of Supervisory Board. No compensations for terminating Supervisory Board status were paid in 2015 - 2016.

In 2015 share option program was issued to the Management Board members (Note 15).

In 2014 convertible bonds (J-bonds) were partly issued to a related party (Note 15).

In 2012, the Company issued I-Bonds partly to related parties. As of 31 December 2015, no applications were received to mark the shares; at the beginning on 2016 all the payments for the shares were paid back. The value of employee services previously recognised in share premium for 313 thousand euros was released in 2015.

NOTE 27 Subsidiaries

Subsidiary	Location	Activity	Holding as at 31 Dec 2016	Holding as at 31 Dec 2015
OÜ Baltika Retail	Estonia	Holding	100%	100%
OÜ Baltman[1]	Estonia	Retail	100%	100%
SIA Baltika Latvija[2]	Latvia	Retail	100%	100%
UAB Baltika Lietuva[2]	Lithuania	Retail	100%	100%
OOO „Olivija"[3]	Russia	Retail	0%	100%
OY Baltinia AB	Finland	Dormant	100%	100%
Baltika Sweden AB	Sweden	Dormant	100%	100%
OÜ Baltika Tailor	Estonia	Production	100%	100%

[1]Interest through a subsidiary.
[2]Interest through Baltman OÜ
[3]OOO "Olivia" consolidation group, which also included OOO "Plazma" and OOO "Stelsing" was sold 22 February 2016. Refer to Note 28 for additional information.

2016 Consolidated Annual Report (in thousands of euros)

NOTE 28 Discontinued operations

In the end of 2015 AS Baltika decided to exit Russian retail market to reduce economic and political risks. In the fourth quarter, prior to sales transaction, AS Baltika classified all assets of the disposal group as held for sale and reameasured to nil. Non-monetary loss from remeasurements in total was 4,645 thousand euros. Goodwill was written-off in full by 885 thousand euros, currency exchange differences previously recognised in a reserve in equity were recycled to income statement in the amount of 2,969 thousand euros, allowance reserve was made for working capital and non-current assets in the amount of 791 thousand euros.

On 22 February 2016 AS Baltika signed an agreement by which all Russian subsidiaries shares were sold to Osaühing Ellipse Group. Baltika Group´s brands will continue in Russian market through 5-year franchise agreement.

As Russian market represented a major line of business in Group´s activities, and its operations and cash flows were clearly distinguished from other Group´s operations and cash flows, it´s results were reported as discontinued operations as of 31 December 2015.

Analysis of the results of discontinued operations, and the result recognised on the re-measurement of assets is as follows:

Revenue and expenses of discontinued operations

	2016	2015
Discontinued operation		
Revenue	0	4,492
Expenses	0	-5,020
Other operating income (-expense)	0	-317
Loss before income tax	**0**	**-845**
Income tax relating to the discontinued operations	0	-25
Loss after income tax	**0**	**-870**
Loss from remeasurement of assets classified as held for sale	0	-4,645
Net loss for the reporting period	**0**	**-5,515**

Cash-flow of the discontinued operation

	2016	2015
Net cash used in operating activities	0	-77
Net cash used in investing activities	0	-7
Total cash flows	**0**	**-84**
Cash and cash equivalents at the beginning of the period	**0**	**84**
Cash and cash equivalents at the end of the period	**0**	**0**
Change in cash and cash equivalents	**0**	**-84**

NOTE 29 Supplementary disclosures on the parent company of the Group

Pursuant to the Accounting Act of the Republic of Estonia, information of the unconsolidated financial statements (primary statements) of the consolidating entity (parent company) shall be disclosed in the notes to the consolidated financial statements. In preparing the primary financial statements of the parent company the same accounting policies have been used as in preparing the consolidated financial statements. The accounting policy for reporting subsidiaries has been amended in the separate primary financial statements disclosed as supplementary information in the Annual Report in conjunction with IAS 27, Consolidated and Separate Financial Statements.

In the parent separate primary financial statements, disclosed to these consolidated financial statements (Supplementary disclosures), investments into the shares of subsidiaries are accounted for at cost less any impairment recognised.

