

AS MERKO EHITUS
GROUP

Consolidated interim report 6M 2006

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Primary activity: General contracting in construction sector

Auditor: AS PricewaterhouseCoopers

COMMENTARY TO 6M 2006 FINANCIAL RESULTS

The net sales of Merko Ehitus Group for the first six months of 2006 were 1712,7 million kroons with a net profit of 169,0 million kroons. Group's net sales increased by 17.9% and net profit by 12.8% as compared to the same period in 2005. One million kroons of the net profit consisted of extraordinary income which was gained from divesting a holding in an associated company. As a result of materialised residential building development projects and more efficient cost management, Group's net profit marginal increased in the second quarter from the 6.4% to 9.8%.

Group's net sales in the 2nd quarter of 2006 were 1168,1 million kroons and net profit amounted to 134,2 million kroons. The sharp increase in turnover and net profit originated from changes in the calculation methods of residential building development operations in 2005. As a result of these changes, proceeds and profit calculation periods shortened significantly, which also increased the volatility of net profit and profit margin in mid-quarter reports.

Most important companies of the Group 6M 2006 consolidated net sales (sales outside the Group) were:

in thousand kroons and euros

	2006 6 months		2005 6 months	
	EEK	EUR	EEK	EUR
Estonian companies				
Construction				
AS Merko Ehitus	885 811	56 614	837 760	53 543
AS Gustaf (100% partnership)	44 629	2 852	37 400	2 390
OÜ Gustaf Tallinn (80% partnership)	60 126	3 843	46 681	2 983
AS Merko Tartu (66% partnership)	86 743	5 544	81 763	5 226
Tallinna Teede AS (100% partnership)	72 333	4 623	71 863	4 593
OÜ Woody (100% partnership)	25 558	1 633	25 890	1 655
Latvian companies				
Construction				
SIA Merks (100% partnership)	346 009	22 114	266 033	17 003
Lithuanian companies				
Construction				
UAB Merko Statyba (100% partnership)	190 832	12 196	85 921	5 491

There were no significant changes in the construction market during the first six months of 2006. Good demand and growth characterised the market in the Baltic countries. According to Estonia's Statistical Office, current prices in the construction market increased 32.7% in Latvia, 33.7% in Lithuania and 36.2% in Estonia in the first quarter of the year. Rapid increase in volume highlighted the unsatisfactory situation prevailing in the workforce and material supply sector, which boosted the on-going increase in construction prices even further.

Limited supply of workforce and the quick price increase are currently the main factors clouding market's future development. Rapidly changing environment hinders planning and increases the risk of extraordinary costs significantly. The continuously increasing construction prices, which currently exceed the consumer price index, may decrease demand in the long run as adjusting project calculations with the continuously rising prices becomes increasingly complicated for developers, which is likely to lead to postponing and abandoning of new projects in future.

The ratios and calculation methods characterizing the operating activities of the Group were as follows:

	2006 6 months	2005 6 months
Net profit margin *	9,8 %	9,2 %
Operating profit margin	10,6 %	10,5 %
Return on equity per annum	29,6 %	39,2 %
Return on assets per annum	13,4 %	20,7 %
Current ratio	1,8	1,6
Equity ratio	42,0 %	49,5 %
General expenses to net sales	4,3 %	4,5 %
Staff costs to net sales	8,6 %	7,0 %
Average number of full-time employees	831	669

* less extraordinary profit

Net profit margin: $\text{Net profit} / \text{Sales}$

Operating profit margin: $\text{Operating profit} / \text{Sales}$

Return on equity: $\text{Net profit} \times 2^* / \text{Average equity during the period}^*$

Return on assets: $\text{Net profit} \times 2^* / \text{Average assets during the period}$

Current ratio: $\text{Current assets} / \text{Current liabilities}$

Equity ratio: $\text{Owners equity}^* / \text{Total assets}$

General expenses to net sales: $\text{General expenses} / \text{Sales}$

Staff costs to net sales: $\text{Staff costs} / \text{Sales}$

* calculated from the share of the parent company's shareholders

In 30.06.2006, the average number of full-time employees in the Group's service was 831, having increased by 41 employees in last quarter. The gross salaries paid to full-time personnel amounted to 123.3 million kroons.

