

# AS MERKO EHITUS GROUP

## Consolidated interim report 3M 2006

Commercial Registry No: 10068022

Address: 9G Järvevana road, 11314 Tallinn

Telephone: +372 680 5105

Fax: +372 680 5106

E-mail: [merko@merko.ee](mailto:merko@merko.ee)

Homepage: [www.merko.ee](http://www.merko.ee)

Primary activity: General contracting in construction sector

Auditor: AS PricewaterhouseCoopers

## COMMENTARY TO 3M 2006 FINANCIAL RESULTS

Sales revenue of Merko Ehitus Group in the first quarter of 2006 was 544.6 million kroons and profit 34.7 million kroons. As compared to the corresponding period of previous year, Group's sales revenue decreased by 13.0 percent and profit by 48.0 per cent.

First quarter results were affected by changes in accounting principles of residential development activities, costs of launching Riga Arena and the continuing rise of labour and construction material costs. Compared to the first quarter of 2005, the results were mostly influenced by changes in the principles governing the recording of apartment buildings. During the compiling of the annual report of 2005, the company changed the accounting principles in residential development activities at the suggestion of the auditor. After the changes in accounting principles the company records development projects in compliance with standards IAS 2 (inventories)/IAS 18 (revenue), according to which the entire revenue from sale of apartments is recorded in the profit and loss account after the title deed has been passed on to the buyer(s). The result of the change is the recording of the entire revenue from a development project in a very short period of time, due to which the volatility of profits and profitability in quarterly reports will increase. The changes in accounting principles affected first quarter sales of the company by - 123 million kroons and profits by - 27 million kroons.

In 2006 first quarter, the average number of full-time employees in the Group's service was 790, having increased by 95 employees in last quarter. The gross salaries paid to full-time personnel amounted to 58.5 million kroons having increase by 68.6% compared to the first quarter of 2005.

Construction sector in 2006 will experience stable growth. The lack of internal resources in the Baltic States will prevent raising the supply of construction services and therefore construction costs will continue to rise. Limited labour and fast price rises will pose a serious challenge to constructors to complete projects on schedule and within the budget limits. The outlook of construction business is becoming increasingly difficult to forecast due to the quickly changing environment, which may negatively impact the profitability of the sector.

Most important companies of the Group 3M 2006 consolidated net sales (sales outside the Group) were:

*in thousand kroons and euros*

	2006 3 months		2005 3 months	
	EEK	EUR	EEK	EUR
Estonian companies				
<b>Construction</b>				
AS Merko Ehitus	278 427	17 795	374 546	23 938
AS Gustaf (100% partnership)	16 949	1 083	13 861	886
OÜ Gustaf Tallinn (80% partnership)	20 416	1 305	27 427	1 753
AS Merko Tartu (66% partnership)	28 204	1 803	27 842	1 779
Tallinna Teede AS (100% partnership)	2 734	175	10 969	701
OÜ Woody (100% partnership)	47 688	3 048	25 332	1 619
Latvian companies				
<b>Construction</b>				
SIA Merks (100% partnership)	93 298	5 963	110 564	7 066
Lithuanian companies				
<b>Construction</b>				
UAB Merko Statyba (100% partnership)	56 799	3 630	35 482	2 268

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

	2006 3 months	2005 3 months
Net profit margin *	6,4 %	8,8 %
Operating profit margin	6,3 %	9,4 %
Return on equity per annum	12,4 %	35,6 %
Return on assets per annum	6,0 %	20,3 %
Current ratio	2,0	2,0
Equity ratio	47,4 %	56,8 %
General expenses to net sales	7,1 %	4,8 %
Staff costs to net sales	13,3 %	7,8 %