2016 Consolidated Annual Report (in thousands of euros)

Statement of financial position of the parent company

	31 Dec 2016	31 Dec 2015
ASSETS		
Current assets		
Cash and cash equivalents	12	55
Trade and other receivables	5,175	4,648
Inventories	6,946	6,365
Total current assets	**12,133**	**11,068**
Non-current assets		
Investments in subsidiaries	1,324	1,324
Other non-current receivables	246	246
Property, plant and equipment	224	286
Intangible assets	1,153	1,395
Total non-current assets	**2,947**	**3,251**
TOTAL ASSETS	**15,080**	**14,319**
LIABILITIES AND EQUITY		
Current liabilities		
Borrowings	5,650	2,841
Trade and other payables	7,899	7,891
Total current liabilities	**13,549**	**10,732**
Non-current liabilities		
Borrowings	1,103	3,067
Other liabilities	0	284
Total non-current liabilities	**1,103**	**3,351**
TOTAL LIABILITIES	**14,652**	**14,083**
EQUITY		
Share capital at par value	8,159	8,159
Share premium	496	496
Statutory reserve	1,182	1,182
Retained losses	-9,601	-15,986
Net profit (loss) for the period	192	6,385
TOTAL EQUITY	**428**	**236**
TOTAL LIABILITIES AND EQUITY	**15,080**	**14,319**

2016 Consolidated Annual Report (in thousands of euros)

Statement of comprehensive income of the parent company

	2016	2015
Revenue	32,828	33,544
Cost of goods sold	-24,020	-26,480
Gross profit	**8,808**	**7,064**
Distribution costs	-5,501	-5,892
Administrative and general expenses	-2,416	-2,543
Other operating income (-expense)	60	289
Operating profit (loss)	**951**	**-1,082**
Impairment and reversal of impairment of investments to and receivables from subsidiaries	0	8,626
Interest expenses, net	-759	-1,159
Net profit for the period	**192**	**6,385**
Total comprehensive income profit for the period	**192**	**6,385**

2016 Consolidated Annual Report (in thousands of euros)

Cash flow statement of the parent company

	2016	2015
Cash flows from operating activities		
Operating profit (-loss)	951	-1,082
Depreciation, amortisation and impairment of PPE and intangibles; gain (loss) from disposal of PPE	335	349
Other non-monetary expenses	-26	-545
Changes in trade and other receivables	-527	387
Changes in trade and other payables	-490	-8,974
Changes in inventories	-581	1,356
Interest received	7	0
Interest paid	-539	-300
Net cash used in operating activities	**-870**	**-8,809**
Cash flows from investing activities		
Acquisition of non-current assets	-49	-66
Proceeds from disposal of non-current assets	24	0
Proceeds from subsidiary share capital reduction	0	10,101
Net cash generated (used in) investing activities	**-25**	**10,035**
Cash flows from financing activities		
Proceeds from borrowings	1,500	0
Repayments of borrowings	-807	-985
Change in overdraft balance	194	-226
Repayments of finance lease	-11	-73
Repayment of convertible notes	-24	0
Net cash generated (used in) from financing activities	**852**	**-1,284**
Total cash flows	**-43**	**-58**
Cash and cash equivalents at the beginning of the period	**55**	**113**
Cash and cash equivalents at the end of the period	**12**	**55**
Net change in cash and cash equivalents	**-43**	**-58**

2016 Consolidated Annual Report (in thousands of euros)

Statement of changes in equity of the parent company

	Share capital	Share premium	Reserves	Retained earnings	Total
Balance at 31 December 2014	**8,159**	**809**	**1,182**	**-15,986**	**-5,836**
Total comprehensive income	0	0	0	6,385	6,385
Equity-settled share-based transactions	0	-313	0	0	-313
Balance at 31 December 2015	**8,159**	**496**	**1,182**	**-9,601**	**236**
Book value of holdings under control or significant influence					-1,324
Value of holdings under control or significant influence, calculated under equity method					6,112
Adjusted unconsolidated equity at 31 December 2015					**4,788**
Total comprehensive income	0	0	0	192	192
Balance at 31 December 2016	**8,159**	**496**	**1,182**	**-9,409**	**428**
Book value of holdings under control or significant influence					-1,324
Value of holdings under control or significant influence, calculated under equity method					6,289
Adjusted unconsolidated equity at 31 December 2016					**4,965**

According to the Estonian Accounting Law, the amount that can be distributed to the shareholders is calculated as follows: adjusted unconsolidated equity less share capital, share premium and reserves.