INCOME STATEMENT
consolidated, unaudited

	Note	EEK		EUR	
		2006 6 months	2005 6 months	2006 6 months	2005 6 months
Sales	1	1 712 707	1 452 790	109 462	92 850
Cost of goods sold		(1 455 737)	(1 234 738)	(93 039)	(78 914)
Gross profit		256 970	218 052	16 423	13 936
Marketing expenses		(11 273)	(10 368)	(720)	(663)
Administrative and general expenses		(62 653)	(54 682)	(4 004)	(3 495)
Other operating income		12 818	3 421	819	219
Other operating expenses		(13 574)	(1 224)	(868)	(78)
Operating profit		182 288	155 199	11 650	9 919
Financial income and expenses		(297)	14 419	(19)	922
incl. financial income (expenses) from investments in subsidiaries		2	-	0	-
financial income (expenses) from investments in associate companies and joint ventures		4 476	11 003	286	703
financial income and expenses from other long-term financial investments		6	118	0	8
interest expense		(5 475)	(1 093)	(350)	(69)
foreign exchange gain		(2 895)	(121)	(185)	(8)
other financial income and expenses		3 589	4 512	230	288
Profit before tax		181 991	169 618	11 631	10 841
Corporate income tax expense		(10 780)	(18 619)	(689)	(1 190)
Net profit for current period		171 211	150 999	10 942	9 651
incl. net profit attributable to equity holders of the parent company		168 961	149 779	10 798	9 573
minority interest		2 250	1 220	144	78
Earnings per share for profit attributable to the equity holders of the parent company (basic and diluted, in EEK and EUR)	2	9,55	8,46	0,61	0,54

INCOME STATEMENT
consolidated, unaudited

	EEK		EUR	
	2006 II quarter	2005 II quarter	2006 II quarter	2005 II quarter
Sales	1 168 131	826 768	74 657	52 840
Cost of goods sold	(985 730)	(700 828)	(63 000)	(44 791)
Gross profit	182 401	125 940	11 657	8 049
Marketing expenses	(5 139)	(5 158)	(328)	(329)
Administrative and general expenses	(30 184)	(27 316)	(1 929)	(1 746)
Other operating income	11 433	2 524	731	161
Other operating expenses	(10 335)	(532)	(661)	(34)
Operating profit	148 176	95 458	9 470	6 101
Financial income and expenses	(1 577)	6 151	(101)	393
incl. financial income (expenses) from investments in subsidiaries	2	-	0	-
financial income (expenses) from investments in associate companies and joint ventures	1 273	4 072	81	260
financial income and expenses from other long-term financial investments	2	37	0	2
interest expense	(3 281)	(712)	(210)	(45)
foreign exchange gain	(1 696)	(881)	(108)	(56)
other financial income and expenses	2 123	3 635	136	232
Profit before tax	146 599	101 609	9 369	6 494
Corporate income tax expense	(10 780)	(18 291)	(689)	(1 169)
Net profit for current period	135 819	83 318	8 680	5 325
incl. net profit attributable to equity holders of the parent company	134 238	82 949	8 579	5 301
minority interest	1 581	369	101	24
Earnings per share for profit attributable to the equity holders of the parent company (basic and diluted, in EEK and EUR)	7,58	4,69	0,48	0,30