\* less extraordinary profit

Net profit margin: Net profit / Sales

Operating profit margin: Operating profit / Sales

Return on equity: Net profit x 4\* / Average equity during the period\*

Return on assets: Net profit x 4\* / Average assets during the period

Current ratio: Current assets / Current liabilities

Equity ratio: Owners equity\* / Total assets

General expenses to net sales: General expenses / Sales

Staff costs to net sales: Staff costs / Sales

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

**INCOME STATEMENT**  
consolidated, unaudited

	Note	EEK		EUR	
		2006 3 months	2005 3 months	2006 3 months	2005 3 months
Sales	1	544 576	626 023	34 805	40 010
Cost of goods sold		(470 008)	(533 911)	(30 039)	(34 123)
<b>Gross profit</b>		74 568	92 112	4 766	5 887
Marketing expenses		(6 134)	(5 210)	(392)	(333)
Administrative and general expenses		(32 469)	(27 365)	(2 075)	(1 749)
Other operating income		1 407	991	90	63
Other operating expenses		(3 260)	(786)	(209)	(50)
<b>Operating profit</b>		34 112	59 742	2 180	3 818
Financial income and expenses		1 280	8 267	82	528
incl. financial income (expenses) from investments in associate companies and joint ventures		3 203	6 931	205	443
financial income and expenses from other long-term financial investments		3	80	0	5
interest expense		(2 194)	(381)	(140)	(24)
foreign exchange gain		(1 199)	760	(77)	48
other financial income and expenses		1 467	877	94	56
<b>Profit before tax</b>		35 392	68 009	2 262	4 346
Corporate income tax expense		-	(327)	-	(21)
<b>Net profit for current period</b>		35 392	67 682	2 262	4 325
incl. net profit attributable to equity holders of the parent company		34 723	66 830	2 219	4 271
minority interest		669	852	43	54
Earnings per share for profit attributable to the equity holders of the parent company (basic and diluted, in EEK and EUR)	2	1,96	3,78	0,13	0,24

**BALANCE SHEET**  
consolidated, unaudited

	EEK		EUR	
	31.03.2006	31.12.2005	31.03.2006	31.12.2005
<b>ASSETS</b>				
<b>Current assets</b>				
Cash and cash equivalents	304 293	268 446	19 448	17 157
Short-term financial investments	2 386	-	152	-
Receivables and prepayments				
Accounts receivable	307 207	296 281	19 634	18 936
Prepaid corporate income tax	3 412	2 471	218	158
Other prepayments and refunds of taxes	31 996	34 199	2 045	2 186
Due from customers	43 914	82 224	2 807	5 255
Other short-term receivables	36 246	57 353	2 317	3 666
Prepayments for services	84 643	72 053	5 410	4 605
	<u>507 418</u>	<u>544 581</u>	<u>32 431</u>	<u>34 806</u>
Inventories				
Raw materials and materials	3 532	1 845	226	118
Work-in-progress	262 546	98 202	16 780	6 276
Finished goods	8 661	4 461	554	285
Goods purchased for resale	815 388	855 080	52 113	54 650
Prepayments for inventories	15 090	4 500	964	288
	<u>1 105 217</u>	<u>964 088</u>	<u>70 637</u>	<u>61 617</u>
<b>Total current assets</b>	<u>1 919 314</u>	<u>1 777 115</u>	<u>122 668</u>	<u>113 580</u>
<b>Non-current assets</b>				
Long-term financial investments				
Shares in associated companies and joint ventures	178 630	179 609	11 417	11 479
Deferred income tax assets	8 753	8 753	559	559
Long-term receivables	9 603	8 524	614	545
	<u>196 986</u>	<u>196 886</u>	<u>12 590</u>	<u>12 583</u>
Investment property				
Land	21 603	35 634	1 381	2 277
Buildings	6 760	6 872	432	439
	<u>28 363</u>	<u>42 506</u>	<u>1 813</u>	<u>2 716</u>
Property, plant and equipment				
Land	145	145	9	9
Buildings	153 921	12 408	9 837	793
Right of superficies	379	382	24	24
Machinery and equipment	48 740	49 226	3 115	3 146
Other property, plant and equipment	43 066	18 175	2 752	1 162
Buildings in process and prepayments	741	118 668	47	7 584
	<u>246 992</u>	<u>199 004</u>	<u>15 784</u>	<u>12 718</u>
Intangible assets				
Development expenses	-	5	-	0
Other intangible assets	1 909	1 513	122	97
Prepayments for intangible assets	4 428	2 847	283	182
	<u>6 337</u>	<u>4 365</u>	<u>405</u>	<u>279</u>
<b>Total non-currents assets</b>	<u>478 678</u>	<u>442 761</u>	<u>30 592</u>	<u>28 296</u>
<b>TOTAL ASSETS</b>	<u>2 397 992</u>	<u>2 219 876</u>	<u>153 260</u>	<u>141 876</u>