Independent auditor's report

To the Shareholders of AS Baltika

(Translation of the Estonian original)*

Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of AS Baltika and its subsidiaries (together the Group) as at 31 December 2016, 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.

What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2016;
- the consolidated statement of profit or loss for the year then ended;
- the consolidated statement of other comprehensive income for the year then ended;
- the consolidated cash flow statement for the year then ended;
- the consolidated statement of changes in equity for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies and other explanatory information.

Basis for opinion

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

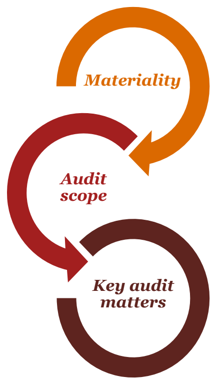
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

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

Our audit approach

Overview



Materiality

Overall Group materiality is EUR 0.4 million, which represents approximately 0.9% of revenue.

Audit scope

We performed audit procedures over all significant transactions and balances across the Group as a whole. In limited areas where we relied on non-PwC component auditors we determined the level of involvement needed to be able to report on the financial statements as a whole.

Key audit matters

- Revenue recognition
- Inventory valuation

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 materiality	EUR 0.4 million
How we determined it	Approximately 0.9% of revenue
Rationale for the materiality benchmark applied	We consider the Group's ability to generate revenue to be key determinant of the Group's value and a key metric used by management, investors, analysts and lenders.

Key audit matters

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

Key audit matters	*How our audit addressed the key audit matters*
Revenue recognition (Refer to Note 1 'General information and summary of significant accounting policies', Note 16 'Segments' and Note 17 'Revenue and client bonus reserve'). In 2016 the Group has recognised net revenue of EUR 47.0 million. Revenue consists mainly of retail revenue generated in shops in the amount of EUR 39.7 million and wholesale revenue from wholesale and franchise partners and e-commerce in the amount of EUR 7.1 million. In our view, the vast majority of the Group's revenue transactions are non-complex, with no judgment required to be applied in respect of the timing of revenue or amounts recorded. However, some judgment and management estimates are needed for a proper accounting in certain areas, including: • client loyalty programme; and • delivery terms and returns relating to wholesale and franchise partners. Revenue recognition requires significant time and resource to audit due to its magnitude, and is therefore considered to be a key audit matter.	We audited revenue recognition through a combination of controls testing and substantive testing. • We assessed the correctness of revenue bookings, by agreeing selected transactions in the accounting systems to supporting evidence, such as customer orders, invoices, agreements and subsequent cash receipts. • We obtained confirmations from largest customers for both annual revenue and year-end receivable balance. • We agreed a selection of retail revenue recorded in general ledger to incoming cash by retail store, day and market, validating the amounts received to bank receipts and card payments. • We tested whether all conditions to recognise revenue were met for wholesale and franchise transactions by examining sales agreements for any specific conditions, such as returns, and by examining returns and credit invoices to assess whether such transactions were recorded in a proper period. • In order to assess the impact of client loyalty programme to revenue recognition, we reviewed the appropriateness of the calculation and tested the validity of respective supporting information, including assumptions. • We obtained the list of manual journal entries impacting revenue and reviewed entries for appropriate supporting evidence. As a result of our work, we noted no material exceptions.
Inventory valuation (Refer to Note 1 'General information and summary of significant accounting policies', Note 2 'Critical accounting estimates and judgements in applying accounting policies', Note 6 'Inventories' and Note 18 'Cost of goods sold'). Inventories are carried at the lower of cost and net realisable value. As of 31 December 2016, the	We assessed the reasonableness of inventory write-downs as follows: • We obtained the Group's policies for inventory write-downs and analysed the management's previous estimates and resulting write-downs by comparing them to historical actual sales patterns. In doing so, we obtained understanding of the relationship between the ageing profile of inventory

total carrying amount of inventories was EUR 11.1 million, including EUR 0.3 million allowance for impairment.