BALANCE SHEET

consolidated, unaudited

	EEK		EUR	
	30.06.2006	31.12.2005	30.06.2006	31.12.2005
ASSETS				
Current assets				
Cash and cash equivalents	377 521	268 446	24 128	17 157
Receivables and prepayments				
Accounts receivable	450 019	296 281	28 761	18 936
Prepaid corporate income tax	2 373	2 471	152	158
Other prepayments and refunds of taxes	34 271	34 199	2 190	2 186
Due from customers	139 328	82 224	8 905	5 255
Other short-term receivables	37 395	57 353	2 390	3 666
Prepayments for services	86 516	72 053	5 529	4 605
	<u>749 902</u>	<u>544 581</u>	<u>47 927</u>	<u>34 806</u>
Inventories				
Raw materials and materials	8 340	1 845	533	118
Work-in-progress	198 672	98 202	12 697	6 276
Finished goods	115 151	4 461	7 360	285
Goods purchased for resale	833 894	855 080	53 296	54 650
Prepayments for inventories	15 210	4 500	972	288
	<u>1 171 267</u>	<u>964 088</u>	<u>74 858</u>	<u>61 617</u>
Total current assets	<u>2 298 690</u>	<u>1 777 115</u>	<u>146 913</u>	<u>113 580</u>
Non-current assets				
Long-term financial investments				
Shares in associated companies and joint ventures	182 554	179 609	11 667	11 479
Deferred income tax assets	31 981	8 753	2 044	559
Long-term receivables	8 984	8 524	574	545
	<u>223 519</u>	<u>196 886</u>	<u>14 285</u>	<u>12 583</u>
Investment property				
Land	21 603	35 634	1 381	2 277
Buildings	6 648	6 872	425	439
	<u>28 251</u>	<u>42 506</u>	<u>1 806</u>	<u>2 716</u>
Property, plant and equipment				
Land	145	145	9	9
Buildings	166 397	12 408	10 635	793
Right of superficies	377	382	24	24
Machinery and equipment	55 260	49 226	3 532	3 146
Other property, plant and equipment	36 102	18 175	2 307	1 162
Buildings in process and prepayments	166	118 668	11	7 584
	<u>258 447</u>	<u>199 004</u>	<u>16 518</u>	<u>12 718</u>
Intangible assets				
Development expenses	-	5	-	0
Other intangible assets	2 078	1 513	133	97
Prepayments for intangible assets	5 046	2 847	322	182
	<u>7 124</u>	<u>4 365</u>	<u>455</u>	<u>279</u>
Total non-currents assets	<u>517 341</u>	<u>442 761</u>	<u>33 064</u>	<u>28 296</u>
TOTAL ASSETS	<u>2 816 031</u>	<u>2 219 876</u>	<u>179 977</u>	<u>141 876</u>

	EEK		EUR	
	30.06.2006	31.12.2005	30.06.2006	31.12.2005
LIABILITIES AND EQUITY				
Current liabilities				
Borrowings				
Short-term loans and bonds	181 622	105 144	11 608	6 720
Long-term loans payable in the following period	11 908	9 697	761	620
	<u>193 530</u>	<u>114 841</u>	<u>12 369</u>	<u>7 340</u>
Trade payables				
Payables to suppliers	439 717	282 087	28 103	18 029
Payables to employees	40 872	37 688	2 612	2 409
Company income tax liability	7 249	950	463	61
Other tax liabilities	25 678	25 020	1 641	1 599
Due to customers	313 150	185 648	20 014	11 865
Other payables	13 787	19 637	881	1 255
Received prepayments	233 506	161 156	14 924	10 299
	<u>1 073 959</u>	<u>712 186</u>	<u>68 638</u>	<u>45 517</u>
Government grants	12 606	22 225	806	1 420
Current provisions	16 817	21 741	1 075	1 390
Total current liabilities	<u>1 296 912</u>	<u>870 993</u>	<u>82 888</u>	<u>55 667</u>
Non-current liabilities				
Loans, bonds and finance lease liabilities	287 687	202 824	18 387	12 963
Other long-term payables	40 122	22 726	2 564	1 452
Deferred income tax liability	-	11 385	-	728
Total non-current liabilities	<u>327 809</u>	<u>236 935</u>	<u>20 951</u>	<u>15 143</u>
Total liabilities	<u>1 624 721</u>	<u>1 107 928</u>	<u>103 839</u>	<u>70 810</u>
Equity				
Minority interests	9 402	10 552	601	674
Equity attributable to equity holders of the parent company				
Share capital	177 000	177 000	11 312	11 312
Statutory reserve capital	17 700	8 850	1 131	566
Currency translation adjustment	(5 008)	(5 059)	(320)	(323)
Retained earnings	992 216	920 605	63 414	58 837
	<u>1 181 908</u>	<u>1 101 396</u>	<u>75 537</u>	<u>70 392</u>
Total equity	<u>1 191 310</u>	<u>1 111 948</u>	<u>76 138</u>	<u>71 066</u>
TOTAL LIABILITIES AND EQUITY	<u>2 816 031</u>	<u>2 219 876</u>	<u>179 977</u>	<u>141 876</u>

