# Winning Customers

## Annual Report

## 2009

X5 RETAIL GROUP

# Contents

# Operational & Financial Highlights

**WINNING CUSTOMERS**

"2009 was a tough year for Russian consumers and the economy as a whole. X5's response was fast and effective. We won customers by making sure we had the right products at the most attractive prices. Just as important, we kept our focus on X5's strategy to create durable competitive advantages and capitalise on the long-term growth of the Russian market."

**Lev Khasis**, Chief Executive Officer

### X5 in 2009

**Nearly 1 billion** Customer Visits

**USD 8.7 billion** in Net Sales

**25% Pro-Forma Sales Growth** in RUR

**33% Consolidated Sales Growth** in RUR

### X5 at 31 December 2009

**Number 1 Russian Retailer**

**1,372 Multi-Format Stores** in Russia & Ukraine

**1.1 million sq. m.** in Selling Space

**Operations in 45 Cities** of Russia and in Ukraine

In 2009 **X5 outperformed** the competition and delivered the highest like-for-like sales growth of any Russian retailer by responding to the needs of consumers:

- A record **996 million customer visits** to our stores in 2009
- Industry-leading **like-for-like (LFL) sales growth** of **10%**
- **LFL** customer **traffic** rose **5%** – including a market-leading **10% at discounters**
- Delivered on our 2009 target of **25% pro-forma revenue growth** in RUR terms

### Financial Highlights

| | 2009 | 2008[1] | *% change, y-o-y* |
|---|---|---|---|
| **Net Sales, USD million** | 8,717 | 8,892 | *(2%)* |
| **Gross Profit, USD million** | 2,108 | 2,279 | *(7%)* |
| *Gross Margin, %* | *24.2%* | *25.6%* | |
| **EBITDA, USD million** | 736 | 803 | *(8%)* |
| *EBITDA Margin, %* | *8.4%* | *9.0%* | |

*[1] Profit& Loss figures for 2008 in this Annual Report are presented on pro-forma basis, unless otherwise stated. Pro-forma figures include results of the acquired Karusel hypermarket chain from 1 January 2008. We believe pro-forma numbers are useful because they allow investors to evaluate X5's operating results and financial performance for different periods on a more comparable basis. These figures should be used in addition to, but not as a substitute for, the Consolidated Financial Statements included in this Annual Report, which include Karusel's results only as from 30 June 2008, when the acquisition was completed.*

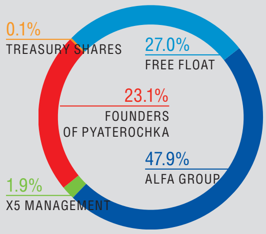
# Shareholder Information

The Company's shares are listed on the London Stock Exchange in the form of Global Depositary Receipts (GDRs) (LSE ticker: FIVE). Each GDR represents an interest of 0.25 of one ordinary share.

As at 31 December 2009, X5's share capital consisted of 67,893,218 issued ordinary shares, with a nominal value of €1.00 each. This represents an equivalent of 271,572,872 GDRs. At 2009 year-end X5's share ownership structure was as follows: Alfa Group – 47.9%, founders of Pyaterochka – 23.1%, X5 Management – 1.9%, treasury shares – 0.1%, free float – 27.0%.

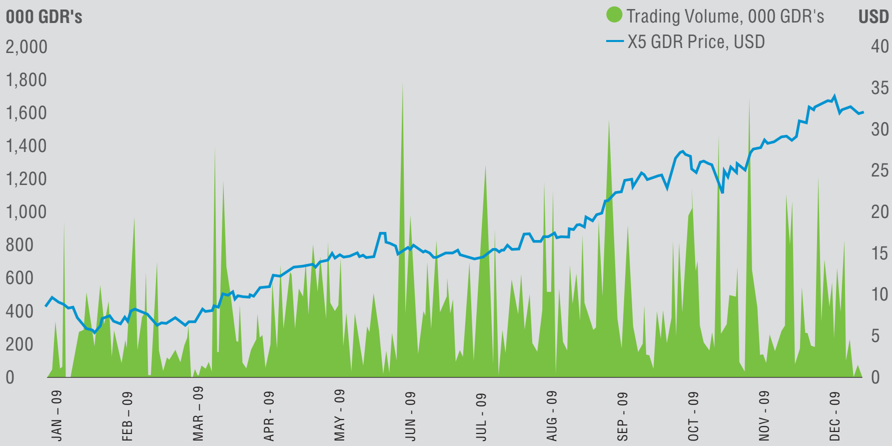
In 2009, X5's GDR price increased 271% to close the year at USD 31.90 per GDR. This nearly fourfold increase was driven by a general recovery in global equity markets and investor appreciation of the Company's business and financial strength and resilient performance during the year. As at 31 December 2009, X5's total market capitalisation amounted to USD 8.7 billion.

**X5 Share Capital as at 31 December 2009**




Total number of shares – 67,893,218
Equivalent of 271,572,872 GDRs

**X5 2009 GDR Price Performance**



# Message from the Chairman of the Supervisory Board

**Hervé Defforey**
Chairman of the Supervisory Board

Amid the challenges of 2009, X5 proved to be a source of strength for consumers and the retail sector of the Russian economy. We gave our customers even better value, continued to open new stores, create new jobs, invest in infrastructure and support thousands of producers weakened by the crisis. I would like to thank X5's employees and management team for their stellar response to the turbulent macro environment and contribution to our Company's strong financial and operational performance.

Russia was hit hard by the global economic crisis. The credit crunch and subsequent sharp drop in demand caused severe dislocation for entire industries and geographic regions. Ordinary Russians – who have seen a steady rise in incomes and living standards for nearly a decade – responded by consuming less and shopping for bargains.

I am especially proud of how our Company reacted to the sudden changes in the marketplace. X5 drew a record of nearly one billion store visits as customers responded enthusiastically to our pricing policy, discounts and promotions. The Company's results underscore the success of our strategy to reinvest in our formats' value propositions.

Following the collapse in Russian equity prices at the end of 2008, the Company has worked hard to restore value for X5's shareholders. We communicated clearly about the Company's strategic priorities and financial discipline, increased transparency about X5's liquidity position, and maintaining a continuous two-way dialogue with investors and analysts on current developments and future plans. As appreciation of X5's business strengths increased, our global depository receipts rose nearly four-fold in value, closing at USD 31.90 per GDR on 31 December 2009 compared to USD 8.60 at the end of 2008.

Looking to the future, we believe the Russian consumer growth story remains intact. Russia is a rapidly developing economy that is still establishing the foundations of a modern, efficient food retail market. We see substantial opportunities for growing X5's position and increasing the penetration of the modern retail channel.

Our objective is to grow significantly faster than the market, by becoming an even stronger, more efficient competitor. In this report, we have outlined how we are executing on the three main pillars of our strategy: Customer focus, operational excellence and disciplined growth. I am confident in X5's prospects to benefit from economic recovery and deliver on our objectives for 2010, while increasing productivity and building competitive advantages to support our long-term success.

**Hervé Defforey**

# Letter from the Chief Executive Officer

2009 was a tough year for Russian consumers and the economy as a whole. X5 Retail Group delivered strong performance in this environment, first, by responding to the plight of consumers more effectively than competitors, and second, through disciplined execution of our long-term strategy for leadership and growth in the Russian retail market.

X5's people can look back with pride on the Company's achievements. We met our 25% pro-forma revenue growth target for 2009 and posted the highest like-for-like sales increases in the Russian retail market. With many retailers weakened by the economic downturn, X5 responded aggressively to win customers with superior offerings and strengthen its leadership in all regions of operations. The Company entered 2010 in an excellent position to drive growth and efficiency while benefiting from future economic recovery.

At the beginning of last year, I laid out a simple game plan for X5's response to Russia's economic crisis: Win customers, expand selectively and manage finances prudently. Let me review our progress against these priorities and then discuss the Company's plans for future customer success, operational efficiency and disciplined growth.

**Winning Customers**

In 2009 we clearly benefited from our multi-format strategy and the phenomenal customer appeal of discounters. Pyaterochka had the highest customer traffic growth of any retailer as customers responded enthusiastically to our brand promise of *lowest price in the market on 100% of assortment*.

In hypermarkets, we re-launched Karusel following successful integration of this acquisition. We are educating Russian consumers on the attractions of hypermarkets for weekend family shopping through our "Everything Under One Roof – At Low Prices" publicity campaigns and promotions.

Supermarkets faced the biggest challenge from trading down trends, especially in regions outside of Moscow and St. Petersburg. Our goal was to maintain loyalty among middle to upper income consumers in areas with favorable demographics for supermarkets.

**Selective Expansion**

Weaker market conditions created opportunities for X5 to accelerate new store openings well in excess of plan. In total we added 271 new stores in 2009, including 189 store openings through organic growth – primarily in discounters, which fit the times and are cheap to add – bringing X5's total store count to 1,372. We shifted our real estate strategy to leasing new locations to take advantage of lower rents and availability of unused retail space.

We were also able to acquire assets at attractive prices while staying within our disciplined investment limit. In addition to organic expansion, we reinforced our number one position in supermarkets with the acquisition of Paterson. Paterson adds high quality locations in key geographic markets with strong demographics for supermarkets, positioning X5 to benefit from future economic recovery.

**Lev Khasis**
Chief Executive Officer,
Chairman of the Management Board

We see substantial scope for raising sales density and profit margins by rebranding and realigning the value proposition of these stores and leveraging X5's scale, distribution and efficiency programmes.

X5 made great progress in developing logistics infrastructure to enhance operational efficiency and competitiveness. We secured at least one distribution centre in each region of our operations and achieved a supply centralisation rate of 61%. This is substantially in excess of our 57% target for 2009, and we now expect further improvement to 67% in 2010.

**Manage Finances Prudently**
The volatility and crisis conditions in the Russian financial markets were a real test of X5's financial strength and endurance in 2009. X5 successfully improved its financial position, ensuring adequate short-term liquidity while increasing cash flows and strengthening the Company's foundation for future growth.

First, we maximised cash flows by growing the top line, controlling costs and managing working capital. Second, we limited capital expenditures, looking closely at all investment projects and identifying the most profitable and strategically important priorities. Third, we managed our liquidity prudently, to optimise our debt structure and improve the maturity profile.

We learned many useful lessons this year for making X5 a stronger, more efficient and disciplined Company. This brings us to our plans for 2010 and beyond. Clearly X5 is now in a unique position to strengthen its growth and leadership in the Russian retail market. Our continued success will be driven by our evolving strategy to balance growth, efficiency and capital discipline:

- We will pursue our strategy of being close to the customer, driving like-for-like sales growth by developing our value propositions, assortment and private label;

- We will execute our Strategic Efficiency Programme to drive operational excellence throughout the supply chain, leveraging our scale, distribution and technology investments to support a much larger and more efficient operation;

- And lastly, we will maintain our focus on disciplined growth, capitalising on positive long-term trends in the Russian market while managing margins and capital expenditures to drive positive cash flow and maximise value for our shareholders.

The new retail law that came into effect in 2010 imposes certain restrictions for modern retail expansion in Russia. The impact on X5, however, will be limited to St. Petersburg, where we are by far the market leader. It is too early to assess the impact of the new supplier relationship rules on the sector and our business until we gain more experience throughout 2010. However, you can be sure that X5 will continue to give customers superior value and assortment with the goal of outperforming the competition.

We will continue to deliver strong growth in 2010 through like-for-like sales increases and stepped up new store openings. We will also look for attractive M&A opportunities, in order to capitalise on consolidation trends in the industry. We are off to a good start following a successful year, and I look forward to reporting to you on our Company's continued progress.

**Lev Khasis**

# Executive Board

**Lev Khasis**
Chief Executive Officer,
Chairman of the Management Board

**Evgeny Kornilov**
Deputy CEO,
Chief Financial Officer

**Teimur Shternlib**
Deputy CEO,
Chief Business Support Officer

**Oleg Vysotsky**
General Director of Discounter Format

**Mikhail Susov**
General Director
of Supermarket Format

**Tatiana Ponomareva**
General Director
of Hypermarket Format

**Dmitry Ishevskiy**
Supply Chain Director

**Ekaterina Ishevskaya**
Commercial Director

**Ekaterina Stolypina**
Human Resources Director

**Mikhail Kuprish**
Development Director

**Karina Chernikova**
Marketing Director

**Andrei Gusev**
Mergers, Acquisitions and
Business Development Director

**Sergey Egorov**
Security Director

**Yury Kobaladze**
Corporate Affairs Director

# Strategic Review


As Russia's largest retailer, X5 is uniquely positioned to capitalise on longer term consumer growth trends. Our goal is to be the number one choice for customers and reinforce X5's leadership in our retail formats – discounters, supermarkets and hypermarkets.

Like many countries, Russia was deeply affected by the global financial crisis and economic downturn in 2009. Consumer confidence dropped to its lowest levels since 1998 due to high unemployment levels and diminished purchasing power. The crisis was an important test of X5 Retail Group's strategy, and we have learned much that will make us a stronger, more efficient and disciplined Company for the future.

First, our response to trading down by consumers was fast and effective. Thanks to aggressive price leadership, especially in discounters, X5 delivered the best like-for-like performance of any Russian food retailer in 2009. We also managed costs to offset price reinvestment and thus support operating margins, and reined in capital expenditures to preserve financial strength.

Just as importantly, the Company continued to execute its longer-term strategy to create durable competitive advantages:

**Customer Focus**
With our three retail formats – discounters, supermarkets and hypermarkets – we have stores for every lifestyle and family budget. Our "Close to the Customer" policy aims to ensure that each of our formats leads its market segment by offering the right products at the most attractive prices. We continue to invest in our value propositions, quality and service in order to build customer loyalty, while innovating to drive growth in areas such as private label and non-food merchandising.

**Operational Excellence**
X5's price leadership is made possible by continuous gains in efficiency. As the Russian market develops, we believe efficiency will be even more important for sustaining leadership and shareholder returns. Our Strategic Efficiency Programme is a multi-year effort to develop X5's operational excellence as a competitive advantage. This means implementing international best practices, increasing in-store productivity, and upgrading distribution infrastructure and IT systems to better manage our supply chain and leverage the Company's growing scale.

**Disciplined Growth**
The third leg of our strategy is disciplined growth and prudent financial management to produce the best long-term returns for our investors. With many retailers weakened by the economic downturn, X5 has responded aggressively to strengthen its leadership in all regions of operations, both through organic expansion of our store base and selective consolidation of smaller retail chains. Our investments focus on prioritising projects with the best potential returns, while increasing cash flows and strengthening our balance sheet to support steady growth in the years to come.

# Customer Focus

## MULTI-FORMAT LEADERSHIP SUPPORTS RESILIENT PERFORMANCE

X5 operates three modern retail formats – soft discounters, supermarkets and hypermarkets – each with a distinctive value proposition. This means we can offer the right products at the most attractive prices for every lifestyle and family budget – and deploy the right format for effective competition in each local area.

2009 was a tough year for Russian consumers and X5 did its utmost to ensure product affordability. Customers came in record numbers – nearly a billion store visits in 2009 – and this enabled us to deliver 10% like-for-like (LFL) sales growth, the highest of any Russian retailer. Our success in staying close to our customers in good times and bad underscored the resilience of X5's multi-format business model:

- Discounters were the clear winner with 17% LFL sales growth on the back of a 10% customer traffic inflow, as consumers responded enthusiastically to Pyaterochka's brand promise of the lowest prices on the market.
- X5 also reinforced Perekrestok's leadership in supermarkets, positioning the format to benefit from recovery in consumer confidence among middle and higher income shoppers.
- In 2009 we re-launched Karusel as the shopping destination for typical families. We are re-positioning the format's value proposition with changes in pricing policy and assortment, while building the brand with consumers.

## "CLOSE TO THE CUSTOMER" POLICY DRIVES SUCCESS

X5's "Close to the Customer" policy guides everything we do to differentiate our formats from the competition. We focus on giving people strong reasons to shop at our stores, including:

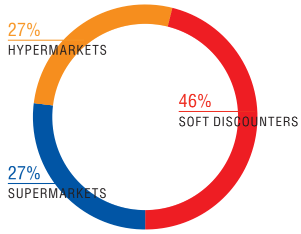
- Price Leadership
- Quality Assortment
- Focus on Fresh
- Loyalty Programs
- Knowledgeable Service
- Innovation – and Fun!

Price leadership across our formats is essential for sustaining customer loyalty and market leadership. X5 constantly reinvests in price and is known for its powerful promotional campaigns and loyalty card rewards. Giving customers the best price is critical for increasing traffic, basket size and sales per square metre – the key drivers of like-for-like sales growth.

X5 has a strong track record of winning customers – including 996 million store visits last year.

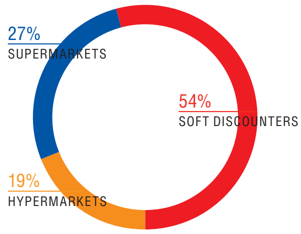
Consumers are looking for bargains, now more than ever – and X5 delivered even more value and the most attractive prices in the market. We are confident these investments in customer loyalty will more than pay back as the Russian economy recovers.

**2009 Net Selling Area Break-Down by Format**



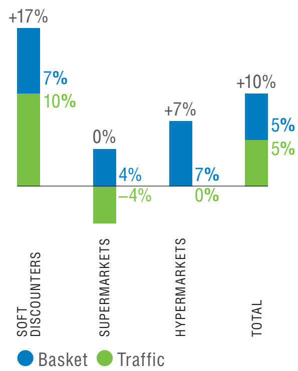

At 31 Dec 2009 total net selling area was 1,063 thousand sq.m.

**2009 Net Retail Sales Break-Down by Format**



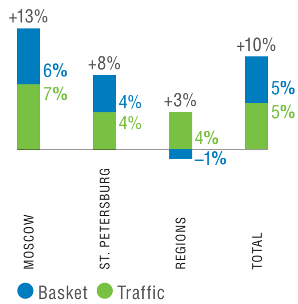

Total FY 2009 net retail sales were USD 8,675 mln

**2009 LFL Performance by Format**




Based on RUR-denominated gross sales

**2009 LFL Performance by Region**




Based on RUR-denominated gross sales

## DIFFERENTIATED ASSORTMENT, PRIVATE LABEL AND LOYALTY PROGRAMMES

X5 continues to fine-tune its value propositions to ensure clear differentiation of each format and successfully serve target customer segments.

Growing private label is a key strategy for X5. We are able to price private label items at a significant discount to leading brands, while maintaining comparable quality and similar or higher margins. In the medium-term, X5 aims to increase private label offerings as a share of total assortment toward the 50% level in soft discounters, up to 30% in supermarkets and up to 10% in hypermarkets.


X5 also plans to take its customer loyalty programmes to the next level. Loyalty and bonus cards are already popular with supermarket and hypermarket customers. Implementation of a state-of-the-art customer relationship management (CRM) system by the end of 2011 will enable upgrades to X5's loyalty programmes as a platform for enhancing each format's value propositions with targeted promotions and personalised service.

We have also begun to introduce modern retailing techniques to strengthen our formats' customer appeals. This includes strategic projects to develop merchandising and category management, working with supplier partners to enhance the range of assortment and price points and drive overall sales growth for entire categories of products.

## DEVELOPING X5'S E-COMMERCE PLATFORM

Internet retailing is still in its infancy in Russia. X5 has the opportunity to develop a leading online retail brand, leveraging our store network, distribution infrastructure and marketing capabilities to drive the growth of e-commerce. In October 2009, X5 entered into a joint project with the founders of internet retailers www.bolero.ru and www.003.ru, in order to develop X5's online platform. X5 has a 51% interest in the newly formed subsidiary with an option to purchase the remaining stake within five years.

# Soft Discounters:
# Pyaterochka – Russia's Price Leader

**VALUE PROPOSITION**

- Lowest price in the market on 100% of assortment
- Close to your home

**TARGET CUSTOMER BASE**

- Over 100 million Russians or 70% of the country's population
- Low to average income
- Price-conscious or looking for value
- Walk to shops
- Shop several times a week
- Food is a simple, affordable pleasure

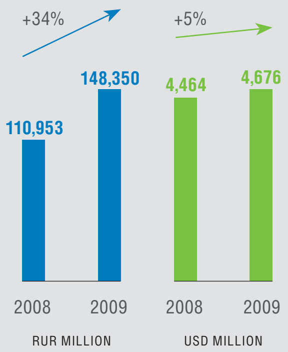
PYATEROCHKA FACT SHEET

| As at 31 December 2009 | Total | Average per Store |
|---|---|---|
| Selling Space, sq. m. | 493,016 | 475 |
| Number of stores | 1,039 | |
| Assortment, # of SKUs | from 2,200 to 3,900 | |
| Number of check-out transactions per day | Over 1.8 mln | Over 1,700 |

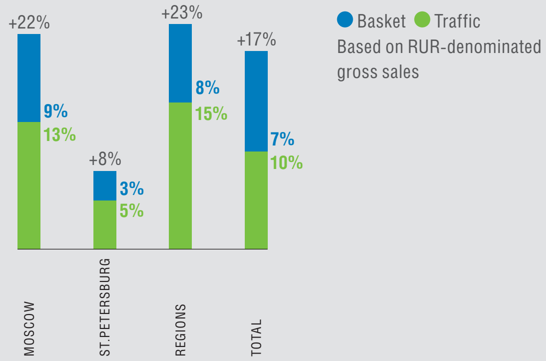
| Full Year 2009 | All Stores | LFL Stores |
|---|---|---|
| Average check[1], RUR | 254 | 260 |
| Sales per square meter[1], RUR/year | 378,349 | 399,154 |

[1] *Based on gross retail sales, i.e. including VAT.*

**Soft Discounters' 2009 Net Retail Sales**




**Soft Discounters' 2009 LFL Performance**




## 2009 PERFORMANCE

For 2009, soft discount stores reported net retail sales of RUR 148,350 million, a year-on-year increase of 34% in RUR terms. Pyaterochka's sales amounted to 54% of X5's total net retail revenue for the year.

X5's exceptionally strong LFL sales performance this year was led by the phenomenal success of soft discounters. Discounter like-for-like sales grew by an industry-leading 17% on strong increases in customer traffic and resilient basket size performance.

Pyaterochka outperformed the competition, attracting new customers and strengthening positions across regions thanks to its *lowest price in the market on 100% of assortment* brand promise. It also scored well with customers with a new advertising campaign playing up Pyaterochka as the brand for ordinary Russians. This is reinforced by our high-profile sponsorship of the Russian National Football Team.

## STRATEGIC OUTLOOK

Soft discounters offer superior prospects in any economic environment, and in 2010 we plan to accelerate expansion and strengthen our leadership in discounters with 200-250 new stores. We will continue to invest in Pyaterochka's position as the Russian price leader, and evolve assortment towards lower price points and private label offerings.

# Supermarkets: Perekrestok – Improving the Quality of Your Life

**VALUE PROPOSITION**
- Best in fresh
- Best in service

**TARGET CUSTOMER BASE**
- ~30 million Russians
- Middle to higher income levels
- Look for quality assortment and service
- Highly value convenience and time
- Shop several times a week

PEREKRESTOK FACT SHEET

| As at 31 December 2009 | Total | Average per Store |
|---|---|---|
| Selling Space, sq. m. | 284,359 | 1,034 |
| Number of stores | 275 | |
| Assortment, # of SKUs | from 6,000 to 16,000 | |
| Number of check-out transactions per day | Over 600,000 | ~2,500 |

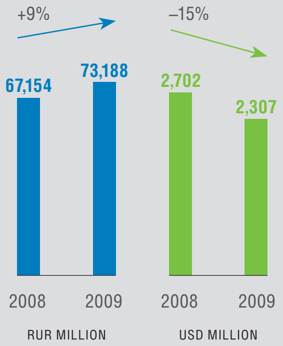
| Full Year 2009 | All Stores | LFL Stores |
|---|---|---|
| Average check(1), RUR | 361 | 367 |
| Sales per square meter(1) , RUR/year | 360,446 | 388,642 |

**Customer Loyalty Fact**

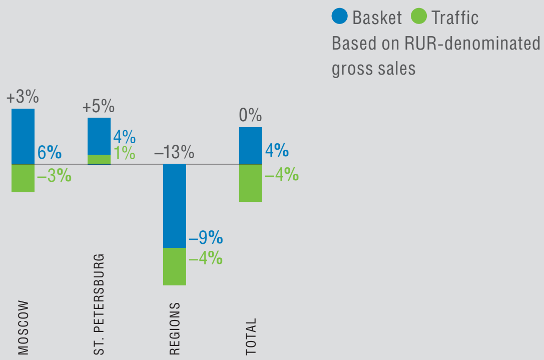
Over ***1.1 million people*** are now members of ***Club Perekrestok***, a personalised loyalty program. Club members account for almost ***30% of*** *total* ***Perekrestok sales***, while average purchase size is typically ***60% higher*** than for regular purchases.

(1) *Based on gross retail sales, i.e. including VAT.*

Supermarkets' 2009 Net Retail Sales




Supermarkets' 2009 LFL Performance




## 2009 PERFORMANCE

For 2009, supermarkets reported net retail sales of RUR 73,188 million, a year-on-year rise of 9% in RUR terms. As a result, Perekrestok's sales amounted to 27% of X5's total net retail revenue for the year.

Supermarkets' performance was affected by trading down by consumers, especially in the regions. Overall, like-for-like sales were flat as 4% basket growth was offset by an equivalent decline in customer traffic. Stores in Moscow and St. Petersburg delivered like-for-like sales growth in the low single digits, but LFL performance in the regions declined 13%.

Despite the economic crisis, there was good news as well: X5's supermarkets gained market share from weakened competitors by strengthening our appeals within Perekrestok's target customer base.

In December 2009 X5 completed the acquisition of Paterson supermarket chain, reinforcing our number one position in supermarkets. Paterson provides high quality locations in key geographic markets with strong demographics for this format. Approximately 57 stores will be converted to Perekrestok by the end of first half 2010.

## STRATEGIC OUTLOOK

Our main objective in 2010 is to gain market share and outperform supermarket competitors while positioning the format to benefit from a recovery in consumer spending. We expect to drive significant growth in sales per square metre at acquired Paterson stores after we convert these to Perekrestok. X5 also plans to open approximately 15 stores organically. We will continue to build Perekrestok's brand on the freshest foods and outstanding service, while maintaining price leadership with the best promotions of any supermarket. We will further develop merchandising and private label, and upgrade our loyalty programme.

# Hypermarkets: Karusel – Everything Under One Roof

**VALUE PROPOSITION**

- Everything under one roof
- At low prices
- Family shopping

**TARGET CUSTOMER BASE**

- ~120 million Russians
- Families with a wide range of household budgets
- Want attractive range of food and non-food items at low prices
- Drive to shops, mainly on weekends
- Want to have fun shopping!

KARUSEL FACT SHEET

| As at 31 December 2009 | Total | Average per Store |
|---|---|---|
| Selling Space, sq. m. | 285,581 | 4,924 |
| Number of stores | 58 | |
| Assortment, # of SKUs | from 20,000 to 50,000 | |
| Number of check-out transactions per day | Over 280,000 | ~5,000 |

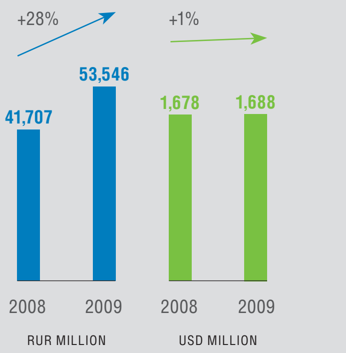
| Full Year 2009 | All Stores | LFL Stores |
|---|---|---|
| Average check[(1)], RUR | 616 | 635 |
| Sales per square meter[(1)], RUR/year | 230,747 | 243,957 |

**Customer Loyalty Fact**

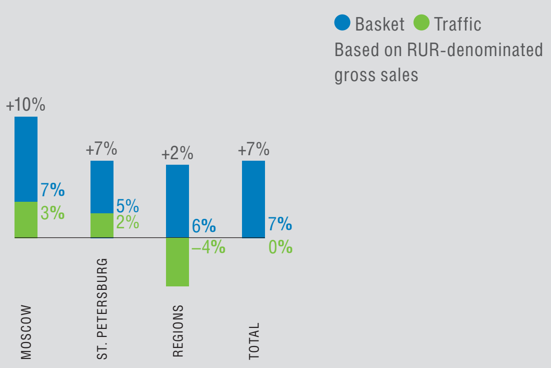
Over ***1.7 million people*** are now Karusel Frequent Customer card holders. 27,000 cards are purchased every month. Card holders' purchases account for ***80% of*** *total* ***Karusel check-out transactions.***

[(1)] *Based on gross retail sales, i.e. including VAT.*

**Hypermarkets' 2009 Net Retail Sales**




**Hypermarkets' 2009 LFL Performance**




## 2009 PERFORMANCE

For 2009, hypermarkets reported net retail sales of RUR 53,546 million, a year-on-year increase of 28% in RUR terms. As a result, Karusel's sales amounted to 19% of X5's total net retail revenue for 2009.

This was a year of significant changes in our hypermarket format. Following the integration of the acquired Karusel chain and conversion of 16 Perekrestok hypermarkets, we re-launched the Karusel brand in the first quarter of 2009.

X5 made substantial changes to Karusel's pricing policy and assortment as part of a fundamental repositioning effort aimed at winning consumers over to the hypermarket format. We believe that recognition of Karusel's *everything under one roof – at a low price* brand promise is gradually increasing thanks to promotions and publicity campaigns to educate customers.

In 2009, hypermarkets performed in line with our expectations. Overall, LFL sales grew 7% due to healthy 10% growth in Moscow and a slightly positive 2% LFL increase in the regions.

## STRATEGIC OUTLOOK

In line with trends in other countries, X5 expects the hypermarket format to increase its penetration of the Russian market. Our goal is to develop a strong, differentiated value proposition aimed at typical Russian families and grow sales densities by optimising our approach. This includes continued improvements to food and non-food assortment with expansion of private label, own-production, ready meals and other offerings. We will also develop Karusel's loyalty programme, re-launching it as a personalised card in 2010. We plan to open 7 to 10 hypermarket stores in 2010, and will capitalise on favourable rents and availability of retail space to secure optimal locations.

# Evolving X5's Private Label Concept

Private label is a major opportunity to enhance our customer value propositions and support margins by offering lower priced, attractive alternatives to branded goods. Consumers are more willing to try private label due to economic conditions – and producers see it as a way to secure large, stable volumes.

X5 is taking private label to the next level in three ways:

- Establishing a unified, coordinated approach across our three formats
- Developing a segmented range of offerings, each with a distinct own-brand identity
- Improving quality and promoting our offerings to increase customer acceptance

Guaranteeing quality is essential for increasing private label take-up by consumers in Russia, where brand loyalty and trust runs high. X5 has introduced strict quality controls within the product development and production process and audits manufacturing facilities on a regular basis.

