



AS BALTIKA
2007 CONSOLIDATED ANNUAL REPORT

(translation of the Estonian original)

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Internet homepage:	www.baltikagroup.com
Main activities	Retail and wholesale of clothes
Auditor	AS PricewaterhouseCoopers
Beginning and end of financial year	01.01.2007 - 31.12.2007

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KEY FIGURES AND RATIOS

	2003	2004	2005	2006	2007
Operating results, EEK '000					
Revenue	497,048	581,878	680,906	899,481	1,151,520
Gross profit ¹	-	278,404	351,079	490,562	636,681
Operating profit	-57,464	18,786	74,907	97,332	64,554
Profit before income tax	-66,794	14,016	70,960	91,295	53,031
Net profit	-67,447	16,701	72,664	87,376	40,773
Balance sheet data, EEK '000					
Total assets	329,376	317,180	377,099	596,390	656,357
Interest-bearing liabilities	138,818	120,427	92,831	147,413	184,498
Shareholders' equity	115,165	141,470	207,952	304,240	339,346
Other data					
Number of stores	66	78	86	112	128
Sales area, m ²	10,109	11,668	12,736	19,594	24,290
Number of employees (31 Dec)	1,714	1,704	1,678	1,915	1,983
Key ratios					
Revenue growth	2.4%	17.1%	17.0%	32.1%	28.0%
Retail sales growth	25.7%	30.9%	30.1%	34.7%	34.1%
Share of retail sales in revenue	65%	72%	80%	82%	86%
Share of exports in revenue	72%	75%	71%	72%	74%
Gross margin ¹	-	47.8%	51.6%	54.5%	55.3%
Operating margin	-11.6%	3.2%	11.0%	10.8%	5.6%
EBT margin	-13.4%	2.4%	10.4%	10.1%	4.6%
Net margin	-13.6%	2.9%	10.7%	9.7%	3.5%
Current ratio	1.5	1.5	2.1	1.5	1.6
Debt to equity ratio	120.5%	85.1%	44.6%	48.5%	54.4%
Net gearing ratio	109.1%	75.9%	31.3%	44.3%	45.1%
Inventory turnover	3.02	3.89	4.92	5.38	5.30
Return on equity	-42.7%	14.6%	44.1%	35.9%	13.1%
Return on assets	-17.5%	5.1%	22.2%	18.3%	6.5%
Key share data, EEK					
Number of shares outstanding (31 Dec)	16,498,350	16,901,850	17,468,850	18,644,850	18,644,850
Weighted average number of shares	16,451,976	16,625,163	17,279,850	18,026,349	18,644,850
Share price (31 Dec)	10.95	9.70	67.80	115.78	61.02
Market capitalisation, in millions (31 Dec)	181	164	1,184	2,159	1,138
Earnings per share (EPS)	-4.10	1.00	4.21	4.85	2.19
Change in EPS, %	-1007%	125%	319%	15.3%	-54.9%
P/E	neg.	9.7	16.1	23.9	27.9
Book value per share	7.0	8.4	11.9	16.3	18.2
P/B	1.6	1.2	5.7	7.1	3.4
Dividend per share (DPS)	0	0.25	0.67	0.80	0 ²
Dividend yield	0%	2.6%	1.0%	0.7%	0% ²
Dividend payout ratio	0%	26.1%	16.6%	17.1%	0% ²

¹Comparable gross profit figures available starting from the change in the income statement format (introduced in 2005)²Proposal to the general meeting

Definitions of key ratios

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

Current ratio = Current assets/Current liabilities

Debt to equity ratio = Interest-bearing liabilities/Equity

Net gearing ratio = (Interest-bearing liabilities-Cash and bank)/Equity

Inventory turnover = Revenue/Average inventories¹

Return on equity = Net profit (attributable to parent)/Average equity¹

Return on assets = Net profit (attributable to parent)/Average total assets¹

Market cap = Share price (31 Dec)xShares outstanding (31 Dec)

EPS = Net profit (attributable to parent)/Weighted average number of shares

P/E = Share price (31 Dec)/EPS

Book value per share = Equity/Shares outstanding (31 Dec)

P/B = Share price (31 Dec)/Book value per share

Dividend yield = DPS/Share price (31 Dec)

Dividend payout ratio = Paid out dividends/Net profit (attributable to parent)

¹Based on 12-month average

MANAGEMENT BOARD'S CONFIRMATION OF THE MANAGEMENT REPORT

The management board confirms that the management report presented on pages 6 to 23 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.



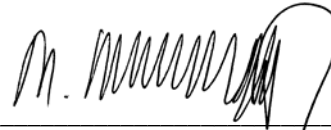
Meelis Milder
Chairman of the Management Board
25 March 2008



Ülle Järv
Member of the Management Board
25 March 2008



Boriss Loifenfeld
Member of the Management Board
25 March 2008



Maire Milder
Member of the Management Board
25 March 2008

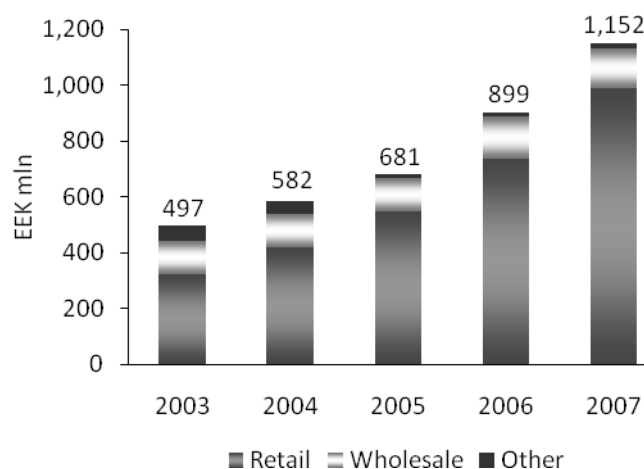
MANAGEMENT REPORT

REVENUE

Revenue by segment

EEK million	2007	2006	+/-
Retail	987.3	736.4	34.1%
Wholesale	144.7	150.6	-3.9%
Subcontracting	14.4	0	-
Other	5.1	12.5	-59.1%
Total	1,151.5	899.5	28.0%

Revenue growth 2003-2007



RETAIL

In 2007, Baltika's retail sales grew 34.1% to 987.3 million kroons, while comparable store sales climbed by 3%. Rapid growth increased the proportion of retail revenue in total consolidated revenue to 86% compared with 82% in 2006.

The retail network continued expanding and the annual average sales area grew by 50%. The average sales efficiency (sales per square metre), on the other hand, declined by 10%. Efficiency is affected by rapid expansion – new stores have more space and in the start-up period their efficiency is generally lower. Moreover, outside Baltika's home market, the Baltic countries, the start-up periods tend to be longer. In 2006 and particularly at the end of the year many new stores were opened in Russia and Ukraine, where the estimated start-up periods of new shopping centres and, consequently, new stores range from 18 to 24 months.

STORES AND SALES AREA

At the year-end, Baltika had 128 stores in seven countries and a total sales area of 24,290 square metres. During the year, 20 stores were opened, four were closed and four were relocated to larger premises in the same shopping centre. The net growth of the retail system was 16 stores and approximately 4,700 square metres, a 24% increase in the sales space operated by Baltika Group.

In terms of markets, the largest number of stores was opened in Lithuania where eight new stores were launched. In Latvia, three stores were opened and four were relocated. Three new stores were opened in Russia and Ukraine each and two in Estonia. At the end of the year, the Group entered a new market – the Czech Republic, where one new store was opened. Two stores were closed in both Russia and Ukraine.

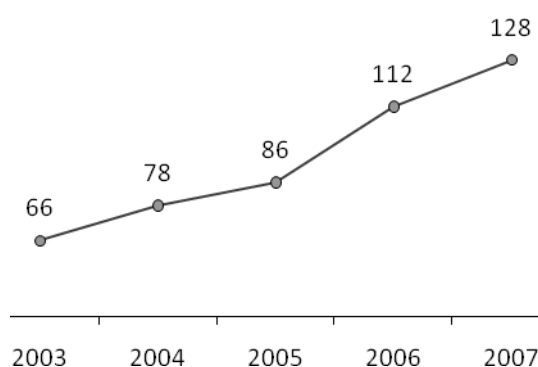
Stores by market

	31 December 2007	31 December 2006
Estonia	30	28
Lithuania	30	22
Russia	24	23
Ukraine	22	21
Latvia	16	13
Poland	5	5
Czech Republic	1	0
Total stores	128	112
Total sales area, m²	24,290	19,594

The largest number of stores was opened under the Monton and Mosaic brands. At the end of 2007, Baltika's retail network included 52 Mosaic, 50 Monton, 16 Baltman, 6 Ivo Nikkolo and 4 factory outlet stores.

Retail network by market and brand at 31 December 2007

	Monton	Mosaic	Baltman	Ivo Nikkolo	Other	Total	m ²
Estonia	6	11	5	4	4	30	4,000
Lithuania	11	11	6	2		30	5,239
Russia	12	11	1			24	5,793
Ukraine	11	10	1			22	4,208
Latvia	6	7	3			16	3,507
Poland	3	2				5	1,047
Czech Republic	1					1	496
Total	50	52	16	6	4	128	24,290

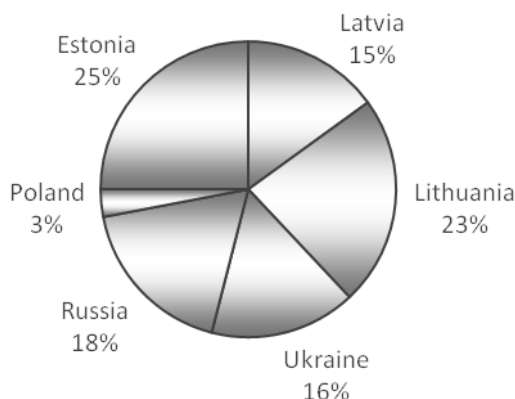
Number of stores**MARKETS**

Although in 2007 annual economic growth in the Baltic countries slowed a bit, Baltika's retail markets sustained rapid development. The GDP growth in the Baltic countries amounted to 7-10% in 2007. Baltic economies are currently in a cooling phase and are expected to hit the bottom of their economic cycle in 2008. In the past few years, Baltic economic growth has been fuelled by strong domestic demand which is also a reason for the present deceleration. Curbing of the generous credit supply and rising interest rates are reducing the growth in consumption and investment. According to analysts, Baltic economies will recover and consumption is going to revive in 2009 at the latest. Thereafter, economic growth should level off at around 6% per year. Robust economic growth for 2007 was also posted by Ukraine and Russia – according to preliminary estimates 7-8%. Similarly to the Baltics, the main growth driver of Russian economy is domestic demand, prompted by a swift rise in the construction, retail, accommodation and financial sectors. The Russian economic outlook for the near future remains positive and gross domestic product should continue growing at above 6% per year. In general, all Baltika's retail markets should continue growing at a higher pace than the so-called old Europe.

Thanks to their great potential, Central and Eastern Europe and Russia in particular are becoming increasingly popular destinations for international retail chains. In 2007, the real estate advisors of Cushman & Wakefield undertook research in order to identify international retail companies' 20 most attractive European expansion

destinations in the next five years. Moscow ranked first, followed by St Petersburg and Prague. Baltika has secured a foothold in all these cities. Other attractive destinations where Baltika is already operating include Tallinn, Kiev, Warsaw, Riga and Vilnius. In terms of countries, the most attractive destination was Russia.

Breakdown of retail sales by market – 2007



In 2007, Russia was also Baltika's fastest growing market and became the third-largest one with 18% of sales. Estonia remained the largest retail market, followed by Lithuania which in some months already outperformed Estonia. The three Baltic countries accounted for 63% of the Group's retail sales (2006: 66%) and Russia and Ukraine for a combined 34% (2006: 29%).

Retail sales by market

EEK million	2007	2006	+/-
Estonia	247.7	202.2	23%
Lithuania	231.9	178.8	30%
Russia	173.7	86.7	100%
Ukraine	156.8	128.5	22%
Latvia	144.7	105.7	37%
Poland	29.8	34.5	-14%
Czech Republic	2.7	0	-
Total	987.3	736.4	34%

Sales space grew the most in Latvia and Lithuania. In Lithuania, Baltika opened the largest number of new stores (eight), increasing the sales area by 43%, and launched its Ivo Nikkolo concept, which was previously operated in Estonia only. Now there are Ivo Nikkolo stores also in Vilnius and Kaunas. Expansion will continue in 2008 and 2009 when several new shopping centres are completed. In 2007, Baltika's retail sales in Lithuania totalled 231.9 million kroons, a 30% improvement on the prior year.

The strongest retail growth in the Baltics was achieved in Latvia where sales expanded by 37% to 144.7 million kroons. In the Latvian market, three stores were opened and four were relocated and the total sales area grew by 73%. Mostly Monton stores were transferred to larger premises where a full collection of the line can now be offered. Baltika's largest, 603-square metre Monton store is also located in Riga. Thanks to the expansion, the biggest city in the Baltics is better covered with Baltika's brands and the stores are more visible among the competition. At the end of the year, the Group opened two stores in yet another Latvian city – Valmiera.

In Estonia, retail sales amounted to 247.7 million kroons, up 23% year-over-year (hereinafter "yoy"). During the year, two new stores were launched including a new-concept Ivo Nikkolo store in Viru Centre in Tallinn.

In Russia, Baltika's retail sales grew by 100% to 173.7 million kroons in 2007. Rapid growth may be attributed to significant expansion in 2006. As the start-up periods of new stores proved longer than average, Baltika focused on enhancing the efficiency of its existing stores. During the year, three stores were opened and two closed. In 2008, Baltika will continue streamlining the store network in Russia. Further expansion will be based on two brands, Monton and Mosaic, and aimed at two metropolises – Moscow and St Petersburg. Despite the above strategy, in 2008 Baltika is going to expand to Kaliningrad. Although in 2007 Baltika's development in

Russia was hampered by political tensions in Russian-Estonian relations, caused by the events in Tallinn in April, Russia remains a market with huge potential. In the next few years, Russia will be the most attractive expansion destination for all major international retailers because the market is enormous and consumption is on the rise.

Baltika's retail sales in Ukraine rose by 22% to 156.8 million kroons. Ukrainian results were adversely affected by the country's political instability and high inflation which have cooled consumption outside the capital. Only six out of the Group's 22 Ukrainian stores are in Kiev, the reason being that in the past few years no large modern shopping centres have been opened there. Nor were any attractive shopping centres opened in 2007 in other Ukrainian cities targeted by the Group. In 2007, Baltika opened three and closed two stores in Ukraine. As a result, the sales area remained practically unchanged. In 2008, the development situation is going to improve and the Group expects to launch some new stores.

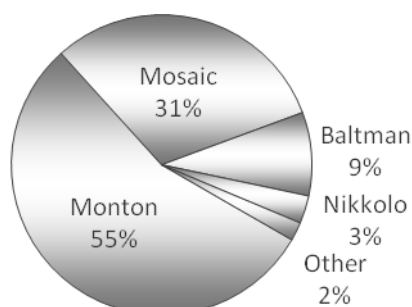
In Poland, the positive developments that began in 2006 continued. Although total sales decreased by 14% owing to the closure of inefficient stores, comparable store sales improved by 8% in 2007 and the Group's retail sales in Poland totalled 29.8 million kroons. No new stores were opened and in the forthcoming periods Baltika will focus on improving the efficiency of its existing stores.

In 2007, Baltika penetrated a new retail market – the Czech Republic. At the end of October, a 500-square metre Monton store was launched in the Palladium Centre in Prague. The centrally located Palladium is the newest shopping and business centre in the Czech capital. Competition in the market is strong but Monton has got off to a good start – in terms of sales the recently launched store is among the ten best in the Group. The strategy for the Czech market is gradual expansion. Two new store openings are planned for 2008.

BRANDS

In terms of brands, the largest contributor is Monton which in 2007 accounted for 55% of the Group's retail sales. Other major brands, Mosaic and Baltman, generated 31% and 9% of retail sales respectively while Ivo Nikkolo which was acquired in 2006 accounted for 3%. The remaining 2% was generated by factory outlets.

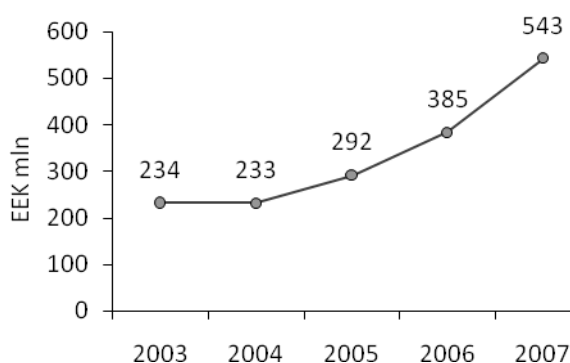
Breakdown of retail sales by brand – 2007



Monton

In 2007, Monton turned five years old. Within that time, Monton has evolved into a successful international fashion brand. In 2007, retail sales of Monton totalled 543 million kroons, up 41% yoy, rendering it the Group's fastest growing brand both in terms of sales and retail space. The largest sales growth was achieved in Russia which became Monton's largest market, outstripping Estonia and Lithuania, the former largest retail markets. Over the year, Monton's retail portfolio was supplemented with ten stores with an upgraded retail environment, which increased the total number of Monton stores to 50.

Retail sales – Monton



In 2007, Monton launched two new product groups. In the second half of the year, the collection was supplemented with footwear and the jean brand Spiced M was launched. The pilot season in footwear sales was a success, providing valuable experience for the future. Sales of lingerie and beachwear, which were launched in 2006, doubled. All this shows that Monton can successfully launch new product groups and its customers accept them readily.

In addition to trendy products, Monton is committed to delivering excellent customer care, a relaxing shopping environment, and innovation in communication. During the year, Baltika's interior designers developed various exciting solutions for Monton's retail environment. In June, Monton launched men's underpants with a condom pocket, in August a jean exhibition was organised, and in October customers could admire fashion photos shot in the sky – all examples of innovative marketing solutions.

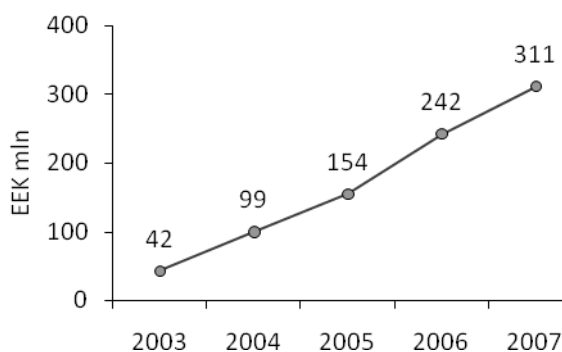
In 2008, Monton is going to focus on sustaining profitable expansion, improving the efficiency of new product groups, and enhancing the efficiency and effectiveness of intra-brand efforts.

Mosaic

For Mosaic brand, the year 2007 was one of refocusing. The first full year under the new name ended in February, marking the time for further specifying the brand's identity and aims. The most important step was repositioning – the brand was more clearly focused on the needs of its target customer.

In 2007, retail sales of Mosaic totalled 311 million kroons, a 29% improvement on 2006. Sales growth stemmed from an increase in the number of stores, the development of the base collections, and the launch of a children's collection. The largest growth occurred in the sales of the men's collection, indicating that the direction of the collection has met with the customer's approval.