STATEMENT OF CHANGES IN EQUITY

unaudited

EEK

	Equity attributable to equity holders of the parent company					Total	Minority interest	Total
	Share capital	Share premium	Statutory reserve capital	Currency translation adjustment	Retained earnings			
Balance as at 31.12.2004	88 500	2 950	8 850	(4 663)	622 333	717 970	7 200	725 170
Effect of exchange rate changes	-	-	-	(405)	-	(405)	-	(405)
Net profit for current period	-	-	-	-	149 779	149 779	1 220	150 999
Equity capitalisation	88 500	(2 950)	-	-	(85 550)	-	-	-
Dividends	-	-	-	-	(57 525)	(57 525)	(2 600)	(60 125)
Balance as at 30.06.2005	177 000	-	8 850	(5 068)	629 037	809 819	5 820	815 639
Balance as at 31.12.2005	177 000	-	8 850	(5 059)	920 605	1 101 396	10 552	1 111 948
Effect of exchange rate changes	-	-	-	51	-	51	-	51
Net profit for current period	-	-	-	-	168 961	168 961	2 250	171 211
Dividends	-	-	-	-	(88 500)	(88 500)	(3 400)	(91 900)
Increase of reserve capital	-	-	8 850	-	(8 850)	-	-	-
Balance as at 30.06.2006	177 000	-	17 700	(5 008)	992 216	1 181 908	9 402	1 191 310

EUR

	Equity attributable to equity holders of the parent company					Total	Minority interest	Total
	Share capital	Share premium	Statutory reserve capital	Currency translation adjustment	Retained earnings			
Balance as at 31.12.2004	5 656	189	566	(298)	39 774	45 887	460	46 347
Effect of exchange rate changes	-	-	-	(26)	-	(26)	-	(26)
Net profit for current period	-	-	-	-	9 573	9 573	78	9 651
Equity capitalisation	5 656	(189)	-	-	(5 467)	-	-	-
Dividends	-	-	-	-	(3 677)	(3 677)	(166)	(3 843)
Balance as at 30.06.2005	11 312	-	566	(324)	40 203	51 757	372	52 129
Balance as at 31.12.2005	11 312	-	566	(323)	58 837	70 392	674	71 066
Effect of exchange rate changes	-	-	-	3	-	3	-	3
Net profit for current period	-	-	-	-	10 799	10 799	144	10 943
Dividends	-	-	-	-	(5 657)	(5 657)	(217)	(5 874)
Increase of reserve capital	-	-	565	-	(565)	-	-	-
Balance as at 30.06.2006	11 312	-	1 131	(320)	63 414	75 537	601	76 138

The share capital of AS Merko Ehitus consists of 17 700 000 common shares with a nominal value of EEK 10 i.e. EUR 0.64.