X5's market leadership, scale and supply chain strengths give the Company unique advantages for developing new offerings and growing volumes. Our goal is to increase private label penetration as a percentage of total assortment (SKUs) towards the 50% level in soft discounters, up to 30% in supermarkets and up to 10% in hypermarkets over the medium term.

**Price Leader Segment:**
*Red Price* own-brand range of products, and other own-brands for alcoholic beverages


**Mainstream Segment:**
*Five Pluses* own-brand range, and other brands for alcohol, seafood and baby care categories


**Premium Segment:**
Own-brand range of products and premium alcohol own-brands under development

# Operational Excellence

X5's price leadership is made possible by continuous gains in efficiency. As the Russian market develops, we believe efficiency will be even more important for sustaining leadership and shareholder returns. Russia's supply chain and logistics infrastructure is still under-developed, and we see major opportunities for raising productivity and building new competitive advantages through our investments and implementation of international best practices.

Cost controls and productivity improvements were essential for supporting X5's profitability in 2009 as we reinvested in our price position to win customers. In addition, the Company launched its Strategic Efficiency Program to take X5's operational excellence to the next level.

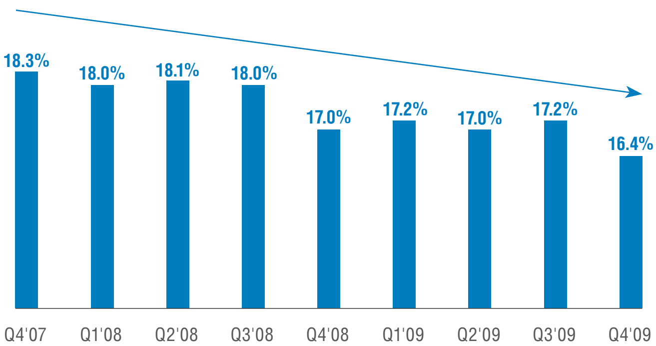
Operational excellence benefits both our customers and shareholders. It enables us to give customers even better prices, higher quality and a more exciting range of product choices. And it helps us run a better business, with the ability to expand rapidly, compete successfully and grow profitably into the future.

## CONTINUED IMPROVEMENT IN EFFICIENCY IN 2009

X5 aims to be Russia's food retail price leader. To ensure that we can profitably and sustainably reinvest in our price position, X5 must continuously improve operational efficiency in addition to leveraging our purchasing power as Russia's largest retailer.

This was especially the case in a crisis year for the Russian economy – X5 delivered the best like-for-like growth in the industry by offering customers the best prices in the marketplace. In line with the Company's "Close to the Customer" policy, in 2009 X5 reduced its gross margin on sales of goods in our stores to 24.2% from 25.6% in 2008. At the same time, we delivered healthy profits for our shareholders as a result of strong top line growth combined with dramatic improvement in our key performance indicator for cost control – Selling, General and Administrative (SG&A) expenses excluding depreciation, amortization and one-off non-cash items, as a percentage of sales. We cut this indicator year-on-year by nearly 90 basis points to 16.9% for full year 2009. Net of Employee Stock Option Programme ("ESOP") cost, this indicator declined by 160 bp year-on-year to 16.2% of sales in 2009.

**SG&A[(1)] as % of Sales**




[(1)] *Excluding deprecation and amortization & one-off non-cash items.*

## STRATEGIC EFFICIENCY PROGRAMME – DRIVING OPERATIONAL EXCELLENCE

In 2009 X5 launched its Strategic Efficiency Programme to drive operational excellence in line with international benchmarks. This is a multi-year effort that covers virtually every area of X5's operations:

- Integrated supply chain management;
- IT systems transformation;
- In-store labour productivity improvement;
- Business process improvement;
- Asset efficiency in real estate, energy use and business portfolio.

The Programme will support the Company's long-term scalable expansion and enhance our ability to drive sales growth, secure substantial cost savings and maximise cash flows. Key elements of the Programme are in planning and test-pilot phases and will be rolled out in stages over the next two to three years.

**Strategic Efficiency Programme Impacts Every Area of X5's Business**

| Project | Support of Long-Term Scalable Expansion | Sales Growth | Cost Savings | Working Capital Improvement |
|---|---|---|---|---|
| Integrated Supply Chain Managment | ● | ● | ◕ | ● |
| IT Systems Transformation | ● | ◑ | ◑ | ◑ |
| In-Store Labour Productivity Improvement | ◕ | ◔ | ● | ◔ |
| Business Process Improvement | ◕ | ◔ | ● | ◔ |
| Asset Efficiency | ◔ | ◔ | ● | ○ |

# Integrated Supply Chain Management: Operational Excellence in Distribution and Logistics

Russia is a rapidly developing economy that is still establishing the foundations of a modern, efficient food retail supply chain infrastructure. X5 is contributing to the country's economic development while strengthening its competitive advantages by better managing the flow of goods throughout the supply chain.

X5 has made significant investments to expand capacity and develop an optimised distribution network using the latest productivity-enhancing technologies. We expect this to positively impact operating expense ratios, service levels, product quality and availability, inventory turnover and shrinkage.

**Distribution Centre Network**

X5 made a major step forward in its goal of increasing the share of volumes it distributes through its own logistics network. We increased our supply centralisation rate from 51% to 61%, well in excess of the Company's 57% objective for 2009 – and we are positioned to take this to 67% in 2010. This will provide more opportunities to drive gains in efficiency as we open new stores and increase sales volumes.

At 2009 year end, X5 operated 23 Distribution Centres (DC) with overall warehouse capacity of 309.1 thousand square metres. X5 opened six new food DCs in the Moscow and Perm regions, St. Petersburg, Voronezh, Rostov-on-Don and Kazan, and expanded storage capacity of several existing DCs. We also launched our first national non-food DC in the Moscow region. The Company closed two small DCs in Perm and one small DC in Lipetsk.

**Warehouse Productivity**

X5 is rolling out a modern Warehouse Management System (WMS). This will improve control over the movement and storage of goods within our warehouses, and optimise processes and transactions involved in shipping, receiving and picking. WMS will be complemented by voice technology to improve order picking accuracy and productivity of warehouse personnel.

Moving from a paper-based system to voice-detected picking will dramatically reduce errors and help us achieve a picking accuracy rate of one error per thousand picks. In addition, WMS and voice picking reduces the logistics cycle from store order to delivery by at least 50%. As a result of implementing new technologies, X5 is targeting a 10% to 15% increase in DC labour productivity by the end of 2011.

## Transportation Efficiency

As at 31 December 2009, X5 operated a fleet of approximately 600 trucks, some 400 of which owned by the Company and 200 leased. X5 also uses railway shipments over large distances as a cost-effective logistics solution.

We have identified significant scope to increase transportation efficiency. This will improve fleet utilization, lower fuel costs and result in greater product availability and freshness. X5 began implementing its new Transportation Management System (TMS) in 2009 to enable route optimisation and reduction of demurrage. TMS is expected to deliver of up to 15% improvement in transportation costs within two years.

| Region | Warehouse space '000 sq.m. | # of DCs | Net Added in 2009 | Functionality | | | | |
|---|---|---|---|---|---|---|---|---|
| | | | | Dry | Fruit&Veg | Fresh | Frozen | Non-Food |
| Central | 153.9 | 8 | 2 | v | v | v | v | v |
| North-West | 65.1 | 5 | 1 | v | v | v | v | |
| Volgo-Vyatsky | 17.5 | 1 | – | v | v | v | | |
| Urals | 21.8 | 4 | (1) | v | v | v | | |
| Centralno-Chernozemny | 11.8 | 2 | – | v | v | v | | |
| Sredne-Volzhsky | 13.4 | 1 | – | v | v | v | | |
| South | 12.6 | 1 | 1 | v | v | v | | |
| Privolzhsky | 13.1 | 1 | 1 | v | v | v | | |
| **X5 Retail Group Total** | **309.1** | **23** | **4** | **v** | **v** | **v** | | |

# IT Systems Transformation: Operational Excellence in Our Business Management Platforms

X5 is implementing SAP as its Company-wide enterprise resource planning system. This is a multi-year project to transform our IT platform, support scalable growth and drive efficiency across our organisation from store operations to strategic planning.

SAP is being implemented in stages. The first phase is the introduction of SAP for Retail, which will cover all operations related to the management of stores, supplier relationships and logistics. After a successful pilot launch in 2009, X5 began rolling out SAP for Retail in all regions of operations in early 2010 and we plan to finalise this by end of 2010.

Two other stages involve the introduction of SAP HCM ("SAP for HR") and SAP for Enterprise Management ("SAP for EM"). SAP for HR, which has modules for managing human resources and payroll functions, is planned for launch in 2010. SAP for EM will cover management functions such as business and financial analysis, planning and reporting, real estate management and non-commercial purchasing. X5 expects to roll this out in 2011 following planning and testing phases and a pilot launch this year. In parallel, X5 is standardising and upgrading the IT systems in its store formats across the Company.

### Curent Status

**In-Store:**
- Unified IT platform at supermarkets and hypermarkets, different platform at discounters

**Logistics:**
- Several warehouse managment systems (WMS)

**Head office:**
- 1C for finance and HR, a number of database management systems, Excel

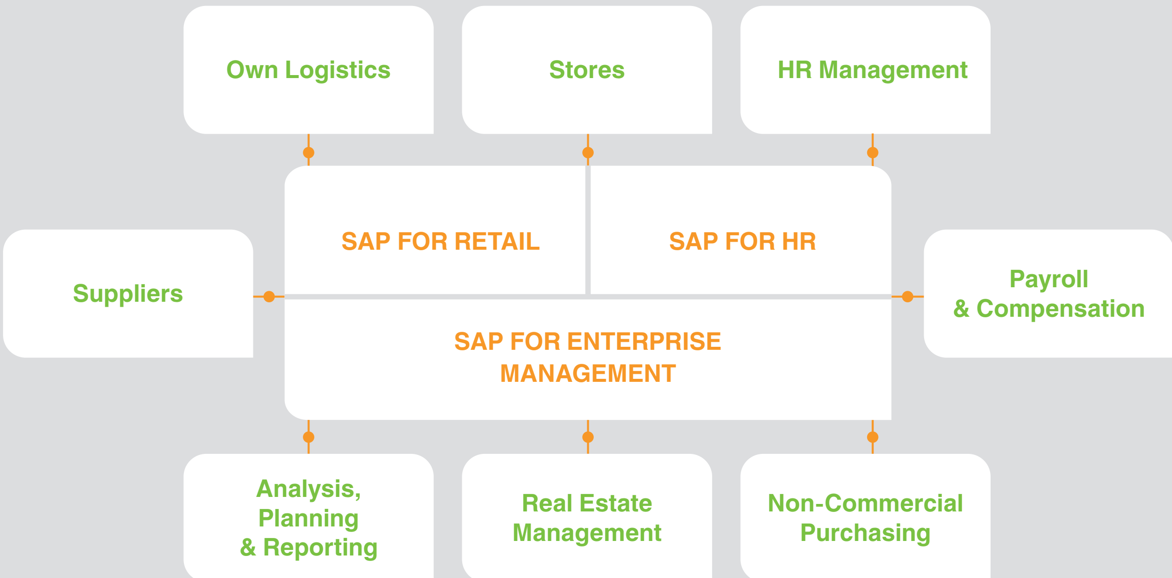
### 2012 IT Infrastructure

**In-Store:**
- Unified IT platform across formats, scalable and fully compatible with SAP

**Logistics:**
- Single WMS, complemented by voice picking, fully compatible with SAP (Exceed)
- Transportation management system (Oracle), fully compatible with SAP

**Head office:**
- SAP for Retail, SAP for HR, SAP for EM

**2012 IT Infrastructure**



# In-Store Labour Productivity Improvement: Operational Excellence in Our Store Management Processes and Technologies

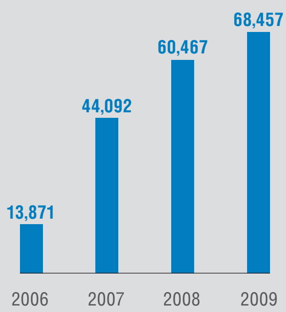
Even in a year of economic crisis, X5 continued to create significant numbers of new jobs thanks to the growth of our business. X5 employed 68,457 people at the end of 2009, an increase of nearly 8,000 or 13% over our 60,467 headcount at year-end 2008. We invest significantly in staff training and development to ensure quality service for our customers, and provide employees and managers with career development opportunities.

While X5 outperforms most of its Russian competitors in terms of sales per employee, there is significant potential to drive further productivity improvements compared to Western retailers. Over 80% of employees are in-store personnel, so in 2009, X5 began to focus on ways to increase productivity levels here towards international benchmarks.

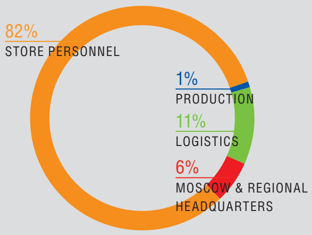
We conducted bottom-up and top-down analyses to assess the efficiency of in-store personnel task fulfilment, as well as the impact of various business processes on staff productivity. Our conclusion is that there are major opportunities for raising productivity significantly by implementing new technologies, processes and staff training and development. To illustrate one simple example, reorganising the baked goods department can lead to a threefold increase in store assistant productivity. As X5 moves toward greater process automation in stores and greater centralisation of supplier, distribution and pricing functions, we expect in-store staffing requirements to decrease over time. Overall, we plan to improve in-store staff productivity by at least 10% to 12% by the end of 2011.

At the same time, we believe X5 total employment will continue to increase steadily in coming years as we open new stores. The productivity improvement measures we have introduced will ensure we have the financial and human resources required to sustain this growth.

**End of Year Number of Employees**




**2009 Staff Breakdown by Function**



# Disciplined Growth

## STRONG GROWTH OUTLOOK FOR RUSSIAN RETAIL

Despite trading down trends in 2009, people continued to buy basic necessities and other items for enjoyable and healthy lifestyles. Looking to the future, we believe the Russian consumer growth story remains intact. We see substantial opportunities for strengthening X5's position and growing the penetration of the modern retail channel as a share of the overall market.

Attractive stores offering an abundance of choice are one of the most visible signs of the country's economic transformation, and ordinary Russians with rising incomes have seen dramatic improvements in their quality of life as a result. The Russian retail market also remains extremely fragmented. Modern food retailing accounts for approximately one third of the market, and the top ten retailers account for just 15% of sales. Measured another way, X5's national market share is approximately 4% despite its number one position.

The 2009 crisis environment was a test of X5's resilience – but it created new opportunities as well. With many retailers weakened by economic downturn, X5 responded aggressively to strengthen its leadership. We also increased our investment discipline, putting a strict limit on capital expenditures even as we significantly exceeded our expansion objectives for the year.

X5 is planning to sustain strong growth in 2010 through like-for-like sales increases and stepped up new store openings. Assuming stabilization of the macro-economic environment, X5 expects to deliver net sales growth comparable to the 2009 pro-forma level.

## SELECTIVE EXPANSION AND STRENGTHENED LEADERSHIP IN 2009

The financial and economic crisis has significantly impacted smaller and weaker retail chains, resulting in even greater prospects for strong market participants. X5 seized unique opportunities in 2009 to further increase market share, obtain high quality store premises in strategically important regions, and acquire smaller retail chains at attractive valuations.

In 2009, X5 continued to add selling space both organically and by acquisition. We added 271 stores on a net basis, bringing X5's total store count to 1,372. We shifted our real estate strategy to leasing new locations to take advantage of lower rents and availability of unused retail space – and also accelerated our distribution network expansion plans due to favourable market conditions.

## PRUDENT FINANCIAL MANAGEMENT AND DISCIPLINED GROWTH

X5 aims to maximise cash flows by growing the top-line, controlling costs and managing working capital. We prioritise investment opportunities to focus on projects with the best strategic fit and optimal returns. While we continue to review potential acquisitions of retail chains and assets, our approach is selective, price-conscious and risk-averse.

In 2009, we set a capital expenditure limit of RUR 14 billion (approximately USD 450 million). While remaining within this limit, we significantly exceeded our new store openings plan, adding organically 189 stores for the year, and in addition, acquired 82 Paterson stores at an attractive price.

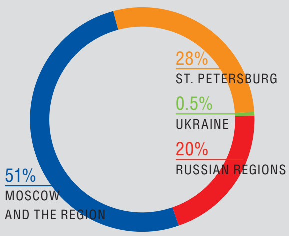
The Company also managed its liquidity prudently to mitigate short-term volatility while optimising our debt structure to improve the maturity profile. And finally, we secured a "forward-start" credit facility from Sberbank, which guarantees the refinancing of USD 1.1 billion of syndicated loan maturing in 2010, and increases our flexibility in defining strategic goals and executing future investment plans.

In 2010, X5 plans to accelerate openings of new stores, particularly in soft discounter format, with selective expansion in hypermarkets and supermarkets. Our objective is to open between 200 and 250 soft discounters, approximately 15 supermarkets and between seven and 10 hypermarkets. We will also continue to invest in logistics and other infrastructure projects. Our CapEx limit for the year is RUR 18 billion (approximately USD 600 million), maintaining investment levels within operating cash flow generation capacity.

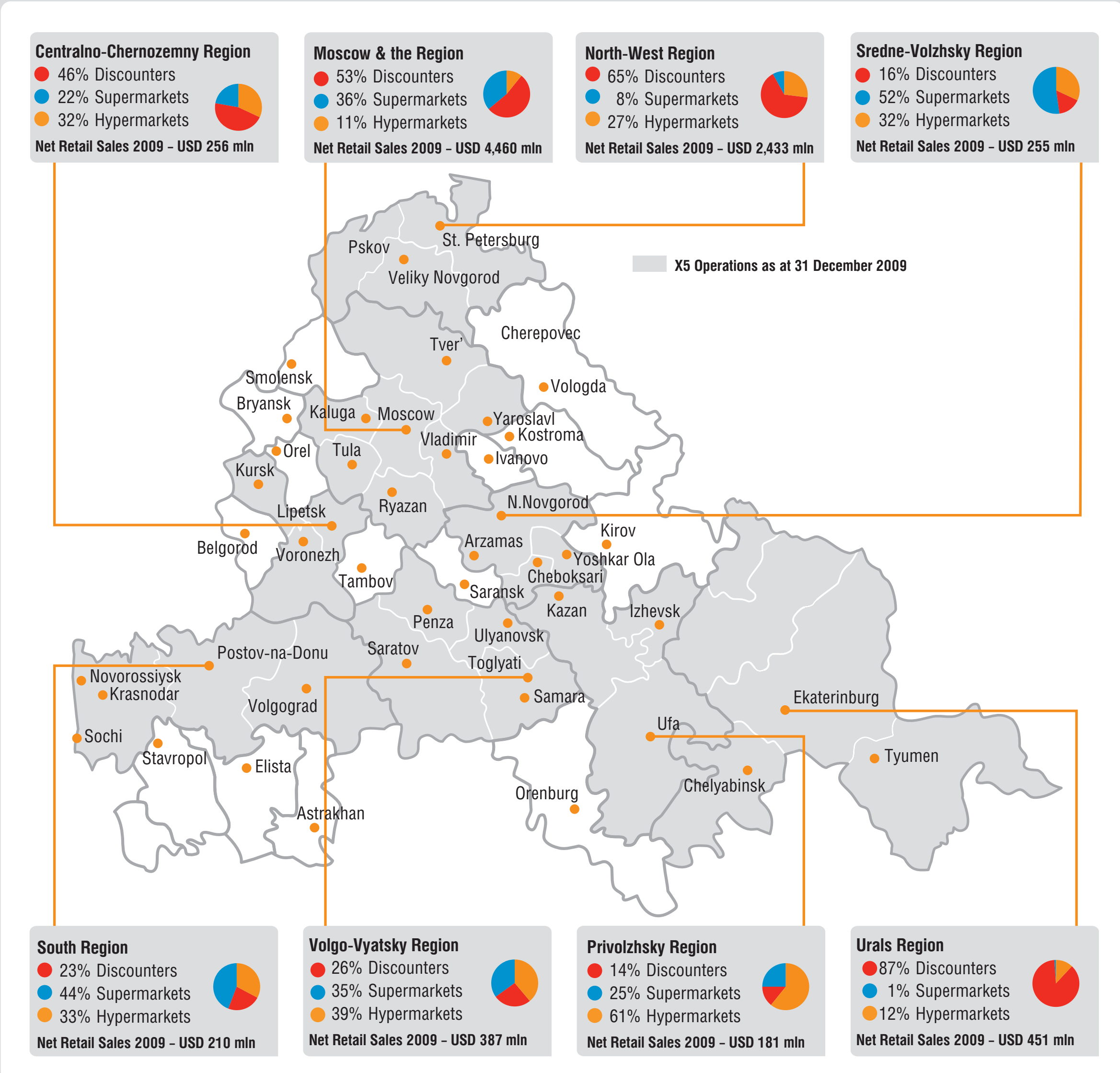

# Balanced Geographical Presence

X5 focuses on regions of European Russia and the Urals, in areas with the highest population densities and net disposable incomes. We are the leader in Moscow and St. Petersburg, occupying the number one position by sales volume in both cities. We also have the leading positions in five large regional cities: Nizhny Novgorod, Lipetsk, Samara, Chelyabinsk and Perm. At the end of 2009, X5 was present in 45 major cities in Western Russia and the Urals, and also in Ukraine. Sales in X5's principal markets, in particular, in Moscow and St. Petersburg, have generally remained healthy during the economic downturn, thereby supporting our overall financial stability.

**2009 Net Retail Sales by Region**




Total FY 2009 net retail sales were USD 8,675 mln



# New Store Openings

In 2009, X5 added 271 stores or 189 thousand sq.m. of selling space on a net basis, including the acquired Paterson stores. At year end, X5 operated 1,372 stores in total (1,063 thousand sq.m. in selling space). This includes 1,039 discounters, 275 supermarkets and 58 hypermarkets.

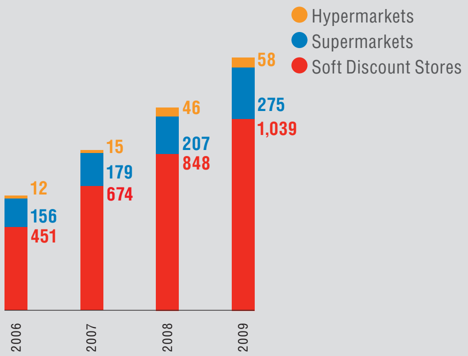
| | As of 31-Dec-08 | As of 31-Dec-09 | Rebranding FY 2009 | Closings FY 2009 | Paterson Acquisition | Net Added FY 2009 | *% change vs 31-Dec-08* |
|---|---|---|---|---|---|---|---|
| **Selling Space, sq. m.** | | | | | | | |
| Hypermarkets | 232,462 | 285,581 | – | – | – | 53,119 | *23%* |
| Supermarkets | 222,362 | 284,359 | (4,092) | (2,435) | 50,027 | 61,996 | *28%* |
| Soft Discounters | 419,207 | 493,016 | 4,092 | (6,065) | 13,051 | 73,809 | *18%* |
| **X5 Retail Group Total** | **874,032** | **1,062,956** | – | **(8,500)** | **63,077** | **188,925** | ***22%*** |
| **# of Stores** | | | | | | | |
| Hypermarkets | 46 | 58 | – | – | – | 12 | *26%* |
| Supermarkets | 207 | 275 | (5) | (3) | 57 | 68 | *33%* |
| Soft Discounters | 848 | 1,039 | 5 | (16) | 25 | 191 | *23%* |
| **X5 Retail Group Total** | **1,101** | **1,372** | – | **(19)** | **82** | **271** | ***25%*** |

X5 plans to open a record number of discounters in 2010 – between 200 and 250 new stores. Discounters have the best short-term profile for new store openings due to their clear competitive strengths in a weak consumer environment. In addition, discounters require less capital per store opening, and the format has a relatively short investment payback period.

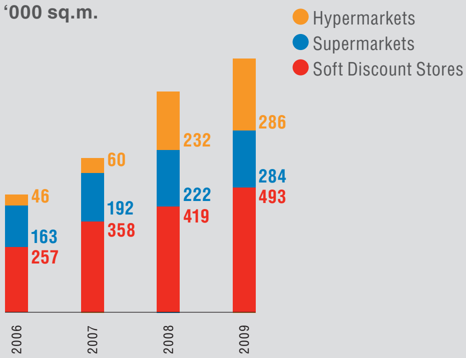
In 2010, X5 plans to open approximately 15 new supermarkets. The Company will continue to open supermarkets on a selective basis in regions with stable middle and higher income demographics – Moscow, St. Petersburg and a few other large cities. This builds on efforts X5 undertook in 2009 to focus its supermarket portfolio to improve returns, including conversion of five supermarkets to discounters and 19 store closures (three supermarkets and 16 discounters).

Our main focus in hypermarkets is to increase LFL sales at existing stores driven by Karusel's repositioning. We plan to open between seven to 10 new hypermarket stores in 2010, making the most of rental market conditions and opportunities to lease attractive vacant locations. As hypermarket construction is a multi-year project requiring significant capital investment, X5 will only consider building new stores in cases where the economics are outstanding.

**Number of Stores**




**Net Selling Space**
**'000 sq.m.**



# Acquisition of Paterson Supermarket Chain

In December 2009 X5 completed the acquisition of Paterson supermarket chain for USD 189.5 million plus assumption of USD 85 million in net debt. Paterson is an excellent fit and offers attractive value for X5's shareholders. It reinforces X5's number one position in supermarkets. It provides high quality locations in key geographic markets with strong demographics for this format.

Paterson operated stores in Moscow, Moscow region, St. Petersburg, Kazan and other cities of European Russia and Urals, with 2009 net retail sales of RUR 10,415 mln or USD 328 mln.

X5 expects to realise significant synergies from the rebranding and operational integration of Paterson stores, with strong upside potential in sales density, profitability and cash flow generation.

Based on current assumptions, X5 plans to integrate 57 Paterson stores as supermarkets under the Pererkrestok brand, and 25 smaller stores as soft discounters under the Pyaterochka brand. A few stores are under review with regard to X5's financial criteria. We expect to finalise the integration by mid-2010.

# 2009 Financial Review

The crisis conditions of 2009 were a successful test of X5's financial strength. We met our 25% pro-forma revenue growth target driven by an industry-beating 10% increase in like-for-like sales and strong organic new store openings. X5 generated USD 734 million in operating cash flow thanks to strong top-line growth, cost control and working capital management. We also strengthened the balance sheet, reducing net debt by USD 250 million by the end of 2009, improving our debt maturity profile, minimising currency exposure and securing resources to refinance the Company's obligations coming due in 2010.

## Profit & Loss – Key Trends and Developments

### P&L HIGHLIGHTS[1]

| USD million | FY 2009 | FY 2008[2] | *% change y-o-y* |
|---|---|---|---|
| **Net Sales** | **8,717.4** | **8,892.4** | ***(2%)*** |
| incl. Retail | 8,674.5 | 8,843.8 | *(2%)* |
| **Gross Profit** | **2,107.9** | **2,278.5** | ***(7%)*** |
| *Gross Margin, %* | *24.2%* | *25.6%* | |
| **EBITDA** | **736.0** | **803.2** | ***(8%)*** |
| *EBITDA Margin, %* | *8.4%* | *9.0%* | |
| Impairment of CIP, Fixed Assets & Goodwill[3] | (48.3) | (2,257.0) | *(98%)* |
| **Operating Profit / (Loss)** | **467.8** | **(1,704.5)** | ***n/a*** |
| *Operating Margin, %* | *5.4%* | *n/a* | |
| **Net Profit / (Loss)** | **165.4** | **(2,145.5)** | ***n/a*** |
| *Net Margin, %* | *1.9%* | *n/a* | |

### EFFECT OF RUR/USD EXCHANGE RATE MOVEMENTS ON PRESENTATION OF X5'S RESULTS AND THEIR DYNAMICS

X5's operational currency is the Russian Ruble (RUR), while our presentation currency is the U.S. Dollar (USD). As RUR/USD rate has substantially changed in the past twelve months, comparisons of the Company's financial results either with the corresponding period a year ago (for profit & loss statement) or with the beginning of the year (for balance sheet statement) have been substantially affected by these movements. Please see Note 2 to the IFRS consolidated financial statements in this Annual Report for additional information.

[1] Please note that in this and other tables of this Annual Report immaterial deviations in calculation of % change, subtotals and totals are explained by rounding.
[2] Profit & Loss figures for 2008 in this Annual Report are presented on pro-forma basis, unless otherwise stated. Pro-forma figures include results of the acquired Karusel hypermarket chain from 1 January 2008. We believe pro-forma numbers are useful because they allow investors to evaluate X5's operating results and financial performance for different periods on a more comparable basis. These figures should be used in addition to, but not as a substitute for, the Consolidated Financial Statements included in this Annual Report, which include Karusel's results only as from 30 June 2008, when the acquisition was completed.
[3] CIP stands for Construction in Progress. Please see section *Impairment of CIP & Fixed Assets* for additional information on 2009 impairment.

## NET SALES & GROSS MARGIN PERFORMANCE

| USD million | FY 2009 | FY 2008 | *% change y-o-y* |
|---|---|---|---|
| **Net Sales** | **8,717.4** | **8,892.4** | ***(2%)*** |
| incl. Retail | 8,674.5 | 8,843.8 | *(2%)* |
| Hypermarkets | 1,687.9 | 1,678.0 | *1%* |
| Supermarkets | 2,307.2 | 2,701.8 | *(15%)* |
| Soft Discounters | 4,676.3 | 4,464.0 | *5%* |
| Online | 3.1 | - | *n/a* |
| **Gross Profit** | **2,107.9** | **2,278.5** | ***(7%)*** |
| *Gross Margin, %* | 24.2% | 25.6% | |

For 2009 X5 reported net sales of USD 8,717 million – a year-on-year decline of 2% in USD terms and 25% growth in RUR terms on pro-forma basis driven by industry-beating like-for-like (LFL)[1] sales growth of 10% and strong continued expansion.

X5 drove the highest like-for-like sales and customer traffic of any Russian retailer in 2009, with a record of nearly 1 billion store visits, thanks to our "Close to the Customer" policy of reinvesting gross margin in stores' value propositions. As a result, X5's gross margin for the year totaled 24.2% compared to 25.6% in 2008 – a year-on-year margin investment of 140 bp in line with management's expectations.

## SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (SG&A)

| USD million | FY 2009 | FY 2008 | *% change y-o-y* |
|---|---|---|---|
| **Staff Costs, incl.** | **(761.2)** | **(839.5)** | ***(9%)*** |
| *% of Net Sales* | *8.7%* | *9.4%* | |
| ESOP | (59.3) | 2.5 | *n/a* |
| *% of Net Sales* | *0.7%* | *0.0%* | |
| **Lease Expenses** | **(264.2)** | **(271.3)** | ***(3%)*** |
| *% of Net Sales* | *3.0%* | *3.1%* | |
| **Other Store Costs** | **(110.8)** | **(129.5)** | ***(14%)*** |
| *% of Net Sales* | *1.3%* | *1.5%* | |
| **D&A, incl.** | **(268.2)** | **(250.7)** | ***7%*** |
| *% of Net Sales* | *3.1%* | *2.8%* | |
| CIP & Fixed Assets Impairment | (48.3) | - | *n/a* |
| *% of Net Sales* | *0.6%* | *0.0%* | |
| **Utilities** | **(154.6)** | **(149.0)** | ***4%*** |
| *% of Net Sales* | *1.8%* | *1.7%* | |
| **Third Party Services** | **(76.5)** | **(102.2)** | ***(25%)*** |
| *% of Net Sales* | *0.9%* | *1.1%* | |
| **Other Expenses** | **(105.2)** | **(86.4)** | ***22%*** |
| *% of Net Sales* | 1.2% | 1.0% | |
| **Total SG&A** | **(1,740.6)** | **(1,828.7)** | ***(5%)*** |
| ***% of Net Sales*** | ***20.0%*** | ***20.6%*** | |

Full year 2009 SG&A expenses decreased as a percentage of revenue by 60 bp year-on-year to 20.0%. Before depreciation, amortization and one-off non-cash impairment charge, SG&A expenses accounted for 16.9% of sales a year-on-year decrease of nearly 90 bp. Net of ESOP cost, this indicator declined by 160 bp year-on-year. SG&A decline as a percentage of sales was achieved through cost control initiatives and implementation of X5's Strategic Efficiency Programme.

[1] Like-for-like (LFL) comparisons of retail sales between two periods are comparisons of retail sales in local currency (including VAT) generated by the relevant stores. The stores that are included in LFL comparisons are those that have operated for at least twelve full months preceding the beginning of the last month of the reporting period. Their sales are included in LFL calculation starting from the first day of the month following the month of the store opening.

Significant savings were obtained from administrative expense and staff cost optimization, renegotiation of leases and energy saving initiatives.

As at 31 December 2009 the Company employed 68,457 people compared to 60,467 as at 31 December 2008. The increase is primarily due to new store additions in 2009, when X5 added a net 271 new stores. Nevertheless, headcount growth of 13% was noticeably below the 22% increase in selling space for the year as X5 began to implement its store labour productivity improvement project. Achieved staff cost savings this year were partially offset by ESOP cost of USD 59 million for 2009 (compared to USD 2.5 million gain reported in 2008). ESOP charge is attributable to X5 GDR price appreciation of over 270% in 2009.

**Impairment of CIP & Fixed Assets**
Based on a regular impairment test of land, buildings and construction in progress ("CIP") performed by X5 at the end of 2009, the Company has taken an impairment charge of USD 48 million with respect to certain real estate assets and construction projects suspended due to the financial crisis or otherwise affected by economic deterioration. This impairment charge is recorded on the profit & loss statement for 2009 along with depreciation & amortization, with a corresponding decrease in property, plant and equipment on the balance sheet. This impairment charge is a non-cash one-off item that does not impact the strategic value of X5's assets or business and is not indicative of the Company's overall ability to generate cash flow.

## NON-OPERATING GAINS AND LOSSES

| USD million | FY 2009 | FY 2008 | *% change y-o-y* |
|---|---|---|---|
| **Operating Profit / (Loss)** | **467.8** | **(1,704.5)** | ***n/a*** |
| Finance Costs (Net) | (154.1) | (163.7) | *(6%)* |
| Net FX Result | (45.7) | (267.2) | *(83%)* |
| Share of Loss of Associates | (4.0) | (0.6) | *512%* |
| **Profit / (Loss) before Tax** | **264.0** | **(2,136.0)** | ***n/a*** |
| Income Tax Expense | (98.6) | (9.4) | *944%* |
| Current Income Tax | (168.4) | (185.7) | *(9%)* |
| Deferred Income Tax | 69.8 | 176.3 | *(60%)* |
| **Net Profit / (Loss)** | **165.4** | **(2,145.5)** | ***n/a*** |
| *Net Margin, %* | *1.9%* | *n/a* | |

**Finance Costs**
Full year 2009 net finance costs decreased 6% year-on-year in USD terms and increased 20% in RUR terms due to higher interest rates on RUR funding, which were especially noticeable at the beginning of 2009 and moderated throughout the year. The effective interest rate on X5's debt for the full year 2009 was approximately 8.0%.

**Foreign Exchange (FX) Gain/(Loss)**
The Company posted a USD 46 million FX loss for full year 2009 due to exchange rate volatility throughout 2009. This is a primarily non-cash item, resulting from revaluation of the Company's USD-denominated debt.

## INCOME TAX

For 2009, X5 reported income tax expense in the amount of USD 99 million. Effective tax rate for the year totaled 37%, which is higher than the statutory tax rate for three main reasons: Inventory shrinkage is not tax deductable in Russia, ESOP cost is not tax deductable and FX loss is only partially tax deductable.

# Cash Flow –
# Key Trends and Developments

| USD million | FY 2009 | FY 2008 | *% change y-o-y* |
|---|---|---|---|
| Net Cash Flows from Operating Activities | 733.7 | 629.3 | *17%* |
| *Net Cash from Operating Activities before Changes in Working Capital* | *835.5* | *774.3* | *8%* |
| *Change in Working Capital* | *166.0* | *243.9* | *(32%)* |
| *Net Interest and Income Tax Paid* | *(267.9)* | *(388.9)* | *(31%)* |
| Net Cash Used in Investing Activities | (433.8) | (1,656.0) | *(74%)* |
| Net Cash (used in)/generated from Financing Activities | (194.3) | 1,194.2 | *n/a* |
| Effect of Exchange Rate Changes on Cash & Cash Equivalents | 29.3 | (70.2) | *n/a* |
| **Net Increase in Cash & Cash Equivalents** | **134.8** | **97.3** | ***39%*** |

Full year 2009 net cash flow from operating activities totaled USD 734 million compared to USD 629 million a year ago. Higher cash generation was driven by strong operating performance and efficient working capital management.

Net cash used in investing activities decreased dramatically to USD 434 million in 2009 from USD 1,656 million in 2008. Organic capital expenditures (“CapEx”) totaled USD 245 million in 2009 versus USD 997 million in 2008, while in 2009 X5 added 126 thousand sq.m. of selling space organically compared to 127 thousand sq.m. in 2008. CapEx savings were attributable to more favourable real estate conditions and a shift in focus to leased versus owned premises (over 70% of selling space added and new stores opened in 2009 were leased), as well as a decrease in construction and repair costs. Increased CapEx efficiency provided flexibility for consolidation opportunities: X5 acquired Paterson for USD 189.5 million (equity value), adding 82 stores with total net selling space of approximately 63 thousand sq.m. on attractive, value enhancing terms while remaining within our 2009 CapEx limit and financing this acquisition from operating cash flow.

Net cash used in financing activities in 2009 amounted to USD 194 million, as the Company utilized generated free cash flow to reduce its debt levels, including redemption of acquired Paterson debt in the amount of approximately USD 90 million (gross debt).

# Debt Financing and Liquidity Management

| USD million | 31-Dec-09 | % in total | 31-Dec-08 | % in total | % change y-o-y |
|---|---|---|---|---|---|
| **Total Debt** | **1,944.0** | | **2,059.4** | | ***(6%)*** |
| Short-Term Debt | 1,656.6 | *85%* | 578.4 | *28%* | *186%* |
| Long-Term Debt | 287.4 | *15%* | 1,481.0 | *72%* | *(81%)* |
| **Net Debt** | **1,532.3** | | **1,782.6** | | ***(14%)*** |
| Denominated in USD | 1,162.8 | *76%* | 1,170.0 | *66%* | *(1%)* |
| Denominated in RUR | 369.5 | *24%* | 612.6 | *34%* | *(40%)* |
| **Net Debt/EBITDA** | **2.08x** | | **2.22x** | | |

Prudent financial management and deleveraging efforts have significantly strengthened the Company's balance sheet and liquidity.
As at 31 December 2009, total debt amounted to USD 1,944 million. Net debt totaled USD 1,532 million – a year-on-year reduction of USD 250 million or 14%. Net debt to EBITDA ratio decreased from 2.22 times as at 31 December 2008 to 2.08 times at year-end 2009.

X5's short-term debt increased from USD 578 million as at 31 December 2008 to USD 1,657 million at the end of 2009, due to reclassification of certain obligations from long-term to short-term debt. These obligations potentially come due within twelve months, and include RUR 9 billion in corporate bonds with a put option exercisable in July 2010, and the USD 1.1 billion syndicated loan maturing in December 2010. Importantly, X5 has already secured a 5-year ruble-denominated credit line equivalent of up to USD 1.1 billion from Sberbank for the purpose of refinancing the loan. This fully-committed long-term credit line is the first large-size "forward-start" facility in the Russian market. It can be utilised in several tranches with varying maturities. This arrangement provides X5 with great flexibility for managing the Company's liquidity position, minimising currency exposure and improving our debt maturity profile.

Net of the aforementioned arrangement with Sberbank, as at 31 December 2009, the Company had access to RUR-denominated credit facilities of approximately RUR 25 billion (approximately USD 812 million). Of this amount, RUR 17 billion (approximately USD 555 million) represented available undrawn credit lines with major Russian and international banks.

# X5 & Society

## Communities – Bettering the Lives of Ordinary Russians

X5 Retail Group is committed to bettering the lives of ordinary Russians in the regions and communities in which we operate. We do this by providing investment and job opportunities, ensuring affordable products for all family budgets, and actively participating in social programmes and humanitarian projects. In addition to demonstrating X5's commitment to good corporate citizenship, our actions advance X5's overall goal of building customer loyalty.

### ACCESS TO AFFORDABLE PRODUCTS

Product affordability is crucial for social development in our country. X5's price leadership played a more important role than ever this year as life got harder for ordinary Russians. Pyaterochka's new brand promise – *lowest price in the market on 100% of assortment* – was the right response at the right time for consumers weathering the effects of the economic crisis, and it led to a record year for discounters. For the Company as a whole, we kept the rise in average prices in X5's stores to below Russian inflation levels throughout the year.

X5 cares about product affordability especially for socially vulnerable sections of the population. We offer special discounts and other benefits to Russian war veterans, pensioners and disabled persons. At Karusel hypermarkets and Perekrestok supermarkets, they receive an additional 5% discount on their purchases during our "Care Time" hours from 9 a.m. to 1 p.m. every weekday except holidays.

In December 2008, X5 opened its first store designed to accommodate the special needs of physically challenged customers. The store, a Pyaterochka located in St. Petersburg, is considered to operate in line with global best practices according to an evaluation by the All-Russian Society of the Disabled.

### EDUCATION AND HEALTH INITIATIVES

This year was the fifth anniversary of X5's education initiative, "Perekrestok Goes to School!" The programme has expanded significantly since it was launched together with the Moscow Department of Education and Moscow City Government. In 2009, 199 Perekrestok stores in more than 40 Russian cities participated in the programme, which donated over 4,000 computers and other IT equipment to 659 schools.

X5 also supports the Liniya Zhizni (Lifeline) fund, which works to reduce child deaths from serious, treatable illnesses by helping to modernise the country's health care system. Perekrestok's customers provide their generous support to Liniya Zhizni by making contributions in special collection boxes displayed in our stores. Our customers' donations raised over RUR 5 million in 2009.

### SUPPORT FOR RUSSIAN FOOTBALL

X5 is the general partner of the Russian Football Union and an official partner of the Russian national football team. The Company provides financial support for Russian football as a way to promote active, healthy lifestyles. This includes funding the construction of community football fields and sports programmes that provide education and training for talented young athletes.

# Employees – Valuing Our People's Potential

X5 is a major provider of investment and employment in regions and communities across Russia. The Company employed 68,457 people at the end of 2009, representing a year-on-year increase of almost 8 thousand or 13% compared to 2008. Even during the economic downturn, the Company has continued to open stores and expand operations – we increased overall job opportunities while controlling costs and enhancing productivity.

This year we sharpened the HR function's focus on the Company's strategic and operational objectives, establishing clear HR action plans for each area of our business to be implemented in 2010. We also listened to our people, conducting the Company's first annual employee survey and incorporating key findings into our plans for improvement.

Some 43,000 employees went through X5's training centres in 2009 versus 26,000 in 2008. We view training and development as a key competitive strength that effectively fosters employee loyalty, productivity and customer orientation. It also strengthens X5's corporate culture, which is built on our core values of Company pride, business ethics and respect for people.

## HR FUNCTIONS MATCHED TO X5'S STRATEGIC GOALS

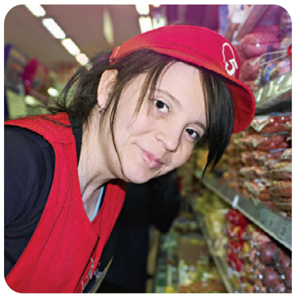
X5 continues to fine-tune its Human Resources (HR) function to support X5's business needs and objectives. In 2009, we established a clear delineation between strategic and operational HR management.

**Strategic HR** is responsible for developing X5's HR policies to support the Company's strategic objectives. In addition, it manages issues with respect to attracting, incentivising and developing X5's executives, working closely with the Supervisory Board's Nomination and Remuneration Committee to ensure the Company has the right talent to support its long-term success.

**Operational HR** manages the needs of X5's large and growing business, supporting the objectives of our retail formats and logistics function. This year was dedicated to diagnosing areas for improvement and developing action plans for 2010:

- **Discounters** – Talent development and succession planning for key store management positions is an important area of focus due of the stepped-up pace of new store openings. Additionally, operational HR strives to create a higher quality working environment in discounters in a cost-effective way for the Company.

- **Supermarkets** – The format is focused on improving service quality and increasing average purchase size. HR supports these goals with training and development of store managers and basic personnel, to improve their product knowledge and understanding of customer needs. The performance management system for supermarket employees will be changed correspondingly in 2010 to support the format's goals for increasing sales.




- **Hypermarkets** – The format's key HR achievement was in-store staffing optimisation, which enabled substantial productivity improvements this year following integration of the acquired Karusel chain in the second half of 2008. The plan for 2010 calls for expanding the format's successor pool, with a special focus on managerial skills training and development for employees.

- **Logistics** – One of X5's key priorities is operational excellence in the supply chain, and HR policy in logistics plays a crucial role. In 2009 X5 audited the organisational structure of the logistics function, conducting workflow analysis, job function evaluation and a review of the remuneration system. HR priorities in 2010 are to establish standardised organisational structures and job descriptions, grow the successor pool and implement a new training & development system for key employees and members of the successor pool.

## LISTENING TO OUR PEOPLE – FIRST ANNUAL EMPLOYEE SURVEY

In 2009 we introduced the X5 Employee Survey as a powerful new HR tool for evaluating satisfaction levels and engagement in the success of our business. The survey was conducted at the end of 2009 and will become an annual event. Key findings have been incorporated into our HR action plan for 2010. This includes strengthening X5's social benefits and improving labour conditions in our stores.

Health insurance, staff meals and various social payments are important components of the Company's compensation and benefits policy. In 2010, X5's social benefits package will be expanded to include various gift certificates, bonus cards and discounts for shopping with X5 and our partners in non-food products, cleaning services, entertainment and transportation. We have also allocated special funds for employee celebrations of format and store anniversaries and professional milestones. In addition, we are focused on enhancing the quality of the work environment, including renovation of canteens and staff premises, transportation services for night-shift workers and other improvements.

## TRAINING & DEVELOPMENT REMAINS A COMPETITIVE ADVANTAGE

The Company has a deep commitment to training and development for executives, managers and staff. Talented leaders and a skilled workforce are essential for driving operational performance and executing strategic projects. We rely on knowledgeable, attentive people to provide quality customer service and increase sales in our stores.

The Company operates 14 regional multi-format training centres for store and logistics personnel. These offer programmes to enhance professional knowledge and skills, and provide employees with career development opportunities. In 2009, we trained almost 43,000 employees in our training centres versus 26,000 in 2008.

X5 is also strengthening the business management skills and operational expertise of midlevel and senior executives. In 2008 we launched X5 Corporate University to provide executive training, with a focus on leadership development, time and conflict management, delegation and communication skills. In 2009 we launched distance-learning to enable managers to develop professional skills at convenient times and in a more cost-effective way for the Company.

To increase new head office employees' understanding of in-store operations, Corporate University runs an orientation programme with week-long field internships in all three formats. In addition, X5's "Shopper" programme is an ongoing initiative, whereby each head office employee is assigned to conduct monthly checks of a "sponsored store," paying special attention to quality, service levels, assortment availability and in-store staff courtesy. Both programmes are mandatory for head office employees, underscoring our top-to-bottom commitment to enhancing retail know-how.


In 2010 we have launched individual development programmes for X5 senior executives, including members of the Executive Board. This focuses on strategic project management, coaching and mentoring. Store personnel training & development programmes in 2010 will focus on customer service and driving sales growth.

## CORPORATE CULTURE & CODE OF CONDUCT

We are proud of the high standards we set for our people. Since 2008 all Company employees operate in accordance with X5's Code of Conduct, developed in line with best international standards. Among its main tenets are strict compliance with the law, professional integrity, respect for people, customer orientation and commitment to excellence.

All HR policies and practices support the development of X5's corporate culture. We select train, develop, promote and retain employees who embrace our corporate values, show respect for colleagues and subordinates in their daily work environment and adhere to corporate rules.

Finally, the Company recognises professional achievements not only through our remuneration policies, but also with corporate awards and prizes. In addition, we actively encourage employees to engage in Company events and to participate in professional and artistic contests.

# Health & Safety –
# From the Supplier to the Consumer

X5 Retail Group aims to be the leader in product safety and quality and promote healthy lifestyles as a key competitive differentiator. We approach our health and safety commitment from the perspective of consumers, employees, and suppliers:

- Our customer philosophy begins with ensuring product quality and safety, which is essential to maintain consumer trust, reduce risks to our business and support the healthy development of the food supply to Russian consumers.
- We cater to the increased demand of Russian consumers for fresh produce and other products that contribute to an active, healthy lifestyle.
- X5 also engages its suppliers and employees to ensure adherence to health and safety standards within the supply chain and in our operations.
- X5 actively complies with and participates in the development of government rules and regulations to protect consumers' rights, and policies to promote the quality, health and safety of the food supply for Russian citizens.

X5 continuously reviews and implements standards and best practices that go beyond compliance with laws and regulations. Our approach to quality control is based on the following principles:

- Systematic approach covering every stage of a product life cycle
- Preemptive approach aimed at preventing product recalls and shrinkage
- Strict definition of producers' responsibility for quality and safety
- External audits of producers by certified quality specialists
- Independent product analysis by certified testing centres
- Documented confirmation of product quality and safety from producers

In 2009 X5 became the first Russian food retailer to join the Chartered Quality Institute (CQI), the London-based association for quality management professionals. Participation in CQI provides X5 with access to the institute's informational resources on the most recent developments in the field. It will support efforts to improve customer satisfaction, implement best practices, increase efficiency, reduce shrinkage and identify and manage key risks.

## CONSUMERS

X5 puts its customers first. We realise that the quality and safety of the products we sell in our stores is crucial to our long-term success and reputation in the marketplace. The Company's policies play a vital role in the development of Russia's food supply chain.

X5 also aims to promote a healthy lifestyle for all of our customers, regardless of their level of income. "Focus on fresh" is a key differentiator for X5's formats and we lead the market in sales of fruit and vegetables, dairy products, meats and fresh fish.

Demand for organic products is very low in Russia at this stage, but X5 has begun to prepare for future consumer trends. In July 2008, X5 launched "Green Perekrestok" as a premium supermarket offering a wider range of healthy and organic foods. Food products that conform to Genetically Modified Ingredients (GMI) standards are already labeled as "Excluding GMI" on a voluntary basis in all our stores, and we undertake random inspections to verify compliance.

## EMPLOYEES

X5's quality control department is responsible for ensuring compliance with quality, health and safety standards. We continuously verify the quality of products and compliance with health and nutrition standards both in our distribution centres and our stores.

When accepting shipments and deliveries, our quality control specialists ensure that goods meet Russian and international standards, technical requirements, and in-house norms, which are often stricter than those required by regulators. We increase our store and warehouse personnel's technical knowledge and skills in this area through special education Programmes, information and training.

## SUPPLIERS

X5 is the partner of choice for almost 4,700 suppliers, and we have taken extra steps in 2009 to ensure a well-functioning supply chain. We continue to work in partnership with suppliers to ensure there is a mutual understanding of the standards we set.

Our contract terms with suppliers stipulate adherence to Russian legislation on quality standards, health and safety, sanitary rules and consumer protection as specified by the Consumer Protection Act and Civil Code. All X5's suppliers go through a strict selection process, which for non-branded goods and private label is managed through electronic auctions. Selection procedures are transparent, distinguishing X5 from many of its competitors.

The fish industry is an example of X5's active involvement in the supply chain. X5 was the first Russian retailer to arrange for fish deliveries straight from the docks. We go above and beyond the standards set in the Consumer Protection Act by providing extended verification of fish suppliers – this policy is vital to providing X5's customers with the highest quality fish. At an industry level, X5 regularly participates in conferences, forums and exhibitions, and we also consult with state bodies, federal agencies and authorities to discuss industry developments, problems and solutions.

As part of X5's private label strategy, we have defined a clear procedure for choosing suppliers based not only on price, but also on quality. In addition to the legal requirements for private label products, all suppliers must adhere to additional contractual requirements set by X5. This includes provision of additional certificates, conformity of products to our specifications, sanitary rules, labeling and packaging requirements. X5 monitors quality both when a new product is being introduced and throughout its production lifecycle. Production plants are audited regularly and we receive certificates confirming the quality of products and compliance with health and nutrition standards.

# X5 2009 Awards

X5 Retail Group's achievements and professional excellence were recognised this year with numerous industry awards.

- X5 topped the list for "Fastest Growing FMCG Retail Chain in 2009" and "M&A Deal in FMCG Sector" in a ranking by Russia's National Trade Association and news agency "INFOLine".
- X5 was named "Company of the Year 2009" by publishing house RosBusinessConsulting Group and also ranked first in the retail sector category.
- X5 was named "Retail Company of the Year" at the International "Retail Business 2009" Summit organised by BBCG in association with the World Retail Congress and the Russian Retail Companies' Association. X5 also won an award for "Marketing Campaign of the Year" for Perekrestok's Prime Minister's Price campaign.
- Lev Khasis, X5's Chief Executive Officer, was named to the President of the Russian Federation's "First Hundred" list of high-potential managers, an initiative to develop the country's professional executive talent pool.
- Lev Khasis, X5's Chief Executive Officer, was awarded the prestigious "Person of the Year 2009" award by RosBusinessConsulting Group for promoting the interests of the retail sector and personal contributions to the development of a modern consumer market. He was also awarded the Glory of Motherland decoration established by RBC, which is listed in the state public decorations register of the Russian Federation.
- Lev Khasis was also named one of the "Top 100 Russian Managers of the Decade" by the National Association of Managers.
- Evgeny Kornilov, X5's Chief Financial Officer, won the award for "Best Investor Relations by a CFO" in the Focus Russia 2009 Thomson Reuters Extel Survey. Anna Kareva, X5's Investor Relations Director, was named "Best Investor Relations Officer" in the Russian retail sector category.
- Yuri Kobaladze, X5's Corporate Affairs Director, and Teimur Shternlib, X5 Chief Information Officer, were ranked number one for the retail sector in various categories of the National Association of Managers' annual survey.
- X5 North-West branch was cited as "Best Taxpayer 2008" by the St. Petersburg City Government.
- X5 South branch was rated "Most Socially-Oriented Company of the Year" by Molot newspaper of the Southern Federal District.
- Pyaterochka was named "Brand with the Best Reputation for Environmental Protection" by Reader's Digest Magazine's Russian edition.

# Corporate Governance & Risk Management

## Corporate Governance Report

As a Dutch public limited liability company whose Global Depositary Receipts are listed on the London Stock Exchange, X5 Retail Group N.V. is obliged to report on compliance with the Dutch Corporate Governance Code in its Annual Report and to explain any instances where it does not apply the principles or best practice provisions of the Code.

In accordance with the Code, a broad outline of the corporate governance structure of the Company is presented in this section, including any deviations from the Code's principles and best practice provisions. The Company adheres to the principles and best practice provisions of the Code as far as may be reasonably expected, while complying with local legislation and applying market practices in the countries in which the Company operates.

### THE MANAGEMENT AND SUPERVISORY BOARDS

X5 Retail Group N.V. adopted a two-tier system of corporate governance, comprising a Management Board and a Supervisory Board. Both the Management Board and the Supervisory Board are accountable to the General Meeting of Shareholders for the performance of their duties.

**Duties of the Management Board**
The Management Board is responsible for X5's overall management. It is accountable for the Company's pursuit and achievement of corporate goals and objectives, its strategies and policies. The Management Board is responsible for complying with all relevant legislation and regulations, for managing the risks associated with the Company's activities, for financing and external communication. The Management Board is required to report related developments to, and discuss the internal risk management and control systems with the Supervisory Board and its Audit Committee.

**Members of the Management Board**
The Management Board currently consists of three members. The table below shows the current members of X5's Management Board and their respective terms of appointment.

| Name | Year of Birth | Position | Year of Initial Appointment | End of Current Term of Appointment |
|---|---|---|---|---|
| Mr. Lev Khasis | 1966 | Chief Executive Officer, Chairman of Management Board | 2006 | 2014 |
| Mr. Evgeny Kornilov | 1969 | Chief Financial Officer | 2008 | 2012 |
| Mr. Frank Lhoëst | 1962 | Corporate Secretary | 2007 | 2011 |

***Lev Khasis***, a Russian citizen, is the former Chairman of the Perekrestok Supervisory Board and a founding member of Investment Company Fosbourne, which invests in various businesses, including retail businesses in Russia. In addition to his activities at Perekrestok, Mr. Khasis previously held a number of senior board and management positions including Chairman of the Board of OJSC Trade House GUM, Chairman of the Board of OJSC Trade House TsUM and Chief Executive Officer of OJSC Samara Trading House. Mr. Khasis is a recognised business leader in Russia and has received a number of public awards including 2004 Businessman of the Year and 2003 Person of the Year in the Head of Retail Business category. For two consecutive years, in 2007 and in 2008, he was ranked Number 1 Retail Manager in a ranking by the National Association of Managers and Kommersant Publishing House.

Since February 2008 Mr. Khasis serves as Chairman of the Russian Association of Companies of Retail Trade (ACORT).

Mr. Khasis graduated from the Aircraft Construction Faculty of Samara Aircraft University, from the Banking Faculty of the Financial Academy of the Government of the Russian Federation and from the Law Faculty of the University of the Interior Ministry of the Russian Federation. He holds a PhD in Economics, Law and Technology.

***Evgeny Kornilov***, a Russian citizen, was appointed Chief Financial Officer of X5 on 18 January 2008. Mr. Kornilov was previously appointed as the Chief Financial Officer of Perekrestok in August 2006 and became the Deputy Chief Financial Officer of X5 in 2007. Prior to joining X5, Mr. Kornilov was the Chief Financial Officer and Chief Controller of SUN Interbrew in Russia and worked in the Management Consultancy and Audit Services practice of PricewaterhouseCoopers in Russia between 1992 and 1999. He graduated from the Moscow Foreign Affairs University with a degree in Economics, International Trade and Foreign Languages.

***Frank Lhoëst***, a Dutch citizen, was appointed a Director B and Corporate Secretary of X5 on 5 November 2007. Since 1991, Mr. Lhoëst has held several positions at Intertrust Group, from account manager in the Netherlands Antilles to founder and director of the Intertrust office in Vienna, Austria. In 2002, Mr. Lhoëst established the Intellectual Property Group of Intertrust in the Netherlands. Mr. Lhoëst graduated from the Leiden University with a degree in Law.

**Duties of the Supervisory Board**
The Supervisory Board is responsible for advising and supervising the Management Board and the general course of affairs of X5 and its businesses. In performing its duties, the Supervisory Board takes into account the relevant interests of the Company's stakeholders, and, to that end, considers all appropriate interests associated with the Company. Major business decisions require the approval of the Supervisory Board. The Supervisory Board also supervises the structure and management of systems of internal controls as well as the financial reporting process. The Supervisory Board meets at least four times per year.

**Members of the Supervisory Board**
The General Meeting of Shareholders determines the number of members of the Supervisory Board. The Supervisory Board currently consists of seven members, with one vacancy to be filled.

The Supervisory Board maintains a profile of its size and composition, which takes into account the nature of the Company's business and its activities and the desired expertise and background of the members of the Supervisory Board. The Supervisory Board generally aims for a diverse composition, but diversity is not a decisive factor when finding the most suitable candidate in line with the Supervisory Board profile. The Supervisory Board evaluates the profile annually.

According to the Rules governing the Principles and Practices of the Supervisory Board, a person may be appointed to the Supervisory Board for a maximum of three terms of four years. The Supervisory Board has prepared a Retirement and Re-appointment Schedule to prevent, to the greatest extent possible, re-appointments occurring simultaneously. Both the Supervisory Board profile and rotation plan can be viewed on the Company's website.

The table below shows the current members of the Supervisory Board and their respective terms of appointment.

| Name | Year of Birth | Position | Year of Initial Appointment | End of Current Term of Appointment |
|---|---|---|---|---|
| Mr. Hervé Defforey | 1950 | Chairman | 2006 | 2010 |
| Mr. Mikhail Fridman | 1964 | Member | 2006 | 2013 |
| Mr. David Gould | 1969 | Member | 2006 | 2010 |
| Mr. Vladimir Ashurkov | 1972 | Member | 2006 | 2012 |
| Mr. Alexander Tynkovan | 1967 | Member | 2008 | 2012 |
| Mr. Stephan DuCharme | 1964 | Member | 2008 | 2012 |
| Mr. Christian Couvreux | 1950 | Member | 2010 | 2014 |

***Hervé Defforey***, a French citizen, is a partner of GRP Partners, London and Los Angeles. He heads GRP Partners' European venture capital activities and serves on the boards of the following companies: IFCO Systems N.V. and Ulta, Corp., Chicago and Kyriba SA, Paris. Mr. Defforey formerly held positions at Carrefour, S.A. (Paris), Azucarera EBRO S.A. (Madrid), BMW A.G. (Munich) and graduated from the University of St. Gallen, Switzerland with a degree in Business Administration.