Retail sales – Mosaic



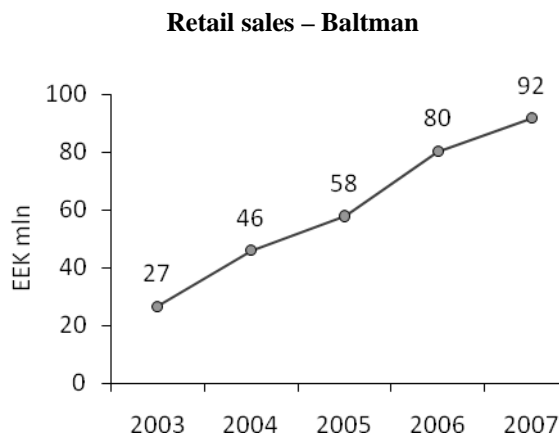
In April, Mosaic launched childrenswear. By the year-end, the collection was available at eleven largest stores, mostly in the Baltic market. Although in the first year, the children's collection accounted for 2% of Mosaic sales, the figure should rise considerably. Together with the children's collection, Mosaic launched its sub-brand Lotte by Mosaic which includes a range of children's clothes and accessories named after the highly popular Estonian cartoon character Lotte. The Lotte by Mosaic collection is especially popular in the Estonian market but the Group expects to increase sales of the sub-brand also in Latvia and Lithuania.

In 2007, Mosaic opened nine new stores taking the total number of stores to 52. In view of the growth of the brand and the development of the store environment, new stores are more spacious, allowing better display of the collections.

The main objective for 2008 is to develop a new store environment which would strengthen the position of the brand in international fashion retailing. The main development efforts will be related to the children's collection, including the Lotte by Mosaic collection.

Baltman

Baltman is Baltika's oldest brand whose motto is to develop with the customer. In 2007, retail sales of Baltman amounted to 92 million kroons, up 14%. During the year, Baltman opened two new stores in Lithuania, increasing the total number of its stores to 16.



In the area of product development, a lot of effort was put in adjusting Baltman's suits to different types of figure and extending the range for the younger customer. Special attention was paid to the quality of inside works, fabrics and finishing. The travel line with its innovative nano-finishing has been extremely well received. In 2007, Baltman also launched suits made of the thermo-regulating Klimeo fabric.

Baltman's aim is to be not only a clothes store but also a reliable businesswear advisor in all the markets where it operates. In 2008, Baltman will focus on sustaining the qualitative development of the collection. The keywords will be innovation, efficiency and reliability.

Ivo Nikkolo

For Ivo Nikkolo, 2007 was the first full year with Baltika Group. Retail sales of the brand totalled 25 million kroons. The main goal was to develop an internationally competitive collection. In the premium segment where Ivo Nikkolo is competing, product quality is essential. Therefore, the focus was on developing women's formal wear by combining the strengths of Baltika's existing production base, quality fabrics and the designers' brand specific style.

The highlight of the year was the opening of Ivo Nikkolo stores outside Estonia. Two of the three new stores were opened in Lithuania while one was launched in Estonia. All new stores boast a completely new, specially developed retail concept, which bears more resemblance to a lounge than a store. The purpose was to create a relaxing, attractive, customer-focused atmosphere. The tenants' association of Viru Centre named the store opened in Viru Centre, Tallinn the most customer-friendly shopping environment in the whole shopping centre.

In 2008, Ivo Nikkolo will continue developing the collection. Top quality and designer style at a reasonable price will undoubtedly increase the brand's customer base.

WHOLESALE

Wholesale of Baltika's collections accounted for 13% of the Group's consolidated revenue for 2007, yielding 144.7 million kroons and posting a 3.9% decrease. The decline in wholesale revenue was planned, stemming from stricter sales policy in relations with Baltika's Russian partner. One of Baltika's largest wholesale partners is a Russian company which operates approximately 30 stores in Siberia and the Ural area which carry Baltika's brands. Other wholesale partners include department stores in Finland and the Baltic countries, such as Stockmann and Tallinn Department Store. Department stores are sold mostly Mosaic, Baltman and Ivo Nikkolo collections whereas Mosaic accounts for approximately one half of Baltika's wholesale revenue. Monton products are sold to the Russian business partner only.

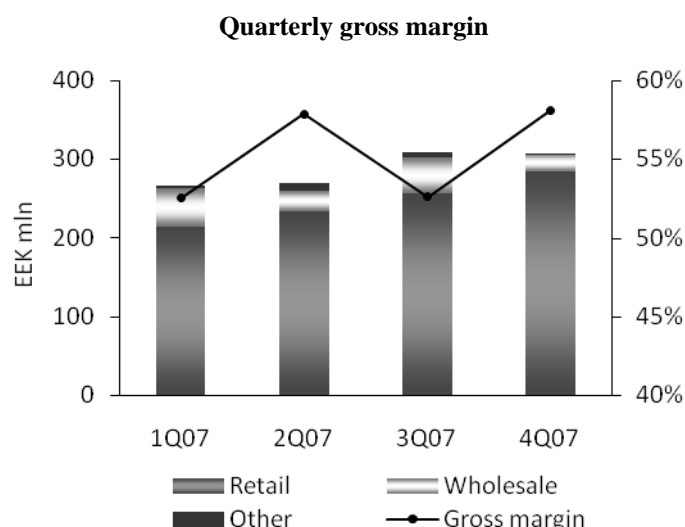
EARNINGS AND MARGINS

The year 2007 was the second one in the Group's three-year strategy period, following the rapid expansion of 2006. A comparison of the two years' opening and closing figures indicates that in 2006 the Group's sales area expanded abruptly, especially in the last quarter. However, the growth in the average sales space which has to be operated and supplied with inventories was substantially larger in 2007 – 50% against 30% in 2006. Consequently, the impacts of expansion were stronger in 2007.

The impacts of rapid expansion are the following: the sales efficiency of new stores is usually lower than that of established ones and a relatively large proportion of new stores in the overall store portfolio weaken the average sales efficiency. In addition, Baltika's average sales efficiency is affected by the expansion of its store formats. In 2007, the Group's average sales efficiency, i.e. sales per square metre declined by 10%. At the same time, the stores generate full operating expenses, putting pressure on the Group's profitability. In 2006, the Group expanded rapidly in the Russian and Ukrainian markets where the start-up periods of new stores are longer and store operating expenses are higher than in the Baltics. In addition to expense growth triggered by the enlargement of the Group's sales space, the average store operating expenses per square metre grew by 7% (including rental expenses per square metre rise of 13%) on account of an increase in the proportion of the Russian retail system in the Group's store portfolio. An enlargement in sales space does not only add to the operating expenses of stores but requires also a larger team at the head office while sustained growth assumes constant financing of new projects.

2007 proved a year of adjustment as the Group focused on improving the efficiency of its existing retail system. New stores were launched at a more moderate pace and the number of new stores opened in Russia and Ukraine was reduced significantly – to six altogether. The Baltic countries posted strong development in the first half of the year but the second half-year brought a decrease in the growth of consumption, affecting also Baltika's sales in those markets. Existing stores in Poland followed a positive trend, ending the year in a profit.

The Group succeeded in raising the gross margin for 2007 to 55.3% (2006: 54.5%). Consolidated gross profit for 2007 amounted to 636.7 million kroons, a 29.8% improvement on the prior year.



Distribution costs for 2007 grew by 49.1% and the period's administrative and general expenses by 26.0%. Administrative and general expenses in 2007 included also non-recurring costs of 3.81 million kroons incurred in connection with the relocation of manufacturing operations to a new factory.

The Group's results were adversely affected by exchange rate fluctuations – the period's other operating expenses include foreign exchange losses of 9.94 million kroons. In 2006, foreign exchange losses totalled 4.71 million kroons.

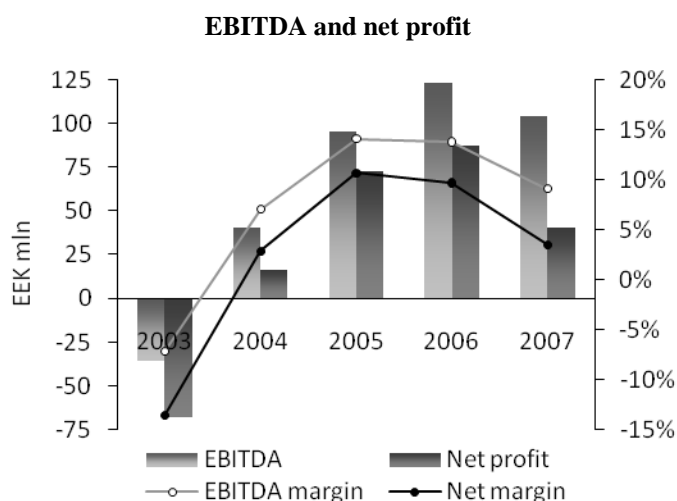
Consolidated operating profit for 2007 includes gains from sale of non-current assets and revaluation of investment property of 24.25 million kroons recognised in other operating income. Sales of non-current assets generated gains of 15.36 million kroons and property revaluation gains amounted to 8.89 million kroons. In 2006, gains from sale of non-current assets and revaluation of investment property totalled 11.82 million kroons.

The Group's operating margin for 2007 was 5.6% compared with 10.8% for 2006. Consolidated operating profit amounted to 64.6 million kroons, 33.7% down from the prior year.

Consolidated financial expenses for 2007 totalled 11.5 million kroons, a 90.9% rise on 2006. The largest financial expense item was interest expense (9.0 million kroons), which increased by 57.9% yoy. The growth in interest expense may be explained by an increase in the loan burden as well as a rise in Euribor. Financial expenses were also increased by a change in foreign exchange losses.

The Group's profit before income tax amounted to 53.0 million kroons, 41.9% down from 2006. Consolidated net profit for 2007 (profit after tax and minority interest) amounted to 40.8 million kroons, a 53.3% decrease compared with 2006. The Group's net margin for 2007 was 3.5% (2006: 9.7%).

In 2007, the Group's return on equity was 13.1% (2006: 35.9%) and return on assets was 6.5% (2006: 18.3%).



BALANCE SHEET

At 31 December 2007, Baltika's consolidated balance sheet total was 656.4 million kroons, a 10% increase yoy.

During the year, the Group's trade receivables decreased by 15.3 million kroons to 71.1 million kroons. The decline resulted mainly from a reduction in sales to the Russian wholesale partner, a measure adopted for hedging the Russian risks. Trade payables followed a similar trend, declining by 24.2 million kroons to 72.3 million kroons at the year-end.

At 31 December 2007, the Group's inventories totalled 220.7 million kroons, up 20.0 million kroons or 10% yoy. Inventory management efficiency remained almost stable – the period's inventory turnover ratio was 5.30 (2006: 5.38).

At the year-end, the Group's borrowings totalled 184.5 million kroons, including bank loans of 145.5 million kroons. The remainder of borrowings was made up of bonds (29.7 million kroons) and finance lease liabilities (9.3 million kroons). During the year, the Group's total debt burden increased by 37.1 million kroons; bank loans

grew by 40.4 million kroons. Borrowings increased in connection with investments made in the expansion of the retail system and the financing of operating activities.

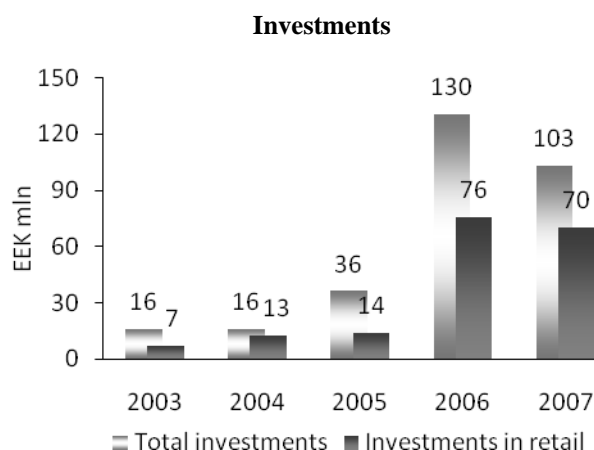
At 31 December 2007, the Group's net debt (interest-bearing liabilities less cash and bank balances) equalled 153.0 million kroons and the net debt to equity ratio was 45.1% against 44.3% at the end of 2006.

In the reporting period, the Group's equity grew by 35.1 million kroons to 339.3 million kroons. The equity structure changed in connection with a bonus issue performed to increase share capital at the expense of retained earnings and share premium. As a result of the bonus issue, share capital increased by 124.3 million kroons to 186.4 million kroons.

INVESTMENTS

In 2007, the Group's investments totalled 102.9 million kroons. The corresponding figure for 2006 was 130.4 million kroons.

Investments in the retail system and information technology amounted to 69.9 million kroons and 13.6 million kroons respectively while investments in manufacturing totalled 12.8 million kroons. Repurchase of the 50% share in joint venture OÜ Baltika Tailor cost 5.6 million kroons. Investments in other fixed assets amounted to 1.0 million kroons.



CASH FLOWS

In 2007, consolidated cash flows from operating activities grew by 23.5 million kroons to 53.7 million kroons. Cash generated by operating activities was used to purchase property, plant and equipment and intangible assets whose acquisition was also financed with proceeds from the sale of property, plant and equipment. Altogether, net cash used in investing activities amounted to 45.8 million kroons. In 2006, net cash used in investing activities amounted to 96.7 million kroons.

In order to finance its business operations, the Group increased bank loans, used overdraft facilities and issued bonds. In 2007, bank loan repayments totalled 25.7 million kroons. In addition, shareholders were distributed dividends of 14.9 million kroons. Net cash raised by financing activities equalled 13.3 million kroons against 54.0 million kroons in 2006.

The Group's net cash flow for 2007 increased cash and cash equivalents by 18.9 million kroons. In 2006, cash flows resulted in a 13.4 million kroon decrease in cash and cash equivalents.

MANUFACTURING

At the end of 2007, Baltika Group included two manufacturing companies: OÜ Baltika Tailor (100%) and AS Virulane (82.66%). In 2007 Baltika continued tightening control over its manufacturing operations and combined two entities – OÜ Baltika Tailor and AS Elina. Manufacturing characterised by high quality, flexibility and prompt response to new requirements is an important part of the vertical business model of Baltika Group which is otherwise focused on the retail business.

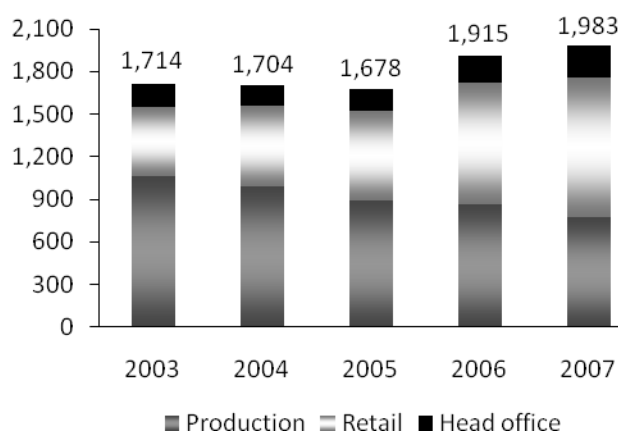
In autumn 2007, the new sewing factory of Baltika Tailor was completed. Owing to its special design, the state of the art factory is the most modern sewing facility in the Baltics. The sewing factory was the last part of the Group's manufacturing and logistics operations which was transferred from Tallinn's city centre to Lasnamäe Industrial Park in the suburbs of Tallinn. Previously, in the summer of 2006, a new higher-capacity logistics centre was opened in the same location. The new complex where logistics and manufacturing are connected allows Baltika to respond to changes in market demand with greater speed and efficiency.

PERSONNEL

At the end of 2007, Baltika Group employed 1,983 (31 December 2006: 1,915) people, including 986 (857) in the retail system, 773 (866) in manufacturing and 224 (192) at the head office. During the year, the number of employees grew by 68. The largest growth occurred in the retail system (+129). The number of people employed in manufacturing, on the other hand, declined in connection with the launch of the new factory and the restructuring of manufacturing operations. The period's average number of employees was 1,982 (2006: 1,777).

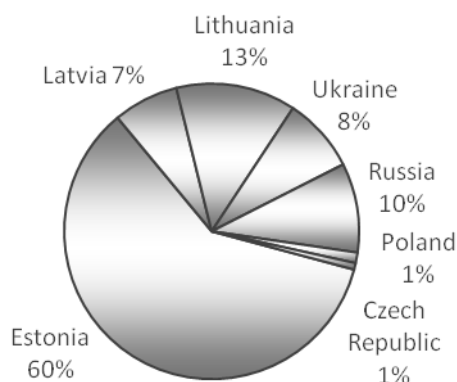
The Group's employee remuneration expenses for 2007 totalled 200.1 million kroons (2006: 137.5 million kroons). The remuneration of members of the supervisory council and management board amounted to 4.8 million kroons (2006: 6.1 million kroons).

Number of employees



At the end of 2007, 40% of the Group's employees were working outside Estonia. The proportion of people employed in Estonia is higher because the head office and manufacturing facilities are located here.

Breakdown of personnel by country – 31 December 2007



To sustain rapid development, a number of successful recruitment projects were performed Group-wide, despite the complicated situation in the labour market. One of the most important ones involved penetrating a new market (the Czech Republic), creating a local organisation and hiring and training store staff in that market. In connection with the launch of a new sewing factory in Lasnamäe Industrial Park, Baltika mounted a large-scale recruitment campaign and found employees for more than fifty new jobs.

The Group's people management strategy for 2006-2008 foresees, among other things, setting up an in-house training system for various internal interest groups. A major step in that direction was the creation of a training program and lecture cycle Retail Academy in 2007. Retail Academy aims at providing the staff with deeper insight into international fashion retailing and Baltika's business processes and their interrelation. In 2008, Retail Academy will focus on developing and enhancing management competencies.

The service and sales trainings conducted by Baltika's in-house trainers for new staff in all the Baltic markets form an integral part of the Group's training and development activities. Once a year, service quality is measured using mystery shopping including test purchases to determine whether a store's service quality complies with the corporate standards and brand values.

OUTLOOK AND GOALS FOR 2008

The year 2008 is the last one in Baltika's three-year strategy period aimed at achieving rapid and profitable growth. At the beginning of 2006, the following financial targets were set for 2008:

- a two-fold increase on the sales of 2005, i.e. revenue of 1.36 billion kroons;
- gross margin at least 52%;
- return on equity at least 30%.

Other keywords of 2008 are efficiency improvement, especially in large markets such as Russia and Ukraine, restoring rapid growth in the retail system in the second half of the year, and real estate development. Because of the company's current development phase, the year may be divided into two parts which have the following goals and prospects:

1) Sales and sales area

- The main objectives of the first half-year are to improve sales efficiency and to streamline the store portfolio. Around five to six stores will be opened and closed so that at the end of the period the number of stores will remain similar to the end of 2007. Retail revenues are expected to increase by 10-12% whereas wholesale revenues should decline by 15-20% yoy.
- In the second half of the year, rapid retail growth should be restored: the Group intends to open 14-18 stores, retail revenues should grow at the rate of 20-25% and wholesale revenues should remain at the level of the prior year.
- The revenue target for 2008 is 1.3 billion kroons, up 13%, which practically corresponds to the target set in 2006.
- At the end of 2008, the number of stores will be 140-145. Although the figure does not comply with the target (160+), the new stores have a larger format than planned at the beginning of 2006 and the 2008 year-end sales area with its approximately 28,000 square metres corresponds to the Group's target.
- While continuing expansion in Central and Eastern Europe, the Group will prepare for the penetration of new markets.