CASH FLOW STATEMENT
consolidated, unaudited

	EEK		EUR	
	2006 6 months	2005 6 months	2006 6 months	2005 6 months
Cash flows from operating activities				
Operating profit	182 288	155 199	11 650	9 919
Adjustments:				
depreciation and amortisation	13 171	7 231	842	462
(profit) loss from sale of non-current assets	(174)	(242)	(11)	(15)
adjustments of revenue from construction contracts under stage of completion method	70 208	(72 915)	4 487	(4 660)
interest income from business activities	(1 274)	(2 621)	(81)	(168)
changes in provisions	(17 938)	(1 951)	(1 146)	(125)
Change in trade receivables related to operating activities	(95 725)	(20 460)	(6 118)	(1 308)
Change in inventories	(192 550)	(124 466)	(12 306)	(7 955)
Change in trade payables related to operating activities	171 612	182 773	10 968	11 681
Interests paid	(7 269)	(1 781)	(465)	(114)
Other financial income	4	3 633	0	232
Corporate income tax paid	(38 999)	(17 794)	(2 493)	(1 137)
	<u>83 354</u>	<u>106 606</u>	<u>5 327</u>	<u>6 812</u>
Cash flows from investing activities				
Investments into subsidiaries	(3 029)	(10 522)	(194)	(672)
Proceeds from sale of subsidiaries	(1)	-	0	-
Investments into associates and joint ventures	(3 771)	-	(241)	-
Proceeds from sale of associates and joint ventures	1 847	5 550	118	355
Investments into other financial investments	-	(10)	-	(1)
Proceeds from sale of other financial investments	3 004	-	192	-
Purchase of investment property	-	(63)	-	(4)
Disposal of investment property	-	13 065	-	835
Purchase of property, plant and equipment	(63 342)	(73 537)	(4 048)	(4 700)
Proceeds from sale of property, plant and equipment	574	1 426	37	91
Purchase of intangible assets	(3 129)	(1 446)	(200)	(92)
Loans granted	(223 158)	(107 463)	(14 262)	(6 868)
Loan repayments received	236 487	38 127	15 114	2 437
Interest received	3 277	1 484	209	95
Dividends received	3 000	3 323	192	212
	<u>(48 241)</u>	<u>(130 066)</u>	<u>(3 083)</u>	<u>(8 312)</u>
Cash flows from financing activities				
Proceeds from borrowings	172 072	67 795	10 997	4 333
Repayments of borrowings	-	(10 694)	-	(683)
Finance lease principal payments	(3 319)	(2 871)	(212)	(183)
Dividends paid	(91 900)	(60 128)	(5 873)	(3 843)
	<u>76 853</u>	<u>(5 898)</u>	<u>4 912</u>	<u>(376)</u>
Change in cash and cash equivalents	111 966	(29 358)	7 156	(1 876)
Cash and cash equivalent at beginning of period	268 446	141 812	17 157	9 063
Effect of exchange rate changes	(2 891)	(1 358)	(185)	(87)
Cash and cash equivalent at end of period	<u>377 521</u>	<u>111 096</u>	<u>24 128</u>	<u>7 100</u>