***Mikhail Fridman***, a Russian citizen, serves as Chairman of the Supervisory Board of Alfa Group and is one of Alfa Group's principal founders. He also serves as the Chairman of the Board of Directors of Alfa Finance Holdings S.A. and of TNK-BP and is a member of the Board of Directors of ABH Holdings S.A. (holding company for Alfa-Banking Group) and of VimpelCom. He is also a member of the International Advisory Board of the Council of Foreign Relations (USA). Mr. Fridman graduated from the Moscow Institute of Steel and Alloys.

***David Gould***, a U.S. citizen, has been serving as Deputy Director for Corporate Development, Finance and Control at Alfa Group Consortium since 2000. He also serves as a member of the Board of Directors of Alfa Finance Holdings S.A. and of ABH Holdings S.A. (holding company for Alfa-Banking Group). From 1992 to 2000, Mr. Gould held various positions at PricewaterhouseCoopers in Boston and in Moscow. He received his BA with honours from Colgate University in 1991 (concentration in Liberal Arts and minor concentration in Economics) and received his MBA-MS (Accounting) from Northeastern University in 1992. He qualified as a Certified Public Accountant in 1993 and as a Chartered Financial Analyst in 1999.

***Vladimir Ashurkov***, a Russian citizen, serves as Director of Group Portfolio Management and Control in Alfa Group. His main non-executive/ancillary positions include member of the Supervisory Board of Alfa Group, member of the Advisory Committee of Rosvodokanal, member of the Altimo Advisory Committee and member of the A1 Group Advisory Committee. Prior to joining Alfa Group, Mr. Ashurkov served as Vice President of Strategic Development in Industrial Investors Group (which owns the controlling stake in Far East Shipping Company) and gained experience in other transport and logistics companies and investment banks. Mr. Ashurkov graduated from the Moscow Institute of Physics and Technology with a Bachelor of Science (Physics) and from the Wharton School, University of Pennsylvania, with an MBA.

***Alexander Tynkovan***, a Russian citizen, is the founder and CEO of "M.Video", a leading consumer electronics and home appliance retailer in the Russian Federation. Mr. Tynkovan graduated summa cum laude from the Moscow Energy Institute, majoring in Aircraft Electric Equipment.

***Stephan DuCharme***, a U.S. citizen, currently holds a portfolio of positions, including as member of the Investment Committee of Alfa Private Equity Partners, a Russian private equity fund. Previously, he held positions with SUN Group, Alfa Group, European Bank for Reconstruction and Development (EBRD) and Salomon Brothers Inc. Mr. DuCharme has served on the Boards of Directors of CSA Czech Airlines, Alfa Bank, SUN-Interbrew Ltd. and JSC SUEK. He graduated with distinction from the University of California at Berkeley and received his MBA from INSEAD.

***Christian Couvreux***, a French citizen, currently acts as a retail consultant in Asia, in particular, in Thailand, Vietnam, Indonesia and the Philippines. He formerly held several leadership positions at Group Casino, including the position of CEO from 1997 until 2003, as well as at CFAO (now part of PPR), in particular, of CFAO-Congo and La Ruche Meridionale. Mr. Couvreux holds a Master's degree in Economic Sciences from the University of Paris and an MBA from the French business school H.E.C.

**Committees of the Supervisory Board**

While retaining overall responsibility, the Supervisory Board assigns certain tasks to its four permanent committees: the Audit Committee, the Nomination and Remuneration Committee, the Related Party Committee and the Strategy Committee. Each committee is composed of at least two members, at least one of whom must be independent within the meaning of the Dutch Corporate Governance Code. The members of each committee are appointed by and from the Supervisory Board. The committees operate pursuant to terms of reference established by the Supervisory Board, in accordance with the Dutch Corporate Governance Code. The terms of reference of these committees can be viewed on X5's website.

***Audit Committee.*** The Audit Committee assists the Supervisory Board in fulfilling its supervision and monitoring responsibilities in respect of the integrity of X5's financial statements, system of internal business control and risk management, financing and finance related strategies and tax planning. It furthermore advises in respect of the appointment of the external auditor by the General Meeting of Shareholders and his remuneration.

***Nomination and Remuneration Committee.*** The Remuneration Committee recommends the remuneration policy for the Management Board to be adopted by the General Meeting of Shareholders, prepares proposals to the Supervisory Board for remuneration of the individual members of the Management Board in line with the remuneration policy and advises the Management Board on the level and structure of compensation for other senior personnel. The Nomination and Remuneration Committee also advises in respect of the selection and appointment of members of the Supervisory Board and the Management Board. At least annually the Nomination and Remuneration Committee evaluates the size and composition of the Supervisory Board and the Management Board, as well as the functioning of the individual members, and reports the results of such evaluations to the Supervisory Board.

***Related Party Committee.*** The Related Party Committee advises the Supervisory Board on handling and deciding on reported (potential) conflicts of interests and any other related party transactions which are contemplated between X5, on the one hand, and conflicted persons or entities, including but not limited to its shareholders, members of the Supervisory Board and members of the Management Board, on the other hand.

***Strategy Committee.*** The Strategy Committee advises the Supervisory Board in respect of the general strategy of X5, including, but not limited to, the future direction to be taken by X5 as a whole and each of its affiliated businesses, overall growth and development strategy, mergers and acquisitions and financing strategy.

### Composition of the Supervisory Board Committees

| Name | Audit Committee | Nomination & Remuneration Committee | Related Party Committee | Strategy Committee |
|---|---|---|---|---|
| H. Defforey | Member | Member | | Member |
| M. Fridman | | | | |
| V. Ashurkov | Member | Member | | Member |
| D. Gould | Chairman | | | |
| A. Tynkovan | | Member | Chairman | Member |
| S. DuCharme | | Chairman | Member | |
| C. Couvreux | | | | Chairman |

### Appointment, Suspension and Dismissal

The General Meeting of Shareholders shall appoint the members of the Management and Supervisory Board from a list of nominees, containing names of at least two persons for each vacancy, to be drawn up by the Supervisory Board. The nomination by the Supervisory Board of the candidates is binding, and therefore the recommended candidate will be appointed by the General Meeting of Shareholders unless the nomination is deprived of its binding character by a qualified majority vote of at least two-thirds of the votes cast, representing more than one-half of the issued share capital of the Company. If the recommended candidate is rejected, the second nominee will be appointed unless similarly rejected by the General Meeting of Shareholders.

Supervisory Board members are appointed for a period of up to four years and may be re-elected twice. Members of the Management Board are also appointed for a period of four years. The Articles of Association do not limit the total term of office for Management Board members.

Each member of the Supervisory Board and Management Board may, at any time, be dismissed or suspended by the General Meeting of Shareholders. A member of the Management Board may at any time be suspended by the Supervisory Board. Such suspension may be discontinued by the General Meeting of Shareholders at any time.

### Remuneration

The remuneration of the individual members of the Management Board will be decided by the Supervisory Board on the recommendation by the Nomination and Remuneration Committee of the Supervisory Board, based on the Company's Remuneration Policy. The remuneration of the members of the Supervisory Board is determined by the General Meeting of Shareholders.

The Remuneration Policy for members of the Management Board and Supervisory Board is incorporated in the Remuneration Report on page 72 and is available on the website of the Company.

### Reporting on Conflicts of Interest

The Supervisory Board is responsible for deciding how to resolve conflicts of interest between members of the Management Board, members of the Supervisory Board and/or the external auditor on the one hand and the Company on the other hand.

A member of the Management Board or of the Supervisory Board is required to immediately report and provide all relevant information to the Chairman of the Supervisory Board (and to the other members of the Management Board, if it concerns a member of that board) on any conflict of interest, or potential conflict of interest, that he may have with the Company and that may be of material significance to him or the Company.

A decision by X5 to enter into a transaction involving a conflict of interest with a member of the Management Board or a member of the Supervisory Board that is of material significance to him or the Company requires the approval of the Supervisory Board and must be concluded on terms customary in the Russian retail sector. The Related Party Committee advises the Supervisory Board on the handling, and deciding on, reported conflicts of interest and prepares resolutions of the Supervisory Board in relation thereto.

In the event of legal proceedings between the Company and a member of the Management Board, the Company may be represented by a member of the Supervisory Board. In all other events in which a member of the Management Board has a conflict of interest with the Company, the Company may be represented by the Management Board, notwithstanding the discretionary power of the General Meeting of Shareholders to designate other person(s) to represent the Company upon execution of such a related party transaction.

## SHAREHOLDERS AND THEIR RIGHTS

### General Meeting of Shareholders

X5 Retail Group N.V. is required to hold a General Meeting of Shareholders within six months after the end of the financial year, among other things, to adopt the financial statements, to decide on any proposal concerning profit allocation and to discharge the members of the Management Board and Supervisory Board from their responsibility for the performance of their respective duties for the previous financial year.

Extraordinary meetings will be held as often as the Management Board or the Supervisory Board deems necessary. In addition, shareholders and holders of Global Depositary Receipts (GDRs) jointly representing 10% of the outstanding share capital may request the Management Board and the Supervisory Board that a General Meeting of Shareholders be held, stating their proposed agenda in detail.

The powers of the General Meeting of Shareholders are defined in the Articles of Association. Apart from the decisions taken at the Annual General Meeting of Shareholders, the main powers of the shareholders are to appoint (subject to the Supervisory Board's right of making binding nominations), suspend and dismiss members of the Management Board and Supervisory Board, to appoint the external auditor, to adopt amendments to the Articles of Association, to issue shares and grant subscriptions for shares, to authorise the Management Board or the Supervisory Board to issue shares and grant subscriptions for shares, to authorise the Management Board or the Supervisory Board to restrict or exclude pre-emptive rights of shareholders upon issuance of shares, to authorise the Management Board to repurchase outstanding shares of the Company, to adopt the remuneration policy of the Management Board, to determine the remuneration of members of the Supervisory Board, and to merge, demerge or dissolve the Company.

One or more shareholders or holders of GDRs representing at least 1% of X5's issued share capital or representing a value of EUR 50 million are entitled to propose items for the agenda of the General Meeting of Shareholders. Such proposals must be honoured by the Company provided that important Company interests do not dictate otherwise, and that the request is received by the Company at least sixty days before the date of the General Meeting of Shareholders.

General Meetings of Shareholders may only be held in Amsterdam, Haarlemmermeer (Schiphol Airport) or The Hague (the Netherlands). Notice of a General Meeting of Shareholders must be given to the shareholders and the holders of depositary receipts of shares no later than the fifteenth day before the date of the meeting and must include an agenda stating the items to be discussed during the meeting.

All shareholders and other persons who, pursuant to Dutch law or the Articles, are entitled to attend and/or vote at a General Meeting of Shareholders are entitled to address the General Meeting of Shareholders. X5 uses the Bank of New York Mellon, the depositary for X5's GDR facility, to enable GDR holders to exercise their voting rights represented by the shares underlying the GDRs. As described in the "Terms and Conditions of the Global Depositary Receipts", holders of GDRs may instruct the Depositary with regard to the exercise of the voting rights connected to the shares underlying their GDRs. Alternatively, upon request of the holders of such depositary receipts, the Depositary will grant a proxy to such holders who wish to vote in person at a General Meeting of Shareholders. Persons who hold a written proxy may represent shareholders at a General Meeting of Shareholders. The written proxy must be duly executed and legalised in accordance with the laws of the country where the proxy is issued.

Subject to the prior approval of the Supervisory Board, the Management Board may set a record date to establish which shareholders are entitled to attend and vote at the General Meeting of Shareholders.

**Voting Rights**

Each share confers the right to cast one vote at the General Meeting of Shareholders. There are no restrictions, either under Dutch law or in the Articles, on the right of non-residents of the Netherlands or foreign owners to hold or vote the shares, other than those also imposed on residents of the Netherlands. Resolutions of the General Meeting of Shareholders will be passed by a simple majority of the votes cast in a meeting where more than 25% of the issued share capital is present or represented. If 25% or less of the issued share capital is present or represented, a second meeting should be convened and held no later than four weeks following the first meeting. At such second meeting, no quorum requirement will apply. However, the General Meeting of Shareholders can only resolve on a merger or demerger with a majority of at least two/thirds of the votes cast, if less than fifty percent of the issued capital is represented in that meeting.

### Dividend Rights

Any distribution of profits to shareholders will be made after the adoption by the General Meeting of Shareholders of the annual accounts of the Company from which it appears that such distribution is permitted. The Company may only declare profit distributions insofar as its net assets exceed the sum of its issued share capital plus any legal reserves required to be maintained pursuant to Dutch law and the Articles. A loss may only be applied against such reserves to the extent permitted by Dutch law. On a proposal of the Supervisory Board, the General Meeting of Shareholders will determine which part of the profits will be added to the reserves and the allocation of the remaining profits.

On a proposal of the Supervisory Board, the General Meeting of Shareholders may resolve to pay an interim dividend insofar as X5's net assets exceed the sum of its issued share capital and the reserves that are required to be maintained pursuant to Dutch law, as evidenced by an interim financial statement prepared and signed by all the members of the Management Board. In addition, on a proposal of the Supervisory Board, the General Meeting of Shareholders may resolve to make distributions to the shareholders out of any reserves that need not to be maintained pursuant to Dutch law.

Dividends and other distributions that have not been claimed within five years after the date on which they became due and payable revert to the Company.

### Significant Ownership of Voting Shares

According to the Dutch Financial Markets Supervision Act *(Wet op het financieel toezicht)*, any person or legal entity who, directly or indirectly, acquires or disposes of an interest in X5's capital and/or voting rights must immediately give written notice to the Netherlands Authority for the Financial Markets ('AFM'), if the acquisition or disposal causes the percentage of outstanding capital interest and/or voting rights held by that person or legal entity to reach, exceed or fall below any of the following thresholds: 5%, 10%, 15%, 20%, 25%, 30%, 40%, 50%, 60%, 75% and 95%.

The following table lists the shareholders on record on 8 March 2010 in the AFM's public register that hold an interest of 5% or more in the share capital of the Company:

| Shareholder | Date of disclosure | Capital interest and voting rights[1] |
|---|---|---|
| CTF Holdings Ltd. | 2 August 2007 | 48.41% |
| Axon Trust | 22 December 2009 | 11.43% |
| The Baker Trust | 11 December 2009 | 8.42% |

### Securities Owned by Board Members

The members of the Management Board and Supervisory Board and X5's other senior management are subject to the Company's Code of Conduct with regard to Insider Trading, which contains rules of conduct to prevent trading in X5's Global Depositary Receipts of shares or other financial instruments when holding inside information. The Code of Conduct with regard to Insider Trading can be viewed on the Company's website.

The Code of Conduct includes a specific section on obligations of members of the Management Board to report to the Compliance Officer in case of changes in their holding of securities in any Dutch listed company, not being X5 securities, in accordance with the Dutch Corporate Governance Code.

[1] In accordance with the filing requirements the percentages shown include both direct and indirect capital interests and voting rights. Further details can be obtained at www.afm.nl.

Furthermore, under the Dutch Financial Markets Supervision Act, members of the Management Board and Supervisory Board shall notify the AFM of X5 securities and voting rights at their disposal. These positions can be viewed on the AFM's public register.

In addition, under the Disclosure and Transparency Rules in the United Kingdom, X5 must notify a Regulatory Information Service (RIS) of the occurrence of all transactions in X5 conducted –on their own account- and notified by members of the Management Board and Supervisory Board.

**Repurchase by the Company of Its Own Shares**

The Company may acquire fully paid shares, or depositary receipts thereof, in its capital for a consideration only following authorisation of the General Meeting of Shareholders and subject to certain provisions of Dutch law and the Company's Articles of Association, if:

- Shareholders' equity minus the purchase price is not less than the sum of X5's issued and fully paid-in capital plus any reserves required to be maintained by Dutch law or X5's Articles of Association; and

- X5 and its subsidiaries would not, as a result, hold shares or depositary receipts thereof with an aggregate nominal value exceeding half of the issued share capital.

The Management Board has been authorised to acquire up to 10% of the shares or depositary receipts thereof. This authorisation is valid through 12 December 2010. In addition, the Supervisory Board has resolved that in case a purchase of shares or depositary receipts thereof by X5 would lead to X5 holding more than 5% of the shares or depositary receipts thereof, the Management Board requires the Supervisory Board's prior approval for such purchase.

Authorisation by the General Meeting of Shareholders is not required if X5's own shares are acquired for the purpose of transferring those shares to X5 employees pursuant to any arrangements applicable to such employees.

Shares or depositary receipts thereof held by X5 or a subsidiary may not be voted on and are not taken into account for determining whether quorum requirements, if any, are satisfied.

**Issue of New Shares and Pre-Emptive Rights**

Shares in X5 may be issued, and rights to subscribe for shares may be granted, pursuant to a resolution of the General Meeting of Shareholders or another corporate body of X5 to which the General Meeting of Shareholders has delegated such authority for a time not exceeding five years. The General Meeting of Shareholders approved a delegation of this authority to the Supervisory Board, relating to the issuance and/or granting of rights to acquire up to 16,226,820 shares (23,90% of the issued share capital) through 12 December 2010.

Upon the issue of new shares, holders of X5's shares have a pre-emptive right to subscribe for shares in proportion to the aggregate amount of their existing holdings of X5's shares. According to the Company's Articles of Association, this pre-emptive right does not apply to any issue of shares to employees of X5 or a group company. Pre-emptive rights may be restricted or excluded pursuant to a resolution of the General Meeting of Shareholders or another corporate body of X5 to which the General Meeting of Shareholders has delegated such authority for a time not exceeding five years. The General Meeting of Shareholders has delegated the authority to restrict or exclude the pre-emptive rights of shareholders upon the issue of shares and/or the granting of rights to subscribe for shares to the Supervisory Board through 12 December 2010.

**Articles of Association**
X5's Articles of Association contain rules on organisation and corporate governance of the Company. The current text of the Articles of Association is available at the Trade Register of the Chamber of Commerce and Industry for Amsterdam and on X5's website.

Amendment of the Articles of Association of the Company requires a resolution of the General Meeting of Shareholders. The proposal to amend the Articles including the text of the proposed amendment must be made available to holders of shares and GDR holders for inspection at the offices of X5 as of the date of the notice convening the meeting of the General Meeting of Shareholders until the end of the meeting of the General Meeting of Shareholders at which the proposed amendment is voted on.

## AUDITOR

The General Meeting of Shareholders appoints the external auditor upon nomination of the Supervisory Board. Both the Audit Committee and the Management Board make a recommendation to the Supervisory Board with respect to the external auditor to be proposed for (re)appointment by the General Meeting of Shareholders. In addition, the Audit Committee evaluates and, where appropriate, recommends the replacement of the external auditor. The Audit Committee also pre-approves the fees for audit and permitted non-audit services to be performed by the external auditor as negotiated by the Management Board. The Audit Committee shall not approve the engagement of the external auditor to render non-audit services prohibited by applicable laws and regulations or that would compromise their independence.

At least every four years, the Management Board, shall, together with the Audit Committee, thoroughly assess the functioning of the external auditor in the various entities and capacities in which the external auditor operates. The main conclusions of the assessment shall be notified to the General Meeting of Shareholders for the purpose of considering the nomination for the appointment of external auditor of the Company.

## CORPORATE GOVERNANCE CODE

X5 is subject to the Dutch Corporate Governance Code (the "Code"), which came into effect on 1 January 2004. On 10 December 2008 the Dutch Corporate Governance Code Monitoring Committee (the "Committee") presented an amended Code, which became effective on 1 January 2009. The full text of the amended Code can be viewed on X5's website.

Some of the Code's best practice provisions have been incorporated into Dutch law, including the obligation for a listed company to state each year in its annual report how it applied the recommendations of the Code in the past financial year and to explain carefully, where applicable, why a provision was not applied in circumstances where the listed company departed from the recommendations of the Code.

X5's corporate governance policy with respect to the implementation of the Code was last discussed with its shareholders at the 2006 Annual General Meeting of Shareholders. Since then, there were no substantial changes in the corporate governance structure of the Company.

For the financial year 2009, the Committee has recommended that listed companies include a chapter in their annual report on the broad outline of their corporate governance structure and compliance with the amended Code and to present this chapter as a separate agenda item for discussion to the general meeting of shareholders in 2010. X5 follows this recommendation of the Committee.

X5 generally adheres to the Code, as amended, but does not comply with the following recommendations:

**II.2.4: Grant of Options to Members of the Management Board**
Pursuant to the Code, if a company grants options to its members of its management board, such grant should be subject to certain performance criteria and the options should not be exercisable within three years following the date of grant.

On 15 June 2007, the General Meeting of Shareholders approved the Company's Employee Stock Option Plan (the "ESOP"), under which options are granted to employees in four tranches over a period of three years with varying vesting periods. The vesting requirement of the programme is the continued employment of participants.

While the ESOP is considered long-term compensation for its participants, and the grant of options will be linked to pre-determined, measurable performance-based targets, X5 acknowledges that in terms of vesting period the ESOP deviates from the Code. However, since X5's operational activities are mainly based in the Russian Federation and Ukraine, and the grant of unconditional options with a shorter than three year vesting period was customary in these markets at the time the ESOP was designed (2007), it is important for X5 to deviate on this point from the Code in order to attract and reward the best professionals in these markets.

**II.2.11: Claw-Back Clause**
Pursuant to the Code, the supervisory board may recover from the management board members any variable remuneration awarded on the basis of incorrect financial or other data (claw-back clause).

X5 acknowledges that currently the contracts with the members of Management Board do not provide for a claw-back provision. The Supervisory Board will address this provision at the time of (re-)appointment of members of the Management Board.

**II.2.14: Immediate Publication of Main Elements of Contracts with Members of the Management Board**
Pursuant to the Code, the main elements of contracts with members of the management board should be made public following the entering into of such contracts but prior to the convening of the General Meeting of Shareholders where the relevant member is scheduled be appointed.

X5 acknowledges that on this point it has deviated from the Code. However, the main elements of the contracts with the members of the Management Board are included in the 2009 Remuneration Report, which will be made available on X5's website upon publication of the 2009 Annual Report. In 2010 the main elements of the contracts between X5 and its current Management Board members will be made public. Going forward such publication will take place no later than the date of the notice calling the meeting of the General Meeting of Shareholders where the (re-)appointment of Management Board members will be proposed.

**II.3.4, III.6.3 and III.6.4: Disclosure of Transactions with Related Parties in the Annual Report**
In accordance with the Code, transactions with members of the Management Board, Supervisory Board, or persons holding at least 10% of shares or depository receipts thereof in which there are significant conflicting interests will be published in X5's Annual Report. However, in deviation from the Code, a detailed statement of the relevant conflict of interest is not published if (i) this conflicts with the law, (ii) the confidential, share-price sensitive or competition-sensitive nature of the transaction prevents publication and/or (iii) the information is so competition-sensitive that the publication could damage X5's competitive position.

**III.2.1: Independence of Members of the Supervisory Board**
Pursuant to the Code, all, but one, of the members of the Supervisory Board must be independent.

Although the number of independent members of the Supervisory Board increased from two to four in 2008, three members of the Supervisory Board (i) have a substantial shareholder interest in X5 or (ii) are related to companies that are owned or controlled by companies that ultimately hold 10% or more of the shares or GDRs in X5. These members of the Supervisory Board are, therefore, not considered to be independent within the meaning of the Code. Mr. Defforey, Mr. Tynkovan, Mr. DuCharme and Mr. Couvreux are independent within the meaning of the Code.

X5 believes that the non-independent members of the Supervisory Board have an in-depth knowledge of the geographic market, of business in general and of food retail specifically in the markets in which X5 operates, which is of particular advantage to X5 and its stakeholders.

**III.5: Committees of the Supervisory Board and Deviation from the Maximum of One Non-Independent Member of the Audit Committee**
In July 2009, the Supervisory Board resolved to merge the Supervisory Board's Remuneration Committee and Selection and Appointment Committee to one "Nomination and Remuneration Committee" and accordingly X5 currently deviates from the Code, which requires these two committees to be separate. However, in light of the respective duties, responsibilities and composition of each of the Remuneration Committee and the Selection and Appointment Committee, and for reasons of practicality, X5 believes that it was in X5's best interest to merge these Committees.

In addition, X5 acknowledges that Mr. Gould and Mr. Ashurkov are non-independent members of the Audit Committee within the meaning of the Code whereas, pursuant to the Code, the terms of reference of each committee of the Supervisory Board may provide that a maximum of one member of each committee may not be independent. Considering Mr. Gould's and Mr. Ashurkov's financial expertise, and for reasons of continuity, X5 believes that it is in X5's best interest that Mr. Gould's and Mr. Ashurkov's membership of the Audit Committee be continued.

**III.7.1: No Grant of Shares and Options to Members of the Supervisory Board**
Pursuant to the Code, members of the Supervisory Board shall not be granted any shares and/or rights to subscribe for shares as remuneration for their membership of the Supervisory Board.

On 15 June 2007, 5 November 2007, 16 June 2008 and 15 January 2010 the General Meeting of Shareholders approved the granting of options to Mr. Defforey, Mr. Criado-Pérez Trefault and/or Mr. DuCharme, all of whom were members of the Supervisory Board at the respective grant dates. X5 acknowledges that such grants deviate from the Code. However, in order to attract and reward experienced individuals with a proven track record in the food retail industry, X5 believes it is necessary to grant stock options also to certain members of the Supervisory Board.

# Risk Management & Internal Controls

This section provides an overview of X5's approach to risk management and internal controls in achieving its strategic objectives. ***Section 1*** describes the principal risks to which X5 is exposed as well as their mitigating factors, grouped into five categories: strategic, compliance (legal and regulatory), operational, financial and financial reporting risks. ***Section 2*** gives an overview of the system of internal control procedures and risk management techniques which are employed by management to manage and mitigate risk in an informed, controlled and transparent manner. This description covers all the components of the system of internal control and risk management determined by the Committee of Sponsoring Organisations (COSO) in its *Internal Control – Integrated Framework*: control environment, risk assessment, control activities, information and communication, monitoring.

## SECTION 1: RISK PROFILE

Like any other entity X5 faces uncertainty in conducting its business. Uncertainty represents both risk and opportunity which are events, situations or possibilities that affect an entity's ability to achieve its objectives, maintain a good reputation and support value creation. The main challenge for any business is to develop appropriate controls and risk management techniques that would help to appropriately identify, assess, manage and mitigate the full set of risks facing the business. A properly functioning system will balance risks and opportunities helping the entity to achieve its objectives efficiently and effectively, which should ultimately enhance its value.

As a fast growing company operating in a developing market, exposed to a number of external risk factors related to a politically and economically changing environment, it is critical for X5's success to be able to utilise opportunities existing in the Russian food market. This requires the Company to constantly evaluate the risks related to operating in an unstable developing market environment and to accept a certain degree of economically justifiable risk. All these factors determine the Company's risk profile, and in particular its risk appetite, namely the level of risk required to achieve X5's active business expansion and growth.

The principal risks faced by the Company and relevant mitigating factors are presented below:

### 1. Strategic Risks

**Business Strategy**
We need to understand and properly manage strategic risks in order to deliver long-term profitable growth for the benefit of all of our stakeholders and secure and enhance X5's leadership in the Russian retail market.

In recent years, the growth in consumer demand in Russia has attracted new market participants and has produced an increasingly competitive environment. Despite the size and significant historical growth of the Russian food retail market it remains highly fragmented which poses both opportunities and challenges in increasing market share for X5.

To ensure the Company continues to pursue the right strategy, the Supervisory Board and its Strategy Committee as well as the Company's Executive Board hold specific sessions to discuss and take decisions on key strategic issues on a regular basis. We also invest significant resources in ensuring that our strategy is communicated well and understood not just by the parties who are key to its execution, but by all our stakeholders including customers, investors, suppliers, government and the media.

**Strategic Objectives**

X5's key strategic objectives are: (1) customer success through development of multi-format retail operations and ensuring strong value propositions; (2) operational excellence to maximise efficiency and support price leadership; (3) disciplined growth with focus on returns supported by prudent financial management (see detailed description in "Strategic Review" section of this Annual Report). The risks associated with the implementation of these strategic objectives can be described as follows:

(1) Risk of failure to differentiate value proposition of each format. To mitigate this risk X5 will continue to market and promote its store formats through advertising, promotional activities and loyalty programmes with an emphasis on how the value proposition of each store format serves the specific needs of its target customers.

(2) Risk of not achieving cost savings at the level adequate to support investment into prices. X5 is highly focused on controlling costs both at the operational level and at its headquarters. This resulted in considerable cost savings during the last several years. In addition, in 2009 X5 launched a multi-year Strategic Efficiency Programme to drive long-term operational excellence in line with international benchmarks. This Programme encompasses: (i) the creation of a fully integrated supply chain; (ii) the transformation of the Company's IT systems; (iii) in-store labour productivity improvement; (iv) business process improvement; and (v) asset efficiency in areas such as real estate, energy efficiency and asset management.

(3) Risk of lack of investment opportunities with returns sufficient to justify higher cost of capital, which has increased due to the current financial and economic crisis. X5 has adjusted its investment approach and closely examines all available opportunities and undertakes projects that offer the highest returns consistent with the Company's expansion strategy.

**Economic & Market Conditions**

While in recent years the economic situation in Russia has generally become more stable and conducive to investment, the Russian economy is vulnerable to fluctuations in the price of oil and natural gas on the world market. As Russia is a major producer and exporter of oil and natural gas, a decline in the price of oil and natural gas could significantly slow or disrupt the Russian economy.

Consumer demand in the markets in which X5 operates depends upon a range of factors which are largely outside of X5's control, including demographic factors, consumer preferences and discretionary consumer spending (which is in turn influenced by factors such as general economic conditions, the availability of disposable income and general levels of consumer confidence). In periods of economic uncertainty, such as the current financial and economic crisis, customers tend to reduce spending both by reducing the volume of their purchases and by shifting their purchasing pattern towards less expensive products.

X5's multi-format business model enables it to respond quickly to changes in consumer preferences and to cater to a diverse range of lifestyles and family budgets. We aim to have a broad appeal in product price and range in a way that allows us to compete successfully despite changing economic conditions that impact on consumer spending.

Importantly, product range, pricing policy, merchandising and marketing concepts are also adapted continually to account for changing consumer behavior.
The feasibility and acceptance of the concepts are first verified in test markets and then implemented Company-wide.

**Expansion**
To maintain its leadership position, X5 must expand at a rate that equals or exceeds that of its competitors. The failure of X5 to open new stores will directly impact on its growth and profitability. Since the start of the financial and economic crisis in the latter part of 2008, numerous bankruptcies of retailers and store closures occurred across Russia. This allows strong and financially sound modern retailers to avail themselves of new opportunities to grow market share through both organic expansion and via acquisitions.

X5 management pays particular attention and allocates significant management resources to optimisation of its organic expansion strategy including identifying and acquiring appropriate sites on commercially reasonable terms, opening new stores on schedule, employing, training and retaining store and supervisory personnel and fully integrating new stores into X5's existing operations.