2) Profitability

- The gross margin reached the targeted level (54.5%) in 2006 and continued rising in 2007 (55.3%). The Group will focus on improving the margin in a situation where input prices are on the rise owing to an increase in raw materials prices and logistics expenses.
- Due to slower than expected development in the second half of 2007 and the first half of 2008, in the core business the targeted return on equity can not be achieved.

3) Real estate development

- In 2008, the Group began developing its city centre property at Veerenni 24, Tallinn, Estonia. In phase I, which should be completed in May 2009, the former factory building will be transformed into a business centre with approximately 10,000 square metres of office, commercial and service space. Baltika will occupy up to 4,500 square metres of the new centre for its head office and retail premises. The rest of the space as well as Baltika's current head office will be let. The company expects to earn income in connection with an increase in the value of the property.

4) Investments

- According to plan, in 2008 the largest investments will be made in the development of phase I in Baltika's business centre and the opening of new stores.

BALTIKA SHARE

The Baltika share has been listed on the Tallinn Stock Exchange since 5 June 1997. The Tallinn Stock Exchange is a member of OMX Group, which owns and operates exchanges in Estonia, Denmark, Sweden, Finland, Latvia, Lithuania and Iceland.

All Baltika shares are ordinary shares which carry equal voting and dividend rights.

Baltika does not have an official market maker for its shares. In January 2008, only two companies listed on the Tallinn Stock Exchange had entered into market maker agreements. The rules enforced in 2005 require newly listed companies to conclude the agreement for a certain period while companies whose shares have been publicly traded for a longer time are not subject to this requirement. Moreover, Baltika has the largest proportion of free-float stock (approx 70%) among companies listed on the Tallinn Stock Exchange.

Information on the shares

OMX symbol: BLT1T

ISIN number: EE3100003609

Minimum number of shares to trade: 1

Number of shares: 18,644,850

Nominal value of a share: 10 kroons

Votes per share: 1

Key share data

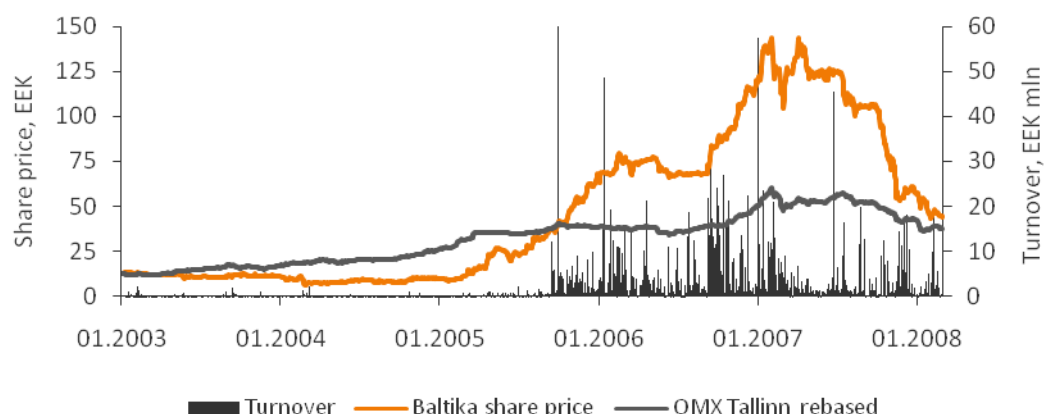
EEK	2003	2004	2005	2006	2007
Number of shares outstanding (31 Dec)	16,498,350	16,901,850	17,468,850	18,644,850	18,644,850
Weighted average number of shares	16,451,976	16,625,163	17,279,850	18,026,349	18,644,850
Share price (31 Dec)	10.95	9.70	67.80	115.78	61.02
Market capitalisation, in millions (31 Dec)	181	164	1,184	2,159	1,138
Earnings per share (EPS)	-4.10	1.00	4.21	4.85	2.19
P/E	neg.	9.7	16.1	23.9	27.9
Book value per share	7.0	8.4	11.9	16.3	18.2
P/B	1.6	1.2	5.7	7.1	3.4
Dividend per share (DPS)	0	0.25	0.67	0.80	0 ¹
Dividend yield	0%	2.6%	1.0%	0.7%	0% ¹
Dividend payout ratio	0%	26.1%	16.6%	17.1%	0% ¹

¹Proposal to the general meeting

SHARE PRICE AND TRADING

In 2007, Baltika's share price decreased by 47.3% to 61.02 kroons and the Group's year-end market capitalisation stood at 1.1 billion kroons. During the same period, OMX Tallinn All-Share Index fell by 13.3%.

Share price and turnover



In the past couple of years, the liquidity and trading activity of Baltika's share have improved significantly. This may be attributed to the company's successful transformation from a clothing manufacturer into a fashion retailer and the exit of a long-term strategic investor, Baltic Republics Fund, in the second half of 2005. The Fund divested of its 34.6% interest by a direct placement to a number of international institutional investors, a development which considerably diversified Baltika's investor base.

Trading history

EEK	2003	2004	2005	2006	2007
High	13.30	10.95	67.80	116.83	149.69
Low	10.01	6.05	8.34	62.06	52.42
Year-end price	10.95	9.70	67.80	115.78	61.02
Change, %	-10.6%	-11.4%	598.9%	70.8%	-47.3%
Traded volume	2,193,111	2,000,751	13,209,708 ¹	14,726,412	8,384,256
Turnover, in millions	25.7	16.1	486.3 ¹	1,138.3	837.9

¹Includes the sale of Baltic Republics Fund's shareholding of 6.0 million shares for 216 million kroons

INDICES

The Nordic and Baltic exchanges of OMX Group use the same index structure. The 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 have a base value of 100 and a base date of 31 December 1999. The base date for OMX Tallinn is 3 June 1996. The composition of tradable and benchmark indices is revised twice a year based on the trading activity of the shares.

At the end of 2007, the Baltika share was part of the following OMX indices:

Index	Description	Type	Short name
OMX Tallinn GI	OMX Tallinn all share index	Gross index	OMXTGI
OMX Baltic PI	Baltic all share index	Price index	OMXBPI
OMX Baltic GI	Baltic all share index	Gross index	OMXBGI
OMX Baltic Benchmark PI	Baltic benchmark index	Price index	OMXBBPI
OMX Baltic Benchmark GI	Baltic benchmark index	Gross index	OMXBBGI
OMX Baltic Benchmark Cap PI	Capped Baltic benchmark index	Price index	OMXBBCAPPI
OMX Baltic Benchmark Cap GI	Capped Baltic benchmark index	Gross index	OMXBBCAPGI
OMX Baltic Consumer Discretionary PI	Baltic sector index	Price index	B25PI
OMX Baltic Consumer Discretionary GI	Baltic sector index	Gross index	B25GI

SHAREHOLDER STRUCTURE

At the end of 2007, Baltika had 1,150 shareholders. The number of shareholders increased by 2% over the year.

The largest shareholder is OÜ BMIG, a company owned by Baltika's management board members, which at 31 December 2007 held 22.85% of Baltika's share capital. At the same date, the management board members' direct and indirect holdings accounted for 29.64% of Baltika's share capital.

The full list of shareholders is available on the website of the Estonian Central Register of Securities (www.e-register.ee).

Major shareholders at 31 December 2007

	Number of shares	Holding
BMIG OÜ	4,261,120	22.85%
Morgan Stanley & Co Incorporated Equity Client Account	1,545,000	8.29%
Svenska Handelsbanken Clients	1,160,500	6.22%
Skandinaviska Enskilda Banken Ab Clients	989,600	5.31%
Clearstream Banking Luxembourg S.A. Clients	987,193	5.29%
Hansabankas Clients	975,101	5.23%
Raiffeisen Zentralbank Österreich AG Clients	841,200	4.51%
Meelis Milder	741,549	3.98%
Tõnis Kotkas	685,000	3.67%
Bank Austria Creditanstalt AG Clients	398,510	2.14%
SEB Eesti Ühispank AS Trading	319,170	1.71%
State Street Bank/Allianz RCM Global Small-Cap Fund	286,770	1.54%
Other	5,454,137	29.25%
Total	18,644,850	100%

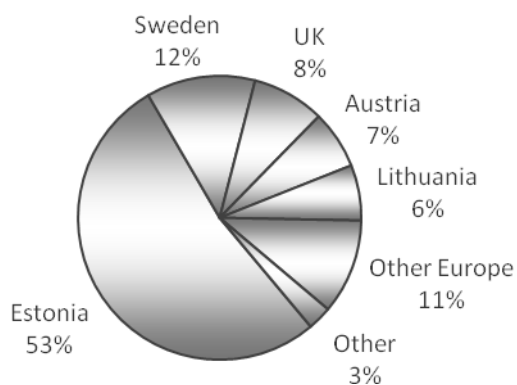
Other major shareholders include international investment funds who usually keep their investments in foreign banks' client accounts. Individuals hold approximately 19% of the shares. Around half of the shareholders are local, most of the rest come from European countries.

Shareholder structure by shareholder type at 31 December 2007

	Number of shares	Holding
Management board members	5,526,688	29.64%
Legal persons, thereof	9,646,208	51.74%
Investment funds and banks' client accounts	8,415,236	45.13%
Other legal persons	1,230,972	6.60%
Individuals	3,471,954	18.62%
Total	18,644,850	100%

Shareholder structure by size of holding at 31 December 2007

Holding	Number of shareholders	Percentage of all shareholders	Number of shares	Percentage of votes held
> 10%	1	0.09%	4,261,120	22.85%
1.0 - 10.0%	16	1.39%	10,120,544	54.28%
0.1 - 1.0%	46	4.00%	2,726,238	14.62%
< 0.1%	1,087	94.52%	1,536,948	8.24%
Total	1,150	100%	18,644,850	100%

Shareholder structure by country at 31 December 2007

SHARE CAPITAL

In June 2007, Baltika arranged a bonus issue with a view to making its share more attractive for retail investors. All shareholders were issued two new shares per each share held and the share price was split by three. As a result of the issue, the number of shares outstanding increased from 6,214,950 to 18,644,850 and share capital grew by 124,299,000 kroons to 186,448,500 kroons.

The annual general meeting of 2007 which convened on 21 May approved a convertible bonds program for the company's executive management. It was decided that the executive management would be issued a total of 124,000 convertible bonds: 62,000 E bonds in 2007 and 62,000 F bonds in 2008. Each bond entitles the holder to subscribe for three shares in the company. As a result of the subscription, Baltika's share capital may be increased by a maximum of 372,000 new shares (2.0% of the current number of shares outstanding).

The terms and conditions of the convertible bonds are provided in the resolutions of the annual general meeting of 2007. Further information on the bonds can be found in note 26 to the consolidated financial statements.

For a share issue to be approved, at least two thirds of the votes represented at the general meeting have to be in favour. According to the Articles of Association, the company's maximum share capital is 400 million kroons.

Changes in share capital

Date	Issue type	Issue price EEK	Number of shares issued	Total number of shares	Share capital at par value EEK '000	Share premium EEK '000
31.12.2002				5,444,450	54,445	41,665
20.02.2003	Conversion of A-bonds into shares	25.00	15,500	5,459,950	54,600	41,898
30.07.2003	Conversion of A-bonds into shares	25.00	39,500	5,499,450	54,995	42,490
31.12.2003				5,499,450	54,995	42,490
15.07.2004	Conversion of A-bonds into shares	25.00	88,000	5,587,450	55,875	43,810
16.12.2004	Conversion of A-bonds into shares	25.00	46,500	5,633,950	56,340	44,508
31.12.2004				5,633,950	56,340	44,508
17.05.2005	Conversion of B-bonds into shares	34.09	189,000	5,822,950	58,230	49,061
31.12.2005				5,822,950	58,230	49,690
30.03.2006	Conversion of C-bonds into shares	37.57	192,000	6,014,950	60,150	55,298
5.10.2006	Conversion of D-bonds into shares	28.95	82,400	6,097,350	60,974	56,860
8.12.2006	Conversion of D-bonds into shares	28.95	117,600	6,214,950	62,150	59,088
31.12.2006				6,214,950	62,150	59,088
11.06.2007	Bonus issue	n/a	12,429,900	18,644,850	186,449	0
31.12.2007				18,644,850	186,449	0

DIVIDENDS

In view of the Group's objectives for the forthcoming periods, the maximum dividend payout ratio has been set at 25% of net profit for the period. The actual ratio will be determined based on the Group's cash flows, development prospects and funding needs.

Baltika ended 2007 with a consolidated net profit of 40.8 million kroons. The management board proposes that profits be retained and no dividends distributed this year. In 2007, Baltika distributed a dividend of 0.80 kroons per share, i.e. 14.9 million kroons or 17.1% of the net profit for 2006.

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

CORPORATE GOVERNANCE REPORT

The Corporate Governance Code (CGC) of the Tallinn Stock Exchange is a set of rules and principles which is designed, above all, for listed companies. Since the provisions of CGC are recommendations by nature, the company need not observe 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.

AS Baltika adheres to all applicable laws and regulations. As a public company, Baltika also observes the rules of the 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, our corporate governance report contains information on the annual general meeting of 2007, the supervisory council, management board and explains Baltika’s governance structure and processes.

CGC Article 2.2.1.

The chairman of the supervisory council shall conclude a contract of service with each member of the management board for discharge of their functions.

Members of Baltika’s management board are responsible for strategic areas and their duties are not limited to the ones provided in the Commercial Code and the company’s Articles of Association (management and representation of the company). Therefore, the company has concluded employment contracts with members of the management board, not contracts of service. The Chairman of the Management Board Meelis Milder is the Group’s CEO, Ülle Järv the CFO, Maire Milder the Director of the Retail Division and Boriss Loifenfeld the Director of Wholesale and CIS Projects.

CGC Article 2.2.7.

The basic salary, performance pay, severance package, and other 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 the website of the issuer and in the corporate governance report. Information 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 provided to members of the supervisory council and management board in the management report section of its interim and annual reports. In 2007, the figure amounted to 4.8 million kroons. The contractual severance benefits of members of the management board range from 6- to 12-fold monthly remuneration.

Members of the management board, like other employees, are eligible to performance pay in accordance with the company’s bonus scheme, which is based on the performance of profit centres. The maximum bonus level for the chairman of the management board/CEO is 1.5% of the company’s net profit for the financial year although the actual disbursement may not exceed one annual salary. The bonuses of other members of the management board/directors are linked to the performance of their respective profit centres but the actual disbursements may not exceed one half to two thirds of their annual salary. Annual bonuses are paid in three portions. Two payments are made in advance and the final one is calculated and made after the financial statements have been audited. The bonus of the chairman of the management board/CEO is determined by the supervisory council. The bonuses of members of the management board are determined by the chairman of the supervisory council based on a proposal made by the chairman of the management board.

Members of the management board, similarly to all executives working under a director’s contract, are eligible to one funded pension contribution of up to one month’s salary per year, provided 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. Members of the management board have participated in the convertible bond (option) programs arranged for Baltika’s employees and are eligible to do so in the future.

In 2007, members of the management board participated in a convertible bond program designed for the company's top and middle management, which was approved by the annual general meeting in 2007. The terms and conditions of the bonds are provided in the resolutions of the annual general meeting. Changes in management board members' interests in the company are disclosed in the company's share register, which is available on the website of the Estonian Central Register of Securities (www.e-register.ee), as well as in the company's interim and annual reports.

CGC Article 3.2.5.

The remuneration of a member of the supervisory council (amount and disbursement procedure) shall be disclosed in the issuer's corporate governance report. Basic and additional remuneration (severance and other monetary benefits) shall be disclosed separately.

The annual general meeting of 2006 passed the motion that the emoluments of members of the supervisory council should remain the same as decided by the extraordinary general meeting of 8 December 2004. The remuneration of the chairman of the supervisory council amounts to 10 thousand kroons per month and the remuneration of a member of the supervisory council to 6 thousand kroons per month. A member of the supervisory council is not eligible to severance compensation or any other monetary benefits.

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 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 which has been made public, including presentations made at meetings, is available on the company'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 not currently 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 the company's Articles of Association, the auditor(s) is (are) appointed by the general meeting for the performance of a single audit or for a specific term. The annual general meeting which convened on 21 May 2007, appointed AS PricewaterhouseCoopers as the auditor of the company's annual financial statements for 2007. According to the audit agreement, the engagement partner is Urmas Kaarlep and the engagement manager Eva Jansen. The audit fee is fixed in an agreement which is concluded by the management board. The company ensures the auditor's independence by rotating the engagement partner and engagement manager every five years.

GOVERNANCE PRINCIPLES AND ADDITIONAL INFORMATION

AS Baltika is a public limited company whose governing bodies are the shareholders' general meeting, the supervisory council and the management board.

General meeting

The general meeting is the company'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 company's financial year. An extraordinary general meeting is called by the management board when the company's net assets have declined below the level required by the law or when calling of a meeting is demanded by the supervisory council, the auditor, or shareholders whose voting power represents at least one tenth of the company'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 2007 was held on 21 May at 24 Veerenni in Tallinn, Estonia. A total of 3,478,776 shares were represented (55.97% of the voting stock). The meeting approved the company's annual report and profit allocation proposal for 2006, amendments to the Articles of Association, an increase in share capital through a bonus issue and a convertible bonds issue. In addition, the general meeting approved the auditor and the audit fee. The chairman of the management board informed shareholders about Baltika's plans and prospects for 2007.

Supervisory council

The supervisory council plans the activities of the company, organises the management of the company and supervises the activities of the management board. The supervisory council meets according to need but not less frequently than once every three months. A meeting of the supervisory council has a quorum when more than half of the members participate. A resolution of the supervisory council is adopted when more than half of the members of the supervisory council who participate in the meeting vote in favour. Each member of the supervisory council has one vote. In 2007, the supervisory council met six times.

According to the Articles of Association, Baltika's supervisory council has three to five members. The members are elected by the general meeting for a period of three years. The current council was elected by the annual general meeting in 2006 and it has five members.

The present members of the supervisory council are Tiina Mõis (chairman), Reet Saks, Gert Tiivas, Allan Remmelkoor and Andres Erm. Mrs Mõis is the director of the investment firm AS Genteel and a member of the councils of several Estonian companies. Mrs Saks is an attorney with Law Office Raidla & Partnerid, a long-term partner of Baltika. Mrs Saks has been a member of Baltika's supervisory council since 1997. Mr Tiivas is the chief executive of East Capital Explorer, a Swedish listed company, and represents East Capital, a leading asset management company with a focus on East European markets and one of Baltika's largest institutional investors. Allan Remmelkoor, the chief executive of AS Kristiine Kaubanduskeskus which operates the Kristiine Centre in Tallinn, Estonia, contributes valuable retail expertise. Andres Erm has extensive experience with emerging markets in Eastern Europe which are also targeted by Baltika. Andres Erm is the only council member that owns shares in the company (108,000 shares or 0.58% of share capital as at the end of 2007).