NOTES**Note 1 Business- and geographical segments****Business segments**

2006 6 months	Construc- tion	Road construction	Concrete elements	Group	
Sales	1 640 373	72 334	-	1 712 707	
Sales between segments	1 303	54 880	-	56 183	
Sales of the segment	1 641 676	127 214	-	1 768 890	
Segment's operating profit	165 530	16 758	-	182 288	
Financial income (expenses)				(297)	
incl. profit (loss) from associates and joint ventures	610	-	3 866	4 476	
Profit before tax				181 991	
Corporate income tax				(10 780)	
Net profit for the Group				171 211	
incl. attributable to equity owners of the parent company				168 961	
minority interest				2 250	
Segment's asset	2 374 858	181 010	-	2 555 868	
Associates and joint ventures	156 386	-	26 168	182 554	
Unallocated assets				77 609	
Total consolidated assets				2 816 031	
Segment's liabilities	1 033 256	77 320	-	1 110 576	
Unallocated liabilities				514 145	
Total consolidated liabilities				1 624 721	
Purchase of property, plant and equipment and intangible assets	64 829	1 642	-	66 471	
Depreciation and amortization	9 062	4 109	-	13 171	
2005 6 months	Construc- tion	Road construction	Concrete elements	Construction of commu- nication networks	Group
Sales	1 384 783	68 007	-	-	1 452 790
Sales between segments	2 248	3 856	-	-	6 104
Sales of the segment	1 387 031	71 863	-	-	1 458 894
Segment's operating profit	145 803	9 396	-	-	155 199
Financial income (expenses)					14 419
incl. profit (loss) from associates and joint ventures	5 706	1 923	4 203	(829)	11 003
Profit before tax					169 618
Corporate income tax					(18 619)
Net profit for the Group					150 999
incl. attributable to equity owners of the parent company					149 779
minority interest					1 220
Segment's asset	1 399 869	110 850	-	-	1 510 719
Associates and joint ventures	2 819	-	18 845	3 752	25 416
Unallocated assets					99 728
Total consolidated assets					1 635 863
Segment's liabilities	682 468	57 040	-	-	739 508
Unallocated liabilities					80 716
Total consolidated liabilities					820 224
Purchase of investment property	63	-	-	-	63
Purchase of property, plant and equipment and intangible assets	72 761	6 142	-	-	78 903
Depreciation and amortization	4 029	3 202	-	-	7 231

Costs, assets and liabilities that cannot be related to a specific asset or it is not practical to do so are considered as unallocated.

In February 2006, AS Merko Ehitus sold a 12% holding in the associated company AS Telegrupp for 1847 thousand kroons (the gained sales profit amounted to 423 thousand kroons), and as a result of this the remaining 19% holding in AS Telegrupp and communication network construction operations are no longer considered an independent business segment. In June 2006, the remaining 19% holding in AS Telegrupp was sold for 3004 thousand kroons (the acquired sales profit amounted to 618 thousand kroons).

Geographical segments

	Sales		Total assets		Purchase of investment property		Purchase of property, plant and equipment and intangible assets	
	2006 6 months	2005 6 months	2006 6 months	2005 6 months	30.06.2006	30.06.2005	2006 6 months	2005 6 months
Estonia	1 129 066	1 100 837	1 332 044	1 049 243	-	39	7 620	14 270
Latvia	375 281	266 033	1 226 300	445 936	-	24	58 543	64 477
Lithuania	208 360	85 920	257 687	140 684	-	-	308	156
Total	1 712 707	1 452 790	2 816 031	1 635 863	-	63	66 471	78 903

Sales revenue is based on the country in which the customer is located; the assets are reported basing on the geographic location of the assets.

Note 2 Earnings (loss) per share

Ordinary net profit (-loss) per share is calculated on the basis of the relation between the net profit (-loss) attributed to parent company's shareholders and the weighted average number of ordinary shares excluding the shareholder's share.

	2006 6 months	2005 6 months
Net profit attributable to shareholders (in thousand kroons)	168 961	149 779
Weighted average number of ordinary shares (thousand pcs)	17 700	17 700
Earnings per share (in kroons)	9,55	8,46

The Group did not have any potential ordinary shares to be issued, therefore the diluted earnings per share equal the basic earnings per share.

MANAGEMENT DECLARATION

The Management Board of Merko Ehitus has prepared the consolidated 6M interim report 2006 as presented on pages 2 to 11.

The Management Board of Merko Ehitus confirms in its best knowledge, that:

- the accounting principles applied in preparing the interim financial statement are in accordance with International Financial Reporting Standards as adopted by the EU;
- the interim financial statement presents a true and fair view of the financial position, financial results and cash flows of the parent and its subsidiaries;
- AS Merko Ehitus and its subsidiaries are going concerns.

Tõnu Toomik	Chairman of the Board		11.08.2006
Alar Lagus	Member of the Board		11.08.2006
Veljo Viitmann	Member of the Board		11.08.2006
Andres Agukas	Member of the Board		11.08.2006
Tõnu Korts	Member of the Board		11.08.2006