The Group manufactures and sells fashion goods that are subject to changing consumer demands and fashion trends. Therefore, estimates are required to assess the net realisable value and the related write-down of inventory.

The estimates are based on the management's expectations regarding future sales and promotion plans as well as on historical sales patterns. The estimates are further adjusted based on post balance sheet date actual sales performance.

Due to the size and related estimation uncertainty, valuation of inventories is considered a key audit matter.

and historical actual loss rates, and validity of management estimates made in previous periods.

- We calculated our own estimate of the required write-down by applying the historical sales data to the surplus stock as at the year-end, considering the stock profile and age. We used historical data to estimate potential losses on discounted sales.
- We tested on a sample basis the ageing categorisation of inventory items to obtain comfort over the categorisation of stock used in the calculation of write-down.
- We obtained the management's expectations for future sales and their inventory management plans, and compared them with our knowledge regarding market trends.

As a result, we found that the write-downs of inventory recognised by the Group are within the range independently developed by us.

How we tailored our audit scope

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

In the Group's financial statements eight reporting units are consolidated. Based on our risk and materiality assessments, we determined the transactions and balances across the Group, which were required to be audited by the group audit team, considering the relative significance to the Group and the overall coverage obtained over each material line item in the consolidated financial statements. In limited areas where the work was performed by non-PwC component auditors, such as procedures on physical inventory counts and taxes outside Estonia, we determined the level of involvement we needed to have in the audit work at those reporting units to be able to conclude whether sufficient appropriate audit evidence had been obtained as a basis for our opinion on the Group's financial statements as a whole.

Other information

Management is responsible for the other information that is disclosed in the Group's Annual Report, in addition to the consolidated financial statements and our auditor's reports 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.

AS PricewaterhouseCoopers

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

Eva Jansen-Diener
Auditor's certificate no.501

22 March 2017

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* *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 (LOSS) ALLOCATION RECOMMENDATION

The Management Board of AS Baltika recommends the net profit for the year ended at 31 December 2016 for 177 thousand euros to allocate as follows:

Retained earnings	177
Total	**177**

DECLARATION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

The Management Board has prepared the management report and the consolidated financial statements of AS Baltika for the year ended at 31 December 2016.

The Supervisory Board of AS Baltika has reviewed the annual report, prepared by the Management Board, consisting of the management report, the consolidated financial statements, the Management Board's recommendation for profit distribution and the independent auditor's report, and has approved the annual report for presentation on the annual shareholders meeting.

Meelis Milder
Chairman of the Management Board
22 March 2017

Jaakko Sakari Mikael Salmelin
Chairman of the Supervisory Board
22 March 2017

Maigi Pärnik-Pernik
Member of the Management Board
22 March 2017

Tiina Mõis
Member of the Supervisory Board
22 March 2017

Reet Saks
Member of the Supervisory Board
22 March 2017

Lauri Kustaa Äimä
Member of the Supervisory Board
22 March 2017

Valdo Kalm
Member of the Supervisory Board
22 March 2017

AS BALTIKA SUPERVISORY BOARD

JAAKKO SAKARI MIKAEL SALMELIN
Chairman of the Supervisory Board since 23 May 2012, Member of the Supervisory Board since 21.06.2010
Partner, KJK Capital Oy
Master of Science in Finance, Helsinki School of Economics
Other assignments:
Member of the Management Board of KJK Fund SICAV-SIF,
Member of the Board of Directors, KJK Management SA,
Member of the Board of Directors, KJK Capital Oy,
Member of the Management Board, KJK Invest Oy,
Member of the Management Board of Amiraali Invest Oy.
Baltika shares held on 31 December 2016: 0

TIINA MÕIS
Member of the Supervisory Board since 03.05.2006
Chairman of the Management Board of AS Genteel
Degree in Economical Engineering, Tallinn University of Technology
Other assignments:
Member of the Supervisory Board of AS LHV Pank and AS LHV Group,
Baltika shares held on 31 December 2016: 977,837 shares (on AS Genteel account)[1]