An important part of X5's expansion strategy includes the selective acquisition of attractive retail chains. The pursuit of any acquisition strategy presumes certain risks, including the failure to accurately assess the operations and / or financial condition of the target, overvaluing of the acquisition target, discovering, post-acquisition, undisclosed liabilities or contingent liabilities, the failure to properly integrate the target and realise economies and synergies, etc. To address these risks, the Company employs an experienced M&A team and utilises professional service providers (legal, tax, due diligence, valuation experts) in the due diligence, negotiation and documentation phases of any transaction. Additionally, appropriate integration plans ensure timely and effective integration of the target company, once acquired. Also, importantly, a system of monitoring and direct accountability for achievement of operational integration and target synergies is established.

## 2. Compliance Risks

**Legal**
Russia is still developing the legal framework required to support a market economy. Risks associated with the Russian legal system include inconsistencies between: (i) federal laws, presidential decrees and regulations issued by the federal government; and (ii) regional and local laws, rules and regulations. There is sometimes a lack of judicial independence from political, social and commercial forces, as well as a relative inexperience of judges and courts in interpreting new Russian legislation and complex commercial arrangements. This is exacerbated by a lack of binding judicial precedent and difficulty in enforcing court judgments.

We protect ourselves against legal (including litigation) risks by seeking to comply with all applicable laws and regulations, and by vigorously preparing and defending our cases and enforcing our rights in relation to contracts and using all means provided by law.

**Regulatory Environment**
X5's operations are subject to supervision and regulation by various government entities and agencies, in connection with obtaining and renewing various licenses and permits and with respect to various quality, health and safety, packaging, labeling and distribution standards. Russia is in a process of structural, economic and political transition and the regulatory regimes applicable to X5's operations are still developing. Many regulations applicable to X5 have only recently been enacted and there is uncertainty regarding their application and enforcement. Regulatory authorities often have little experience in analysing regulatory issues arising from commercial transactions and exercise considerable discretion in matters of enforcement and interpretation of applicable laws, regulations and standards.

The new Retail Legislation that came into force as at 1 February 2010 may have a significant impact on the operation of retail companies such as X5, as it implies, among other things: (i) the introduction of restrictions on the acquisition by retail chains of additional trade areas in municipal districts where a retail chain has a market share of over 25%; (ii) the reduction of deferral period for payments for goods, such period being dependent on the specific category of goods; (iii) the limitation of permitted grounds for payments from suppliers related with the supply of food retail products; (iv) the extension of powers of federal state bodies to regulate retail prices for socially important categories of goods. This may constrain the operation of X5's business and could prevent the Company's future expansion in selective regions.

The Company monitors regulatory developments and has a strong compliance regime enforced by regular reviews and audits of stores and distribution centres to ensure that compliance and training needs are regularly reviewed and addressed. We also engage with public and governmental organisations to ensure that the interests of our customers are represented and we are often consulted and invited to contribute to important government regulations regarding the retail industry.

**Food Products Safety**
The packaging, marketing, distribution and sale of food products entail an inherent risk of contamination or deterioration, which could potentially lead to product liability, product recall and, as a result, negative publicity. The quality and safety of our products is of the highest importance. We have strict product safety procedures for ensuring product integrity at all times. We work in partnership with suppliers to ensure mutual understanding of the standards required. The Company also monitors the changes in the regulations regarding food safety and regularly reviews its respective policies and procedures to ensure compliance.

**Taxation**
Russian tax, currency and customs legislation is subject to varying interpretations and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activities of X5 may be challenged by the relevant regional and federal tax authorities. In recent years the tax authorities in the Russian Federation have taken a more assertive approach in their enforcement of tax legislation, and it is possible that transactions and activities that have not been challenged in the past may now be challenged.

Management regularly reviews the Company's taxation compliance with applicable legislation, laws and decrees and current interpretations published by the authorities. It also thoroughly reviews the judicial precedents that come out of tax disputes of other companies operating in Russia. The Company further protects itself against tax risks by establishing provisions in its IFRS consolidated financial statements.

Note 34 "Commitments and Contingencies" to the IFRS consolidated financial statements in this Annual Report contains the description of the main tax uncertainties and an estimate of the related liability.

**Fraud**
Whilst we persistently strive to high integrity standards among our staff, there remains the potential for fraud and other dishonest activity at all levels of the business, from store level to senior management. X5 gives clear guidance on behaviour to employees through the Company values and its Guiding Principles of Business Conduct. The Company constantly emphasises its Corporate Code for Reporting of Alleged Irregularities (referred to as "Whistleblower Policy") and operates an ethics hot line. The Corporate Audit Department and /or the Security Department undertake investigations into fraud cases. Results of such investigations are highlighted to the Audit Committee of the Supervisory Board and the Supervisory Board as necessary.

## 3. Operational Risks

### Reputational Risk

As X5's success depends to a significant extent upon brand recognition, the brand names Pyaterochka, Perekrestok and Karusel and their associated reputations are key assets of X5's business. X5 believes it has taken appropriate steps to protect its trademarks and other intellectual property rights but cannot be certain that such steps will be sufficient or that third parties will not infringe or challenge such rights. This is partly because Russia and the other countries in which X5 operates generally offer a lower level of intellectual property rights enforcement than countries in Western Europe and North America.

Additionally, we emphasise the Guiding Principles of Business Conduct in the way we conduct our business and deal with customers, employees and suppliers. X5 is committed to being a responsible corporate citizen that strives to meet international standards and best practices in the operation of its business and in its relationships with shareholders, partners and society.

The brand name Pyaterochka is additionally exposed, as it is used by a significant number of franchisee stores. We work only with the most successful and efficient partners and monitor their operations as well as compliance with franchise agreements separating from those who do not meet our high standards. In addition, the Company has a strategy of selective buy-outs of franchisees, which reduces this reputational risk exposure.

Furthermore, we focus on the importance of our corporate social responsibilities and place a high level of emphasis on charitable activities and the patronage of Russia's historical, cultural and spiritual heritage.

### Performance Risk

There is a risk that the Company may not achieve its performance targets, particularly since the business is susceptible to economic downturn that affects consumer spending. Through our multi-format strategy we try to respond to the needs and behaviour of customers from different market segments. Our aim is to have broad appeal to all customers, minimising the impact of changes in the economic climate.

All of our business units, including soft discounters, supermarkets and hypermarkets, have stretch targets and their performance is monitored continually and reported monthly to the Executive Board and the Supervisory Board.

### Human Resources

Our greatest asset is our employees. Though it is critical for our success to attract, retain, develop and motivate the best people with the right capabilities at all levels of operation, X5's competitive position and future prospects especially depend on its senior management experience and expertise and X5's ability to recruit and retain qualified personnel. The competition for attracting and retaining the best talent in Russia is particularly intense due to the relatively limited number of qualified individuals.

In 2008 X5 implemented a successful programme to develop and promote talented managers with vertical and horizontal career-building opportunities within the organisation. In addition, X5 uses a system of key performance indicators (KPIs) to determine compensation for executives and managers. X5 reviews its KPIs on an annual basis to ensure that they correspond with the Company's strategic objectives.

The Company has a strong commitment to employee education, operating 14 regional multi-format training and development centers and running numerous programmes to provide employees with professional development opportunities. Since 2008 X5 operates the X5 Corporate University to provide orientation for all new office employees on the Company's values, principles, operations and strategy.

**Real Estate**
X5's ability to open new stores is heavily dependent on identifying and leasing and/or purchasing properties that are suitable for its needs on commercially reasonable terms. The market for property in large metropolitan areas in Russia prior to the current financial and economic crisis was highly competitive and, when economic conditions are favourable, competition for, and therefore the cost of, high-quality sites may increase.

On the other hand, the prices of the properties may also decrease due to changes in the competitive environment, changes in the attractiveness of real property as an investment asset in Russia as a whole or in certain regional markets in which our real property is located. As a result of any unfavourable changes in the real property market, the value of X5's real property may decrease. As Russia recovers from the current financial and economic crisis, competition for, and therefore the cost of, high-quality sites may increase, as has been the case in the past.

In the process of identifying and leasing and / or purchasing suitable properties, the Company performs comprehensive feasibility studies to identify and reduce risks of not obtaining approvals from the various regional authorities required to undertake construction and to secure X5's rights to the use of stores or to refit or refurbish those stores. However, if X5 procures the rights to suitable sites, it may experience difficulty or delay in obtaining approvals from the various regional authorities required to undertake construction and to secure X5's rights to the use of stores or to refit or refurbish those stores. In addition, for all the potential investments into property we calculate cash flows and return on investment taking into account store locations, traffic and accessibility studies, etc. to make sure that we obtain attractive real estate that is suitable for our business and for which we do not over-pay.

**Supply Chain & Logistics**
X5 stores are part of a complex supply chain and the Company works in partnership with its suppliers to manage the risk of any delays or interruptions in this supply, which might affect its retail operations. The Company continues implementation of an ambitious long-term project to create a fully integrated supply chain infrastructure across the full geography of the Company's operations that will enable X5 to enhance its operational efficiency and competitiveness. The key steps involved in creating a fully integrated supply chain include: (i) the expansion and optimisation of the Company's distribution centre network; (ii) the enhancement of warehouse productivity; and (iii) improved efficiency of transportation. In 2008 and 2009, X5 made substantial progress in implementing these initiatives, which are described in detail in "Strategic Review" section of this Annual Report.

Much of Russia's transport infrastructure needs to be modernised with the help of long-term government and private sector investment programmes. Poor condition of physical infrastructure may disrupt the transportation of goods and adds costs to doing business in Russia. X5 relies on the satisfactory condition of roads to allow for movement of its goods by trucks between distribution centres and stores. X5 aims to improve the efficiency of X5's transportation management through the introduction of the Transportation Management System (TMS), which was initiated in 2009.

**IT Systems & Infrastructure**
X5 manages its inventory and logistical operations through a variety of electronic media, including intranet, networked personal computers and automated inventory management systems.

These operations are heavily dependent on the integrity of the electronic systems supporting them. The Company's systems and operations are vulnerable to interruption from natural disasters, power loss, breach of security and similar events. X5 has contingency plans in place to deal with such events, however, X5's information systems could suffer failures or delays and IT equipment breakdowns may result in temporary inoperability of the majority of stores trading software with the exception of cash registers.

X5 is in the process of implementing an IT systems upgrade as part of its Strategic Efficiency Programme. The Company has launched a phased implementation of the SAP system as its enterprise resource planning system to provide X5 with a strong platform for further scalable growth and to drive Company-wide efficiency gains. X5 believes SAP will enable it to facilitate controls over processes across all major levels of Company management, from store operations to strategic planning. In parallel, X5 is standardising and upgrading the IT systems in its store formats across the Company. Detailed information on the transformation of X5's IT systems is provided in "Strategic Review" section of this Annual Report.

**4. Financial Risks**

The main financial risks faced by the Company relate to the availability of funds to meet business needs and fluctuations in interest and foreign exchange rates. The central treasury function is responsible for managing the Company's liquid resources, funding requirements, interest rate, currency and credit exposures and the associated risks, as well as insurance of assets. The treasury function does not operate as a profit centre and the undertaking of speculative transactions is not permitted.

**Funding and Liquidity Risk**

The Company finances its operations by a combination of internal cash flows, long and medium-term debt, capital market issues, commercial paper, bank borrowings and leases. The objective is to ensure continuity of funding on the best available market terms. The policy is to diversify the Company's credit portfolio, to improve the debt maturity profile, to arrange funding ahead of requirements and to maintain sufficient undrawn committed bank facilities, and a strong credit rating so that maturing debt may be refinanced as it falls due.

As a result of the current global financial crisis the availability of financing in Russia has decreased dramatically, and the terms of any available financings have become significantly less favourable for borrowers. Nevertheless, the company enjoyed lower cost of funding at the end of 2009 compared to the beginning of the year. In addition, in the second half of 2009 the Company was able to increase the size of available credit facilities and improve its liquidity position. Management believes it has taken appropriate measures to resolve the risk of refinancing by securing several debt financing instruments, including available committed lines with major Russian and international banks and access to the Ruble bond market which can be utilised in addition to the cash balances and cash flows from operating activities that are used to finance X5's discretionary capital expenditure programme.

**Interest Rate Risk**

The objective is to limit our exposure to increases in interest rates while retaining the opportunity to benefit from interest rate reductions. From time to time, interest rate swaps are used to achieve the desired mix of fixed and floating rate debt.

**Foreign Currency Risk**

Our principal objective is to reduce the effect of exchange rate volatility and transactional currency exposures through available hedging instruments. From time to time, currency forwards and options are used to manage foreign currency exposures. The Company does not hedge non-cash accounting translation exposures.

**Credit Risk**
The Company is exposed to credit risk mainly through the use of financial instruments mentioned above and placement of cash balances with financial institutions. The objective is to reduce risk of loss arising from defaulting or insolvent counterparties. This is achieved primarily by the ongoing assessment of financial institutions credit strength and counterparty limits.

Note 30 "Financial Risks Management" to the Consolidated Financial Statements in this Annual Report contains the detailed description of the currency risk, interest rate risk, and liquidity risk as well as how the Company currently manages them.

**Insurance**
X5's insurance policies cover most of its supermarket and hypermarket operations and part of its soft discount store operations. X5 also maintains third-party liability insurance to the extent required by Russian law. Still there is a risk that the Company's insurance policies may be insufficient to cover losses arising as a result of a business interruption or damage to X5's property as a result of fire, explosion, flood or other circumstances. The Company negotiated across-the-group schemes ensuring uniform cover for all its subsidiaries, which are arranged and managed centrally.

**5. Financial Reporting Risk**
Financial reporting risk relates to the failure in proper recording and classification of accounting entries arising from business activities of the Company, as well as to inability to make accurate and reliable estimates. All these factors may lead to misstatements in financial statements.

In preparing the consolidated financial statements, X5 management is responsible for maintaining proper accounting records, selecting suitable accounting policies and applying them consistently, and implementing and maintaining an effective and sound system of internal control over financial reporting, key elements of which are described below:

- The financial control team helps managers across the Company's various departments to draw up and control budgets, participate in validation phases, propose action plans made necessary by discrepancies found in their implementation and to generally help ensure the reliability of the entire process and of the financial data collected. Each month, actual performance is compared to the budgeted performance and that of the previous year. A summary of the performance of the Company is presented to the Company's Executive Board. The Supervisory Board is provided with a summary of trends in sales and of performance indicators on a monthly basis.

- The accounting function is centralised with the main accounting and financial reporting office located in Moscow and St. Petersburg and an accounting data processing centre located in Nizhny Novgorod.

- X5 uses legacy accounting software from a local provider which has been significantly improved to enable the Company to utilise a standard chart of accounts for all the entities that are consolidated into X5 Retail Group, as well as mapping and partial automation of the process of transforming statutory accounting records into a format consistent with International Financial Reporting Standards (IFRS). In addition to this, X5 is currently working on the implementation of SAP financial applications where simultaneously with statutory accounting the Company will maintain, on a daily basis, financial and managerial accounting records according to IFRS principles. The utilisation of SAP for finance and accounting purposes will also improve the internal controls over the financial reporting process and will allow X5 to adhere with best practices in this area.

- In addition, the Company utilises a reporting process that uses identical sources of accounting data for consolidated financial and managerial accounts, so periodic reconciliation of consolidated financial reporting to managerial accounting data helps to guarantee the reliability of external financial reporting.

## SECTION 2: SYSTEM OF INTERNAL CONTROL PROCEDURES AND RISK MANAGEMENT

The Management Board of X5 is responsible for designing, implementing and operating an adequately functioning Internal Control and Risk Management Framework in the Company. Internal controls are designed and implemented by executive management and Company personnel under the control of the Management Board intended to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations;
- Reliability of financial reporting;
- Compliance with applicable laws and regulations.

One of the goals of internal control procedures is to highlight, manage and monitor the risks resulting from the Company's activity and the risks of misstatements or fraud, especially in the accounting and financial fields. However, like any system of control, it cannot provide an absolute guarantee that these risks will be totally eliminated.

The Company has adopted criteria set forth by the Committee of Sponsoring Organisations (COSO) in its *Internal Control – Integrated Framework* and implemented it across the organisation. In addition, the Corporate Audit Department (the Company's internal audit function) has been actively using COSO requirements for its audit engagements by assigning its findings to COSO categories. Finally, the COSO criteria for evaluating the effectiveness of control systems are required to be used by business process owners during the implementation of new and the improvement of existing control procedures.

**The Internal Control Environment**

In order to develop a shared culture, X5 has enforced a Code of Business Conduct that outlines corporate values and rules, as well as guiding principles of ethical behaviour. Our key corporate values are: respect for people, customer orientation and commitment to excellence.

X5's Guiding Principles of Business Conduct are the following:

(1) Comply with the applicable laws of countries to which X5 is subject. Strictly adhere to corporate policies and procedures.

(2) Act in the best interest of X5 while performing your job for the Company.

(3) Ensure the accuracy of all Company business and financial records.

(4) Protect the Company's assets, and use those assets in the manner intended.

(5) Safeguard the Company's non-public information.

(6) Always deal fairly with customers and suppliers, treating them honestly and with respect. Do not engage in unfair, deceptive or misleading practices.

(7) Do not give or accept any gift where the value of the gift could cause, or give the appearance of causing, X5 to grant or receive any favor as a result.

Awareness and compliance with these corporate values and Guiding Principles of Business Conduct are enhanced first by training, but also by becoming part of the organisation and management of the Company. The values and corporate rules outlined in the Code of Business Conduct have been integrated into the system of evaluating top management performance.

**Risk Assessment**

The Company introduced the formal risk assessment & analysis process. It consists of a periodic identification, measurement and prioritisation of business risks with the help of risk maps. It is intended to identify potential internal and external risks, to measure their relative importance and the probability of their occurrence, as well as the significance of their impact. In performing risk assessment X5 utilises the standard "risk universe" for the retail business, which covers about 100 risks under strategic, operational, financial and compliance categories.

In 2009 the Company set up a central risk management office to ensure that the Management Board is continuously and promptly informed of important developments in risk management by a risk management officer. The establishment of a central risk management function will also facilitate the Company-wide exchange of information on risk relevant issues and develop risk management activities in all the corporate functions, as well as recording and systematic assessment of all essential risks according to uniform standards.

The most recent assessment of risks was performed at the end of 2009 by central risk management office with an active involvement of line managers and financial controllers who filled in questionnaires to assess respectively inherent risks and control activities that mitigate them. Residual risks were then assessed and risks maps produced. The evaluation of the residual risks has made it possible to develop remediation plans and to focus specifically on managing and mitigating the most critical risks that the Company needs to address.

**Control Activities**

Under the authority delegated by the Management Board, the management teams at all levels of the organisation are responsible for monitoring the risks and for designing internal control systems appropriate to their respective business processes. The finance function assists management at all levels in developing internal control procedures that are risk-oriented and built into the business processes. In addition, financial controllers are an integral part of the Company's Internal Control and Risk Management System and perform ongoing monitoring of its effectiveness.

**Communication of Risks and Controls**

In an effort to focus all X5 personnel on their internal control responsibilities, approximately 360 line managers and financial controllers in the Company's corporate center have been formally trained in the COSO internal control framework since 2007.

The Director of the Corporate Audit Department, who functionally reports to the Audit Committee, acts as the Compliance Officer for the Company's Whistleblower Policy, and supervises the operation of the ethics hotline which was implemented in 2009. All the cases reported through the ethics hotline are thoroughly reviewed and investigations are performed by a professional forensic team when needed.

In addition, the quality of the Company's systems of business controls and the findings of internal and external auditors are regularly reported to the Management Board and discussed on the Audit Committee of the Supervisory Board as well as on the Supervisory Board, as necessary.

**Monitoring of Internal Controls by Corporate Audit Department**

The main task of X5's Corporate Audit Department (CAD) is to provide independent and objective assurance and value-adding advisory activity that assists the Company in achieving business objectives and improve operations.

The CAD conducts systematic and disciplined evaluations of operational, financial and information systems regarding risk management, internal control and governance processes aimed to improve the effectiveness of these processes. Additionally, during 2009 CAD's responsibilities were expanded to formally include forensic audit work which focuses on cases of fraud, misuse of company assets, abuse of authority, unlawful acts and other matters which are not consistent with the Company's policies.

The CAD's organisational independence is guaranteed by its reporting lines: CAD reports functionally to the Audit Committee of the Supervisory Board and, from an administrative standpoint, to the Management Board.

Following a risk based audit approach the CAD reviews the design of internal controls, and performs tests of controls on business processes that are critical for the Company's operations and provides recommendations on improvement of the respective internal controls. Implementation of such recommendations is carefully monitored and controlled by CAD, the Management Board and the Audit Committee of the Supervisory Board.

X5's CAD was the first internal audit department in Russia to successfully complete the external quality assessment procedures and has been certified by Ernst & Young on conformity with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing.

**Management Summary**

The Management Board has reviewed and analysed the strategic, operational, compliance, financial and financial reporting risks to which the Company is exposed, as well as the design and operating effectiveness of the Company's internal risk management and control systems over 2009. The outcome of this review and analysis has been shared with the Audit Committee of the Supervisory Board and the Supervisory Board and has been discussed with X5's external auditors.

The Management Board believes that the risk management and control systems regarding the financial reporting risks have worked properly during 2009, and provide reasonable assurance that the financial statements 2009 do not contain any errors of material importance.

In view of the above, the Management Board believes that it is in compliance with the requirements of II.1.4 and II.1.5 of the Dutch Corporate Governance Code.

In addition, in accordance with section 5.25c of the Dutch Financial Supervision Act the Management Board confirms that to the best of its knowledge:

- The annual financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and its consolidated companies; and

- The annual report gives a true and fair overview of the situation as per the balance sheet date, the state of affairs during the financial year of the Company and its group companies included in the annual financial statements, together with a description of principal risks it faces.

**Lev Khasis, CEO**
**Evgeny Kornilov, CFO**

**8 April 2010**

# Report of the Supervisory Board

The Supervisory Board is charged with supervising the policies of the Management Board and the general course of affairs of the Company and the business connected with it, as well as assisting the Management Board by providing advice.

In performing its duties the Supervisory Board is charged with acting in accordance with the interests of the Company and its affiliated businesses. It shall take into account the relevant interest of the Company's stakeholders and, to that end, consider all appropriate interests associated with the Company.

While retaining overall responsibility, the Supervisory Board assigns certain tasks to its four permanent committees: The Audit Committee, the Nomination and Remuneration Committee, the Related Party Committee and the Strategy Committee.

## COMPOSITION OF THE SUPERVISORY BOARD

X5's General Meeting of Shareholders determines the number of members of the Supervisory Board. Currently X5's Supervisory Board consists of seven members, with one vacancy to be filled.

The Supervisory Board reviews, on an annual basis, the profile of its size and composition taking into account the evolving nature of X5's business and activities and the desired expertise and background of the members of the Supervisory Board. The Supervisory Board profile is published on X5's corporate website.

The composition of the Supervisory Board changed in 2009, due to the resignation of Mr. Savin on 17 September 2009. Furthermore, as announced on 15 December 2009, Mr. Criado-Pérez Trefault resigned as per 1 January 2010. The Supervisory Board expresses its gratitude for the contributions that Mr. Savin and Mr. Criado-Pérez Trefault have made to the Company.

In November 2009 the Supervisory Board nominated Mr. Christian Couvreux as an additional board member. He was appointed by the Extraordinary General Meeting of Shareholders held on 15 January 2010. Mr. Couvreux is an independent Supervisory Board member with a considerable track record in the global retail industry.
An overview of the current composition of the Supervisory Board is presented in the Corporate Governance Report.

Mr. Fridman and Mr. Savin were re-appointed by the Annual General Meeting of Shareholders on 12 June 2009 for an additional four-year term. In accordance with the retirement and re-appointment schedule of the Supervisory Board, the terms of both Mr. Defforey and Mr. Gould will expire in 2010. Both Mr. Defforey and Mr. Gould are eligible for re-appointment.

## COMPOSITION OF THE COMMITTEES

Given the highly related nature of the respective duties and responsibilities of the Remuneration Committee and the Selection and Appointment Committee the Supervisory Board resolved to merge both committees in 2009 into the new "Nomination and Remuneration Committee".

Following the resignation of Mr. Criado-Pérez Trefault as per 1 January 2010, the Nomination and Remuneration Committee will be composed of four members. Mr. Criado-Pérez Trefault's position as chairman of the Related Party Committee was taken over by Mr. Tynkovan, while Mr. DuCharme replaced Mr. Defforey as member of the Related Party Committee. Furthermore, when Mr. Couvreux was appointed to the Supervisory Board in January 2010, he took over Mr. Ashurkov's position as chairman of the Strategy Committee, with Mr. Ashurkov remaining a member of this committee.

There were no further changes in the composition of the committees in 2009 and until the date of publication of this report. An overview of the current composition of the committees is presented in the Corporate Governance Report.

## INDUCTION

Following his appointment Mr. Couvreux went through the strategic, financial, legal and reporting affairs of X5 Retail Group with senior directors of the Company. In addition, prior to his appointment in January 2010, Mr. Couvreux attended the meetings of the Supervisory Board in November and December 2009.

## MEETINGS OF THE SUPERVISORY BOARD

The Supervisory Board meets at least four times per year. In 2009 the Supervisory Board held seven meetings, including two meetings by teleconference. On each of five occasions in 2009 the meeting of the Supervisory Board was preceded by meetings of the Audit Committee and the Nomination and Remuneration Committee. Furthermore, the Supervisory Board meetings in September and November were preceded by a meeting of the Strategy Committee.

All meetings were attended by the full Supervisory Board apart from the teleconference meetings on 16 November and 13 December 2009 which were not attended by Mr. Criado-Pérez Trefault. The members of the Management Board attended the meetings, and other members of senior management were regularly invited to present to the Supervisory Board. On two occasions the Supervisory Board meetings included private sessions, with no members of the Management Board present, to independently discuss matters related to the performance, functioning and development of the Management Board and members of senior management. The external auditor attended the meeting in April at which the 2008 Annual Report and financial statements were endorsed. In March 2009 the Supervisory Board discussed its own functioning, its profile, competence and composition, based on an elaborate self-assessment. The self-assessment was based on a questionnaire, completed by all Supervisory Board members and regular meeting attendees, as well as a series of interviews conducted by the Chairman of the Nomination and Remuneration Committee. The members of the Supervisory Board had frequent (telephone) meetings with members of the Management Board and other Company management in between the Supervisory Board meetings.

On an ongoing basis the Supervisory Board reviewed various matters related to the Company's activities, its operational results, strategies and management, including:

- The financial reporting process and, in particular, the approval of the 2008 Annual Report and review of the 2009 half-yearly and quarterly financial statements and management accounts;

- The regular assessment of the members of the Management Board of the Company, including the Company's talent management and succession planning;

- The nomination of the CEO for re-appointment in 2010;

- The remuneration of the Management Board, in accordance with the remuneration policy;
- The Employee Stock Option Programme, in particular the granting of options under the fourth tranche and adjustments to the plan (see: Remuneration Report);
- The next generation Long Term Incentive Plan, to be implemented in 2010;
- The appointment and remuneration of senior managers of the Company;
- The composition of the Committees of the Supervisory Board;
- The nomination of Mr. Fridman and Mr. Savin for re-appointment to the Supervisory Board, and the nomination of Mr. Christian Couvreux as new Supervisory Director;
- The Guiding Principles on Business Conduct and the Company's statute on fraud investigation and reporting protocol (Fraud Protocol);
- A review of the Company's Five Year Strategy Plan at the annual strategy meeting in November;
- The assessment of the Company's organisation structure in line with the evolution of the business;
- The Company's financing strategy, in particular the refinancing of the syndicated loan facility with maturity December 2010;
- The draft federal law on Retail Trade in Russia, and its impact on the retail industry and X5 in particular;
- The amendment of X5's Articles of Association, with respect to the threshold of transactions subject to approval of the Supervisory Board, and the merger of the Selection and Appointment Committee and the Remuneration Committee;
- The progress of post-merger integration efforts and synergy effects throughout the various operational and staff divisions of the group;
- The Company's M&A Strategy, in particular the acquisition of the retail chain "Paterson" during the fourth quarter;
- The review of the Enterprise Risk Management (ERM) and control systems of the group;
- The budget and key performance indicators for 2010.

## MEETINGS OF THE COMMITTEES

**Audit Committee**
The role of the Audit Committee is described in its charter, which is available on the Company's website. On 31 December 2008 the Audit Committee consisted of Mr. Gould (Chairman), Mr. Defforey and Mr. Ashurkov.

In 2009 the Audit Committee held five meetings. All meetings were attended by the CFO, the external auditor and the Head of the Corporate Audit Department (CAD). Other members of senior management where invited when necessary or appropriate.

The Audit Committee discussed and approved the full year 2008 and quarterly 2009 consolidated financial statements of the Company audited / reviewed by PricewaterhouseCoopers, the Company's external auditor. It also reviewed press releases (financial results and trading updates) and analyst reports related thereto. The Audit Committee reviewed the external auditors' report with respect to accounting and audit issues in respect of their audit of the 2008 consolidated financial statements. In April 2009, the Audit Committee met with the auditors without the presence of management. Audit and review fees and permitted non-audit / review fees for 2009 and 2010 were approved in July and November, respectively.

During the fourth quarter the Audit Committee, together with management, conducted its periodic assessment of the functioning of the external auditor, and compliance with the Company's policy on external auditor independence, audit scope and approach within the various group entities and in the different capacities in which the external auditor acts. The main conclusions of this assessment shall be communicated to the 2010 Annual General Meeting of Shareholders for the purpose of assessing the nomination for the re-appointment of the external auditor.

Throughout the year the Audit Committee reviewed the financing strategy 2009/2010, including hedging strategies, with particular emphasis on the challenges in refinancing X5's syndicated loan facility maturing in 2010, given the pressure on the global financial debt markets as a result of the financial crisis. In April the Audit Committee reviewed the Company's estimated range of contingent tax liabilities and tax planning issues in general, including a tax risk assessment performed by the Company.

In March the Audit Committee reviewed and discussed the proposed USD 2.2 billion goodwill impairment charge in the fourth quarter of 2008, related to goodwill created as a result of the merger between Perekrestok and Pyaterochka in 2006.

An update of IT matters, in particular the implementation of SAP for Retail and SAP for Finance, was presented and discussed in July in the presence of X5's CIO and CFO. Additionally, outside of the Audit Committee, the Chairman of the Supervisory Board conducted a number of meetings during 2009 with key IT staff including X5's CIO to discuss strategic and other IT issues of importance.