	EEK		EUR	
	31.03.2006	31.12.2005	31.03.2006	31.12.2005
<b>LIABILITIES AND EQUITY</b>				
<b>Current liabilities</b>				
Borrowings				
Short-term loans and bonds	144 976	105 144	9 266	6 720
Long-term loans payable in the following period	10 264	9 697	656	620
	<u>155 240</u>	<u>114 841</u>	<u>9 922</u>	<u>7 340</u>
Trade payables				
Payables to suppliers	233 550	282 087	14 927	18 029
Payables to employees	45 789	37 688	2 926	2 409
Company income tax liability	950	950	61	61
Other tax liabilities	30 554	25 020	1 953	1 599
Due to customers	232 496	185 648	14 859	11 865
Other payables	41 927	19 637	2 680	1 255
Received prepayments	177 456	161 156	11 341	10 299
	<u>762 722</u>	<u>712 186</u>	<u>48 747</u>	<u>45 517</u>
Government grants	22 233	22 225	1 421	1 420
Current provisions	19 711	21 741	1 260	1 390
<b>Total current liabilities</b>	<u>959 906</u>	<u>870 993</u>	<u>61 350</u>	<u>55 667</u>
<b>Non-current liabilities</b>				
Loans, bonds and finance lease liabilities	242 753	202 824	15 515	12 963
Other long-term payables	36 554	22 726	2 336	1 452
Deferred income tax liability	11 389	11 385	728	728
<b>Total non-current liabilities</b>	<u>290 696</u>	<u>236 935</u>	<u>18 579</u>	<u>15 143</u>
<b>Total liabilities</b>	<u>1 250 602</u>	<u>1 107 928</u>	<u>79 929</u>	<u>70 810</u>
<b>Equity</b>				
Minority interests	11 221	10 552	717	674
Equity attributable to equity holders of the parent company				
Share capital	177 000	177 000	11 312	11 312
Statutory reserve capital	8 850	8 850	566	566
Currency translation adjustment	(5 009)	(5 059)	(320)	(323)
Retained earnings	955 328	920 605	61 056	58 837
	<u>1 136 169</u>	<u>1 101 396</u>	<u>72 614</u>	<u>70 392</u>
<b>Total equity</b>	<u>1 147 390</u>	<u>1 111 948</u>	<u>73 331</u>	<u>71 066</u>
<b>TOTAL LIABILITIES AND EQUITY</b>	<u>2 397 992</u>	<u>2 219 876</u>	<u>153 260</u>	<u>141 876</u>

**STATEMENT OF CHANGES IN EQUITY**

unaudited

EEK

	Equity attributable to equity holders of the parent company						Minority interest	Total
	Share capital	Share premium	Statutory reserve capital	Currency translation adjustment	Retained earnings	Total		
<b>Balance as at 31.12.2004</b>	88 500	2 950	8 850	(4 663)	622 333	717 970	7 200	725 170
Effect of exchange rate changes	-	-	-	(651)	-	(651)	-	(651)
Net profit for current period	-	-	-	-	66 830	66 830	852	67 682
Dividends	-	-	-	-	-	-	(600)	(600)
<b>Balance as at 31.03.2005</b>	88 500	2 950	8 850	(5 314)	689 163	784 149	7 452	791 601
<b>Balance as at 31.12.2005</b>	177 000	-	8 850	(5 059)	920 605	1 101 396	10 552	1 111 948
Effect of exchange rate changes	-	-	-	50	-	50	-	50
Net profit for current period	-	-	-	-	34 723	34 723	669	35 392
<b>Balance as at 31.03.2006</b>	177 000	-	8 850	(5 009)	955 328	1 136 169	11 221	1 147 390