Management board

The management board is a governing body which represents and manages the company in its daily activity in accordance with the law and the Articles of Association. The management board has to act in the best economic interests of the company. According to the Articles of Association, Baltika's management board may have three to seven members who are elected by the supervisory council for a period of three years. The supervisory council may also remove a member of the management board.

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.

Baltika's management board has four members: Meelis Milder (chairman), Ülle Järv, Maire Milder and Boriss Loifenfeld. On 28 August 2006, the supervisory council decided to extend the board members' term of office for another three years. Members of the management board have been with the company from 8 to 23 years.

Management board members are Baltika's largest shareholders through the holding company OÜ BMIG, which at the end of 2007 held 22.85% of Baltika's share capital. In addition, management board members have their individual shareholdings. Consequently, through their direct and indirect holdings, at the end of 2007 management board members controlled 29.64% of the company's share capital.

Shareholdings of members of the management board at 31 December 2007

	Number of shares	Holding
OÜ BMIG	4,261,120	22.85%
Meelis Milder	741,549	3.98%
Maire Milder	316,083	1.70%
Boriss Loifenfeld	150,366	0.81%
Ülle Järv	57,570	0.31%
Total OÜ BMIG and management board members	5,526,688	29.64%
Baltika's share capital	18,644,850	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 2007 consolidated financial statements as presented on pages 25 to 70.

The management board confirms that:

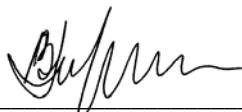
1. the accounting policies and presentation of information is in compliance with International Financial Reporting Standards as adopted by the European Union;
2. the financial statements present a true and fair view of the financial position, the results of the operations and the cash flows of the Group;
3. all Group companies are going concerns.



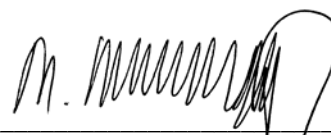
Meelis Milder
Chairman of the Management Board
25 March 2008



Ülle Järv
Member of the Management Board
25 March 2008



Boriss Loifenfeld
Member of the Management Board
25 March 2008



Maire Milder
Member of the Management Board
25 March 2008

CONSOLIDATED BALANCE SHEET

	Note	31.12.2007	31.12.2006
ASSETS			
Current assets			
Cash and bank	4	31,494	12,584
Trade and other receivables	5	113,563	128,471
Inventories	6	220,698	200,702
Non-current assets held for sale	10	500	0
Total current assets		366,255	341,757
Non-current assets			
Deferred income tax asset	7	5,897	4,750
Other non-current assets	8	11,448	11,077
Investment property	9	11,250	23,572
Property, plant and equipment	10	203,098	166,448
Intangible assets	11	58,409	49,074
Total non-current assets		290,102	254,921
TOTAL ASSETS		656,357	596,678
EQUITY AND LIABILITIES			
Current liabilities			
Borrowings	13,14	100,167	88,179
Trade and other payables	15	129,364	144,737
Total current liabilities		229,531	232,916
Non-current liabilities			
Borrowings	13,14	84,319	59,234
Other liabilities	15	1,086	0
Deferred income tax liability	7	2,075	288
Total non-current liabilities		87,480	59,522
TOTAL LIABILITIES		317,011	292,438
EQUITY			
Share capital at par value		186,449	62,150
Share premium		0	59,088
Reserves		26,133	9,721
Retained earnings		67,949	73,521
Net profit for the period		40,773	87,376
Currency translation differences		8,131	4,319
Total equity attributable to equity holders of the parent		329,435	296,175
Minority interest		9,911	8,065
TOTAL EQUITY	16	339,346	304,240
TOTAL LIABILITIES AND EQUITY		656,357	596,678

The Notes to the financial statements presented on pages 29 to 70 are an integral part of the Annual Report.

CONSOLIDATED INCOME STATEMENT

	Note	2007	2006
Revenue	17,18	1,151,520	899,481
Cost of goods sold	19	-514,839	-408,919
Gross profit		636,681	490,562
Distribution costs ¹	20	-522,620	-350,471
Administrative and general expenses ¹	21	-60,911	-48,334
Other operating income	22	25,219	12,482
Other operating expenses	23	-13,815	-6,907
Operating profit		64,554	97,332
Financial income (expenses)		-11,523	-6,037
Share of joint venture results		0	-234
Gains from other investments, net		0	322
Interest expenses, net		-9,049	-5,730
Foreign exchange losses, net		-2,389	-863
Other financial expenses, net		-85	468
Profit before income tax		53,031	91,295
Income tax	24	-9,189	-3,136
Net profit		43,842	88,159
Net profit attributable to equity holders of the parent company		40,773	87,376
Net profit attributable to minority shareholders		3,069	783
Basic earnings per share, EEK	25	2.19	4.85
Diluted earnings per share, EEK	25	2.19	4.71

¹Distribution costs and administrative and general expenses for the year 2006 have been reclassified. For further information see Notes 1 (Comparability), 20 and 21.

The Notes to the financial statements presented on pages 29 to 70 are an integral part of the Annual Report.

CONSOLIDATED CASH FLOW STATEMENT

	Note	2007	2006
Operating activities			
Operating profit		64,554	97,332
Adjustments:			
Depreciation, amortisation and impairment of PPE and intangibles	10,11	39,832	26,158
Loss (gain) from disposal of PPE and investment property		-13,799	-6,277
Loss (gain) from revaluation of investment property	9	-8,893	-4,380
Other non-monetary expenses ¹		7,080	315
Changes in working capital: ²			
Change in trade and other receivables	5	6,720	-66,717
Change in inventories	6	-19,996	-56,243
Change in trade and other payables	15	-10,176	53,422
Interest paid		-7,501	-5,537
Income tax paid		-4,089	-7,846
Net cash generated from operating activities		53,732	30,227
Investing activities			
Purchase of property, plant and equipment, intangibles, thereof	10,11	-101,946	-104,176
Under the finance lease terms	12	6,581	5,804
Within business combinations	27	4,647	-11,667
Proceeds from disposal of property, plant and equipment	10	50,463	435
Proceeds from disposal of investment property		0	11,055
Investments in subsidiaries	27	-5,699	-786
Interest received		184	89
Dividend received		0	15
Proceeds from disposal of current financial assets		0	2,131
Repayments of loans granted	26	0	352
Net cash used in investing activities		-45,770	-96,748
Financing activities			
Received borrowings	13	50,628	22,517
Repayment of borrowings	13	-25,712	-12,695
Change in bank overdraft	13	15,524	31,911
Finance lease payments and settlements of other liabilities	12,15	-9,216	-1,236
Receipts from contributions into share capital		0	12,791
Dividend paid	16	-14,910	-12,020
Proceeds from issue of bonds	14	28,523	30,239
Redemption of bonds	14	-31,500	-17,500
Net cash generated from financing activities		13,337	54,007
Effect of exchange gains (losses) on cash and cash equivalents		-2,389	-863
Total cash flows		18,910	-13,377
Cash and cash equivalents at the beginning of the period	4	12,584	25,961
Cash and cash equivalents at the end of the period	4	31,494	12,584
Change in cash and cash equivalents		18,910	-13,377

¹Other non-monetary expenses consist of foreign exchange gains (losses) arising in foreign subsidiaries.

²For changes in working capital, the effect of the acquisition of 100% ownership in joint venture to the consolidated financial statements has been taken into consideration (Note 27) (the balances with joint venture have been eliminated from the opening balances). The effect of the acquisition of joint venture has been presented separately under investment activities.

The Notes to the financial statements presented on pages 29 to 70 are an integral part of the Annual Report.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Share capital	Share premium	Reserves	Retained earnings	Currency translation reserve	Total attributable to parent	Minority interest	Total
Balance at 31.12.2005	58,230	49,690	9,532	85,741	4,131	207,324	628	207,952
Currency translation differences	0	0	0	0	188	188	-7	181
Net income (expense) recognised directly in equity	0	0	0	0	188	188	-7	181
Net profit for the period	0	0	0	87,376	0	87,376	783	88,159
Total recognised income (expense)	0	0	0	87,376	188	87,564	776	88,340
Equity-settled share-based transactions	0	315	0	0	0	315	0	315
Dividends paid (Note 16)	0	0	0	-12,031	0	-12,031	0	-12,031
Transfers to statutory reserve	0	0	189	-189	0	0	0	0
Increase of share capital	3,920	9,083	0	0	0	13,003	0	13,003
Change in minority interest	0	0	0	0	0	0	6,661	6,661
Balance at 31.12.2006	62,150	59,088	9,721	160,897	4,319	296,175	8,065	304,240
Balance at 31.12.2006	62,150	59,088	9,721	160,897	4,319	296,175	8,065	304,240
Currency translation differences	0	0	0	0	3,812	3,812	14	3,826
Net income (expense) recognised directly in equity	0	0	0	0	3,812	3,812	14	3,826
Net profit for the period	0	0	0	40,773	0	40,773	3,069	43,842
Total recognised income (expense)	0	0	0	40,773	3,812	44,585	3,083	47,668
Dividends paid (Note 16)	0	0	0	-14,916	0	-14,916	0	-14,916
Transfers to statutory reserve (Note 16)	0	0	12,822	-12,822	0	0	0	0
Increase of share capital (Note 16)	124,299	-59,088	0	-65,211	0	0	0	0
Revaluation of investment property (Notes 9, 16)	0	0	3,590	0	0	3,590	0	3,590
Acquisition of minority interest (Note 27)	0	0	0	0	0	0	-1,237	-1,237
Balance at 31.12.2007	186,449	0	26,133	108,722	8,131	329,435	9,911	339,346

Additional information on share capital and changes in equity is provided in Note 16.

The Notes to the financial statements presented on pages 29 to 70 are an integral part of the Annual Report.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 General information and summary of significant accounting policies

General information

The Baltika Group, with the parent company AS Baltika, is an international fashion retailer operating in the Baltic States, Central and Eastern Europe. The Baltika Group operates four retail concepts: Monton, Mosaic, Baltman and Ivo Nikkolo. At the end of 2007, the Group had 128 stores in seven countries and a total sales area of 24,290 square metres. The Group employs a vertically integrated business model which means that it controls all stages of the fashion process: design, manufacturing, supply chain management, distribution/logistics and retail sales. The Group also sells its collections wholesale. At 31 December 2007, the Baltika Group employed 1,983 people (31 December 2006: 1,915).

AS Baltika's shares are listed on the Tallinn Stock Exchange. The largest shareholder (Note 16) of AS Baltika is OÜ BMIG controlled by the members of the management board of the company.

AS Baltika (the Parent company) (registration number: 10144415, address: Veerenni 24, Tallinn, Estonia) is a company registered in the Republic of Estonia and operating in Estonia, Latvia, Lithuania, Russia, Ukraine, Poland and the Czech Republic. The consolidated financial statements prepared for the financial year ended at 31 December 2007 include the financial information of the Parent company and its subsidiaries (together referred to as the Group): OÜ Baltman, SIA Baltika Latvija, UAB Baltika Lietuva, Baltika Ukraina Ltd, OOO Kompania "Baltman Rus", Baltika Poland Sp.z.o.o., Baltika Retail Czech Republic s.r.o., OY Baltinia AB, Baltika Sweden AB, OÜ Baltika Tailor, AS Virulane and OÜ Baltika TP.

The management board of AS Baltika authorised these consolidated financial statements at 25 March 2008. Pursuant to the Commercial Code of the Republic of Estonia, the financial statements are subject to approval by the supervisory council of the Parent company and the general meeting of shareholders.

Basis of preparation

The Group's 2007 consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (EU). The financial statements have been prepared under the historical cost convention, as modified by the revaluations of investment property, as disclosed in the accounting policies below. 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. See also section "Comparability" below.

All information in the financial statements is presented in thousands of kroons, unless otherwise stated. The Estonian kroon is pegged to the euro at the rate of EUR 1=EEK 15.6466. The financial statements presented in euros can be obtained from the company's website www.baltikagroup.com.

Comparability

The financial statements have been prepared in accordance with the consistency and comparability principles, the nature of the changes in methods and their effect is explained in the respective notes. When the presentation of items in the financial statements or their classification method has been amended, then the comparative information of previous periods has also been restated.

Change in presentation of items

The Group has made certain changes in presentation of items in the balance sheet and in the cash flow statement.

Change in classification of expenses

The Group changed the classification of expenses between distribution costs and administrative and general expenses of the Parent company from year 2007. In prior years, the expenses incurred by the Parent company have been classified under "Administrative and general expenses" for the Group's financial reporting purposes. From 2007, expenses and personnel related costs incurred by the Parent company but rather related to retail activities of the Group are recognised under "Distribution costs". As a result of changes in classification, the distribution costs and administrative and general expenses for the previous reporting period have been restated. The effect of reclassification of financial information is disclosed in Notes 20 and 21 respectively.

Changes in presentation of financial information in the notes

From year 2007, the financial information disclosed for segment reporting (Note 17) and deferred income tax (Notes 7 and 24) is based on geographical regions rather than countries to simplify and improve the presentation of financial information for reporting purposes. The comparable information of year 2006 has been restated accordingly.

The definition of regions is as follows:

- Baltic region consists of operations in Estonia, Latvia and Lithuania;
- Eastern European region consists of operations in Russia and Ukraine;
- Central European region consists of operations in Poland and the Czech Republic; and
- Other regions consist of operations in countries (Finland, Sweden, etc.) having insignificant impact on the Group's results and strategy.

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

a) Standards, amendments to published standards and interpretations effective from 1 January 2007

IFRS 7, Financial instruments: Disclosures. IFRS 7 introduced new requirements for the notes in order to improve the presentation of information in the financial statements. This requires presentation of qualitative and quantitative information on the risks arising from financial instruments, containing specific minimum requirements for credit risk, liquidity risk and market risk (incl. sensitivity analysis of these risks). This replaced standard IAS 30, Disclosures in the Financial Statements and Other Financial Institutions and adds to and replaced some of the requirements in IAS 32, Financial Instruments: Disclosure and Presentation. IFRS 7 adoption did not have any impact on measurement or recognition principles. The Group made certain changes in presentation and new disclosures are made in these financial statements (comparatives provided).

IAS 1, Presentation of Financial Statements – Capital disclosures. The amended standard requires additional disclosures in the financial statements about parent company's capital and capital management. IAS 1 adoption did not have any impact on measurement or recognition principles. The Group made certain changes in presentation and new disclosures are made in these financial statements (comparatives provided).

IFRIC 8, Scope of IFRS 2. The interpretation requires consideration of transactions involving the issuance of equity instruments, where the identifiable consideration received is less than the fair value of the equity instruments issued in order to establish whether or not they fall within the scope of IFRS 2. This standard does not have any impact on the Group's financial statements.

IFRIC 10, Interim Financial Reporting and Impairment. The interpretation prohibits the impairment losses recognised in an interim period on goodwill and investments in equity instruments and in financial assets carried at cost to be reversed at a subsequent balance sheet date. This standard does not have any impact on the Group's financial statements.

Standards, amendments and interpretations effective in 2007 but not relevant

IFRS 4, Insurance Contracts;

IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies; and

IFRIC 9, Re-assessment of Embedded Derivative.

b) New accounting pronouncements issued but not yet effective

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 March 2007 or later periods and which the Group has not early adopted.

Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009). IFRS 8 supersedes IAS 14 Segment Reporting. The standard specifies new requirements in respect of the disclosure of information on business segments, as well as information on products and services, geographical areas where the business is conducted and major customers. IFRS 8 requires a "managerial approach" to reporting the performance of business segments. The Group is currently assessing the impact of the standard on segment disclosures in the consolidated financial statements.

IAS 23, Borrowing Costs (effective for annual periods beginning on or after 1 January 2009). The main change to IAS 23 is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalise such borrowing costs as part of the cost of the asset. The revised standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. The amended standard will not have an impact on the Group's accounting policies.

IAS 1, Presentation of Financial Statements (effective for annual periods beginning on or after 1 January 2009). The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances.

IAS 27, Consolidated and Separate Financial Statements (effective for annual periods beginning on or after 1 July 2009). The revised standard requires that the effects of transactions with minority shareholders be recognised directly in equity, on the condition that control over the entity is retained by the parent company. In addition, the standard elaborates on the accounting treatment of the loss of control over a subsidiary, i.e. it requires that the remaining shares be restated to fair value, with the resulting difference recognised in the income statement. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

IFRS 3, Business Combinations (effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 includes the choice to disclose minority interests either at fair value or their share in the fair value of the net assets identified; a restatement of shares already held in an acquired entity to fair value, with the resulting differences to be recognised in the income statement; and additional guidance on the application of the purchase method, including the recognition of transaction costs as an expense in the period in which they were incurred, measuring goodwill in step acquisition, and recognising post-acquisition changes in value of liability for contingent purchase consideration. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment (effective for annual periods beginning on or after 1 January 2008). The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

IFRIC 13, Customer Loyalty Programmes (effective for annual periods beginning on or after 1 July 2008). IFRIC 13 includes guidance on the accounting treatment of transactions resulting from loyalty programmes implemented by an entity for its customers, such as loyalty cards or awarding of "points". In particular, IFRIC 13 indicates the correct accounting for the entity's obligation to provide free or discounted goods or services if and when the customers redeem the points. The Group operates currently certain customer loyalty programmes. However, as the current conditions of the introduced programmes are of different nature, the IFRIC is expected to have no impact on the Group's consolidated financial statements.

Standards, amendments and interpretations to existing standards that are not yet effective and not relevant for the Group's operations

Puttable financial instruments and obligations arising on liquidation – IAS 32 and IAS 1 Amendment (effective from 1 January 2009). The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability. The Group does not expect the amendment to affect its consolidated financial statements.

IFRIC 11 IFRS 2 – Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007). The interpretation contains guidelines on the following issues: applying IFRS 2 Share-based Payment, for transactions of payment with shares which are entered into by two or more related entities; and

adopting an accounting approach in the following instances: an entity grants its employees rights to its equity instruments that may or must be repurchased from a third party in order to settle obligations towards the employees; or an entity or its owner grants the entity's employees rights to the entity's equity instruments, and the provider of those instruments is the owner of the entity. The Group does not expect the interpretation to affect its consolidated financial statements as the Group has no history in granting equity instruments via third parties.

IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008). The interpretation contains guidelines on applying the existing standards by entities being parties to service concessions between the public and the private sector. IFRIC 12 pertains to arrangements where the ordering party controls what services are provided by the operator using the infrastructure, to whom it provides the services and at what price. The Group does not expect the interpretation to affect its consolidated financial statements as none of Group companies provide for public sector.

IFRIC 14 IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for annual periods beginning on or after 1 January 2008). The interpretation contains general guidance on how to assess the limit of the surplus of fair value of a defined benefit plan over the present value of its liabilities which can be recognised as an asset, in accordance with IAS 19. In addition, IFRIC 14 explains how the statutory or contractual requirements of the minimum funding may affect the values of assets and liabilities of a defined benefit plan. The Group does not expect the interpretation to affect its consolidated financial statements as the Group has no qualifying assets.