In 2009 the Audit Committee reviewed the Company's internal risk management and control systems, and the proper functioning of operational and business processes mainly through the work of the CAD. The CAD assisted various departments to perform control self assessment testing and conducted their own diagnostic reviews, developed risk maps and built such findings into its annual audit plan. Additionally, management presented to the Audit Committee its plans with respect to ERM development, updated risk mapping with assignment to specific personnel, and general evolution of the risk management function in the ensuing years. Significant audit and forensic investigation findings of the CAD were reported to the Audit Committee on a regular basis. Status of follow-up actions by management in addressing CAD findings were regularly reviewed by the Audit Committee. The CAD's internal audit plan 2010 was discussed with the external auditor, and approved by the Audit Committee.

In 2009 the Audit Committee continued to assess the financial and management reporting function of the Company and paid particular attention during the year to impairment issues, including store-level impairment, ageing inventory (mark-down policy) and impairment of intangible assets (e.g. goodwill). In July the Audit Committee approved the Coordination Plan between CAD and the external auditor with respect to review of internal controls over financial accounting and reporting.

The Audit Committee reviewed regular updates on integrity matters. A new statute on fraud investigation and reporting (Fraud Protocol) was discussed and approved in July, complementing the Company's Whistleblower Policy that was revised and approved during the previous year. In November the Audit Committee approved the Company's financial reporting calendar and the black-out trading calendar for the year 2010.

**Nomination and Remuneration Committee**
The Nomination and Remuneration Committee combines the Selection and Appointment Committee and the Remuneration Committee, which committees were merged by the Supervisory Board in 2009, in light of the highly related nature of their respective duties and responsibilities.

The role of the Nomination and Remuneration Committee is described in its charter which is available on the Company's website. On 31 December 2009 the Nomination and Remuneration Committee consisted of Mr. DuCharme (Chairman), Mr. Defforey, Mr. Ashurkov, Mr. Criado-Pérez Trefault and Mr. Tynkovan.

The Nomination and Remuneration Committee held six meetings in 2009. During the first half of 2009 the Nomination and Remuneration Committee evaluated the performance of the members of the Management Board based on the achievement of corporate and personal objectives for 2008. In this context, and based on the Company's 2009 overall objectives and its budget, the Committee also discussed and proposed to the Supervisory Board the targets and remuneration levels for the members of the Management Board in 2009.

In the second half of the year, the components of the remuneration of the Company's Management Board and senior management were checked against market practice and trends.

The composition and succession planning of the Management Board was reviewed during the second half of the year, within the context of a broader review of the organisation structure, including talent management and succession planning at top executive level.

In April the Nomination and Remuneration Committee discussed and proposed the re-appointment of the Supervisory Directors Mr. Fridman and Mr. Savin for a new term until 2013, in accordance with the retirement and re-appointment schedule of the Supervisory Board. In November the Committee proposed the appointment of Mr. Couvreux as additional independent member of the Supervisory Board.

In April the Nomination and Remuneration Committee reviewed the allocation principles of options under the Employee Stock Option Programme (ESOP). Simultaneously, following the ESOP restructuring proposals in the previous year, the Committee proposed an extension of the exercise period of options granted under tranches 2, 3 and 4. These adjustments, aimed at preserving and optimising the long term incentive character of the ESOP, were approved by the Annual General Meeting of Shareholders in June 2009.

Revised remuneration principles for the Supervisory Board were proposed in July and approved by the General Meeting of Shareholders in January 2010.

In October the Nomination and Remuneration Committee conducted a separate meeting, partially in the presence of the Management Board and senior managers, to the Company's next generation Long Term Incentive Plan.

The Remuneration Policy for the Management Board was subject to further review during 2009, also against the background of further alignments with the Dutch Corporate Governance Code. The amended Remuneration Policy will be submitted to the General Meeting of Shareholders in 2010.

The Remuneration Report on page 72 provides further details on remuneration for the Management Board and the Supervisory Board, and includes current Remuneration Policy for the Management Board, as well as the outlook for 2010 and beyond. The Remuneration Policy is also available on the website of the Company.

**Related Party Committee**
The role of the Related Party Committee is described in its charter which is available on the Company's website.  On 31 December 2009 the Related Party Committee consisted of Mr. Criado-Pérez Trefault (Chairman), Mr. Defforey and Mr. Tynkovan.

The Related Party Committee had three meetings in 2009, including one meeting held by teleconference.  Further resolutions in writing were taken when necessary during the year.  The Related Party Committee considered a number of transactions which gave rise to the appearance of a conflict of interest with the Company.
The following transactions were discussed and/or approved by the Related Party Committee and the Supervisory Board during 2009, with due observance of best practice provisions II.3.2 to II.3.4 and III.6.1 to III.6.4 of the Dutch Corporate Governance Code, and the rules set forth in Chapter VI (Conflict of Interests) of the Rules Governing the Principles and Practices of the Supervisory Board, which Rules are available on the Company's website:

- The approval of the budget 2009-2010 for advisory and administrative services rendered by CTF Holdings Ltd.;
- A Ruble Bond issue with Alfabank as Mandated Lead Arranger;
- Supplementary services agreements with Alfabank, in connection with factoring arrangements between Alfabank and X5 suppliers;
- Revolving credit facilities, and other credit products within approved credit limits, with Alfabank;
- Acquisition of store equipment from "Stolichnaya Torgovaya Compania", belonging to the retail chain Venetsiya operating under the tradename "Globus Gurmet";
- Mr. DuCharme's position as Supervisory Board member of OJSC Galnaftogaz in Ukraine.

**Strategy Committee**
The role of the Strategy Committee is described in its charter, which is available on the Company's website.  On 31 December 2009 the Strategy Committee consisted of Mr. Ashurkov (Chairman), Mr. Defforey, Mr. Carlos Criado-Pérez Trefault and Mr. Tynkovan.

The responsibilities of the Strategy Committee include the review of the general strategy of the Company, including but not limited to the following main areas: overall growth and development strategy, financing strategy, budget and key performance indicators, mergers and acquisitions.

The Strategy Committee had a first meeting in September, and its annual conference in November.  The meeting in November was attended by the CEO and CFO, as well as the chairmen of the Audit Committee and the Nomination and Remuneration Committee. The Committee addressed, in particular, the Company's Five Year Strategy Plan, including detailed reports and discussions on X5's retail format strategies, supply chain and logistics, HR strategy, IT strategy and investment strategy.  The Committee also addressed the impact of the draft federal law on Retail Trade on the Russian retail industry and X5 in particular.

Furthermore, the Committee discussed the Company's key performance indicators and budget for 2010, as well as the organisational structure and performance indicators for the Company in the years to come.

## CORPORATE GOVERNANCE

Both the Supervisory Board and the Management Board continued their efforts to ensure that the Company's practices and procedures comply with the Dutch Corporate Governance Code. In accordance with the Dutch Corporate Governance Code, a broad outline of the corporate governance structure of the Company is presented in the Corporate Governance Report.

## FINANCIAL STATEMENTS

This annual report and the 2009 consolidated financial statements, audited by PricewaterhouseCoopers Accountants N.V., were presented to the Supervisory Board in the presence of the Management Board and the external auditor. PricewaterhouseCoopers' report can be found on page 145.

The Supervisory Board recommends that the Annual General Meeting of Shareholders adopts the 2009 consolidated financial statements of X5 Retail Group N.V. The Annual General Meeting of Shareholders will be asked to release the members of the Management Board from liability for the exercise of the management of the Company's affairs and management. The appropriation of results approved by the Supervisory Board can be found on page 144.

The Supervisory Board wishes to thank the Management Board and all employees of X5 for their outstanding contributions in 2009.

**The Supervisory Board**

**8 April 2010**

# Remuneration Report

This report has been prepared by the Supervisory Board of X5 Retail Group N.V. (the "Company") in accordance with the Dutch Corporate Governance Code. It contains the remuneration policy of the Management Board of the Company (the "Remuneration Policy") as well as the remuneration specifics of both the Management Board and the Supervisory Board for the financial year 2009. This report also addresses the way in which the Remuneration Policy will be pursued for the financial year 2010 and beyond.

## NOMINATION AND REMUNERATION COMMITTEE

Apart from its responsibilities in the area of selection, appointment and assessment of the Management Board and Supervisory Board members, the Nomination and Remuneration Committee (the "Committee") is responsible for:

- Preparing proposals for the Supervisory Board concerning the remuneration policy for the Management Board to be adopted by the General Meeting of Shareholders;
- Preparing proposals concerning the remuneration of individual members of the Management Board.

In carrying out its work in the area of remuneration, the Committee also takes into account the assessment and remuneration of the senior management reporting to the Management Board (the "Executive Board") and the remuneration climate in general within the Company.

In 2009 the Committee engaged in a thorough review of remuneration, as follows:

- An independent salary survey of senior management of companies comparable with X5, based on distinct principles, in order to benchmark short and long term remuneration components, respectively, against the market;
- A defined set of allocation principles with respect to options granted under tranche 4 of the ESOP based on, inter alia, a newly introduced "Hay" function grading structure;
- A review, in the context of the annual performance targets, of how such targets contribute to the achievement of the short-term and long-term objectives of the Company;
- A definition of the principles and framework of the Company's next generation long-term incentive plan, given that the final tranche of options under the current Employee Stock Option Programme was granted in 2009. The decision-making process for the next generation long term incentive plan included a comparative scenario analysis of different LTI arrangements currently in the market, their impact on the remuneration, motivation and retention of the individual members of the Management Board and senior management as well as the impact on the achievement of the Company's long-term objectives.

This review, including further alignments with the Dutch Corporate Governance Code, will result in an amended policy that shall be submitted to the 2010 Annual General Meeting of Shareholders.

The Committee prepares its proposals independently after careful consideration, including taking into account the advice of independent advisors. In 2009, external advisors were engaged to provide advice regarding current market practices and developments relating to remuneration, and the next generation long term incentive plan in particular. These advisors do not advise the members of the Management Board personally on their remuneration.

The current members of the Nomination and Remuneration Committee are Stephan DuCharme (chairman), Hervé Defforey, Vladimir Ashurkov and Alexander Tynkovan.

## CURRENT REMUNERATION POLICY

The 2007 Annual General Meeting of Shareholders adopted the Remuneration Policy 2007, which was amended and adopted in 2008 to reflect the further developments and insights gained in this area.

The objective of the Remuneration Policy is twofold:

- to create a remuneration structure that will allow the Company to attract, reward and retain qualified executives who will lead the Company in achieving its strategic objectives; and
- to provide and motivate these executives with a balanced and competitive remuneration.

The remuneration structure of the members of the Management Board may include four elements: base salary, annual incentive (cash bonus), long-term incentive (stock options and/or equity linked instruments), and other arrangements. The remuneration structure mirrors short-term and long-term elements of the responsibilities of members of the Management Board.

Upon proposal of the Remuneration Committee, and if in the interest of the Company, the Supervisory Board may at its own discretion deviate from the Remuneration Policy when offering a remuneration package to a newly appointed member of the Management Board or when amending the remuneration package of a current member of the Management Board, in the event of exceptional circumstances or if deemed appropriate.

**Base Salary**

Base salaries are specified in the individual contracts with members of the Management Board and reflect competence and responsibilities of a member of the Management Board, the relevant experience of a member of the Management Board, and other factors. The levels of base salaries are determined by (i) benchmarking with industry peers of comparable size and complexity, operating in comparable geographical areas; and (ii) the specific responsibilities and achievements of the individual member of the Management Board. The annual review date for the base salary is December 31.

**Annual Incentive (Cash Bonus)**

As a general rule, in accordance with the Remuneration Policy adopted in 2007, and amended and adopted in 2008, the annual performance bonus has an on-target level of 100% of the base salary, to be increased, upon proposal of the Committee and approval of the Supervisory Board, by a maximum of 50% of the base salary subject to extraordinary performance. Upon proposal of the Nomination and Remuneration Committee, and if in the interest of the Company, the Supervisory Board may deviate from the Remuneration Policy and further increase the annual performance bonus in the event of exceptional circumstances or if deemed appropriate.

The bonus scheme for the members of the Management Board rewards both financial performance (quantitative corporate indicators) and mission-related performance, including personal key objectives. Performance criteria are specified in advance for each Management Board member. Financial performance targets are determined from time to time by the Supervisory Board and include net sales and EBITDA. The mission-related performance targets, financial and non-financial, for each member of the Management Board consist of a limited number of personal objectives that may include targets related to divisional performance, mission-related or key project-related targets, as well as qualitative behavioral targets. Both the corporate and personal performance measures are considered success factors for the Company in the short term, while also contributing to the achievement of the long-term objectives of the Company, including in particular building out and strengthening the Company's leading position in the Russian retail sector. X5 does not disclose the actual targets set, as this qualifies as commercially sensitive information.

**Long Term Incentive: Employee Stock Option Programme**
In order to align the objectives of the Management Board and other key employees with the longer term value-creation objectives of shareholders, members of the Management Board and other key employees are granted options under the Company's Employee Stock Option Programme (the "ESOP"). The ESOP was approved by the General Meeting of Shareholders on 15 June 2007. The options granted under the ESOP each confer the right to a number of Global Depositary Receipts ("GDRs"), each GDR representing one fourth of an ordinary share of Euro 1 par value in the capital of the Company. The aggregate number of GDRs, for which options may be granted under the ESOP, amounts to 11.261.264 GDRs, which number is within the limit approved by the General Meeting of Shareholders on 15 June 2007 (i.e. 5% of the issued share capital of the Company). The options are granted in four tranches issued over a period of three years (2007 through 2009). The options outstanding are conditional upon employment with the Group. The number of options that are granted to Management Board members and key employees are linked to pre-determined criteria of participation in the program, based on the level of responsibility within the Company.

**Other Remuneration Components**
A number of other arrangements may be offered to members of the Management Board, such as expense and relocation allowance, medical insurance and accident insurance. The Company's policy does not allow personal loans and guarantees to members of the Management Board. The Company does not provide for pension arrangements in favor of members of the Management Board.

**Severance Payment**
The severance payment is in principle limited to a maximum of one year's base salary (the "fixed" remuneration component) of the relevant member of the Management Board. The Supervisory Board reserves the right to agree to a different amount should individual circumstances require this.

**Contracts of Employment**
The members of the Management Board have a written contract of employment with X5 Retail Group N.V. in The Netherlands and/or its operational Russian subsidiaries. The fixed and variable salary components stipulated in each employment contract reflect the relevant responsibilities of each member of the Management Board in The Netherlands and Russia.

The current members of the Management Board are employed and appointed for a four-year period, in accordance with the Dutch Corporate Governance Code. For future new appointments to the Management Board, the term of the contract is also set at four years.

## REMUNERATION 2009

**Management Board Remuneration**
As announced in the Remuneration Report for the financial year 2008, starting in 2009 the short term compensation payable to the members of the Management Board by the operational Russian subsidiaries is denominated in Russian Rubles. The conversion was made by applying the USD/RUR exchange rate of 1 January 2009 (USD 1 = RUR 33) to the 2008 salaries of the CEO and the CFO.

In the context of the global financial and economic crisis, 2008 base salaries (in Russian Rubles) were maintained in 2009 throughout all levels of the Company, including the Management Board. In addition, no salary indexation was applied.

In 2009 the Supervisory Board reviewed the annual cash incentive policy for members of the Management Board and senior management. It was resolved that in 2009, 60% of the bonus opportunity at target level related to quantitative corporate targets and 40% to mission-related performance, including personal key objectives. For the year ended 31 December 2009 the Management Board was entitled to a total short term compensation of USD 5,326,668 (2008: USD 5,932,441).

In 2009, the members of the Management Board were granted 1,100,625 options under the ESOP.

On 30 November 2009 the CEO exercised 810,000 options granted under tranche 1 of the ESOP. At 31 December 2009 the total outstanding number of options amounted to 3,021,250 options (31 December 2008: 2,730,625 options). The intrinsic value[1] of the outstanding options at 31 December 2009 was USD 22,589,044 (31 December 2008: nil).

Specification of the fixed and variable cash remuneration of the Management Board for the financial year 2009:

| Amounts in USD | Base Salary 2009 | Cash bonus 2009[2] |
|---|---|---|
| L. Khasis | 2,122,301 | 1,456,352 |
| E. Kornilov | 865,640 | 520,126 |
| F. Lhoëst | 278,653 | 83,596 |

All amounts are paid in either Russian Rubles or Euro and converted to USD for reporting purposes, using the average USD rate for 2009 to convert RUR amounts into USD, and average cross-rate EUR/USD for amounts paid in Euro. The rates are available in Note 2 to the consolidated financial statements included in this Annual Report.

**Supervisory Board Remuneration**
In the reporting year, the total remuneration of the Supervisory Board amounts to EUR 855,209 or USD 1,197,294 (2008: USD 860,993).

In 2009 the members of the Supervisory Board were granted 123,750 options under the ESOP.

[1] Intrinsic value is calculated as a difference between the exercise price of the option and the market quote of the underlying GDR as at the end of respective reporting period multiplied by number of options.
[2] Bonus for the performance of the year reported and paid in cash in 2010.

On 11 December 2009, Mr. Criado-Pérez Trefault exercised 20,000 options granted under tranche 2 of the ESOP. Furthermore, in connection with his resignation as per 1 January 2010, Mr. Criado-Pérez Trefault waived his entitlement to options granted under the fourth tranche of the ESOP in exchange for a cash settlement in the gross amount of USD 200,000.

The total outstanding number of options amounted to 166,250 options (31 December 2008: 83,750 options). The intrinsic value of the options at 31 December 2009 was USD 1,843,975 (31 December 2008: nil).

Specification of the cash remuneration of the Supervisory Board for the financial year 2009:

| Amounts in USD | Remuneration 2009 | |
|---|---|---|
| Hervé Defforey (Chairman) | 167,192 | |
| Mikhail Fridman | 69,663 | |
| Alexander Savin | 49,873 | Resigned as per 17 September 2009 |
| Vladimir Ashurkov | 104,495 | |
| David Gould | 104,495 | |
| Carlos Criado-Pérez Trefault | 367,192 | Includes remuneration (167,192) and cash settlement (200,000) in connection with resignation as per 1 January 2010 |
| Alexander Tynkovan | 167,192 | |
| Stephan DuCharme | 167,192 | |
| **Total** | **1,197,294** | |

All remuneration amounts are paid in Euro and converted to USD for reporting purposes, using the average cross-rate EUR/USD. The rate is available in Note 2 to the consolidated financial statements included in this Annual Report.

**Stock Options**

In 2009 the Committee proposed an extension of the exercise period of options granted under tranches 2, 3 and 4 up to four and a half years from the grant date of each respective tranche. These adjustments, aimed at preserving and optimizing the long-term incentive character of the ESOP, were approved at the Annual General Meeting of Shareholders in June 2009.

As a result, participants of the ESOP can exercise their options granted under the first, second, third and fourth tranches over the period from vesting until 19 November 2010, 16 December 2011, 20 November 2012 and 20 November 2013, respectively, at any time except during black-out periods defined by the Company's Code of Conduct with regard to Insider Trading.

In 2009 the fourth tranche of options under the ESOP was granted in accordance with the approved ESOP allocation principles. The vesting date for these options is 19 May 2010. Details of options held by members of the Management Board and Supervisory Board are set forth below.

| | Granted in 2007 | Granted in 2008 | Granted in 2009 | Tranche | Vesting date | Value per vesting date[1] | Exercised in 2009 | Position 31 December | Exercise price[2] | GDR price on exercise date | Expiration date |
|---|---|---|---|---|---|---|---|---|---|---|---|
| L. Khasis | 810,000 | | | 1 | 15/06/2007 | $9,720,000 | 810,000 | | $15.96 | $29.00 | 19/11/2010 |
| | 810,000 | | | 2 | 18/05/2008 | $8,237,700 | | 810,000 | $28.58 | | 16/12/2011 |
| | | 860,625 | | 3 | 19/05/2009 | nil | | 860,625 | $33.43 | | 20/11/2012 |
| | | | 860,625 | 4 | 19/05/2010 | | | 860,625 | $13.91 | | 20/11/2013 |
| E. Kornilov | 30,000 | | | 2 | 18/05/2008 | $305,100 | | 30,000 | $28.58 | | 16/12/2011 |
| | | 220,000 | | 3 | 19/05/2009 | nil | | 220,000 | $33.43 | | 20/11/2012 |
| | | | 220,000 | 4 | 19/05/2010 | | | 220,000 | $13.91 | | 20/11/2013 |
| F. Lhoëst | | | 20,000 | 4 | 19/05/2010 | | | 20,000 | $13.91 | | 20/11/2013 |
| **Total Management Board** | | | **1,100,625** | | | | | **3,021,250** | | | |
| H. Defforey | 10,000 | | | 1 | 15/06/2007 | $120,000 | | | $15.96 | | 19/11/2010 |
| | 20,000 | | | 2 | 18/05/2008 | $203,400 | | | $28.58 | | 16/12/2011 |
| | | 42,500 | | 3 | 19/05/2009 | nil | | 42,500 | $33.43 | | 20/11/2012 |
| | | | 70,000 | 4 | 19/05/2010 | | | 70,000 | $13.91 | | 20/11/2013 |
| C. Criado-Pérez Trefault | 20,000 | | | 2 | 18/05/2008 | $203,400 | 20,000 | | $28.58 | $33.20 | 16/12/2011 |
| | | 21,250 | | 3 | 19/05/2009 | nil | | 21,250 | $33.43 | | 20/11/2012 |
| | | | 21,250 | 4 | 19/05/2010 | | | Cash settlement | $13.91 | | 20/11/2013 |
| S. DuCharme | | | 32,500 | 4 | 19/05/2010 | | | 32,500 | $13.91 | | 20/11/2013 |
| **Total Supervisory Board** | | | **123,750** | | | | | **166,250** | | | |

(1) Intrinsic value (GDR closing price per 15 June 2007: USD 30.00; 19 May 2008: USD 38.75; 19 May 2009: USD 15.18; exercise price tranche 1 on 15 June 2007, i.e. before adjustment in 2008: USD 18.00).

(2) The exercise price, before adjustment, of the options under the first tranche is defined as the share price at the date of the merger between Pyaterochka Holding N.V. and Perekrestok Holdings Limited on 16 May 2006.

The exercise price, before adjustment, of the options under the second tranche is defined as the price equal to the Average Market Value (as defined below) per Depositary receipt as of 18 May 2007.

The exercise price of the options under the third and fourth tranche is defined as the price equal to the Average Market Value (as defined below) per Depositary Receipt as of the grant dates 19 May 2008 and 19 May 2009 respectively.

The Average Market Value is defined as 'on any particular day the volume weighted average price of a Depositary Receipt over the 30 immediately preceding calendar days. The volume weighted average price is calculated using the closing price of a Depositary Receipt taken from the Official List of the LSE'.

## REMUNERATION POLICY IN 2010 AND BEYOND

In 2009 the Remuneration Policy as described in this report was applied, including taking into account the new ratio between qualitative and quantitative performance criteria for determining the annual cash incentive (as described in the previous section of this Report).

In 2010 the Company will finalize the development of its next generation long term incentive plan which, together with any further material changes to the Remuneration Policy in alignment with the Dutch Corporate Governance Code, will be submitted for approval to the 2010 Annual General Meeting of Shareholders. The next generation long term incentive plan will consist of performance shares with a three year vesting period for a select group of the most senior managers. In parallel, a deferred bonus program for a wider group of senior managers will be implemented. A full description, including performance criteria, will be set out in the Remuneration Policy 2010.

Furthermore, in an effort to create more consistency in the remuneration principles of the Supervisory Board and to adequately reflect the responsibilities and work-load of each Supervisory Board member, the Supervisory Board proposed the following new remuneration principles for its members in 2009:

- Supervisory Board membership: EUR 100,000
- Chairman of Audit Committee, Strategy Committee, Nomination and Remuneration Committee: EUR 200,000 (including remuneration for Supervisory Board membership)
- Chairman of the Supervisory Board: EUR 250,000 (including remuneration for Supervisory Board membership)

On 15 January 2010, these remuneration principles were approved by the General Meeting of Shareholders, with effective date 1 January 2010.

**The Supervisory Board**

**8 April 2010**

# 2009 Financial Statements

X5 Retail Group

International Financial Reporting Standards
Consolidated Financial Statements,

Dutch GAAP Company's Financial Statements and

Independent Auditor's Report

31 December 2009

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# DIRECTORS' RESPONSIBILITY STATEMENT

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of X5 Retail Group N.V. and its subsidiaries (the "Group").

Management is responsible for the preparation of the consolidated financial statements that present fairly the financial position of the Group at 31 December 2009, and the results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with International Financial Reporting Standards as adopted by the European Union.

In preparing the consolidated financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether IFRS as adopted by the European Union and IFRS as issued by the International Accounting Standards Board have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- Preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS as adopted by the European Union and IFRS as issued by the International Accounting Standards Board;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2009 were approved on 8 April 2010 by:

**Lev Khasis**
Chief Executive Officer

**Evgeny Kornilov**
Chief Financial Officer

# X5 Retail Group
# Consolidated Statement of Financial Position at 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | Note | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | 10 | 2,995,329 | 3,039,044 |
| Investment property | 11 | 133,425 | 125,693 |
| Goodwill | 12 | 767,523 | 554,559 |
| Intangible assets | 13 | 496,111 | 499,324 |
| Prepaid leases | 10 | 84,805 | 80,677 |
| Investment in associates | 8 | 5,609 | 10,054 |
| Other non-current assets | | 1,304 | 2,443 |
| Deferred tax assets | 29 | 151,786 | 94,558 |
| | | 4,635,892 | 4,406,352 |
| **Current assets** | | | |
| Inventories of goods for resale | 14 | 612,722 | 476,475 |
| Derivative financial assets | 18 | - | 765 |
| Loans originated | | 2,848 | 350 |
| Current portion of non-current prepaid lease | 10 | 13,705 | 10,154 |
| Trade and other accounts receivable | 16 | 309,571 | 176,313 |
| Current income tax receivable | | 18,663 | 60,866 |
| VAT and other taxes recoverable | 17 | 174,762 | 239,418 |
| Cash and cash equivalents | 9 | 411,681 | 276,837 |
| | | 1,543,952 | 1,241,178 |
| **Total assets** | | **6,179,844** | **5,647,530** |
| **EQUITY AND LIABILITIES** | | | |
| **Equity attributable to equity holders of the parent** | | | |
| Share capital | 21 | 93,712 | 93,712 |
| Share premium | 21 | 2,049,144 | 2,049,144 |
| Cumulative translation reserve | | (559,576) | (520,184) |
| Retained earnings | | 199,292 | 33,941 |
| Hedging reserve | 18 | (10,108) | (18,180) |
| **Total equity** | | **1,772,464** | **1,638,433** |
| **Non-current liabilities** | | | |
| Long-term borrowings | 20 | 287,378 | 1,480,968 |
| Long-term finance lease payable | | 4,586 | 1,843 |
| Deferred tax liabilities | 29 | 207,689 | 219,161 |
| Long-term deferred revenue | | 1,839 | 3,482 |
| Share-based payments liability | 28 | 25,986 | 30,665 |
| | | 527,478 | 1,736,119 |
| **Current liabilities** | | | |
| Trade accounts payable | | 1,556,325 | 1,175,279 |
| Short-term borrowings | 20 | 1,656,622 | 578,433 |
| Share-based payments liability | 28 | 59,559 | 7,256 |
| Derivative financial liabilities | 18 | 10,108 | 18,180 |
| Short-term finance lease payables | | 1,950 | 2,197 |
| Interest accrued | | 8,863 | 8,384 |
| Short-term deferred revenue | | 18,979 | 4,872 |
| Current income tax payable | | 33,790 | 20,887 |
| Provisions and other liabilities | 19 | 533,706 | 457,490 |
| | | 3,879,902 | 2,272,978 |
| **Total liabilities** | | **4,407,380** | **4,009,097** |
| **Total equity and liabilities** | | **6,179,844** | **5,647,530** |

# X5 Retail Group
# Consolidated Income Statement for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | Note | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **Revenue** | 23 | 8,717,399 | 8,353,250 |
| Cost of sales | 24 | (6,609,522) | (6,206,324) |
| **Gross profit** | | **2,107,877** | **2,146,926** |
| Selling, general and administrative expenses | 24 | (1,740,604) | (1,698,524) |
| Lease/sublease and other income | 25 | 100,496 | 94,776 |
| **Operating profit before impairment** | | **467,769** | **543,178** |
| Impairment of Goodwill | 12, 24 | - | (2,257,020) |
| **Operating profit/(loss) after impairment** | | **467,769** | **(1,713,842)** |
| Finance costs | 26 | (157,964) | (159,016) |
| Finance income | 26 | 3,817 | 10,511 |
| Share of loss of associates | 8 | (3,964) | (647) |
| Net foreign exchange loss | | (45,692) | (267,187) |
| **Profit/(Loss) before tax** | | **263,966** | **(2,130,181)** |
| Income tax expense | 29 | (98,615) | (8,106) |
| **Profit/(Loss) for the year** | | **165,351** | **(2,138,287)** |
| **Profit for the year attributable to:** | | | |
| Equity holders of the parent | | 165,351 | (2,138,287) |
| **Basic earnings/(losses) per share for profit/(losses) attributable to the equity holders of the parent** (expressed in USD per share) | 22 | 2.44 | (33.45) |
| **Diluted earnings/(losses) per share for profit/(losses) attributable to the equity holders of the parent** (expressed in USD per share) | | 2.43 | (33.45) |

# X5 Retail Group
# Consolidated Statement of Comprehensive Income for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| **Profit/(Loss) for the year** | **165,351** | **(2,138,287)** |
| **Other comprehensive income/(loss)** | | |
| Exchange differences on translation from functional to presentation currency | (39,392) | (814,353) |
| Changes in fair value of financial instruments | 8,072 | (18,180) |
| **Other comprehensive loss** | **(31,320)** | **(832,533)** |
| **Total comprehensive income/(loss) for the year** | **134,031** | **(2,970,820)** |
| **Total comprehensive income/(loss) for the year attributable to:** | | |
| Equity holders of the parent | 134,031 | (2,970,820) |