EUR

	Equity attributable to equity holders of the parent company						Minority interest	Total
	Share capital	Share premium	Statutory reserve capital	Currency translation adjustment	Retained earnings	Total		
<b>Balance as at 31.12.2004</b>	5 656	189	566	(298)	39 774	45 887	460	46 347
Effect of exchange rate changes	-	-	-	(42)	-	(42)	-	(42)
Net profit for current period	-	-	-	-	4 271	4 271	54	4 325
Dividends	-	-	-	-	-	-	(38)	(38)
<b>Balance as at 31.03.2005</b>	5 656	189	566	(340)	44 045	50 116	476	50 592
<b>Balance as at 31.12.2005</b>	11 312	-	566	(323)	58 837	70 392	674	71 066
Effect of exchange rate changes	-	-	-	3	-	3	-	3
Net profit for current period	-	-	-	-	2 219	2 219	43	2 262
<b>Balance as at 31.03.2006</b>	11 312	-	566	(320)	61 056	72 614	717	73 331

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 3 months	2005 3 months	2006 3 months	2005 3 months
<b>Cash flows from operating activities</b>				
Operating profit	34 112	59 742	2 180	3 818
Adjustments:				
depreciation and amortisation	5 451	3 074	348	196
(profit) loss from sale of non-current assets	(11)	(197)	(1)	(13)
adjustments of revenue from construction contracts under stage of completion method	84 987	(29 000)	5 432	(1 853)
interest income from business activities	(350)	(686)	(22)	(44)
changes in provisions	(2 324)	1 396	(149)	89
Change in trade receivables related to operating activities	67 875	(60 858)	4 338	(3 890)
Change in inventories	(126 736)	(17 869)	(8 100)	(1 142)
Change in trade payables related to operating activities	(60 243)	35 350	(3 850)	2 259
Interests paid	(2 910)	(499)	(186)	(32)
Corporate income tax paid	(940)	(1 164)	(60)	(74)
	<u>(1 089)</u>	<u>(10 711)</u>	<u>(70)</u>	<u>(686)</u>
<b>Cash flows from investing activities</b>				
Investments into subsidiaries	(2 677)	(1 830)	(171)	(117)
Proceeds from sale of associates and joint ventures	1 847	-	118	-
Investments into other financial investments	-	(10)	-	(1)
Purchase of property, plant and equipment	(51 504)	(23 660)	(3 292)	(1 512)
Proceeds from sale of property, plant and equipment	14	698	1	45
Purchase of intangible assets	(2 140)	(421)	(137)	(27)
Loans granted	(1 221)	(50 389)	(78)	(3 220)
Loan repayments received	14 763	21 044	944	1 345
Interest received	1 304	923	83	59
Dividends received	-	1 823	-	117
	<u>(39 614)</u>	<u>(51 822)</u>	<u>(2 532)</u>	<u>(3 311)</u>
<b>Cash flows from financing activities</b>				
Proceeds from borrowings	79 294	9 359	5 068	598
Repayments of borrowings	-	(781)	-	(50)
Finance lease principal payments	(1 517)	(881)	(97)	(56)
	<u>77 777</u>	<u>7 697</u>	<u>4 971</u>	<u>492</u>
<b>Change in cash and cash equivalents</b>	37 074	(54 836)	2 369	(3 505)
Cash and cash equivalent at beginning of period	268 446	141 812	17 157	9 063
Effect of exchange rate changes	(1 227)	(571)	(78)	(36)
<b>Cash and cash equivalent at end of period</b>	<u>304 293</u>	<u>86 405</u>	<u>19 448</u>	<u>5 522</u>