Principles of consolidation, accounting for business combinations and subsidiaries

A subsidiary is an entity in which the Group, directly or indirectly, has interest of more than one half of the voting rights or otherwise has power to govern the operating and financial policies so as to obtain economic benefits. All subsidiaries have been consolidated in the Group's financial statements. An associate is an entity, in which the Group owns between 20% and 50% of shares with voting rights and over which the Group has significant influence. As at the balance sheet date, the Group had no associates.

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 purchase method of accounting is used to account for the acquisition of a subsidiary. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases. Under the purchase method, acquired and separately identifiable assets and liabilities as well as contingent liabilities of the acquired subsidiary are recognised at their fair values at the acquisition date.

In the consolidated financial statements, the financial statements of the subsidiaries under the control of the Parent company (except for the subsidiaries acquired for trading) 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.

Minority interest

Minority interest is that part of the net results and of the net assets of a subsidiary, including the fair value adjustments, which is attributable to interests which are not owned, directly or indirectly, by the Group. Minority interest forms a separate component of the Group's equity.

Transactions with minority interest

Transactions with minorities are treated as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the income statement. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

Joint ventures

A joint venture is based on a contractual agreement according to which two parties carry out their jointly controlled economic activities. Joint venture's activities are accounted for under the equity method in the balance sheet of a venturer, according to which the interest in a jointly controlled entity is initially recognised at cost and subsequently adjusted with the changes that have occurred in the venture interest in the net assets of the jointly controlled entity after the acquisition. In the income statement, the venture accounts for its interest in the operating results, financial income and financial expenses in the jointly controlled entity.

From 31 March 2007, the former joint venture became a 100% owned subsidiary (Note 27) and is from there on consolidated into Group results.

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"). The functional currency of the Parent company and subsidiaries located in Estonia is Estonian kroon. The consolidated financial statements have been prepared in Estonian kroons, which is the presentation currency of these financial statements.

Financial statements of foreign operations

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

- assets and liabilities for each balance sheet presented are translated into Estonian kroons at the closing rate at the date of that balance sheet;
- income and expenses for each income statement are translated at 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); and
- 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.

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

Foreign currency transactions

During the year, all foreign currency transactions of the parent company have been recorded in Estonian kroons based on the foreign currency exchange rates of the Bank of Estonia prevailing on the transaction date. Receivables and liabilities denominated in a foreign currency have been translated into Estonian kroons based on the foreign currency exchange rates of the Bank of Estonia prevailing on the balance sheet date. Profits and losses from foreign currency transactions, 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 income statement 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 (expenses) (Notes 22 and 23). Gains and losses arising from cash and cash equivalents are recognised net under financial expenses.

Cash and cash equivalents

For the purposes of the balance sheet and the cash flow statement, 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 borrowings in the balance sheet. Cash and cash equivalents are measured at fair value.

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; and
- available-for-sale financial assets.

At 31 December 2007 (and 31 December 2006) the Group had no other classes of financial assets than those classified under the category 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 (more than 90 days overdue) 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 market rate of interest for similar borrowers. 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 income statement within "Distribution costs". 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 balance sheet 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.

Renegotiated trade receivables

Trade receivables that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as receivables due according to the renegotiated terms. In subsequent years, the receivables are considered to be past due and disclosed only if renegotiated. Management starts the renegotiation when the counterparty has not been able to meet the due dates in a longer period of time and the settlements of debts are irregular.

Inventories

Inventories are recorded in the balance sheet 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 balance sheet 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.

Investment property

Real estate properties (land, buildings) that the entity owns or leases under finance lease terms to earn lease income or for capital appreciation, or both, and which are not occupied by the Group are recorded under investment property. An investment property is initially recognised at its acquisition cost. It is subsequently re-measured at its fair value which is based on the market value determined annually by external valuers and the management's judgement based on the comparable transactions at the same location. Earned lease income is recorded in profit or loss within revenue. Gains and losses resulting from changes in the fair value of investment property are recognised under "Other operating income (expenses)".

If non-current assets used in operating activities are reclassified as investment property, the difference between the carrying amount and the fair value is recognised as revaluation surplus under reserves in equity. Should the difference arising from revaluation reverse an impairment loss recorded in previous periods, the change in fair value is recognised directly in the income statement to the extent it reverses the previous impairment loss. The revaluation surplus included in equity is transferred to retained earnings on the subsequent disposal of investment property.

Property, plant and equipment

Property, plant and equipment are non-current assets used in the operating activities of the entity 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. Cost includes borrowing costs incurred on specific or general funds borrowed to finance construction of qualifying assets.

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.

Land is not depreciated. 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 | 5-40 years; |
| - machinery and equipment | 2-7 years; |
| - other fixtures | 2-7 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 income statement. 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 profit or loss in the income statement item "Other operating income (expenses)".

Non-current assets held for sale

Assets classified as assets held for sale are recognised in the balance sheet at the lower of carrying amount and fair value (less costs to sell). Assets are classified as held for sale, when the carrying amount is principally recovered through a sale transaction rather than through continuing use. Non-current assets held for sale are items of property, plant and equipment and intangible assets which the management intends to sell within the next 12 months and with regard to which the management has started active marketing activities and the assets are offered for sale at a realistic price as compared to their fair value. The depreciation of assets held for sale is ceased. Assets held for sale are reported in the balance sheet as a separate item "Non-current assets held for sale".

Intangible assets (excluding goodwill)

An intangible asset is initially recognised at its acquisition cost, comprising its purchase price and any directly attributable expenditure on preparing the asset for its intended 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 (5-20 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 (5-10 years).

Goodwill

Goodwill represents the excess of the acquisition cost over the fair value of the Group's share of the net assets of the acquired subsidiary, reflecting the part of acquisition cost which was paid for such assets of the acquired company which cannot be separated and accounted for separately. Goodwill which arose in the acquisition of a subsidiary is recognised as an intangible asset in the consolidated financial statements.

At the transaction date, goodwill is recognised in the balance sheet 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). 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".

Goodwill which arose in the acquisition of an associate or joint venture is included in the carrying amount of the investment and tested for impairment.

Goodwill which arose in the acquisition of foreign subsidiaries is translated using the foreign exchange rate of the Bank of Estonia prevailing on the balance sheet date.

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 or Cash Generating Unit).

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 income statement of the financial year as a reduction of the impairment losses. Impairment loss recognised for goodwill is not reversed.

Finance and operating leases

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

The Group is 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 income statement 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 income statement 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:

- agreements without term are expected to be valid for five years;
- should the termination of the agreement require a mutual agreement, lease payments for the six-month period are taken into consideration; and
- should the termination of the agreement require an advance notice, lease payments due within the advance notice period are taken into consideration.

The Group is the lessor

Assets leased out under operating leases are recognised similarly to non-current assets. Operating lease payments are recognised as income on a straight-line basis over the lease term.

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 environmental restoration, 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.

A financial guarantee contract is initially recognised at fair value and is subsequently measured at the higher of (a) the best estimate of the expenditure required to settle any financial obligation arising at the balance sheet date and (b) the amount initially recognised less, when appropriate, cumulative amortisation. Consequently, any financial guarantees issued on behalf of parties outside of the Group will result in recognition of a liability, unless the likelihood of occurrence is zero.

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 or on trade date. The amortised cost of current liabilities normally equals their nominal value; therefore current liabilities are stated in the balance sheet 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

Shares are classified in equity. The Group does not have any preference shares. The costs directly related to the issuance of shares are recognised as a reduction of the equity item "Share premium".

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.

Revaluation surplus

The reserve has arisen upon reclassification of property, plant and equipment to investment property carried at fair value. See accounting policy for investment property.

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 income statement 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

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. See section "Interest income and expenses" for further information. Dividend income is recognised when the right to receive payment is established.

Revenue from the sale of goods and services is included in the income statement line "Revenue" and revenue from the sale of investments in the line "Gains from other investments, net".

Interest income and expenses

Interest income/expenses have been recognised in the income statement 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 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 discounts. 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 enterprise 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 "Interest expenses, net".

Segment reporting

The primary format of segment reporting of the Group is the geographical segment by the area of location of customers and the secondary format of segment reporting is the business segment which distinguishes retail trade from wholesale trade with other activities and production activities.

The geographical regions are defined as separate geographical segments, each region generating significantly different risks and returns and each region forming a significant enough part from the Group's scale of operations. See section "Comparability" for changes in definition of geographical segments.

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from those of segments operating in other economic environments.

The allocation of the Group's subsidiaries and business units into segments is based on the structure of the internal management reporting.

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. Unallocated items result from utilisation or disposal of unallocated assets and liabilities as well from administrative costs taken by the Parent company.

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. Financial assets, interest bearing borrowings and the administrative facilities of the Parent company are disclosed as unallocated assets and liabilities.

Current and deferred income tax

Corporate income tax in Estonia

According to the Income Tax Act, the annual profit earned by enterprises 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 from 1 January 2008 subject to income tax of 21/79 (until 31 December 2007: 22/78 and until 31 December 2006: 23/77) of the amount paid out as dividends from which income tax paid before 1 January 2000 can be deducted using a respective coefficient. 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.

Corporate income tax in other countries

In accordance with the local income tax laws, the net profit of companies located in Latvia, Lithuania, Poland, the Czech Republic, Ukraine and Russia that has been adjusted for the permanent and temporary differences as stipulated by law is subject to corporate income tax (the income tax rate is 15% in Latvia and Lithuania, 19% in Poland, 25% in Ukraine and 24% in Russia and the Czech Republic). There have been no changes in tax rates compared to year 2006.

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 issued. 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. Management also makes certain judgements, apart from those involving estimations, 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: inventory (Note 6), valuation of deferred income tax assets (Note 7), valuation of investment property (Note 9), determination of the useful life of property, plant and equipment (Note 10) and valuation of goodwill (Note 11).

Inventory valuation (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 of 162,108 thousand kroons at 31 December 2007 and 126,528 thousand kroons at 31 December 2006), upon valuation of raw materials, their potential as a source of finished goods and generating income is considered (carrying amount of 47,495 thousand kroons at 31 December 2007 and 70,715

thousand kroons at 31 December 2006); upon valuation of work in progress, their stage of completion that can reliably be measured is considered (carrying amount of 4,419 thousand kroons at 31 December 2007 and 2,239 thousand kroons at 31 December 2006).

Deferred income tax (Note 7)

Deferred income tax asset has mostly arisen through tax loss carry-forwards from subsidiaries operating in foreign markets and is recoverable through future deductions from taxable profits. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future the management makes judgements and applies estimation based on the future development of the market and its outcomes to evaluate future expected revenue. The profit assumption is based on the attainment of the Group's strategic goals. The carrying amount of net deferred income tax asset recognised in the balance sheet amounts to 3,822 thousand kroons at 31 December 2007 and 4,462 thousand kroons at 31 December 2006.

Valuation of investment property (Note 9)

Investment property is initially recognised at the acquisition cost and subsequently measured at fair value in the balance sheet. The management uses the estimate of an asset's market value provided by an independent expert as a basis for fair value estimation. In its absence, the management board uses alternative measurement methods.

The management used the range provided by an independent expert's opinion as a base to evaluate the land located at Veerenni 24, Tallinn, Estonia (carrying amount of 11,250 thousand kroons at 31 December 2007) that was reclassified from owner-occupied properties to investment property during the current reporting period. An independent expert's opinion has been used to evaluate the production facility located at Veerenni 24, Tallinn, Estonia (carrying amount of 23,572 thousand kroons at 31 December 2006) prior to the transfer from investment property to property, plant and equipment in 2007. However, as the expert has given the valuation for the real estate as a whole whereas just parts of it are recognised under investment property, the value of the investment property has been separated and taken into consideration.

Determination of the useful life of property, plant and equipment (Note 10)

The management has evaluated the economic lives of production equipment and other non-current assets related to production depending on their estimated useful lives. The estimation of economic lives is based on historical experience and takes into consideration production capacity and conditions. The estimation of economic lives of non-current assets used in retail trade is based on the period over which the asset is expected to participate in the generation of revenue as well as the guaranteed duration of lease agreements. The economic life of assets with unlimited use (land) is assessed as infinite. The total carrying amount of property, plant and equipment with a limited useful life is 200,985 thousand kroons at 31 December 2007 and 155,475 thousand kroons at 31 December 2006. The total carrying amount of land is 2,113 thousand kroons at 31 December 2007 and 10,973 thousand kroons at 31 December 2006.

Valuation of goodwill (Note 11)

Goodwill is the excess of the cost of the acquisition over the fair value of the acquired net assets, reflecting the part of cost that was paid for the acquisition of such assets that cannot be separately identified and recognised. Goodwill as an intangible asset with an indefinite useful life is not amortised but it is tested for impairment at least once a year. The management has performed an impairment test for goodwill that arose on the acquisition of the subsidiary OOO Kompania "Baltman RUS" (carrying amount of 19,679 thousand kroons at 31 December 2007 and 20,423 thousand kroons at 31 December 2006) and the subsidiary OÜ Baltika Tailor (carrying amount of 5,555 thousand kroons at 31 December 2007). 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 investments. 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 goodwill is lower than its carrying amount, an impairment loss is recognised.

NOTE 3 Financial risks

In its daily activities, the Group is exposed to different types of risk management, which is an important and integral part of the business activities of the company. The company'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.

The basis for risk management at the Group are the requirements set by the Tallinn Stock Exchange, 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 council of the Group's Parent company supervises the management's risk management activities.

The management of the Group's Parent company considers market risk, including foreign exchange risk as the most significant risk for the Group.

Market risk

Foreign exchange risk

Sales in foreign currencies constitute 74% of the revenues of the Group and are denominated in LTL (Lithuanian lit), LVL (Latvian lat), UAH (Ukrainian hryvnia), PLN (Polish zloty), RUR (Russian rouble), CZK (Czech koruna) for the foreign subsidiaries of the Group and in EUR (euro) for the Parent company and the subsidiaries located in Estonia. The majority of raw materials used in production is acquired from countries located outside of European Union. The major currencies for purchases are EUR (euro) and USD (US dollar).

Trading with the counterparties in countries belonging to the European Monetary Union is handled only in euros. Estonian kroon is pegged to the euro thus no foreign exchange gains (losses) arise on the transactions in euro. As the Group's main revenues arise from retail sales, the prices of goods in the markets are fixed in a local currency and consequently, changes in foreign currency exchange rates directly affect the Group's revenue through the pricing of goods at the stores in those markets. In addition, a change in the economic environment and relative appreciation/depreciation of a local currency may greatly affect the purchasing power of customers in the market of the respective segment.

The weakening of the US dollar against the euro poses liquidity risk, which affects the Group's collectible amounts from the countries most affected by the changes in the dollar's exchange rate (Ukraine, Russia and Poland). On the other hand, the weakening of the dollar has a positive impact on importing from the countries (China, Japan and Korea) with which accounts are settled in dollars.

The Group's results are open to fluctuations in foreign currency rates against Estonian kroon in those countries where AS Baltika has subsidiaries. The changes in average foreign currency rates against Estonian kroon in the reporting period were the following: Polish zloty +2.96% (2006: +3.29%), Ukrainian hryvnia -8.10% (2006: +0.13%), Russian rouble -2.53% (2006: +3.13%), Latvian lat -0.55% (2006: +0.00%) and Czech koruna +2.08% (2006: +5.10%). The Lithuanian lit and Estonian kroon are pegged to the euro. The change in average rate of US dollar in the reporting period was -8.24% (2006: -0.97%).

If foreign exchange rates at 31 December 2007 had been 0.05-5.00% higher (lower), the impact on the net profit for the year would have been 2,722 thousand kroons (2006: 2,214 thousand kroons). The risk assessment is based on the assumptions that the fluctuations in foreign currency exchange rates of the main trading currencies of the Group (Russian rouble, Ukrainian hryvnia, Czech koruna, Lithuanian lit, US dollar and Polish zloty), do not exceed +/-5.00%. The exchange rates of Latvian lat and other currencies are not expected to fluctuate more than 0.05% and 2.00% respectively. As the Estonian kroon and Lithuanian lit are pegged to the euro, there is no foreign exchange risk arising from cash and cash equivalents, trade receivables and trade payables denominated in those currencies.

Foreign exchange risk arises from cash and cash equivalents (Note 4), trade receivables (Note 5) and trade payables (Note 15).

The Group's non-current borrowings carrying floating interest rate were denominated in euros, therefore no currency risk is assumed.

No instruments were used to hedge foreign currency risks in 2007 and 2006. Based on the management's assessment, the effect of losses resulting from changes in foreign currencies does not exceed the risk tolerance determined by the Group. If feasible, foreign currencies collected are used for the settling of liabilities measured in the same currency.

Interest rate risk

As the Group's cash and cash equivalents carry fixed interest rate, 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 non-current borrowings issued at floating interest rate and thus exposing the Group to cash flow interest rate risk. The exposure to the fair value interest rate risk of the Group's borrowings is insignificant according to the management's estimate as the borrowings with fixed interest rate have short maturities, expiring within a year, or have no term (overdraft). Interest rate risk is primarily caused by the potential fluctuations of Euribor and the changing of the average interest rates of banks.

All non-current borrowings at 31 December 2007 and 2006 were subject to a floating interest rate based on Euribor, which is fixed every three or six months. The Group analyses its interest rate exposure on a dynamic basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and alternative financing.

At 31 December 2007, if interest rates on foreign currency denominated borrowings had been 50 basis points lower (higher) with all other variables held constant, post-tax profit for the year would have been 431 thousand kroons (2006: 278 thousand kroons) higher (lower).

The Group uses no hedging instruments to manage the risks arising from fluctuations in interest rates.

Price risk

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

Credit risk

Credit risk arises from cash and cash equivalents, deposits with banks and financial institutions, as well as credit exposures to wholesale and retail customers, including outstanding receivables and committed transactions.

Cash and cash equivalents

For banks and financial institutions, only independently rated parties with a minimum rating of "A" are accepted for operations in the Baltic and Central European region as long-term counterparties. For Eastern Europe the "B" rating is considered acceptable. The Group has chosen banks with "A" rating to be the main partners for managing the cash and cash equivalents and financing the Group's operations in Estonia and overseas.

Cash and cash equivalents at bank classified by credit rating¹

	31.12.2007	31.12.2006
A	16,496	4,044
B	7,252	632
Other banks	4,321	4,029
Total	28,069	8,705

¹The credit rating applies on long-term deposits as published by Moody's.

Trade receivables

The most significant credit risk concentration to the Group arises from the wholesale activities in Eastern Europe (Note 5). For the wholesale customers, their financial position, past experience and other factors are taken into consideration as the basis for credit control. According to the Group's credit policy, no collaterals to secure the trade receivables are required from counterparties but instead, deliveries, outstanding credit amount and adherence to agreed dates are monitored continuously.

At the balance sheet date, the maximum exposure to credit risk from trade receivables (Note 5) amounted to 71,148 thousand kroons (2006: 86,402 thousand kroons), including balances with the Eastern European wholesale partners of 61,051 thousand kroons (2006: 71,644 thousand kroons).

Trade receivables (gross) from the clients located in Eastern European region

	31.12.2007	31.12.2006
Not due, thereof	48,623	54,411
Renegotiated	28,559	13,504
Past due 6 months and more, gross ¹	15,066	18,541
Total	63,689	72,952

¹Trade receivables past due six months and more were partially impaired thus the difference between the carrying value and recoverable amount was recognised as an impairment loss (Notes 5 and 20).