REET SAKS
Member of the Supervisory Board since 25.03.1997
Attorney at Raidla Ellex Law Office
Degree in Law, University of Tartu
Other assignments
Member of the Management board of Non-profit organization AIPPI Estonian workgroup
Baltika shares held on 31 December 2016: 0

LAURI KUSTAA ÄIMÄ
Member of the Supervisory Board since 18.06.2009
Managing Director of Kaima Capital Oy
Master of Economics, University of Helsinki
Other assignments:
Member of the Supervisory Board of AS Tallink Grupp,
Member of the Board of Oy Tallink Silja Ab,
Member of the Board of KJK Invest Oy,
Member of the Board of Kaima Capital Eesti OÜ,
Member of the Board of Aurejärvi Varainhoito Oy,
Member of the Board of UAB Malsena Plius,
Member of the Board of UAB D Investiciju Valdymas,
Member of the Board of Bostads AB Blåklinten Oy,
Member of the Board of KJK Serbian Holdings BV,
Member of the Board of AS Baltic Mill,
Member of the Board of KJK Investicije d.o.o,
Member of the Board of KJK Investicije d.o.o 2,
Member of the Board of KJK Investicije d.o.o 3,
Member of the Board of KJK Investicije d.o.o 4,
Member of the Board of KJK Investicije d.o.o 5,
Member of the Board of KJK Investicije d.o.o 6,
Member of the Board of KJK Investicije d.o.o 7,
Vice-chairman of the Board of AAS BAN,
Vice-chairman of the Management Board of Amber Trust Management SA,
Chairman of the Management Board of Amber Trust II Management SA,
Chairman of the Management Board of KJK Fund SICAV-SIF,
Chairman of the Management Board of KJK Fund II SICAV-SIF,
Chairman of the Supervisory Board of Salva Kindlustuse AS,
Chairman of the Supervisory Board of AS PRFoods,
Member of the Supervisory Board of Managetrade OÜ,
Member of the Supervisory Board of Toode AS,
Chairman of the Supervisory Board of JSC Rigas Dzirnavnieks,
Chairman of the Board of Directors, KJK Management SA,
Chairman of the Board of Directors, KJK Capital Oy.
Baltika shares held on 31 Dec 2015: 24,590 shares (on Kaima Capital Eesti OÜ account)[1]

VALDO KALM
Member of the Supervisory Board since 20 April 2012
Chairman of the Board of Port of Tallinn
Automation and telemechanics, Tallinn University of Technology
Other assignments:
Member of the Management Board of OÜ VK CO.
Baltika shares held on 31 December 2016: 0

[1]Members of the Supervisory Board of AS Baltika own shares through the companies AS Genteel and Kaima Capital Eesti OÜ (see Corporate governance report section “Supervisory Board”).

AS BALTIKA MANAGEMENT BOARD

MEELIS MILDER
Chairman of the Management Board, Group CEO
Chairman of the Board since 1991, in the Group since 1984
Degree in Economic Cybernetics, University of Tartu
Baltika shares held on 31 December 2016: 1,013,735 shares[1]

MAIGI PÄRNIK-PERNIK
Member of the Management Board, Chief Financial Officer
Member of the Board since 2011, in the Group since 2011
Degree in Economics, Tallinn University of Technology,
Master of Business Administration, Concordia International University
Baltika shares 31 December 2016: 0

[1]The members of the Management Board of AS Baltika also own shares through the holding company OÜ BMIG (see Corporate governance report section “Management Board”).

2016 Consolidated Annual Report (in thousands of euros)

Revenues (not consolidated) by EMTAK (the Estonian classification of economic activities)

Code	Definition	2016	2015
46421	Wholesale of clothing and footwear	32,250	32,817
46151	Brokerage of furniture, other products	384	510
46191	Wholesale of other products	153	174
70221	Management and support services	0	0
14131	Other sewing services	37	36
68201	Other rental revenue	4	7
Total		**32,828**	**33,544**

* *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.*