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

<b>2006 3 months</b>	<b>Construc- tion</b>	<b>Road construction</b>	<b>Concrete elements</b>	<b>Group</b>	
Sales of the segment	541 796	24 782	-	566 578	
Sales between segments	-	(22 002)	-	(22 002)	
Sales	541 796	2 780	-	544 576	
Segment's operating profit	33 940	172	-	34 112	
Financial income (expenses) incl. profit (loss) from associates and joint ventures	539	-	2 664	3 203	
Profit before tax				35 392	
Corporate income tax				-	
Net profit for the Group				35 392	
incl. attributable to equity owners of the parent company				34 723	
minority interest				669	
Segment's asset	2 057 195	108 403	-	2 165 598	
Associates and joint ventures	150 664	-	27 966	178 630	
Unallocated assets				53 765	
Total consolidated assets				2 397 993	
Segment's liabilities	796 727	43 270	-	839 997	
Unallocated liabilities				410 606	
Total consolidated liabilities				1 250 603	
Purchase of property, plant and equipment and intangible assets	53 417	226	-	53 643	
Depreciation and amortization	3 441	2 010	-	5 451	
<b>2005 3 months</b>	<b>Construc- tion</b>	<b>Road construction</b>	<b>Concrete elements</b>	<b>Construc- tion of communication networks</b>	<b>Group</b>
Sales of the segment	617 043	11 486	-	-	628 529
Sales between segments	(2 247)	(259)	-	-	(2 506)
Sales	614 795	11 228	-	-	626 023
Segment's operating profit	62 014	(2 272)	-	-	59 742
Financial income (expenses) incl. profit (loss) from associates and joint ventures	5 955	-	1 695	(719)	6 931
Profit before tax					68 009
Corporate income tax					(327)
Net profit for the Group					67 682
incl. attributable to equity owners of the parent company					66 830
minority interest					852
Segment's asset	1 223 169	72 849	-	-	1 296 018
Associates and joint ventures	10 252	3 627	17 837	3 863	35 579
Unallocated assets					47 736
Total consolidated assets					1 379 333
Segment's liabilities	501 874	31 111	-	-	532 985
Unallocated liabilities					54 747
Total consolidated liabilities					587 732
Purchase of property, plant and equipment and intangible assets	21 844	12 590	-	-	34 434
Depreciation and amortization	1 871	1 203	-	-	3 074

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 per cent share in its associated company AS Telegrupp for 1 847 thousand kroons. The gained profit was 423 thousand kroons. AS Merko Ehitus now has a 19 per cent share in AS Telegrupp and communication network construction activities are no longer considered a separate business segment.

#### Geographical segments

	Sales		Total assets		Purchase of property, plant and equipment and intangible assets	
	2006 3 months	2005 3 months	31.03.2006	31.03.2005	2006 3 months	2005 3 months
Estonia	379 757	479 977	1 120 338	945 187	2 883	14 163
Latvia	105 691	110 564	1 077 690	312 669	50 452	20 271
Lithuania	59 128	35 482	199 964	121 477	308	-
<b>Total</b>	<u>544 576</u>	<u>626 023</u>	<u>2 397 992</u>	<u>1 379 333</u>	<u>53 643</u>	<u>34 434</u>

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 3 months	2005 3 months*
Net profit attributable to shareholders (in thousand kroons)	34 723	66 830
Weighted average number of ordinary shares (thousand pcs)	17 700	17 700
<b>Earnings per share (in kroons)</b>	<u>1,96</u>	<u>3,78</u>

\* The influence of the bonus issue carried out in the 2<sup>nd</sup> quarter of 2005 is included in the first quarter figures of 2005.

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 3M interim report 2006 as presented on pages 2 to 9.

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		16.05.2006
Alar Lagus	Member of the Board		16.05.2006
Veljo Viitmann	Member of the Board		16.05.2006
Jaan Mäe	Member of the Board		16.05.2006
Andres Agukas	Member of the Board		16.05.2006