# X5 Retail Group
# Consolidated Statement of Cash Flows for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | Note | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **Profit/(Loss) before tax** | | **263,966** | **(2,130,181)** |
| Adjustments for: | | | |
| Depreciation, amortisation and impairment | 24 | 268,243 | 225,238 |
| Goodwill impairment | 12 | - | 2,257,020 |
| Loss on disposal of property, plant and equipment | | 3,113 | 835 |
| Loss on disposal of intangible assets | | - | 245 |
| Finance costs, net | 26 | 154,147 | 148,505 |
| Impairment of trade and other accounts receivable | 24 | 12,955 | 7,350 |
| Share-based options expense/(income) | 28 | 59,316 | (7,647) |
| Amortisation of deferred expenses | | 10,226 | 5,087 |
| Net foreign exchange loss | | 45,692 | 267,187 |
| Loss from associate | 8 | 3,964 | 647 |
| Other non-cash items | | 13,877 | - |
| **Net cash from operating activities before changes in working capital** | | **835,499** | **774,286** |
| (Increase)/Decrease in trade and other accounts receivable | | (91,463) | 39,043 |
| (Increase) in inventories of goods for resale | | (128,095) | (164,858) |
| Increase in trade payable | | 343,752 | 239,744 |
| Increase in other accounts payable | | 41,844 | 130,007 |
| **Net cash generated from operations** | | **1,001,537** | **1,018,222** |
| Interest paid | | (156,914) | (150,493) |
| Interest received | | 4,449 | 12,078 |
| Income tax paid | | (115,390) | (250,460) |
| **Net cash from operating activities** | | **733,682** | **629,347** |
| **Cash flows from investing activities** | | | |
| Purchase of property, plant and equipment | 10 | (175,317) | (883,020) |
| Purchase of investment property | 11 | (8,574) | (3,034) |
| Non-current prepaid lease | | (4,555) | (57,384) |
| Acquisition of subsidiaries and non-controlling interest | 7 | (229,367) | (711,072) |
| Proceeds from sale of property, plant and equipment | | 3,290 | 6,826 |
| Purchase of intangible assets | 13 | (19,321) | (8,361) |
| **Net cash used in investing activities** | | **(433,844)** | **(1,656,045)** |
| **Cash flows from financing activities** | | | |
| Proceeds from short-term loans | | 259,934 | 2,061,428 |
| Repayment of short-term loans | | (656,357) | (1,999,787) |
| Proceeds from long-term loans | | 248,733 | - |
| Repayment of long-term loans | | (40,074) | - |
| Proceeds from issue of share capital | 21 | - | 999,454 |
| Proceeds from sale of treasury shares | 21 | - | 144,217 |
| Acquisition of treasury shares | 21 | - | (9,102) |
| Acquisition of derivative financial assets | | (2,512) | - |
| Principal payments on finance lease obligations | | (4,018) | (2,017) |
| **Net cash (used in)/generated from financing activities** | | **(194,294)** | **1,194,193** |
| Effect of exchange rate changes on cash and cash equivalents | | 29,300 | (70,154) |
| **Net increase in cash and cash equivalents** | | **134,844** | **97,341** |
| **Movements in cash and cash equivalents** | | | |
| Cash and cash equivalents at the beginning of the year | | 276,837 | 179,496 |
| Net increase in cash and cash equivalents | | 134,844 | 97,341 |
| **Cash and cash equivalents at the end of the year** | | **411,681** | **276,837** |

# X5 Retail Group
# Consolidated Statement of Changes In Equity for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | | Attributable to the shareholders of the Company | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Note | Number of shares | Share capital | Share premium | Hedging reserve | Cumulative translation reserve | Accumulated profit / (deficit) | Total shareholders' equity | Minority interest | Total |
| **Balance as at 1 January 2008** | | **53,177,760** | **70,883** | **2,896,355** | **-** | **294,169** | **(17,960)** | **3,243,447** | **220** | **3,243,667** |
| Other comprehensive loss for the year | | - | - | - | (18,180) | (814,353) | - | (832,533) | - | (832,533) |
| Loss for the year | | - | - | - | - | - | (2,138,287) | (2,138,287) | - | (2,138,287) |
| **Total comprehensive loss for the year** | | **-** | **-** | **-** | **(18,180)** | **(814,353)** | **(2,138,287)** | **(2,970,820)** | **-** | **(2,970,820)** |
| Issue of shares | 21 | 12,026,675 | 18,979 | 980,475 | - | - | - | 999,454 | - | 999,454 |
| Sale of treasury shares | 21 | 949,778 | 1,268 | 142,949 | - | - | - | 144,217 | - | 144,217 |
| Acquisition of Formata | 21 | 1,746,505 | 2,714 | 228,523 | - | - | - | 231,237 | - | 231,237 |
| Acquisition of treasury shares | 21 | (86,771) | (132) | (8,970) | - | - | - | (9,102) | - | (9,102) |
| Acquisition of Minority interest in Chelyabinsk | | - | - | - | - | - | - | - | (220) | (220) |
| Transfer of Goodwill impairment to Share premium | | - | - | (2,190,188) | - | - | 2,190,188 | - | - | - |
| **Balance as at 31 December 2008** | | **67,813,947** | **93,712** | **2,049,144** | **(18,180)** | **(520,184)** | **33,941** | **1,638,433** | **-** | **1,638,433** |
| Other comprehensive income/(loss) for the year | | - | - | - | 8,072 | (39,392) | - | (31,320) | - | (31,320) |
| Profit for the year | | - | - | - | - | - | 165,351 | 165,351 | - | 165,351 |
| **Total comprehensive income/(loss) for the year** | | **-** | **-** | **-** | **8,072** | **(39,392)** | **165,351** | **134,031** | **-** | **134,031** |
| **Balance as at 31 December 2009** | | **67,813,947** | **93,712** | **2,049,144** | **(10,108)** | **(559,576)** | **199,292** | **1,772,464** | **-** | **1,772,464** |

# X5 Retail Group
# Notes to Consolidated Financial Statements for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

## 1 PRINCIPAL ACTIVITIES AND THE GROUP STRUCTURE

These consolidated financial statements are for the economic entity comprising X5 Retail Group N.V. (the “Company”) and its subsidiaries, as set out in Note 6 (the “Group”).

X5 Retail Group N.V. is a joint stock limited liability company established in August 1975 under the laws of the Netherlands. The principal activity of the Company is to act as a holding company for a group of companies that operate retail grocery stores. The Company’s address and tax domicile is Prins Bernhardplein 200, 1097 JB Amsterdam, the Netherlands.

The main activity of the Group is the development and operation of grocery retail stores. As at 31 December 2009 the Group operated a retail chain of 1,372 soft-discount, supermarket and hypermarket stores under the brand names “Pyaterochka”, “Perekrestok” and “Karusel” in major population centres in Russia, including but not limited to Moscow, St. Petersburg, Nizhniy Novgorod, Rostov-on-Don, Kazan, Samara, Lipetsk, Chelyabinsk, Perm, Ekaterinburg and Kiev, Ukraine (31 December 2008: 1,101 soft-discount, supermarket and hypermarket stores under the brand names “Pyaterochka”, “Perekrestok” and “Karusel”), with the following number of stores:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| **Supermarket** | | |
| Central | 152 | 114 |
| North-West | 33 | 20 |
| Sredne-Volzhsky | 22 | 14 |
| Privolzhsky | 15 | 7 |
| South | 14 | 13 |
| Volgo-Vyatsky | 19 | 20 |
| Central-Chernozem | 9 | 13 |
| Ukraine | 6 | 6 |
| Ural | 5 | - |
| | **275** | **207** |
| **Discounter** | | |
| Central | 433 | 368 |
| North-West | 306 | 276 |
| Ural | 152 | 139 |
| Volgo-Vyatsky | 39 | 29 |
| South | 32 | 4 |
| Sredne-Volzhsky | 28 | 13 |
| Privolzhsky | 25 | - |
| Central-Chernozem | 24 | 19 |
| | **1,039** | **848** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

| | | |
|---|---|---|
| **Hypermarket** | | |
| North-West | 17 | 15 |
| Central | 13 | 10 |
| Privolzhsky | 6 | 5 |
| Volgo-Vyatsky | 6 | 5 |
| Sredne-Volzhsky | 5 | 2 |
| South | 4 | 4 |
| Central-Chernozem | 4 | 3 |
| Ural | 3 | 2 |
| | **58** | **46** |
| **Total stores** | **1,372** | **1,101** |

In addition as at 31 December 2009, the Group's franchisees operated 620 stores (31 December 2008: 607 stores) across Russia.

The Group is a member of the Alfa Group Consortium. As at 31 December 2009 the Company's immediate principal shareholders were Luckyworth Limited and Cesaro Holdings Limited, Alfa Group Consortium companies, owning 25.54% and 21.62% of total issued shares, respectively. As at 31 December 2009 the Company's shares are listed on the London Stock Exchange in the form of Global Depositary Receipts (GDRs), with each GDR representing an interest of 0.25 in an ordinary share, except for 1,746,505 shares issued within the Karusel acquisition (Note 7). As at 31 December 2009 the ultimate parent company of the Group is CTF Holdings Ltd. ("CTF"), an Alfa Group Consortium company registered at Suite 2, 4 Irish Place, Gibraltar, owning directly 0.7% of total issued shares. CTF is under the common control of Mr Fridman, Mr Khan and Mr Kousmichoff (the "Shareholders"). None of the Shareholders individually controls and/or owns 50% or more in CTF.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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 years presented, unless otherwise stated.

### 2.1 Basis of preparation

These consolidated financial statements for the year ended 31 December 2009 have been prepared in accordance with, and comply with International Financial Reporting Standards as adopted by the European Union, and with Part 9 Book 2 of The Netherlands Civil Code. In accordance with article 402 Book 2 of The Netherlands Civil Code the income statement in the Company Financial Statements is presented in abbreviated form.

All International Financial Reporting Standards issued by the IASB and effective at the time of preparing these consolidated financial statements have been adopted by the European Union through the endorsement procedure established by the European Commission.

The consolidated financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets and financial liabilities (including derivative instruments) at fair value through profit or loss.

The preparation of the consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 3.

Certain reclassifications have been made to prior year balances in the consolidated statement of financial position and notes to consolidated financial statements to reflect the changes in provisional value of subsidiaries acquired in prior reporting periods (Note 2.29).

### 2.2 Accounting for the effects of inflation

The Russian Federation was considered hyperinflationary prior to 1 January 2003. As a result, balances and transactions were restated for the changes in the general purchasing power of the Russian Rouble up to 31 December 2002 in accordance with IAS 29 ("Financial Reporting in Hyperinflationary Economies"). IAS 29 requires that the consolidated financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflation had ceased effective from 1 January 2003, the Group does not apply the provisions of IAS 29 to assets acquired or revalued and liabilities incurred or assumed after that date. For other assets and liabilities, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts in these consolidated financial statements.

### 2.3 Consolidated financial statements

Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are de-consolidated from the date that control ceases.

Associates are entities over which the Group has significant influence, but not control, generally accompanying a shareholding of between 20 and 50 percent of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group's share of the post-acquisition profits or losses of associates is recorded in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

The purchase method of accounting is used to account for the acquisition of subsidiaries. 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. However, when a business combination is achieved in stages by successive share purchases, the date of exchange is the date of each exchange transaction; whereas the acquisition date is the date on which acquirer obtains control of the subsidiary.

The Group accounts for options to acquire subsidiaries in business combinations at cost.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date.

The excess of the cost of acquisition over the fair value of the Group's share in net assets of the acquiree at each exchange transaction represents goodwill. 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 recognized immediately in the consolidated income statement.

Intercompany transactions, balances and unrealized gains on transactions between Group companies are eliminated; unrealized losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group’s policies.

### 2.4 Non-controlling interest

Non-controlling 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 Company. Non-controlling interest forms a separate component of the Group’s equity.

When the Group purchases a non-controlling interest, the difference between its carrying amount and the amount paid to acquire it is recorded as goodwill. Gains or losses on disposal of a non-controlling interest, determined as the difference between its carrying amount and proceeds received or receivable, are recorded in the statement of income.

### 2.5 Foreign currency translation and transactions

#### *(a) Functional and presentation currency*

***Functional currency.*** The functional currency of each of the Group’s consolidated entities is the currency of the primary economic environment in which the entity operates. The functional currencies of the Group’s entities are the national currency of the Russian Federation, Russian Rouble (“RR”) and the national currency of Ukraine, Ukrainian Hryvnia (“UAH”). The Group’s presentation currency is the US Dollar (“USD”), which management believes is the most useful currency to adopt for users of these consolidated financial statements.

***Translation from functional to presentation currency.*** The results and financial position of each Group entity (none of which have a functional currency that is the currency of a hyperinflationary economy) are translated into the presentation currency as follows:

(i) assets and liabilities for each statement of financial position presented are translated at the closing rates at the date of that statement of financial position;

(ii) 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

(iii) all resulting exchange differences are recognised as a separate component of equity as a cumulative translation reserve.

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 disposed of through sale, liquidation, repayment of share capital or abandonment of all, or part of, that entity, the exchange differences deferred in equity are reclassified to profit or loss.

#### *(b) Transactions and balances*

Monetary assets and liabilities denominated in foreign currencies are translated into each entity’s functional currency at the official exchange rate of the Central Bank of Russian Federation (“CBRF”) and the Central Bank of Ukraine at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into each entity’s functional currency at period-end official exchange rates of the CBRF are recognized in profit or loss. Translation at period-end rates does not apply to non-monetary items.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

At 31 December 2009, the official rate of exchange, as determined by the Central Bank of the Russian Federation, was USD 1 = RR 30.2442 (31 December 2008: USD 1 = RR 29.3804). The average rate for year ended 31 December 2009 was USD 1 = RR 31.7231 (12 months 2008: USD 1 = RR 24.8553).

### 2.6 Segment reporting

Operating segment is reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker has been identified as the Management Board. The Management Board determined retail operations as a single reportable segment.

### 2.7 Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and provision for impairment, where required. Cost includes expenditure that is directly attributable to the acquisition or construction of the item.

Costs of minor repairs and maintenance are expensed when incurred. Costs of replacing major parts or components of property, plant and equipment are capitalised and the replaced parts are retired. Capitalised costs are depreciated over the remaining useful life of the property, plant and equipment or part's estimated useful life whichever is sooner.

At each reporting date management assesses whether there is any indication of impairment of property, plant and equipment including construction in progress. If any such indication exists, 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 consolidated income statement. An impairment loss recognised for an asset in prior years is reversed if there has been a favourable change in circumstances affecting 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 the proceeds with the carrying amount are recognised in profit or loss.

Land is not depreciated. Depreciation on other items of property, plant and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives. The depreciation periods, which approximate the estimated useful economic lives of the respective assets, are as follows:

| | |
|---|---|
| Buildings | 20-50 years |
| Machinery and equipment | 5-10 years |
| Refrigerating equipment | 7-10 years |
| Vehicles | 5-7 years |
| Other | 3-5 years |

Leasehold improvements are capitalised when it is probable that future economic benefits associated with the improvements will flow to the Company and the cost can be measured reliably. Capitalised leasehold improvements are depreciated over their useful lives but not longer than the terms of the respective leases.

The residual value of an asset is the estimated amount that the Group would currently obtain from the disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

### 2.8 Investment property

Investment property consists of buildings held by the Group to earn rental income or for capital appreciation, or both, and which are not occupied by the Group. The Group recognises the part of an owned shopping center that is leased to third party retailers as investment property, unless it represents an insignificant portion of the property and is used primarily to provide auxiliary services to retail customers not provided by the Group rather than to earn rental income. After purchase or construction of the building the Group assesses the main purpose of its use, if the main purpose is to earn rental income or for capital appreciation, or both, the building is classified as investment property.

Investment properties are stated at cost less accumulated depreciation and provision for impairment, where required. If any indication exists that investment properties may be impaired, the Group estimates the recoverable amount as the higher of value in use and fair value less costs to sell. Subsequent expenditure is capitalised only when it is probable that future economic benefits associated with it will flow to the Group and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to property, plant and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

Depreciation on items of investment property is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives. The depreciation periods, which approximate the estimated useful economic lives of the respective assets, are 20-50 years.

Fair value represents the price at which a property could be sold to a knowledgeable, willing party and has generally been determined using the comparative valuation approach. The Group did not engage an independent valuation specialist to assess the fair value of investment properties.

### 2.9 Intangible assets

***(a) Goodwill***

Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the net identifiable assets, liabilities and contingent liabilities of the acquired subsidiary at the date of exchange.

The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired. Goodwill is allocated to groups of cash-generating units, which are expected to benefit from the synergies of the business combination. Such units or groups of units represent the lowest level at which the Group monitors goodwill and are not larger than a segment.

***(b) Lease rights***

Lease rights represent rights for favourable operating leases acquired in business combinations. Lease rights acquired in a business combination are recognised initially at fair value. Lease rights are amortised using the straight-line method over the lease term of the respective lease contracts – ranging from 5 to 50 years (20 on average).

***(c) Brand and private labels***

Brand and private labels acquired in a business combination are recognised initially at fair value. Brand and private labels are amortised using the straight-line method over their useful lives:

| | Useful lives |
|---|---|
| Brand | 15-20 years |
| Private labels | 1-8 years |

***(d) Franchise agreements***

Franchise agreements represent rights to receive royalties. Franchise agreements acquired in a business combination are recognised initially at fair value. Franchise agreements are amortised using the straight-line method over their useful lives that are, on average, ranging from 7 to 10 years (8 on average).

***(e) Other intangible assets***

Expenditure on acquired patents, trademarks and licenses is capitalized and amortised using the straight-line method over their useful lives ranging from 1 to 10 years (5 on average).

***(f) Impairment of intangible assets***

Where an indication of impairment exists, the recoverable amount of any intangible asset, including goodwill, is assessed and, when impaired, the asset is written down immediately to its recoverable amount. Goodwill and intangible assets not yet available for use are tested for impairment at least annually and whenever impairment indicators exist.

### 2.10 Operating leases

Leases of assets under which substantially all the risks and benefits of ownership are effectively retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the consolidated income statement on a straight-line basis over the period of the lease.

The Group leases retail outlets under terms of fixed and variable lease payments. The variable lease payments depend on revenue earned by the respective retail outlets. The Group classifies variable lease payments as contingent rents unless the Group is virtually certain of the expected amount of the future lease payments in which case they are classified as minimum lease payments (Note 34).

Initial direct costs incurred by the Group in negotiating and arranging an operating lease including key money paid to lessors or previous tenants for entering into lease contracts are recognised as prepaid lease costs and expensed on a straight-line basis over the lease term.

### 2.11 Finance lease liabilities

Where the Group is a lessee in a lease, which transfers substantially all the risks and rewards incidental to ownership to the Group, the leased assets are capitalized in property, plant and equipment at the commencement of the lease at the lower of the fair value of the leased asset and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of future finance charges, are included in borrowings. The interest cost is charged to the consolidated income statement over the lease period using the effective interest method. The assets acquired under finance leases as well as leasehold improvements are depreciated over their useful life or the lease term, if shorter and if the Group is not reasonably certain that it will obtain ownership by the end of the lease.

### 2.12 Trade receivables

Trade receivables are initially recognised at their fair values and are subsequently carried at amortised cost using the effective interest method. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The Group determines that there is objective evidence of impairment by assessing groups of receivables against credit risk factors established based on historical loss experience for each group. Indications that the trade receivable may be impaired include financial difficulties of the debtor, likelihood of the debtor's insolvency, and default or significant failure of payment. The amount of the provision is recognised in the consolidated income statement.

### 2.13 Inventories of goods for resale

Inventories at warehouses and retail outlets are stated at the lower of cost and net realizable value. Cost comprises direct costs of goods, transportation and handling costs. Cost is determined by the first-in, first-out (FIFO) method. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

The Group provides for estimated inventory losses (shrinkage) between physical inventory counts on the basis of a percentage of cost of sales. The provision is adjusted to actual shrinkage based on regular inventory counts. The provision is recorded as a component of cost of sales. The Group also provides for slow moving inventory where the expected time to sell exceeds norms established by the Group.

### 2.14 Financial assets and liabilities

The Group classifies its financial assets into the following measurement categories: at fair value through profit or loss, loans and receivables and available-for-sale investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition and re-evaluates this designation at every reporting date, if required under IFRS. The Group designates investments as available-for-sale only when they fall outside the other categories of financial assets.

***Initial recognition of financial instruments***

Financial assets at fair value through profit or loss are initially recorded at fair value. All other financial assets and liabilities are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. Subsequent to initial recognition, the fair values of financial instruments are measured at fair value by bid prices quoted on active markets. A gain or loss on initial recognition is only recorded if there is a difference between fair value and the transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

***Impairment***

The Group reviews the carrying value of its financial assets on a regular basis. If the carrying value of an investment is greater than the recoverable amount, the Group records an impairment loss and reduces the carrying amount of assets by using an allowance account.

***Derecognition of financial assets***

The Group derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets have otherwise expired or (ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Group has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

***Derivative financial instruments and hedging activities***

Financial assets at fair value through profit or loss are mainly derivatives.

Derivative financial instruments are recognised initially on a settlement date basis and subsequently remeasured at fair value. The Group generally acquires derivative financial instruments quoted on active markets and therefore subsequent remeasurement is based on active market quotations rather than valuation techniques. Derivative financial instruments including foreign exchange contracts, forward rate agreements, interest rate swaps and currency options are carried as trading assets or liabilities at fair value through profit or loss. All derivative instruments are carried as assets when fair value is positive and as liabilities when fair value is negative.

The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as hedges of a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedge).

The Group documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

The fair values of various derivative instruments used for hedging purposes are disclosed in Note 18. Movements on the hedging reserve in shareholders' equity are shown in Note 18.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in equity.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any these derivative instruments are recognised immediately in the consolidated income statement.

***Loans and receivables***
Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Group intends to sell in the near term. Loans receivable and other receivables are carried at amortised cost using the effective interest rate method. Receivables are written off only in case of debtor's insolvency.

***Available for sale***
Available for sale investments are carried at fair value. Interest income on available for sale debt securities is calculated using the effective interest method and recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Group's right to receive payment is established. All other elements of changes in the fair value are deferred in other comprehensive income until the investment is derecognised or impaired at which time the cumulative gain or loss is removed from equity to profit or loss.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of available-for-sale investments. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the current period's profit or loss.

***Financial liabilities***
Financial liabilities are classified according to the substance of the contractual arrangements entered into the following measurement categories: (a) financial derivatives and (b) other financial liabilities. Financial derivatives are carried at fair value with changes in value recognised in the consolidated income statement in the period in which they arise. Other financial liabilities are carried at amortised cost.

### 2.15 Cash

Cash and cash equivalents include cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less.

### 2.16 Provisions

Provisions 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 embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. Provisions are measured as the best estimate of the expenditure required to settle the present obligation at the balance sheet date.

### 2.17 Value added tax

Output VAT related to sales is payable to tax authorities on the earliest of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice and fulfilment of other conditions in compliance with Russian tax legislation.

The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases is recognized in the consolidated statement of financial position on a gross basis and disclosed separately as an asset and liability, except for VAT, presented within other non-current assets. Where a provision has been made for the impairment of receivables, the impairment loss is recorded for the gross amount of the debtor, including VAT.

### 2.18 Employee benefits

Wages, salaries, bonuses, paid annual leave and sick leave are accrued in the period in which the associated services are rendered by the employees of the Group. The Group's entities contribute to the Russian Federation's state pension and social insurance funds in respect of its employees. These contributions are accrued when incurred. The Group's commitment ends with the payment of these contributions.

### 2.19 Share-based payments

The Group issues options to certain employees that give the employees the right to choose whether a share-based payment transaction is settled in cash or by issuing equity instruments.

Share-based payment transactions, or the components of such transactions, are accounted for as a cash-settled share-based payment transaction if, and to the extent that, the entity has incurred a liability to settle in cash or other assets, or as an equity-settled share-based payment transaction if, and to the extent that, no such liability has been incurred.

Share-based payments transactions are measured at the fair value of the compound financial instrument at the measurement date, taking into account the terms and conditions on which the rights to the cash or equity instruments were granted. The fair value is determined using the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions and behavioural considerations.

A liability equal to the portion of the services received is recognised at the current fair value determined at each balance sheet date. The Group records an expense based on the fair value of options related to the shares expected to vest on a straight-line basis over the vesting period.

At the date of settlement, the Group will remeasure the liability to its fair value. If the Group issues equity instruments on settlement rather than paying cash, the liability will be transferred directly to equity, as the consideration for the equity instruments issued.

### 2.20 Borrowings

Borrowings are initially recognised at their fair value, net of transaction costs, and are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated income statement over the period of the borrowings using the effective interest method. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date. Borrowing costs directly attributable to the acquisition, construction or production of assets necessarily take a substantial time to get ready for intended use or sale (qualifying assets) are capitalised as part of the costs of those assets, if the commencement date for capitalisation is on or after 1 January 2009.

Capitalisation of borrowing costs continues up to the date when the assets are substantially ready for their use or sale.

### 2.21 Trade and other payables

Trade and other payables are accrued when the counterparty performs its obligation under the contract and are carried at amortised cost using the effective interest method.

### 2.22 Share capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares are shown as a deduction in equity from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recognised as share premium.

### 2.23 Dividends

Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared on or before the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the consolidated financial statements are authorised for issue.

### 2.24 Treasury shares

Where any Group company purchases the Company's equity share capital, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

### 2.25 Earnings per share

Earnings per share are determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the reporting period. Diluted earnings per share are calculated by adjusting the earnings and the number of shares for the effects of dilutive options.

For the purpose of calculating the weighted average number of ordinary shares outstanding during the period in which the reverse acquisition occurs:

- the number of ordinary shares outstanding from the beginning of that period to the acquisition date is the number of ordinary shares issued by the legal parent to the owners of the legal subsidiary

- the number of ordinary shares outstanding from the acquisition date to the end of that period is the actual number of ordinary shares of the legal parent outstanding during that period.

### 2.26 Taxes

Current income tax liabilities (assets) are measured in accordance with IAS 12, *Income Taxes*, based on legislation that is enacted or substantively enacted at the balance sheet date, taking into consideration applicable tax rates and tax exemptions.

Deferred income tax is provided, using the balance sheet liability method, for temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. In accordance with the initial recognition exemption, deferred tax liabilities are not recorded for temporary differences on initial recognition of goodwill and subsequently for goodwill which is not deductible for tax purposes. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period in which the asset is realised or the liability is settled, based on tax rates which are enacted or substantially enacted at the balance sheet date.

Taxes other than on income, interest and penalties are measured in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent*. The Group provides against tax contingencies and the related interest and penalties where management can make a reliable estimate of the amount of the additional taxes that may be due. Provisions are maintained, and updated if necessary, for the period over which the respective tax positions remain subject to review by the tax and customs authorities, being 3 years from the year of filing.

Liabilities for such taxes, interest and penalties are measured at the best estimate of the expenditure required to settle the present obligation at the balance sheet date (Notes 29 and 34).

### 2.27 Income and expense recognition

Income and expenses are recognised on an accrual basis as earned or incurred. Recognition of the principal types of income and expenses is as follows:

***(a) Revenue***

Revenue from the sale of goods through retail outlets is recognised at the point of sale. Revenue from franchisee fees is recognised based on contractual agreements over the term of the contracts. The up-front non-refundable franchisee fees received by the Group are deferred and recognised over the standard contractual term of 10 years. Revenue from advertising services is recognised based on contractual agreements. Revenues are measured at the fair value of the consideration received or receivable. Revenues are recognised net of value added tax.

The Group launched a loyalty card scheme in 2007. Discounts earned by customers through loyalty cards, are recorded by the Group by allocating some of the consideration received from the initial sales transaction to the award credits and deferring the recognition of revenue.

***(b) Cost of sales***

Cost of sales include the purchase price of the products sold and other costs incurred in bringing the inventories to the location and condition ready for sale, i.e. retail outlets. These costs include costs of purchasing, storing, rent, salaries and transporting the products to the extent it relates to bringing the inventories to the location and condition ready for sale.

The Group receives various types of allowances from suppliers in the form of slotting fees, volume discounts, and other forms of payment. In accounting for supplier bonuses received by the Group, the Group determined that these bonuses are a reduction in prices paid for the product and are reported as part of the cost of sales as the related inventory is sold. Bonuses receivable from suppliers in cash are presented as trade receivables.

***(c) Interest income and expense***
Interest income and expense are recognised on an effective yield basis.

***(d) Selling, general and administrative expenses***
Selling expenses consist of salaries and wages of stores employees, store expenses, rent or depreciation of stores, utilities, advertising costs and other selling expenses. General and administrative expenses include costs of salaries and wages of support office employees, rent and depreciation of support offices, impairment and amortisation charges of non-current assets and other general and administrative expenses. Selling, general and administrative expenses are recognised on an accrual basis as incurred.

### 2.28 Impairment of non-current assets other than goodwill
The Group periodically assesses whether there is any indication that non-current assets may be impaired. If any such indicators exist, the Group estimates the recoverable amount of the asset. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash generating unit to which it belongs. Individual stores are considered separate cash-generating units for impairment testing purposes. Impairment loss is recognised whenever the carrying amount of an asset or the related cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the consolidated income statement.

### 2.29 Fair value of assets and liabilities at the acquisition date
In June 2008 the Group acquired 100% of the voting shares of Formata Holding B.V. which is the owner of the Karusel hypermarket chain ("Karusel"). In December 2008 the Group acquired 100% of the voting shares of OOO "Agrotorg Rostov" operating retail grocery stores in Rostov-na-Donu and Rostov region.

A primary valuation of assets and liabilities of acquired companies was performed on a provisional basis.

During the reporting period provisional values of Karusel and OOO "Agrotorg Rostov" were updated based on final fair value estimates of independent appraisers. As a consequence of the adjustment the previously reported Consolidated Statement of Financial Position as at 31 December 2008 was changed to reflect the updated provisional values from the date of acquisition (Note 7).

## 3 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 accounting policies. Judgements that have the most significant effect on the amounts recognised in the consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities include:

***Impairment of goodwill.*** The Group tests goodwill for impairment at least annually. The recoverable amount of a cash-generating unit has been determined based on the higher of fair value less costs to sell or value-in-use calculations. These calculations require the use of estimates as further detailed in Note 12. No impairment loss on goodwill was recognized for the year ended 31 December 2009. The impairment loss on goodwill amounted to USD 2,257,020 for the year ended 31 December 2008.

Since part of this goodwill was originally recognised on the acquisition of businesses with a corresponding entry to share premium account, an amount of USD 2,190,188 has been transferred from accumulated deficit to share premium reserve.

***Provisional fair value of Paterson net assets.*** The Group acquired 100% of the voting shares of OOO "Firma "Omega-97" which is the owner of the Paterson supermarket chain ("Paterson") during the reporting period (Note 7) and applied a number of estimates to define the provisional fair value of Paterson net assets. In estimating the provisional values of property and lease rights, direct references to observable prices in an active market are used (market approach). Estimates of other assets and liabilities are consistent with the Group policies with regard to other subsidiaries.

***Tax legislation.*** Russian tax, currency and customs legislation is subject to varying interpretations (Note 34).

***Property, plant and equipment.*** The Group's management determines the estimated useful lives and related depreciation charges for its plant and equipment (Note 10). This estimate is based on projected product lifecycles and technical requirements. Management will increase the depreciation charge where useful lives are less than previously estimated lives or it will write-off or write-down technically obsolete or non-strategic assets that have been abandoned or reclassified as held for sale.

The Group periodically assesses whether there is any indication that property, plant and equipment may be impaired. In the current period such indications exist and therefore assets impairment testing was performed (Note 10). In these cases, the Group estimates the recoverable amount of the asset or cash generating unit and if it is less than the carrying amount of an asset or cash generating unit an impairment loss is recognised in the consolidated income statement.