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. Credit risks arising from the Group's seasonal production and sales cycle are temporary.

Liquidity risk

Liquidity risk is the potential loss that would occur from the 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, monitoring of receivables and purchase contracts. A Group current account/overdraft facility is in use for more flexible management of liquid assets, enabling Group companies to use the Group's resources up to the limit established by the Parent company (Note 13).

Financial liabilities analysed by maturity at 31 December 2007

	Undiscounted cash flows ²					
	Carrying amount	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Bank borrowings (Note 13) ¹	145,456	52,361	20,037	72,561	16,010	160,969
Finance lease liabilities (Note 13)	9,333	699	2,053	7,616	0	10,368
Bonds (Note 14)	29,697	30,000	0	0	0	30,000
Trade payables (Note 15)	72,345	72,345	0	0	0	72,345
Other payables (Note 15)	57,009	55,935	68	364	642	57,009
Total	313,840	211,340	22,158	80,541	16,652	330,691

Financial liabilities analysed by maturity at 31 December 2006

	Undiscounted cash flows ²					
	Carrying amount	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Bank borrowings (Note 13) ¹	105,017	57,055	15,353	52,900	3,238	128,546
Finance lease liabilities (Note 13)	11,223	289	860	10,493	0	11,642
Bonds (Note 14)	31,173	20,000	11,500	0	0	31,500
Trade payables (Note 15)	96,535	96,535	0	0	0	96,535
Other payables (Note 15)	47,810	45,230	2,580	0	0	47,810
Total	291,758	219,109	30,293	63,393	3,238	316,033

¹Overdraft facilities are shown under bank borrowings payable within 1-3 months in the amount of maximum exposure available for the Group.

²For interest bearing borrowings carrying floating interest rate based on Euribor, the spot rate has been used.

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 markets – Russia and Ukraine).

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 the one hand and adequately consider local conditions on the other.

As 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. Another important risk is that the Group's information technology system is unable to ensure sufficiently fast and accurate transmission of information for decision-making purposes.

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 upgrade information systems, the transition to an integrated system encompassing several areas of operations has been initiated in 2006 and has continued through 2007. 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.

Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a 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.

Consistent with industry practice, the Group monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Net debt is calculated as total borrowings (including current and non-current borrowings as shown in the consolidated balance sheet) less cash and cash equivalents. Total capital is calculated as the sum of equity as shown in the consolidated balance sheet and net debt. During 2007 the Group's strategy was to maintain the gearing ratio within the range of 30% to 35%.

The gearing ratios of the Group were as follows:

	31.12.2007	31.12.2006
Total borrowings (Note 13)	184,486	147,413
Cash and cash equivalents (Note 4)	-31,494	-12,584
Net debt	152,992	134,829
Total equity	339,346	304,240
Total capital	492,338	439,069
Gearing ratio	31%	31%

Fair value

The Group estimates that the fair values of the assets (Notes 4-5) and liabilities (Notes 13-15) denominated in the balance sheet at amortised cost do not differ significantly from their carrying amounts presented in the Group's consolidated balance sheet at 31 December 2007 and 31 December 2006. As the Group's long-term borrowings 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. Therefore, management estimates that the fair value of long-term borrowings does not significantly differ from their carrying amounts. The carrying amount less an impairment provision of trade receivables and payables is assumed to approximate their fair values. 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.

Recent volatility in global financial markets

Since the second half of 2007, there has been a sharp rise in foreclosures in the US subprime mortgage market. The effects have spread beyond the US housing market as global investors have re-evaluated their exposure to risks, resulting in increased volatility and lower liquidity in the fixed income, equity, and derivative markets. Europe still looks better than the US, however, the stronger euro, tighter credit conditions and higher inflation may provide the volatility and lower liquidity situation on the Group's retail markets. Such circumstances may also affect the ability of the Group to obtain new borrowings and refinance its existing borrowings at terms and conditions that applied to similar transactions in recent periods. The Group's debtors may also be affected by the lower liquidity situation which could in turn impact their ability to repay their amounts owed. Management is unable to reliably estimate the effects on the Group's financial position of any further possible deterioration in the liquidity of the financial markets and their increased volatility.

NOTE 4 Cash and bank

	31.12.2007	31.12.2006
Cash in hand	3,425	3,879
Cash at bank	19,113	8,705
Short-term deposits	8,956	0
Total	31,494	12,584

At 31 December 2007, the Group had 8,956 thousand kroons (2006: 0) in overnight deposit. The interest rates of overnight deposits by currency were as follows: 3.59% for EUR and 3.84% for USD.

Cash and bank analysed by currency

	31.12.2007	31.12.2006
RUR (Russian rouble)	6,289	862
EEK (Estonian kroon)	6,035	4,871
EUR (euro)	5,826	451
UAH (Ukrainian hryvnia)	2,777	2,381
CZK (Czech koruna)	2,359	0
LVL (Latvian lat)	2,347	1,744
USD (US dollar)	2,142	21
PLN (Polish zloty)	2,070	656
LTL (Lithuanian lit)	1,649	1,598
Total	31,494	12,584

NOTE 5 Trade and other receivables

	31.12.2007	31.12.2006
Trade receivables, net	71,148	86,402
Other prepaid expenses ¹	22,808	18,648
Tax prepayments and tax reclaims, thereof	15,649	14,356
Value added tax	15,490	10,596
Prepaid income tax	97	3,642
Other taxes	62	118
Other current receivables ²	3,958	9,065
Total	113,563	128,471

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

²Other current receivables consist of receivables from the banks for credit card sales and short-term deposits.

For further information on income taxes see Notes 7 and 24.

Trade receivables

	31.12.2007	31.12.2006
Trade receivables, gross	73,786	87,710
Allowance for impairment of trade receivables (Note 20)	-2,638	-1,308
Trade receivables, net	71,148	86,402

Trade receivables (net) analysed by region (client location)

	31.12.2007	31.12.2006
Eastern-European region	61,051	71,644
Baltic region	9,946	14,496
Other regions	151	262
Total	71,148	86,402

Trade receivables (net) analysed by due date

	31.12.2007	31.12.2006
Not due ¹	57,416	64,636
Up to 1 month past due	585	2,106
1-3 months past due	689	2,279
3-6 months past due	30	148
Over 6 months past due	12,428	17,233
Total	71,148	86,402

¹Trade receivables classified as not due at 31 December 2007 include receivables from the wholesale partner from Eastern European region in the amount of 28,559 thousand kroons (31 December 2006: 13,504 thousand kroons) for which the due date has been renegotiated. Should the initial due dates remain unchanged, the carrying amount of those receivables had been classified under receivables over six months past due. Payments received from the wholesale partner in accordance with the renegotiated terms after the balance sheet date amount to 8,432 thousand kroons in 2008.

A significant risk concentration exists regarding the wholesale partner from Eastern European region (Note 3). During 2007, an impairment loss in the amount of 1,330 thousand kroons (2006: 4 thousand kroons) (Note 20) has been recognised for trade receivables from an Eastern European counterparty. The impairment loss has been calculated considering the existence of trade payables to the same counterparties, which upon mutual agreement can be used in offsetting the receivable. Impairment losses were recognised under "Distribution costs".

Trade receivables (net) are denominated in the following currencies:

	31.12.2007	31.12.2006
EUR (euro)	55,687	67,361
EEK (Estonian kroon)	4,400	8,442
UAH (Ukrainian hryvnia)	3,615	2,989
RUR (Russian rouble)	2,542	2,376
LTŁ (Lithuanian lit)	2,514	2,782
LVL (Latvian lat)	2,390	2,452
Total	71,148	86,402

NOTE 6 Inventories

	31.12.2007	31.12.2006
Fabrics and accessories	47,695	71,239
Allowance for impairment of fabrics and accessories (Note 19)	-200	-524
Work-in-progress	4,419	2,293
Finished goods and goods purchased for resale	163,708	129,335
Allowance for impairment of finished goods and goods purchased for resale (Note 19)	-1,600	-2,807
Prepayments to suppliers	6,676	1,166
Total	220,698	200,702

At 31 December 2007, inventories of the Group with a carrying amount of 1,391 thousand kroons (31 December 2006: 3,191 thousand kroons) were in the custody of third parties.

The allowance for impairment for fabrics and finished goods at 31 December 2007 compared to previous balance sheet date has decreased due to reduced quantities of stock from old seasons.

Movable properties of the Parent company in the amount of 106,404 thousand kroons have been pledged to secure the bank borrowings (Note 13).

NOTE 7 Deferred income tax**Deferred income tax at 31 December 2007**

	Baltic region	Eastern European region	Central European region	Total
Deferred income tax liability				
On property, plant and equipment	2,075	0	0	2,075
Deferred income tax asset				
On property, plant and equipment	0	1,147	341	1,488
On tax loss carry-forwards	0	2,568	1,841	4,409
Total	0	3,715	2,182	5,897
Deferred income tax asset, net, thereof	-2,075	3,715	2,182	3,822
Current portion (recovered within 12 months)	-688	356	766	434
Non-current portion	-1,387	3,359	1,416	3,388
Deferred income tax expense (income) (Note 24)	2,386	-2,077	331	640

Deferred income tax at 31 December 2006

	Baltic region	Eastern European region	Central European region	Total
Deferred income tax liability				
On property, plant and equipment	288	0	0	288
Deferred income tax asset				
On property, plant and equipment	74	335	377	786
On tax loss carry-forwards	525	1,303	2,136	3,964
Total	599	1,638	2,513	4,750
Deferred income tax asset, net, thereof	311	1,638	2,513	4,462
Current portion (recovered within 12 months)	311	898	769	1,978
Non-current portion	0	740	1,744	2,484
Deferred income tax expense (income) (Note 24)	1,677	-1,638	-904	-865

The recovery of the deferred income tax asset arising from tax loss carry-forwards is dependent on future taxable profits at 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 profit assumption is based on the attainment of each respective company's 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.

For deferred income tax assets carried off-balance sheet and contingent income tax liability see Notes 24 and 28 respectively.

NOTE 8 Other non-current assets

	31.12.2007	31.12.2006
Loan receivable from joint venture (Note 26)	0	1,359
Non-current lease prepayments	11,448	9,718
Total	11,448	11,077

Non-current lease prepayments arise from lease agreements of the Group's retail subsidiaries operating in the Latvian, Lithuanian, Polish and Russian markets.

NOTE 9 Investment property

Balance at 31.12.2005	27,193
Disposals	-8,001
Revaluation	4,379
Balance at 31.12.2006	23,572
Reclassification from property, plant and equipment (Note 10)	909
Revaluation (Note 16, 22)	12,483
Reclassification to property, plant and equipment (Note 10)	-25,715
Balance at 31.12.2007	11,250

	2007	2006
Lease revenue from investment properties	825	3,150
Direct operating expenses from investment properties	825	3,150
Net lease revenue from investment properties	0	0

At 31 December 2006, investment property consisted of the production facility located at Veerenni 24, Tallinn, Estonia carried at fair value of 23,572 thousand kroons. The facility was used by the joint venture on the basis of an operating lease agreement. Due to the acquisition of 100% ownership in the joint venture (Note 27), the production facility has been reclassified from investment property to property, plant and equipment as it became occupied by the Group. The gain from increase in fair value prior to the reclassification amounted to 2,143 thousand kroons and was recognised in the income statement under "Other operating income" (Note 22).

4,500 square metres of land located at Veerenni 24, Tallinn, Estonia was reclassified from owner-occupied property, plant and equipment to investment property due to the end of owner occupation of the part of the property. At the date of the reclassification, the land was restated at fair value and the resulting increase in value of 3,590 thousand kroons recognised in owners' equity under "Reserves" (Note 16). Further revaluation gain during the reporting period in the amount of 6,750 thousand kroons was recognised in the income statement under "Other operating income" (Note 22). At 31 December 2007, the land is carried at fair value of 11,250 thousand kroons.

The investment property located at Veerenni 24, Tallinn, Estonia has been pledged to secure the Group's bank borrowings (Note 13).

NOTE 10 Property, plant and equipment

	Land and construction rights	Buildings and structures	Machinery and equipment	Other fixtures	Construc- tion in progress	Pre- payments	Total
At 31 December 2005							
Acquisition cost	10,973	74,005	71,321	51,440	2,009	3,305	213,053
Accumulated depreciation	0	-27,516	-64,299	-33,149	0	0	-124,964
Net book amount	10,973	46,489	7,022	18,291	2,009	3,305	88,089
Additions	0	43,104	7,195	48,342	1,448	1,414	101,503
Acquired within business combinations	0	0	0	882	0	0	882
Disposals	0	-615	-236	-822	0	0	-1,673
Reclassification	0	3,795	67	1,054	-1,796	-3,120	0
Depreciation (Notes 19-21)	0	-7,248	-3,885	-9,634	0	0	-20,767
Currency translation differences	0	-484	-80	-919	-56	-47	-1,586
At 31 December 2006							
Acquisition cost	10,973	116,708	78,982	94,154	1,605	1,552	303,974
Accumulated depreciation	0	-31,667	-68,899	-36,960	0	0	-137,526
Net book amount	10,973	85,041	10,083	57,194	1,605	1,552	166,448
Additions	0	29,528	19,826	35,472	920	105	85,851
Acquired within business combinations (Note 27)	0	0	4,280	0	0	225	4,505
Disposals	-7,969	-32,973	-13	-6	-181	0	-41,142
Reclassifications from investment property (Note 9)	0	0	0	0	25,715	0	25,715
Reclassifications to investment property (Note 9)	-891	-18	0	0	0	0	-909
Reclassifications to non-current assets held for sale	0	-1,818	0	0	0	0	-1,818
Reclassification	0	8,643	-533	-6,528	-1,140	-442	0
Depreciation (Notes 19-21)	0	-12,093	-5,365	-15,603	0	0	-33,061
Currency translation differences	0	-620	-180	-1,573	-40	-78	-2,491

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At 31 December 2007

Acquisition cost	2,113	113,430	98,437	116,685	26,879	1,362	358,906
Accumulated depreciation	0	-37,740	-70,339	-47,729	0	0	-155,808
Net book amount	2,113	75,690	28,098	68,956	26,879	1,362	203,098

In March 2007, the Group sold the construction rights and the logistics centre located in Lasnamäe Industrial Park (Tallinn, Estonia). At the same time, the Group signed an operating lease agreement with the purchaser to lease the logistics centre over the ten-year lease period. The transaction price was 50,186 thousand kroons. Gain from sales in the amount of 16,210 thousand kroons was recognised under "Other operating income".

The storage facility located at Veerenni 24, Tallinn, Estonia was transferred to non-current assets held for sale. Impairment loss from revaluation the asset to fair value less selling expenses, amounting to 1,318 thousand kroons was recognised under "Other operating expenses" (Note 23).

Assets acquired under finance lease terms and recognised under property, plant and equipment amounted to 6,581 thousand kroons (2006: 5,804 thousand kroons) at acquisition cost. The total net book amount of assets acquired through finance lease at 31 December 2007 amounts to 11,643 thousand kroons (31 December 2006: 13,998 thousand kroons). See Note 12 for additional information on finance leases.

Non-current assets of the Group in the amount of 67,113 thousand kroons have been pledged to secure the bank borrowings (Note 13).

NOTE 11 Intangible assets

	Licenses, software and other	Trade- marks	Advances	Goodwill	Total
At 31 December 2005					
Acquisition cost	21,125	0	0	14,129	35,254
Accumulated amortisation	-8,763	0	0	0	-8,763
Net book amount	12,362	0	0	14,129	26,491
Additions	6,871	0	1,459	0	8,330
Acquired in business combinations	3,333	10,060	0	6,326	19,719
Disposals	-26	0	0	0	-26
Amortisation (Notes 20-21)	-5,346	-45	0	0	-5,391
Currency translation differences	-8	0	-9	-32	-49
At 31 December 2006					
Acquisition cost	31,114	10,060	1,450	20,423	63,047
Accumulated amortisation	-13,928	-45	0	0	-13,973
Net book amount	17,186	10,015	1,450	20,423	49,074
Additions	11,448	0	0	0	11,448
Acquired within business combinations (Note 27)	141	0	0	5,555	5,696
Disposals	-261	0	0	0	-261
Reclassification	66	0	-66	0	0
Amortisation (Notes 20-21)	-6,144	-626	0	0	-6,770
Currency translation differences	9	0	-43	-744	-778
At 31 December 2007					
Acquisition cost	32,549	10,060	1,341	25,234	69,184
Accumulated amortisation	-10,104	-671	0	0	-10,775
Net book amount	22,445	9,389	1,341	25,234	58,409

Impairment tests for goodwill

Goodwill, carried at 25,234 thousand kroons (2006: 20,423 thousand kroons) is tested for impairment at each balance sheet date. The carrying amount of goodwill, applicable to CGUs (Cash Generating Units) of Baltman RUS and Baltika Tailor (Note 27), at 31 December 2007 was tested for impairment. The recoverable amount of a CGU is determined based on value-in-use calculations. The value-in-use calculations use detailed pre-tax cash flow projections covering the five-year period. Cash flows beyond the five-year period are extrapolated using the estimated growth rates.

The key assumptions used for value-in-use calculations are as follows:

	Baltika Tailor CGU 31.12.2007	Baltman RUS CGU 31.12.2007	31.12.2006
Carrying amount of goodwill	5,555	19,679	20,423
Growth in revenue ¹	20.79% ⁵	11.38% ⁶	6.94% ⁶
Growth in revenue ²	4.65%	3.63%	4.35%
Growth rate ³	0%	0%	0%
Discount rate ⁴	9.15%	10.73% ⁷	14.00% ⁷

¹Management determined average annual growth in revenue and sales efficiency per square metre (decreasing growth trend over the period of cash flow projections) for the five-year period.

²Average growth rate used to extrapolate cash flows beyond year 2012.

³Growth rate used to extrapolate cash flows beyond year 2020.

⁴Pre-tax discount rate applied to the cash flow projections (WACC).

⁵The growth in revenue is determined taking into consideration the improved efficiency in production achieved during year 2008 resulting from new production facilities taken into use late 2007.

⁶The assumptions used for determining the growth in revenue at 31 December 2007 have changed along with the improved knowledge of assessing the growth trends for an extensively expanding market.

⁷The 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 goodwill and consequently no impairment losses have been recognised. Average annual growth in sales may decrease by 3.61% (31 December 2006: 7.80%) and 0.49% for Baltman RUS and Baltika Tailor respectively before the recoverable amount will be equal to the carrying amount.

NOTE 12 Accounting for leases**Operating lease – the Group as the lessee****Future minimum lease payments under non-cancellable operating leases**

	31.12.2007	31.12.2006
Up to 1 year	169,519	69,831
1-5 years	297,594	163,944
Over 5 years	124,776	71,952
Total	591,889	305,727

Operating lease expenses arise from lease of retail outlets. The lease agreements for stores are predominantly not binding for long-term in Estonia, Latvia and Lithuania and can be terminated in a two to six months notice. In Poland and Ukraine, the lease agreements usually require finding a new lessee when cancelling the lease agreement.

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 within the lease term based on

changes in consumer price index or inflation. In 2007, operating lease payments amounted to 213,866 thousand kroons (2006: 124,508 thousand kroons).

Operating lease – the Group as the lessor

Future minimum lease receivables from non-cancellable subleases

	31.12.2007	31.12.2006
Up to 1 year	141	5,175

Operating lease income consists of premises leased to third parties. From 31 March 2007, production facilities located at Veerenni 24, Tallinn, Estonia and machinery leased to the joint venture up to that date were classified as property, plant and equipment (Note 9-10) and became occupied by the Group.

In 2007, the Group earned operating lease income in the amount of 1,894 thousand kroons (2006: 5,919 thousand kroons) from assets leased to third parties under operating lease agreements. The direct expenses attributable to lease income amounted to 810 thousand kroons (2006: 3,685 thousand kroons).

Finance lease – the Group as the lessee

	Construction rights	Machinery and equipment	Passenger cars and equipment	Total
At 31 December 2005				
Acquisition cost	15,970	3,640	951	20,561
Accumulated depreciation	0	-2,669	-142	-2,811
Net book amount	15,970	971	809	17,750
Additions	0	5,804	0	5,804
Depreciation	0	-1,197	-176	-1,373
Disposals (at net book amount)	-8,001	0	-181	-8,182
At 31 December 2006				
Acquisition cost	7,969	9,444	674	18,087
Accumulated depreciation	0	-3,866	-223	-4,089
Net book amount	7,969	5,578	451	13,998
Additions	0	6,581	0	6,581
Depreciation	0	-849	-130	-979
Disposals (at net book amount)	-7,969	0	-181	-8,150
Currency translation differences	0	0	12	12
At 31 December 2007				
Acquisition cost	0	12,385	692	13,077
Accumulated depreciation	0	-1,075	-359	-1,434
Net book amount	0	11,310	333	11,643

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 13. For further information on disposal of construction rights see Note 10.

For the year ended at 31 December 2007, the Group settled finance lease payments in the amount of 2,466 thousand kroons (2006: 1,236 thousand kroons).

NOTE 13 Borrowings

	31.12.2007	31.12.2006
Current borrowings		
Current portion of non-current bank loans (Note 3)	20,733	13,946
Current bank loans (Note 3)	47,435	41,911
Current finance lease liabilities (Note 3)	2,302	1,149
Bonds (Note 3, 14)	29,697	31,173
Total	100,167	88,179
Non-current borrowings		
Non-current bank loans (Note 3)	77,288	49,160
Non-current finance lease liabilities (Note 3)	7,031	10,074
Total	84,319	59,234

Interest bearing borrowings at 31 December 2007 at nominal value are denominated in the following currencies:

	Carrying amount	Less than 1 year	Between 1 and 5 years	Over 5 years
EUR (euro)	98,021	20,733	62,288	15,000
EEK (Estonian kroon)	86,156	79,300	6,856	0
Other currencies	309	134	175	0
Total	184,486	100,167	69,319	15,000

Interest bearing borrowings at 31 December 2006 at nominal value are denominated in the following currencies:

	Carrying amount	Less than 1 year	Between 1 and 5 years	Over 5 years
EUR (euro)	73,106	23,946	46,022	3,138
EEK (Estonian kroon)	73,886	64,112	9,774	0
Other currencies	421	121	300	0
Total	147,413	88,179	56,096	3,138

Interest bearing borrowings consist of bank loans, finance leases and bonds.

Bank loans of the Group at 31 December 2007

	Carrying amount	Average risk premium
Borrowings at floating interest rate (based on 3-month Euribor)	10,012	1.75%
Borrowings at floating interest rate (based on 6-month Euribor)	88,009	1.81%
Borrowings at fixed interest rate (overdraft)	47,435	6.05%
Total	145,456	

Bank loans of the Group at 31 December 2006

	Carrying amount	Average risk premium
Borrowings at floating interest rate (based on 3-month Euribor)	13,349	1.75%
Borrowings at floating interest rate (based on 6-month Euribor)	49,757	2.12%
Borrowings at fixed interest rate (overdraft and short-term loan)	41,911	4.60%
Total	105,017	

The maximum exposure of the Group's overdraft facilities with the banks at 31 December 2007 amounted to 46,259 thousand kroons (31 December 2006: 43,259 thousand kroons). One overdraft facility in the amount of 40,000 thousand kroons (31 December 2006: 37,000 thousand kroons) is used by multiple Group companies

whereas users of the Group account are jointly responsible for the fulfilment of obligations arising from the Group account agreement.

The Group's bank borrowings are secured by the following collaterals:

Type of collateral	Specification and location of collateral	Collateral value at 31.12.2007	Collateral value at 31.12.2006
Commercial pledge	Movables of the Parent company	69,680	69,680
Commercial pledge	Movables of the Parent company	14,200	14,200
Mortgage	Real estate located at Veerenni 24, Tallinn, Estonia	107,500	40,000
Mortgage	Real estate located at Kalda 10A, Rakvere, Estonia	7,400	7,400
Mortgage	Real estate located at Õpetajate 5, Ahtme, Estonia	12,000	12,000
Mortgage	Real estate located at Lasnamäe Industrial Park, Tallinn, Estonia	0	24,400
Total		210,780	167,680

During the reporting period, the Group made loan repayments in the amount of 25,712 thousand kroons (2006: 12,695 thousand kroons). Interest expense of the reporting period amounted to 6,960 thousand kroons (2006: 5,858 thousand kroons). Interest expenses have been recognised net with interest income under interest expenses.

The carrying amount of assets pledged is disclosed in Note 6, 9 and 10.

According to the management's assessment, the carrying amount of borrowings does not significantly differ from the fair value.

NOTE 14 Bonds

Closed issue of bonds at 31 December 2007

	Quantity	Nominal (EEK)	Issue price	Carrying amount	Interest rate	Maturity
Bonds	3,000	10,000	28,553	29,697	5.00%	14.03.2008

Closed issue of bonds at 31 December 2006

	Quantity	Nominal (EEK)	Issue price	Carrying amount	Interest rate	Maturity
Bonds	2,000	10,000	19,208	19,835	4.08%	16.03.2007
Bonds	1,150	10,000	11,111	11,338	4.60%	18.04.2007
Total	3,150		30,319	31,173		

On 15 March 2007, AS Baltika issued 3,000 bonds with the nominal value of 10,000.00 kroons and price of 9,517.51 kroons per bond. The total amount of the closed bond issue was 30,000 thousand kroons. The redemption date of the bonds was 14 March 2008. The difference between the nominal value and issue price yields an interest of 5.00% per annum. The bonds were unsecured.

The proceeds were used to finance the redemption of the bond issues due on 16 March and 18 April 2007. The redemption value of the bond issues was 20,000 thousand kroons and 11,500 thousand kroons respectively.

The fair values of the bonds are considered to be very close to the carrying values, as the maturities are short and the effect of changes in interest rates are insignificant.

NOTE 15 Trade and other payables

	31.12.2007	31.12.2006
Trade payables	72,345	96,535
Tax liabilities, thereof	33,065	23,006
Personal income tax	5,156	3,895
Social security tax and unemployment insurance premium	10,576	7,444
Value added tax	12,319	10,565
Corporate income tax liability	3,985	406
Other taxes	1,029	696
Payables to employees and other accrued expenses ¹	22,857	18,174
Customer prepayments	1,096	392
Other current payables ²	1	6,630
Other non-current liabilities ³	1,086	0
Total	130,450	144,737

¹Payables to employees consist of accrued wages and salaries and vacation accrual in the amount of 22,152 thousand kroons (31 December 2006: 17,250 thousand kroons). Accrued expenses consist of dividend payable in the amount of 13 thousand kroons (31 December 2006: 7 thousand kroons), interest payable in the amount of 37 thousand kroons (31 December 2006: 43 thousand kroons) and other accrued expenses in the amount of 655 thousand kroons (31 December 2006: 874 thousand kroons).

²Other current payables at 31 December 2006 consist of discounted payable for Ivo Nikkolo trademark.

³Other non-current liabilities consist of prepaid future revenues.

Trade payables are denominated in the following currencies:

	31.12.2007	31.12.2006
EUR (euro)	20,385	36,747
EEK (Estonian kroon)	17,808	22,235
USD (US dollar)	16,105	21,212
RUR (Russian rouble)	12,315	12,447
CZK (Czech koruna)	3,234	0
LTL (Lithuanian lit)	1,193	1,615
Other currencies	1,305	2,279
Total	72,345	96,535

NOTE 16 Equity**Share capital**

	31.12.2007	31.12.2006
Share capital	186,449	62,150
Number of shares (pcs)	18,644,850	6,214,950
Nominal value of shares (EEK)	10.00	10.00

Change in the number of shares

	Issue	Number of shares
Number of shares 31.12.2005		5,822,950
Issued 30.03.2006	Conversion of C-bonds	192,000
Issued 05.10.2006	Conversion of D-bonds	82,400
Issued 08.12.2006	Conversion of D-bonds	117,600
Number of shares 31.12.2006		6,214,950
Issued 11.06.2007	Bonus issue	12,429,900
Number of shares 31.12.2007		18,644,850

Under the Articles of Association, the company's minimum share capital is 100,000 thousand kroons and the maximum share capital is 400,000 thousand kroons. All shares have been paid for.

According to the decision of the annual general meeting held on 21 May 2007, the share capital of AS Baltika was increased through a bonus issue by 124,299 thousand kroons (thereof 65,211 thousand kroons from retained earnings and 59,088 thousand kroons from share premium), 12,822 thousand kroons were transferred to statutory reserve and 14,916 thousand kroons distributed as dividends to the shareholders.

As a result of the bonus issue, two bonus shares were issued for each existing share and the number of shares outstanding increased from 6,214,950 to 18,644,850.

In 2007, dividends distributed to the shareholders amounted to 0.80 kroons per share equalling a total of 14,916 thousand kroons (2006: 0.67 kroons per share equalling a total of 12,020 thousand kroons). Dividend per share data has been restated by applying the conditions of the bonus issue (two bonus shares issued for each existing share) carried out in June 2007. Income tax expense on dividends (Note 24) amounted to 3,359 thousand kroons in 2007 (2006: 1,797 thousand kroons).

Reserves

	31.12.2007	Change	31.12.2006	Change	31.12.2005
Statutory reserve	18,645	12,822	5,823	189	5,634
Revaluation surplus	7,488	3,590	3,898	0	3,898
Total	26,133	16,412	9,721	189	9,532

The revaluation surplus increased by 3,590 thousand kroons due to reclassification of assets from owner-occupied properties to investment property and their subsequent measurement at fair value (Note 9).

Shareholders at 31 December 2007

	Number of shares	Holding
1. BMIG OÜ	4,261,120	22.85%
2. Morgan Stanley + CO Incorporated Equity Client Account	1,545,000	8.29%
3. Svenska Handelsbanken Clients	1,160,500	6.22%
4. Members of management board and supervisory council and persons related to them		
Meelis Milder	741,549	3.98%
Maire Milder	316,083	1.70%
Boriss Loifenfeld	150,366	0.81%
Andres Erm	108,000	0.58%
Ülle Järv	57,570	0.31%
5. Other shareholders	10,304,662	55.27%
Total	18,644,850	100.00%

Shareholders at 31 December 2006

	Number of shares	Holding
1. BMIG OÜ	1,295,072	20.84%
2. Skandinaviska Enskilda Banken Ab Clients	417,020	6.71%
3. Raiffeisen Zentralbank Österreich AG Clients	305,940	4.92%
4. Members of management board and supervisory council and persons related to them		
Meelis Milder	247,183	3.98%
Maire Milder	115,361	1.86%
Boriss Loifenfeld	50,122	0.81%
Andres Erm	36,000	0.58%
Ülle Järv	23,158	0.37%
5. Other shareholders	3,725,094	59.94%
Total	6,214,950	100.00%

The shares of the Parent company are listed on the Tallinn Stock Exchange. The Parent company does not have a controlling shareholder or any shareholders jointly controlling the entity. The investment company OÜ BMIG is under the control of the management board members of the Parent company.

NOTE 17 Segments**Geographical segment by client's location – primary segment for the year ended at 31 December 2007**

	Baltic region	Eastern European region	Central European region	Other regions	Elimina- tions	Total
External revenue	687,602	399,801	32,531	31,586	0	1,151,520
Inter-segment revenue	219,889	123,047	15,772	0	-358,708	0
Total revenue (Note 18)	907,491	522,848	48,303	31,586	-358,708	1,151,520
Segment operating profit (loss)	114,092	-1,038	-79	4,328	0	117,303
Unallocated operating income (expenses)						-52,749
Total operating profit						64,554
Other financial income (expenses)						-11,523
Income tax (Note 24)						-9,189
Net profit before minority interest						43,842
Minority interest						3,069
Net profit						40,773
Assets	356,108	336,266	25,652	35	-180,552	537,509
Group's unallocated assets, thereof						118,848
Assets used in production						65,207
Assets used for administration						8,625
Other unallocated assets						45,016
Total assets						656,357
Liabilities	93,373	212,364	11,898	0	-252,618	65,017
Group's unallocated liabilities, thereof						251,994
Liabilities related to production						60,818
Other unallocated liabilities						191,176
Total liabilities						317,011
Additions to PPE and intangibles (Notes 10-11), thereof	50,983	21,057	7,982	0	0	107,500
Unallocated						27,478
Depreciation and amortisation (Notes 10-11), thereof	21,166	12,998	1,592	0	0	39,831
Unallocated						4,075

Geographical segment by client's location – primary segment for the year ended at 31 December 2006

	Baltic region	Eastern European region	Central European region	Other regions	Elimina- tions	Total
External revenue	543,319	303,194	34,440	18,528	0	899,481
Inter-segment revenue	187,860	118,120	14,541	0	-320,521	0
Total revenue (Note 18)	731,179	421,314	48,981	18,528	-320,521	899,481
Segment operating profit (loss)	135,350	45,865	-2,548	4,699	0	183,366
Unallocated operating income (expenses)						-86,034
Total operating profit						97,332
Other financial income (expenses)						-6,037
Income tax (Note 24)						-3,136
Net profit before minority interest						88,159
Minority interest						783
Net profit						87,376
Assets	281,490	342,724	9,873	303	-166,909	467,481
Group's unallocated assets, thereof						129,197
Assets used in production						72,092
Assets used for administration						6,337
Other unallocated assets						50,768
Total assets						596,678
Liabilities	92,040	159,669	4,466	0	-190,868	65,307
Group's unallocated liabilities, thereof						227,131
Liabilities related to production						78,885
Other unallocated liabilities						148,246
Total liabilities						292,438
Additions to PPE and intangibles (Notes 10-11), thereof	38,807	57,281	63	0	0	130,434
Unallocated						34,283
Depreciation and amortisation (Notes 10- 11), thereof	15,761	5,079	1,864	0	0	26,158
Unallocated						3,454

According to the Parent company management's estimate, the inter-segment transactions have been carried out at arm's length and the conditions applied do not differ materially as compared to the transactions with third parties.

Business segment by area of operations – secondary segment

At 31 December 2007, the Group operated in the following areas, generating significantly different risks and returns compared to each other and each activity being material enough to form a separate segment:

- retail and managing of retail store chains in the markets;
- wholesale and other services;
- production.

Other areas of operations are of lower strategic importance and less material compared to the core activities and consequently do not form a separate segment.

The Group's assets and investments that relate to more than one business segment and cannot be allocated are recognised as unallocated assets and investments in property, plant and equipment.

Financial information by area of operations

	Revenue		Assets		Additions to property, plant and equipment	
	2007	2006	31.12.2007	31.12.2006	2007	2006
Retail	987,297	736,366	312,207	250,075	74,519	71,660
Wholesale and other	144,696	150,585	55,477	67,204	0	0
Production	14,396	0	65,207	72,092	23,010	5,158
Unallocated	5,131	12,530	223,466	207,307	9,971	53,616
Total	1,151,520	899,481	656,357	596,678	107,500	130,434

NOTE 18 Revenue

	2007	2006
Sale of goods	1,131,993	886,951
Sale of sewing services	14,396	0
Lease revenue (Note 12)	1,894	5,919
Other	3,237	6,611
Total	1,151,520	899,481

NOTE 19 Cost of goods sold

	2007	2006
Materials and supplies	425,578	363,874
Payroll costs in production	73,028	39,351
Other production costs	10,025	4,174
Operating lease expenses (Note 12)	4,018	1,734
Depreciation of assets used in production (Notes 10-11)	3,277	2,363
Change in inventories	443	-1,878
Change in allowance for inventories (Note 6)	-1,530	-699
Total	514,839	408,919

NOTE 20 Distribution costs

	2007	Reclassified 2006 ¹	2006
Operating lease expenses (Note 12)	202,338	121,004	119,245
Payroll costs	178,005	129,815	92,322
Advertising expenses	32,341	22,776	22,776
Depreciation and amortisation (Notes 10-11)	31,206	18,896	15,919
Municipal services and security expenses	7,340	3,040	2,899
Fuel, heating and electricity expenses	7,050	4,862	4,379
Fees for card payments	6,953	4,988	4,988
Travel expenses	5,339	4,352	1,167
Freight costs	5,254	11,127	11,127
Communication expenses	3,567	2,252	2,252
Training expenses	3,205	2,216	1,832
Renovation expenses of retail outlets	3,098	1,414	1,414
Information technology expenses	3,051	2,090	2,090
Bank fees	3,028	2,042	2,042
Expenses for uniforms	2,089	1,262	1,262
Packaging expenses	1,450	1,708	1,708
Impairment for trade receivables (Note 5)	1,330	4	4
Consulting fees	721	911	911
Other sales expenses ²	25,255	15,712	12,542
Total	522,620	350,471	300,879

¹For reclassification of distribution costs see Note 1 “Comparability”.

²Other sales expenses consist of insurance, customs expenses and services connected to administration of retail offices.

NOTE 21 Administrative and general expenses

	2007	Reclassified 2006 ¹	2006
Payroll costs	25,630	23,096	60,588
Depreciation and amortisation (Notes 10-11)	5,348	4,899	7,498
Operating lease expenses (Note 12)	7,510	1,770	3,529
Information technology expenses	4,992	2,824	2,902
Move into new facilities	3,814	0	0
Municipal services and security expenses	1,707	1,186	1,658
Sponsorship	1,064	1,341	1,416
Fuel, heating and electricity expenses	1,296	971	1,453
Bank fees	1,015	994	994
Training expenses	922	455	1,371
Communication costs	807	860	894
Travel expenses	380	604	3,809
Management and consulting fees	184	2,581	2,976
Other administrative expenses ²	6,242	6,753	8,838
Total	60,911	48,334	97,926

¹For reclassification of administrative and general expenses see Note 1 “Comparability”.

²Other administrative expenses consist of insurance, office expenses, auditing and accounting and other services.

NOTE 22 Other operating income

	2007	2006
Gain from sale of non-current assets	15,362	7,443
Gain from revaluations of investment property (Note 9)	8,893	4,379
Other operating income	964	660
Total	25,219	12,482

NOTE 23 Other operating expenses

	2007	2006
Foreign exchange losses	9,945	4,710
Impairment of non-current assets held for sale (Note 10)	1,318	0
Fines, penalties and tax interest	1,470	626
Representation costs	551	220
Other operating expenses	531	1,351
Total	13,815	6,907

NOTE 24 Income tax

Income tax expense

	2007	2006
Income tax expense	8,549	4,001
Deferred income tax expense (income) (Note 7)	640	-865
Total income tax expense (income)	9,189	3,136

The income tax calculated on 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 by region for the year ended at 31 December 2007

	Baltic region	Eastern European region	Central European region	Total
Profit (loss) before tax	113,221	-59,067	-1,123	53,031
Range of nominal tax rate	15-28%	24-25%	19-24%	15-28%
Tax calculated from profit (loss) at the nominal tax rate	4,456	-14,257	-370	-10,171
Income tax on dividends (Note 16)	3,359	0	0	3,359
Expenses not deductible for tax purposes	1,088	5,485	179	6,752
Expenses decreasing the profit for tax purposes	-2,436	-2,679	-187	-5,302
Utilisation of tax losses carried forward	-909	0	-306	-1,215
Changes in recognised and off balance sheet deferred tax assets (liabilities)	2,386	12,180	1,081	15,647
Changes in currency rates	0	185	-66	119
Income tax expense	5,558	2,991	0	8,549
Deferred income tax expense (income) (Note 7)	2,386	-2,077	331	640

Income tax by region for the year ended at 31 December 2006

	Baltic region	Eastern European region	Central European region	Total
Profit (loss) before tax	113,559	-18,031	-4,231	91,295
Range of nominal tax rate	15-30%	24-25%	19%	15-30%
Tax calculated from profit (loss) at the nominal tax rate	1,655	-4,402	804	-1,943
Income tax on dividends (Note 16)	1,797	0	0	1,797
Expenses not deductible for tax purposes	371	2,077	0	2,448
Expenses decreasing the profit for tax purposes	-256	-86	0	-342
Utilisation of tax losses carried forward	-1,626	0	0	-1,626
Changes in recognised and off balance sheet deferred tax assets (liabilities)	1,677	2,764	-1,708	2,733
Changes in currency rates	0	69	0	69
Income tax expense	1,941	2,060	0	4,001
Deferred income tax expense (income) (Note 7)	1,677	-1,638	-904	-865

Deferred income tax assets were recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group did not recognise deferred income tax assets of 17,358 thousand kroons (2006: 2,733 thousand kroons) in respect of losses amounting to 70,850 thousand kroons (2006: 12,630 thousand kroons) that can be carried forward against future taxable income. Losses amounting to 2,331 thousand kroons (2006: 5,467 thousand kroons) and 68,519 thousand kroons (2006: 7,163 thousand kroons) expire within 12 months after the balance sheet date and within the following nine years respectively.

Information about contingent income tax liability is disclosed in Note 28.

NOTE 25 Earnings per share**Basic earnings per share**

		2007	2006
Weighted average number of shares	pcs	18,644,850	18,026,350
Net profit attributable to the equity holders of the parent	EEK '000	40,773	87,376
Basic earnings per share	EEK	2.19	4.85

Diluted earnings per share

		2007	2006
Weighted average number of shares	pcs	18,644,850	18,556,609
Net profit attributable to the equity holders of the parent	EEK '000	40,773	87,376
Diluted earnings per share	EEK	2.19	4.71

The comparable information for year 2006, including the basic and diluted earnings per share, the number of shares and the arithmetic average of daily closing prices of the share, has been restated by applying the conditions of the bonus issue (two bonus shares issued for each existing share) carried out in June 2007 (Note 16).

The weighted average number of shares for diluted earnings per share of the previous reporting period has been adjusted by convertible bonds issued to executive management and converted into the registered shares by the end of the reporting period taking into account the actual conversion date and assuming that all outstanding bonds will be converted.

The average price (arithmetic average based on daily closing prices) of AS Baltika share on the Tallinn Stock Exchange in 2007 was 109.99 kroons (2006: 78.39 kroons).

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 either significant influence or control, generally implying an ownership interest of 20% or more (Note 16);
- members of the management, the management board and the supervisory council;
- close family members of the persons stated above;
- entities under the control or significant influence of the members of the management board and the supervisory council;
- joint venture (until 31 March 2007 – see Note 27 for further information).

AS Baltika has purchased (sewing services, goods for resale, non-current assets) and sold its goods and rendered services (management services, other services) to related parties.

Transactions with joint venture

	2007		2006	
	Purchases	Sales	Purchases	Sales
Purchases and sales of goods	9	952	26	2,641
Purchases and sales of services	9,079	1,735	32,734	5,163
Total	9,088	2,687	32,760	7,804

Balances with joint venture

	31.12.2007	31.12.2006
Trade receivables	0	4,659
Other current receivables	0	1,736
Non-current receivables	0	1,359
Trade payables	0	3,125

Convertible bonds

The annual general meeting held in May 2007 approved the convertible bonds program for the company's executive management. It was decided that the executive management would be issued a total of 124,000 convertible bonds: 62,000 E-bonds in 2007 and 62,000 F-bonds in 2008. Each bond entitles the holder to subscribe for three shares in the company. The nominal value of the bonds is 10.00 Estonian kroons per bond. According to the convertible bonds conditions the share subscription price is the weighted average price of the traded shares of AS Baltika on the first day of the bond subscription period.

The subscription price of E-bond was determined based on the share price of 14 June 2007 being 125.07 Estonian kroons per share. During the period from the subscription date to the end of year 2007, the share price has decreased by 51.20%. As a result, the probability of E-bonds to be realised is unreal. E-bonds are not transferred to the bond subscribers' security accounts. The cash consideration in the amount of 57 thousand kroons (cash received less cash returned) is recognised under "Trade and other payables".

Management has decided to make a proposal to the annual general meeting to cancel the subscription of E-bonds and reimburse the paid in funds to the bond subscribers in the amount of 57 thousand kroons.

Loans to management members

	2007	2006
Balance at beginning of year	0	352
Repayments of loans received	0	-352
Balance at end of year	0	0

Compensation for the members of the management board and supervisory council (9 persons)

	2007	2006
Salaries and remuneration	4,751	6,092

The termination benefits for the members of the management board are limited to 6-12 month's salary expense in the amount that is approximately 3,000 thousand kroons in total.

NOTE 27 Subsidiaries and business combinations

Subsidiary	Location	Activity	Holding at 31.12.2007	Holding at 31.12.2006
OÜ Baltman	Estonia	Retail	100%	100%
SIA Baltika Latvia	Latvia	Retail	75%	75%
UAB Baltika Lietuva	Lithuania	Retail	100%	100%
Baltika Ukraina Ltd	Ukraine	Retail	99%	99%
ООО Компания "Baltman RUS"	Russia	Retail	100%	100%
Baltika Poland Sp.z.o.o.	Poland	Retail	100%	100%
Baltika Retail Czech Republic s.r.o.	Czech Republic	Retail	100%	0%
OY Baltinia AB	Finland	Distribution	100%	100%
Baltika Sweden AB	Sweden	Distribution	100%	100%
AS Elina STC	Estonia	Production	-	62.50%
OÜ Baltika Tailor	Estonia	Production	100%	50%
AS Virulane	Estonia	Production	82.66%	82.66%
OÜ Baltika TP	Estonia	Real estate management	100%	100%

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 PricewaterhouseCoopers, Tallinn

Acquisition of minority interest in AS Elina STC

In March 2007, AS Baltika acquired 37.50% of the shares of the subsidiary AS Elina STC becoming the sole owner of the subsidiary. The purchase consideration amounted to 1,300 thousand kroons, which was paid in cash. The registry entry in the Central Register of Securities was concluded on 17 April 2007. The goodwill arising from the transaction was insignificant and has therefore been accounted for using the simplified approach.

Foundation of a subsidiary in the Czech Republic

In 2007, the Group initiated the foundation of the subsidiary in the Czech Republic. In March 2007, the share capital of the subsidiary was paid in. The subsidiary Baltika Retail Czech Republic s.r.o. was registered on 7 May 2007. AS Baltika is the sole owner of the subsidiary.

Acquisition of an additional stake in the joint venture OÜ Baltika Tailor

According to the agreement signed on 27 February 2007 AS Baltika acquired additional 50% of the shares of the joint venture OÜ Baltika Tailor and thereby increased its ownership to 100%. The title to the shares was transferred with the first instalment paid in April. The transaction price was 4,412 thousand kroons paid in cash according to the agreement. The difference between the acquisition cost and acquired share in carrying value of the company's net assets was recognised as goodwill (Note 11). The goodwill is related to control achieved over the flexibility and volumes of the production capacity.

The assets and liabilities at 31 March 2007 arising from the acquisition

	Fair value	Acquiree's carrying amount
Cash and cash equivalents	13	13
Trade and other receivables	7,161	7,161
Inventories	3,143	3,143
Fixed assets (Note 10-11)	4,647	4,647
Borrowings	2,725	2,725
Payables to parent company	6,298	6,298
Trade and other payables	7,084	7,084
Net assets acquired	-1,143	-1,143
Purchase consideration (settled in cash)		4,412
Cash and cash equivalents acquired		-13
Cash outflow on acquisition		4,399
Goodwill arising from acquisition (Note 11)		5,555

The effect of acquired business combination on revenues and net income of the Group was insignificant.

Merger of the fully owned subsidiaries

On 28 May 2007, an agreement was signed to merge the two fully owned subsidiaries of AS Baltika – AS Elina STC and OÜ Baltika Tailor, whereby AS Elina STC was merged with OÜ Baltika Tailor.

NOTE 28 Contingent liabilities

Contingent income tax liability

The retained earnings of AS Baltika at 31 December 2007 amounted to 108,722 thousand kroons (31 December 2006: 160,897 thousand kroons). The income tax rate applicable to the net profit distributable as dividends is 21/79 from 1 January 2008 (from 1 January 2007: 22/78). Thus, the retained earnings payable as dividends to the shareholders would amount to 85,890 thousand kroons at 31 December 2007 (31 December 2006: 125,500 thousand kroons) and the corresponding income tax to 22,832 thousand kroons (31 December 2006: 35,397 thousand kroons).

Contingent liabilities arising from potential tax audit

Tax audit has been performed in the Group's subsidiary in Russia during year 2007. The findings of the tax audit have no significant influence on the Group's results or the Group's risk assessment.

The tax authorities may at any time within six years subsequent to the reported tax year perform a tax audit of the Group's companies books and financial and tax records and may as a result of the inspection impose additional tax assessment and penalties.

The Parent company's management is not aware of any circumstances which may give rise to a potential material liability in any Group company in this respect.

NOTE 29 Events after the balance sheet date

Acquisition of an additional stake in AS Virulane

AS Baltika concluded an agreement on 22 January 2008 to acquire 4,250 shares (10.10%) in AS Virulane for 3,150 thousand kroons. The purchase price shall be settled in two payments. The ownership of the shares will be transferred with the settlement of the second payment on 25 March 2008.

On 19 February 2008 AS Baltika acquired additional 240 shares (0.57%) in AS Virulane. The purchase consideration amounted to 178 thousand kroons.

As a result of the transactions described above, AS Baltika's ownership in AS Virulane at 25 March 2008 shall be 93.30%.

Development of the real estate located at Veerenni 24, Tallinn, Estonia

In 2008, the Group began developing the real estate located in city centre (Veerenni 24, Tallinn, Estonia). In phase I, which should be completed by May 2009, the former production premises are reconstructed into a business centre with approximately 10,000 square metres of office, commercial and service space. In January 2008, the Group signed a long-term loan contract and construction contract in the amount of 160,000 thousand kroons. The mortgage on real estate located at Veerenni 24, Tallinn, Estonia has been increased by 200,000 thousand kroons.

NOTE 30 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), the investments into the shares of subsidiaries are accounted for at cost less any impairment recognised.

Balance sheet of the parent company

	31.12.2007	31.12.2006
ASSETS		
Current assets		
Cash and bank	7,996	547
Trade and other receivables	290,729	239,227
Inventories	115,685	98,876
Total current assets	414,410	338,650
Non-current assets		
Investments in subsidiaries	75,057	49,785
Investments in joint venture	0	1,000
Other non-current assets	63,083	51,005
Investment property	0	23,572
Property, plant and equipment	8,477	19,486
Intangible assets	23,510	25,045
Total non-current assets	170,127	169,893
TOTAL ASSETS	584,537	508,543
EQUITY AND LIABILITIES		
Current liabilities		
Borrowings	94,349	83,077
Trade and other payables	126,217	116,161
Total current liabilities	220,566	199,238
Non-current liabilities		
Borrowings	75,710	40,764
Total non-current liabilities	75,710	40,764
TOTAL LIABILITIES	296,276	240,002
EQUITY		
Share capital at par value	186,449	62,150
Share premium	0	59,088
Statutory reserve	18,644	5,823
Other reserves	7,489	3,898
Retained earnings	75,679	137,582
TOTAL EQUITY	288,261	268,541
TOTAL LIABILITIES AND EQUITY	584,537	508,543

Income statement of the parent company

	2007	2006
Revenue	640,562	604,053
Cost of goods sold	482,492	420,860
Gross profit	158,070	183,193
Distribution costs	-80,861	-67,270
Administrative and general expenses	-46,238	-41,774
Other operating income	20,311	10,532
Other operating expenses	-15,783	-5,344
Operating profit	35,499	79,337
Dividend income	0	3,000
Financial income from other investments	0	1,514
Impairment of investments	4,637	-23,863
Interest expenses, net	-4,918	-2,684
Foreign exchange loss, net	-751	6
Other financial expenses, net	-62	-85
Income tax	-3,359	-1,796
Net profit for the financial year	31,046	55,429

Cash flow statement of the parent company

	2007	2006
Operating activities		
Operating profit	35,499	79,337
Depreciation, amortisation and impairment losses	8,459	7,950
Gain from disposal of non-current assets	-17,886	0
Gain from revaluation of investment property	-2,143	-4,380
Other non-monetary expenses	13,081	3,810
Change in trade and other receivables and payables	-87,725	-72,811
Change in inventories	-16,808	-20,536
Interest paid	-6,635	-4,758
Income tax paid	-2,654	-2,189
Net cash generated from operating activities	-76,812	-13,577
Investing activities		
Acquisition of non-current assets and investment property, thereof	-8,024	-17,948
Under the finance lease terms	1,833	3,945
Proceeds from disposal of non-current assets	300	39
Investments in subsidiaries	-6,839	-785
Interest received	811	100
Dividend received	0	3,015
Proceeds from disposal of current financial assets	0	2,131
Loans granted	-22,568	-51,036
Repayments of loans granted	28,860	13,100
Net cash used in investing activities	-5,627	-47,439
Financing activities		
Received borrowings	123,157	10,000
Repayments of borrowings	-22,466	-9,300
Change in bank overdraft	15,525	31,911
Repayments of finance lease	-7,690	-742
Dividend paid	-14,910	-12,020
Receipts from contributions into share capital	0	12,791
Proceeds from issue of bonds	28,523	30,239
Redemption of bonds	-31,500	-17,500
Net cash generated from financing activities	90,639	45,379
Effect of exchange gains (losses) on cash and cash equivalents	-751	6
Total cash flows	7,449	-15,631
Cash and cash equivalents at the beginning of the period	547	16,178
Cash and cash equivalents at the end of the period	7,996	547

Statement of changes in equity of the parent company

	Share capital	Share premium	Reserves	Retained earnings	Total
Balance at 31.12.2005	58,230	49,690	9,532	94,373	211,825
Dividends paid	0	0	0	-12,031	-12,031
Transfers to statutory reserve	0	0	189	0	189
Increase of share capital	3,920	9,083	0	0	13,003
Reclassification of reserves	0	0	0	-189	-189
Equity-settled share-based transactions	0	315	0	0	315
Net profit for the period (adjusted)	0	0	0	55,429	55,429
Balance at 31.12.2006	62,150	59,088	9,721	137,582	268,541
Book value of holdings under control or significant influence					-50,785
Value of holdings under control or significant influence, calculated under equity method					78,419
Adjusted unconsolidated equity at 31.12.2006					296,175
Dividends paid	0	0	0	-14,916	-14,916
Transfers to statutory reserve	0	0	12,822	-12,822	0
Increase of share capital	124,299	-59,088	0	-65,211	0
Revaluation of investment property	0	0	3,590	0	3,590
Net profit for the period (adjusted)	0	0	0	31,046	31,046
Balance at 31.12.2007	186,449	0	26,133	75,679	288,261
Book value of holdings under control or significant influence					-62,094
Value of holdings under control or significant influence, calculated under equity method					103,268
Adjusted unconsolidated equity at 31.12.2007					329,435

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

NOTE 31 Revenues by EMTAK (the Estonian classification of economic activities)

Code	Definition	Parent company		Group	
		2007	2006	2007	2006
1413	Manufacture of other outerwear	0	0	14,583	189
4641	Wholesale of textiles	5,399	7,286	2,456	4,572
4642	Wholesale of clothing and footwear	626,522	579,521	144,696	150,585
4771	Retail sales of clothing in specialised stores	2,115	10,134	987,891	736,838
6820	Renting and operating of own or leased real estate	6,526	7,112	1,894	7,297
Total		640,562	604,053	1,151,520	899,481

INDEPENDENT AUDITOR'S REPORT

(Translation of the Estonian original)*

To the Shareholders of AS Baltika

We have audited the accompanying consolidated financial statements of AS Baltika and its subsidiaries (the Group) which comprise the consolidated balance sheet as of 31 December 2007 and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management Board's Responsibility for the Financial Statements

Management Board is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2007, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.



Urmas Kaarlep
AS PricewaterhouseCoopers



Eva Jansen
Authorised Auditor

25 March 2008

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

PROFIT ALLOCATION RECOMMENDATION

The management board of AS Baltika recommends that the net profit for the year ended at 31 December 2007 in the amount of 40,773 thousand kroons to be transferred to the retained earnings.

Retained earnings from previous periods at 31 December 2007	67,949
Net profit for the year 2007	40,773
Total retained earnings at 31 December 2007	108,722

DECLARATION OF THE MANAGEMENT BOARD AND SUPERVISORY COUNCIL

The management board has prepared the management report and the consolidated financial statements of AS Baltika for the year ended at 31 December 2007.

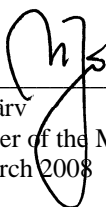
The supervisory council of AS Baltika has reviewed the annual report, prepared by the management board, consisting of the management report, the consolidated financial statements, the management board's recommendation for profit distribution and the independent auditor's report, and has approved the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



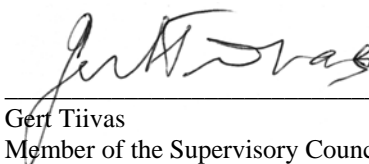
Meelis Milder
Chairman of the Management Board
26 March 2008



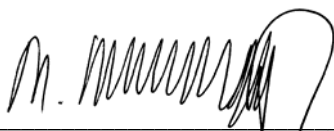
Tiina Mõis
Chairman of the Supervisory Council
26 March 2008



Ülle Järv
Member of the Management Board
26 March 2008



Gert Tiivas
Member of the Supervisory Council
26 March 2008



Maire Milder
Member of the Management Board
26 March 2008



Reet Saks
Member of the Supervisory Council
26 March 2008



Boriss Loifenfeld
Member of the Management Board
26 March 2008



Allan Remmelkoo
Member of the Supervisory Council
26 March 2008



Andres Erm
Member of the Supervisory Council
26 March 2008