***Fair value of lease rights.*** The Group's management determines the fair value of lease rights acquired in business combinations. The assessment of the fair value of lease rights is based on the estimate of the market rates of the lease prepared by an independent valuation specialist (Note 13).

***Inventories of goods for resale provisions.*** The Group provides for estimated inventory shrinkage on the basis of a historical shrinkage as a percentage of cost of sales. This provision is adjusted at the end of each reporting period to reflect the historical trend of the actual physical inventory count results. The Group also provides for slow moving inventory where the expected time to sell exceeds norms established by the Group (Note 14).

***Provision for impairment of trade and other receivables.*** The Group determines an allowance for doubtful accounts receivable at the end of the reporting period (Note 16). In estimating an allowance for uncollectible accounts receivable the Group takes into account the historical collectability of the outstanding accounts receivable balances supplemented by the judgement of management to exclude the impact of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

***Fair value of franchise agreements.*** The Group's management determines the fair value of franchise agreements acquired in business combinations. The assessment of the fair value of franchise agreements is based on the income method using discounted royalty payments during the period of the agreements (Note 13).

***Fair value of brand and private labels.*** The Group' management determines the fair value of brand and private labels acquired in business combinations. The assessment of the fair value of a brand is based on the income approach using the relief-from-royalty method. The assessment of fair value of private labels is based on either the income method using discounted annual savings for the remaining useful life of the labels or the cost method (Note 13).

***Share-based payments.*** In 2007 the Group introduced an employee stock option program (ESOP) for its key executives and employees. The fair value of services received in return for the share options granted to employees is measured by reference to the fair value of the share options granted which is determined at each reporting date. The estimate of the fair value of the share options is measured based on the Black-Scholes model. Major assumptions are summarized in Note 28.

## 4 ADOPTION OF NEW AND REVISED STANDARDS AND INTERPRETATIONS AND NEW ACCOUNTING PRONOUNCEMENT

Certain new interpretations became effective for the Group from 1 January 2009:

***Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate – IFRS 1 and IAS 27 Amendment.*** The amendment allows first-time adopters of IFRS to measure investments in subsidiaries, jointly controlled entities or associates at fair value or at previous GAAP carrying value as deemed cost in the separate financial statements. The amendment also requires distributions from pre-acquisition net assets of investees to be recognised in profit or loss rather than as a recovery of the investment.

***Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment.*** 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.

***IFRS 8, Operating Segments.*** IFRS 8 requires an entity to report financial and descriptive information about its operating segments, with segment information presented on a similar basis to that used for internal reporting purposes. Operating segment is reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker has been identified as the Management Board. The Management Board determined retail operations as a single reportable segment.

***IAS 1, Presentation of Financial Statements** (revised).* 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 entity chose to present two statements: a separate consolidated income statement and a consolidated statement of comprehensive income.

***IAS 23, Borrowing Costs** (revised).* The main change to IAS 23 is the removal of the option of immediately recognizing 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 capitalize 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 capitalization is on or after 1 January 2009. The effect on consolidated financial statements as at 31 December 2009 was not material.

***Puttable Financial Instruments and Obligations Arising on Liquidation – IAS 32 and IAS 1 Amendment.*** The amendment requires classification as equity of some financial instruments that meet the definition of financial liabilities.

***IFRIC 13, Customer Loyalty Programmes.*** IFRIC 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. It is the policy of the Group to recognize the deferred revenue on their customer loyalty program as a reduction of revenue, thus, this interpretation had no impact on consolidated financial statements.

The following new standards, amendments to standards and interpretations have been issued but are not effective for 2009 and have not been early adopted:

***Group Cash-settled Share-based Payment Transactions – Amendments to IFRS 2, Share-based Payment*** (effective for annual periods beginning on or after 1 January 2010, not yet adopted by the EU). The amendments provide a clear basis to determine the classification of share-based payment awards in both consolidated and separate financial statements. The amendments incorporate into the standard the guidance in IFRIC 8 and IFRIC 11, which are withdrawn. The amendments expand on the guidance given in IFRIC 11 to address plans that were previously not considered in the interpretation. The amendments also clarify the defined terms in the Appendix to the standard.

***IFRS 3, Business Combinations*** (revised January 2008; 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 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or at fair value. The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, in a business combination achieved in stages, the acquirer will have to remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognize the resulting gain or loss, if any, in profit or loss. Acquisition-related costs will be accounted for separately from the business combination and therefore recognized as expenses rather than included in goodwill. An acquirer will have to recognize at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognized in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

***IFRS 9, Financial Instruments*** (issued in November 2009, effective for annual periods beginning on or after 1 January 2013, with earlier application permitted; not yet adopted by the EU). IFRS 9 replaces those parts of IAS 39 relating to the classification and measurement of financial assets. Key features are as follows:

- Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.

- An instrument is subsequently measured at amortised cost only if it is a debt instrument and both (i) the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and (ii) the asset's contractual cash flows represent only payments of principal and interest (that is, it has only "basic loan features"). All other debt instruments are to be measured at fair value through profit or loss.

- All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There is to be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.

The Group is considering the implications of the standard, the impact on the Group and the timing of its adoption by the Group.

***Improving Disclosures about Financial Instruments – Amendment to IFRS 7, Financial Instruments: Disclosures*** (issued in March 2009; effective for annual periods beginning on or after 1 January 2009; not yet adopted by the EU). The amendment requires enhanced disclosures about fair value measurements and liquidity risk. The entity will be required to disclose an analysis of financial instruments using a three-level fair value measurement hierarchy. The amendment (a) clarifies that the maturity analysis of liabilities should include issued financial guarantee contracts at the maximum amount of the guarantee in the earliest period in which the guarantee could be called; and (b) requires disclosure of remaining contractual maturities of financial derivatives if the contractual maturities are essential for an understanding of the timing of the cash flows. An entity will further have to disclose a maturity analysis of financial assets it holds for managing liquidity risk, if that information is necessary to enable users of its consolidated financial statements to evaluate the nature and extent of liquidity risk.

***IAS 24, Related Party Disclosures*** (amended November 2009, effective for annual periods beginning on or after 1 January 2011; not yet adopted by the EU). The amended standard simplifies the disclosure requirements for government-related entities and clarifies the definition of a related party. The Group is currently assessing the impact of the amended standard on disclosures in its consolidated financial statements.

***IAS 27, Consolidated and Separate Financial Statements*** (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value. The Group is currently assessing the impact of the amended standard on its consolidated financial statements.

***Classification of Rights Issues – Amendment to IAS 32, Financial Instruments: Presentation*** (effective for annual periods beginning on or after 1 February 2010; not yet adopted by the EU). The amendment addresses the accounting for rights issues (rights, options or warrants) that are denominated in a currency other than the functional currency of the issuer. The amendment states that, if such rights are issued pro rata to an entity's existing shareholders for a fixed amount of any currency, they should be classified as equity, regardless of the currency in which the exercise price is denominated. The Group is currently assessing the impact of the amendment on its consolidated financial statements.

***Eligible Hedged Items – Amendment to IAS 39, Financial Instruments: Recognition and Measurement*** (effective with retrospective application for annual periods beginning on or after 1 July 2009). The amendment clarifies how the principles that determine whether a hedged risk or portion of cash flows is eligible for designation should be applied in particular situations.

***Embedded Derivatives – Amendments to IFRIC 9 and IAS 39*** (effective for annual periods ending on or after 30 June 2009; amendments to IFRIC 19 and IAS 39 as adopted by the EU are effective for annual periods beginning after 31 December 2009, with early adoption permitted). The amendments clarify that on reclassification of a financial asset out of the 'at fair value through profit or loss' category, all embedded derivatives have to be assessed and, if necessary, separately accounted for.

***IFRIC 12, Services Concession Arrangements*** (effective for annual periods beginning on or after 30 March 2009; IFRIC 12 as adopted by the EU is effective for annual periods beginning on or after 30 March 2009, with early adoption permitted). The interpretation contains guidance on applying the existing standards by service providers in public-to-private service concession arrangements.

***IFRIC 15, Agreements for the Construction of Real Estate*** (effective for annual periods beginning on or after 1 January 2009; IFRIC 15 as adopted by the EU is effective for annual periods beginning after 31 December 2009, with early adoption permitted). The interpretation applies to the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors, and provides guidance for determining whether agreements for the construction of real estate are within the scope of IAS 11 or IAS 18. It also provides criteria for determining when entities should recognise revenue on such transactions.

***IFRIC 16, Hedges of a Net Investment in a Foreign Operation*** (effective for annual periods beginning on or after 1 October 2008; IFRIC 16 as adopted by the EU is effective for annual periods beginning after 30 June 2009, with early adoption permitted). The interpretation explains which currency risk exposures are eligible for hedge accounting and states that translation from the functional currency to the presentation currency does not create an exposure to which hedge accounting could be applied. The IFRIC allows the hedging instrument to be held by any entity or entities within a Group except the foreign operation that itself is being hedged. The interpretation also clarifies how the gain or loss recycled from the currency translation reserve to profit or loss is calculated on disposal of the hedged foreign operation. Reporting entities will apply IAS 39 to discontinue hedge accounting prospectively when their hedges do not meet the criteria for hedge accounting in IFRIC 16.

***IFRIC 17, Distribution of Non-Cash Assets to Owners*** (effective for annual periods beginning on or after 1 July 2009; IFRIC 17 as adopted by the EU is effective for annual periods beginning after 31 October 2009, with early adoption permitted). The amendment clarifies when and how distribution of non-cash assets as dividends to the owners should be recognised. An entity should measure a liability to distribute non-cash assets as a dividend to its owners at the fair value of the assets to be distributed. A gain or loss on disposal of the distributed non-cash assets will be recognised in profit or loss when the entity settles the dividend payable. IFRIC 17 is not expected to have any impact on the Group's consolidated financial statements.

***IFRIC 18, Transfers of Assets from Customers*** (effective prospectively to transfers of assets from customers received on or after 1 July 2009, earlier application permitted; IFRIC 18 as adopted by the EU is effective for annual periods beginning after 31 October 2009, with early adoption permitted). The interpretation clarifies the accounting for transfers of assets from customers, namely, the circumstances in which the definition of an asset is met; the recognition of the asset and the measurement of its cost on initial recognition; the identification of the separately identifiable services (one or more services in exchange for the transferred asset); the recognition of revenue, and the accounting for transfers of cash from customers. IFRIC 18 is not expected to have any impact on the Group's consolidated financial statements.

***IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments*** (effective for annual periods beginning on or after 1 July 2010; not yet adopted by the EU). This IFRIC clarifies the accounting when an entity renegotiates the terms of its debt with the result that the liability is extinguished through the debtor issuing its own equity instruments to the creditor. A gain or loss is recognised in the profit and loss account based on the fair value of the equity instruments compared to the carrying amount of the debt. The Group is currently assessing the impact of the interpretation on its consolidated financial statements.

***Improvements to International Financial Reporting Standards*** (issued in April 2009; amendments to IFRS 2, IAS 38, IFRIC 9 and IFRIC 16 are effective for annual periods beginning on or after 1 July 2009; amendments to IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36 and IAS 39 are effective for annual periods beginning on or after 1 January 2010; the improvements have not yet been adopted by the EU). The improvements consist of a mixture of substantive changes and clarifications in the following standards and interpretations: clarification that contributions of businesses in common control transactions and formation of joint ventures are not within the scope of IFRS 2; clarification of disclosure requirements set by IFRS 5 and other standards for non-current assets (or disposal groups) classified as held for sale or discontinued operations; requiring to report a measure of total assets and liabilities for each reportable segment under IFRS 8 only if such amounts are regularly provided to the chief operating decision maker; amending IAS 1 to allow classification of certain liabilities settled by entity's own equity instruments as non-current; changing IAS 7 such that only expenditures that result in a recognised asset are eligible for classification as investing activities; allowing classification of certain long-term land leases as finance leases under IAS 17 even without transfer of ownership of the land at the end of the lease; providing additional guidance in IAS 18 for determining whether an entity acts as a principal or an agent; clarification in IAS 36 that a cash generating unit shall not be larger than an operating segment before aggregation; supplementing IAS 38 regarding measurement of fair value of intangible assets acquired in a business combination; amending IAS 39 (i) to include in its scope option contracts that could result in business combinations, (ii) to clarify the period of reclassifying gains or losses on cash flow hedging instruments from equity to profit or loss and (iii) to state that a prepayment option is closely related to the host contract if upon exercise the borrower reimburses economic loss of the lender; amending IFRIC 9 to state that embedded derivatives in contracts acquired in common control transactions and formation of joint ventures are not within its scope; and removing the restriction in IFRIC 16 that hedging instruments may not be held by the foreign operation that itself is being hedged.

Unless otherwise described above, the new interpretations are not expected to significantly affect the Group's consolidated financial statements.

## 5 SEGMENT REPORTING

X5 Retail Group N.V. identifies retailing operations as a single reportable segment.

The Group is engaged in management of retail stores located in Russia and Ukraine. The Group identified the segment in accordance with the criteria set forth in IFRS 8 and based on the way the operations of the Company are regularly reviewed by the chief operating decision maker to analyze performance and allocate resources among business units of the Group.

The chief operating decision-maker has been determined as the Management Board. The Management Board reviews the Group's internal reporting in order to assess performance and allocate resources. Management has determined a single operating segment being retailing operations including royalties, advertising, communications and rent income based on these internal reports data.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The segment represents the Group's retail business in the European part of Russia and Ukraine. Currently the Group's Ukraine business unit's contribution to the financial results of the Group is immaterial.

Within the segment all business components demonstrate similar economic characteristics and are alike as follows:

- the products and customers;
- the business processes are integrated and uniform: the Group manages its store operations centrally, sources products centrally, support functions like Purchasing, Logistics, Development, Finance, Strategy, HR, IT, etc. are centralized;
- the Group's activities are limited to a common market zone (i.e. Russia) with uniform legislation and regulatory environment.

The Management Board assesses the performance of the operating segment based on a measure of sales and adjusted earnings before interest, tax, depreciation, and amortization (EBITDA). Other information provided to the Management Board is measured in a manner consistent with that in the consolidated financial statements.

The accounting policies used for segments are the same as accounting policies applied for these consolidated financial statements as described in Note 2.

The segment information for the year ended 31 December 2009 is as follows:

| | Year ended 31 December 2009 | Year ended 31 December 2008 |
|---|---|---|
| Retail sales | 8,683,821 | 8,319,821 |
| Other revenue | 33,578 | 33,429 |
| **Revenue** | **8,717,399** | **8,353,250** |
| **EBITDA** | **736,012** | **768,416** |
| Capital expenditure | 169,597 | 898,899 |
| **Total assets** | **6,179,844** | **5,647,530** |
| **Total liabilities** | **4,407,380** | **4,009,097** |

Assets and liabilities are presented in a manner consistent with that in the consolidated financial statements. Capital expenditure does not include additions to intangible assets (Note 13).

A reconciliation of EBITDA to profit for the year is provided as follows:

| | Year ended 31 December 2009 | Year ended 31 December 2008 |
|---|---|---|
| **EBITDA** | **736,012** | **768,416** |
| Depreciation and amortization | (268,243) | (225,238) |
| Impairment of Goodwill | - | (2,257,020) |
| **Operating profit/(loss)** | **467,769** | **(1,713,842)** |
| Finance cost | (154,147) | (148,505) |
| Net foreign exchange result | (45,692) | (267,187) |
| Share of profit/(loss) of associates | (3,964) | (647) |
| **Profit/(loss) before income tax** | **263,966** | **(2,130,181)** |
| Income tax expense | (98,615) | (8,106) |
| **Profit/(Loss) for the year** | **165,351** | **(2,138,287)** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 6 SUBSIDIARIES

Details of the Company's significant subsidiaries at 31 December 2009 and 31 December 2008 are as follows:

| | | | Ownership (%) | |
|---|---|---|---|---|
| Company | Country | Nature of operations | 31 December 2009 | 31 December 2008 |
| Agroaspekt OOO | Russia | Retailing | 100 | 100 |
| Agrotorg OOO | Russia | Retailing | 100 | 100 |
| Alpegru Retail Properties Ltd. | Cyprus | Real estate | 100 | 100 |
| Grasswell Ltd. | Cyprus | Financing | 100 | 100 |
| Kaizer OOO | Russia | Real estate | 100 | 100 |
| Kama Retail OOO | Russia | Retailing | 100 | 100 |
| Key Retail Technologies Ltd. | Gibraltar | Trade mark | 100 | 100 |
| Perekrestok Holdings Ltd. | Gibraltar | Holding company | 100 | 100 |
| Perekrestok-2000 OOO | Russia | Retailing | 100 | 100 |
| Sladkaya Zhizn N.N. OOO | Russia | Retailing | 100 | 100 |
| Speak Global Ltd. | Cyprus | Real estate and trade mark | 100 | 100 |
| TH Perekrestok ZAO | Russia | Retailing | 100 | 100 |
| Ural Retail OOO | Russia | Retailing | 100 | 75 |
| Ural-Agro-Torg OOO | Russia | Retailing | 100 | 75 |
| X5 Finance OOO | Russia | Bond issuer | 100 | 100 |
| X5 Nedvizhimostn ZAO | Russia | Real estate | 100 | 100 |
| X5 Retail Group Ukraine ZAT | Ukraine | Retailing | 100 | 100 |
| Firma Omega-97 OOO | Russia | Retailing | 100 | - |

## 7 ACQUISITION OF SUBSIDIARIES

***Paterson***

In December 2009 the Group acquired 100% of the business and assets of Paterson, a non-public supermarket chain of 82 stores located in Moscow, the Moscow region, St. Petersburg, Kazan and other cities of European Russia and Urals.

In the year ended 31 December 2009 the acquired business of Paterson contributed revenue of USD 34,068 and a net loss of USD 706 from the date of acquisition. If the acquisition of Paterson had occurred on 1 January 2009, the Group's revenue for the year ended 31 December 2009 would have been USD 9,014,525 and the Group's net profit for the year ended 31 December 2009 would have been USD 148,498. Estimates of contribution of revenue and profit to the Group are based on unaudited information derived from previous management accounts of Paterson.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

Details of assets and liabilities acquired and the related goodwill are as follows:

| | Acquiree's carrying amount at the acquisition date, Russian GAAP* | Provisional values at the acquisition date |
|---|---|---|
| Cash and cash equivalents | 3,361 | 3,311 |
| Inventories of goods for resale | 29,912 | 14,829 |
| Loans originated | 3,622 | 1,728 |
| Trade and other accounts receivable | 80,889 | 14,524 |
| Intangible assets | 14 | 22,677 |
| Property, plant and equipment (Note 10) | 31,278 | 126,286 |
| Deferred tax assets | 358 | 5,649 |
| Short-term borrowings | (10,251) | (82,385) |
| Trade and other accounts payable | (64,578) | (69,969) |
| Provisions and liabilities for tax uncertainties (Note 34) | - | (41,253) |
| Long-term borrowings | (79,402) | (6,883) |
| Deferred tax liability | (28) | (14,116) |
| Net liability acquired | (4,825) | (25,602) |
| Goodwill (Note 12) | | 216,471 |
| **Total acquisition cost** | | **190,869** |
| **Net cash outflow arising from the acquisition for the year ended 31 December 2009** | | **187,508** |

* Russian GAAP numbers are disclosed since IFRS financial statements were not prepared by the entities before acquisition.

The Group assigned provisional values to net assets acquired based on estimates of the independent appraisal. The Group will finalise the purchase price allocation within 12 month from the acquisition date.

The purchase consideration comprises cash and cash equivalents paid of USD 189,500 and directly attributable transactions costs of USD 1,369, part of which in the amount of USD 1,319 was paid in 2009 and USD 50 to be paid in 2010.

The goodwill recognised is attributable to: i) the business concentration in the Moscow, Saint-Petersburg and other Russian regions and their neighbouring areas and ii) expected cost synergies from the business combination.

***Internet Retail***

In October 2009 the Group has acquired 51% of voting shares of Epylon Limited. Epylon Limited is the owner of the internet stores www.bolero.ru and www.003.ru ("Internet Retail").

In the year ended 31 December 2009 the acquired business of Internet Retail contributed revenue of USD 3,741 and a net loss of USD 526 from the date of acquisition. If the acquisition of Internet Retail had occurred on 1 January 2009, the Group's revenue for the year ended 31 December 2009 would have been USD 8,719,454 and the Group's net profit for the year ended 31 December 2009 would have been USD 165,151. Estimates of contribution of revenue and profit to the Group are based on unaudited information derived from previous management accounts of Internet Retail.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

Details of assets and liabilities acquired and the related goodwill are as follows:

| | Acquiree's carrying amount at the acquisition date, Russian GAAP* | Provisional values at the acquisition date |
|---|---|---|
| Cash and cash equivalents | 20 | 20 |
| Inventories of goods for resale | 1,279 | 1,279 |
| Trade and other accounts receivable | 1,118 | 1,113 |
| Intangible assets | - | 4 |
| Property, plant and equipment (Note 10) | 59 | 13 |
| Deferred tax assets | - | 14 |
| Trade and other accounts payable | (2,662) | (2,662) |
| Net liability acquired | (186) | (219) |
| Goodwill (Note 12) | | 1,374 |
| **Total acquisition cost** | | **1,155** |
| **Net cash outflow arising from the acquisition for the year ended 31 December 2009** | | **1,135** |

* Russian GAAP numbers are disclosed since IFRS financial statements were not prepared by the entities before acquisition.

The Group assigned provisional values to net assets acquired. The Group will finalise the purchase price allocation within 12 month from the acquisition date.

The purchase consideration comprises cash and cash equivalents paid of USD 871 and directly attributable transactions costs of USD 284.

The goodwill recognised is attributable to expected cost synergies from the business combination.

### *Perfumes Planet*

In December 2009 the Group entered into partnership agreement with Perfumes Planet Switzerland. In accordance with the agreement the Group acquired from Perfumes Planet Switzerland 20% of voting shares in Perfumes Planet Cyprus Limited that will develop perfume selling points in or near Group food retail stores in Moscow, Saint-Petersburg, Nizhny Novgorod and respective regions. At the initial stage perfume selling points will be opened mainly in Moscow and the Moscow region in 2010. The cost of acquisition of associate was insignificant, no significant transactions occurred in 2009.

### *Karusel*

In June 2008 the Group acquired 100% of the voting shares of Formata Holding B.V. Formata Holding B.V. is the owner of the Karusel hypermarket chain ("Karusel"), pursuant to the conditions of the Call Option Agreement, obtained in 2006 as a part of Pyaterochka acquisition. Karusel owns and operates hypermarkets located in St. Petersburg and the North West of Russia, the Moscow region, Nizhny Novgorod, Dzerzhinsk, Volgograd and Izhevsk. As at 30 June 2008 there were 24 hypermarkets operated under the Karusel brand.

During the year ended 31 December 2009 the provisional values were updated as the Group has the final fair value estimates of the independent appraisers. The Group has finalized the purchase price allocation within 12 months from the acquisition date. Details of assets and liabilities acquired and the related goodwill are as follows:

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

| | Acquiree's carrying amount at the acquisition date, Russian GAAP* | Fair values at the acquisition date | Effect of change in purchase price allocation on the Consolidated Statement of Financial Position as at 31 December 2008 |
|---|---|---|---|
| Cash and cash equivalents | 25,699 | 25,699 | - |
| Inventories of goods for resale | 102,509 | 77,956 | (5,082) |
| Loans originated | 612 | 261 | (282) |
| Trade and other accounts receivable | 248,849 | 212,088 | (26,309) |
| Intangible assets | - | 124,610 | - |
| Property, plant and equipment (Note 10) | 492,235 | 943,854 | (56,167) |
| Prepaid lease | 9 | 622 | - |
| Deferred tax assets | 6,994 | 7,052 | - |
| Other assets | 582 | 251 | - |
| Short-term borrowings | (293,492) | (293,492) | - |
| Trade and other accounts payable | (258,384) | (263,236) | (887) |
| Provisions and liabilities for tax uncertainties (Note 34) | - | (56,478) | - |
| Long-term borrowings | (120,985) | (120,986) | - |
| Deferred tax liability | (8,467) | (146,077) | 12,809 |
| Net assets acquired | 196,161 | 512,124 | |
| Goodwill (Note 12) | - | 404,212 | |
| **Total acquisition cost** | - | **916,336** | |
| **Net cash outflow arising from the acquisition for the year ended 31 December 2008** | | **658,927** | |

* Russian GAAP numbers are disclosed since IFRS financial statements were not prepared by the entities before acquisition.

### *Agrotorg Rostov*

In December 2008 the Group acquired 100% of the voting shares of OOO "Agrotorg Rostov" operating retail grocery stores in Rostov-na-Donu and Rostov region. The Group acquired a total of 21 discount stores.

The Group has finalized the purchase price allocation within 12 months from the acquisition date.

Details of assets and liabilities acquired and the related goodwill are as follows:

| | Acquiree's carrying amount at the acquisition date, Russian GAAP* | Fair values at the acquisition date | Effect of change in purchase price allocation on the Consolidated Statement of Financial Position as at 31 December 2008 |
|---|---|---|---|
| Cash and cash equivalents | 77 | 77 | - |
| Inventories of goods for resale | 1,460 | 482 | (601) |
| Trade and other accounts receivable | 1,359 | 390 | (210) |
| Intangible assets | - | 714 | 136 |
| Property, plant and equipment | 15,306 | 11,794 | (2,329) |
| Deferred tax assets | 2,538 | 415 | 415 |
| Trade and other accounts payable | (1,930) | (4,249) | 1,113 |
| Provisions and liabilities for tax uncertainties (Note 34) | - | (583) | - |
| Deferred tax liability | (312) | - | 254 |
| Net assets acquired | 18,498 | 9,040 | |
| Goodwill (Note 12) | | 3,264 | |
| **Total acquisition cost** | - | **12,304** | |
| **Net cash outflow arising from the acquisition for the year ended 31 December 2008** | - | **77** | |
| **Net cash outflow arising from the acquisition for the period ended 31 December 2009** | - | **10,264** | |

* Russian GAAP numbers are disclosed since IFRS financial statements were not prepared by the entities before acquisition.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The purchase consideration comprises cash paid of USD 637, loan of USD 9,625 from “BinBank” assigned to the Group from Agrotorg Rostov and attributable costs of USD 2,042.

***Chelyabinsk and Yekaterinburg***

In June 2009 the purchase option was exercised and the Group increased its shareholding in OOO “Ural-Agro-Torg”, OOO “Leto”, OOO “Ural-Retail” and OOO “Legion” from 75% to 100%. Total acquisition cost comprised of the option utilised of USD 765 and cash paid USD 18,389 in 2009. Goodwill arising on the purchase of the minority amounted to USD 19,154 (Note 12).

***Korzinka***

In November 2007 the Group acquired a 100% shareholding in OOO “Uzhnyi” operating the largest and fastest growing retail chain in the Lipetsk region under “Korzinka” brand. The Group acquired a total of 22 stores. Total acquisition cost amounted to USD 119,439, part of which in the amount of USD 12,071 was paid during the year ended 31 December 2009.

## 8 RELATED PARTY TRANSACTIONS

Parties are generally 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 other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the relationships for those related parties with which the Group entered into significant transactions or had significant balances outstanding at 31 December 2009 are provided below. The ultimate controlling party is disclosed in Note 1.

***Alfa Group***

The following transactions were carried out with members or management of Alfa Group:

| | Relationship | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **CTF Holdings Ltd.** | Ultimate parent company | | |
| Management services received | | 1,178 | 1,302 |
| Recharged expenses | | 749 | 545 |
| **OAO “Alfa-Bank”** | Under common control | | |
| Interest expense on loan received | | 17,970 | 21,578 |
| Interest income | | 1,458 | - |
| Bank Charges | | 1,114 | 1,487 |
| Rent revenue | | 794 | 200 |
| Penalty | | - | 29 |
| **AlfaStrahovanie** | Under common control | | |
| Insurance expenses | | 5 | 14 |
| **VimpelCom** | | | |
| Communication services received | Under significant influence of CTF Holdings Ltd. | 3,585 | 3,601 |
| Commission for mobile phone payments processing rendered by the Group to VimpelCom | | 698 | 765 |
| Rent revenue | | 105 | - |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The consolidated financial statements include the followings balances with members of the Alfa Group:

| | Relationship | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **CTF Holding Ltd.** | Ultimate parent company | | |
| Other accounts payable | | 115 | - |
| **OAO "Alfa-Bank"** | Under common control | | |
| Cash and cash equivalents | | 208,610 | 17,237 |
| Receivable from related party | | 277 | 118 |
| Short-term loans payable | | 75,000 | 168,480 |
| Other accounts payable | | 112 | 570 |
| **AlfaStrahovanie** | Under common control | | |
| Receivable from related party | | 1,098 | 493 |
| Other accounts payable | | 10 | - |
| **VimpelCom** | | | |
| Receivable from related party | Under significant influence of CTF Holdings Ltd. | 512 | 945 |
| Other accounts payable | | 536 | 439 |

### *Alfa-Bank*

The Group has an open credit line with Alfa-Bank with a maximum limit of RUR 9,100 mln or USD 300,884 (31 December 2008: RUR 9,100 mln or USD 309,730). At 31 December 2009 the Group's liability under this credit line amounted to USD 75,000 with interest rates of 3.60 - 3.86% p.a. (31 December 2008: USD 168,480) and available credit line of USD 225,884 (31 December 2008: USD 141,250).

### *Retail Express Ltd. (associate of the Group)*

The following transactions were carried out with Retail Express Ltd.:

| | Relationship | 2009 | 2008 |
|---|---|---|---|
| **Retail Express Ltd.** | | | |
| Trade revenue | associate of the Group | 7,625 | - |
| Other operating income | | 143 | - |
| Rent revenue | | 106 | - |
| Interest income | | 25 | 37 |

The consolidated financial statements include the followings balances with Retail Express Ltd.:

| | Relationship | 2009 | 2008 |
|---|---|---|---|
| **Retail Express Ltd.** | | | |
| Loans and receivables | associate of the Group | 3,213 | 27 |
| Trade payables | | 594 | - |
| Investment in associate | | 5,609 | 10,054 |

At 31 December 2009 and for the year then ended summarised financial information of Retail Express Ltd., including total assets, liabilities, revenue and loss, were as follows:

| | 2009 | 2008 |
|---|---|---|
| Assets | 31,338 | 59,220 |
| Liabilities | (18,674) | (35,463) |
| Revenue for the period | 60,464 | 12,153 |
| Loss for the period | (9,909) | (1,618) |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

### *Key management personnel compensation*

Key management personnel compensation is disclosed in Note 27.

## 9 CASH AND CASH EQUIVALENTS

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Cash in hand – Roubles | 22,930 | 18,742 |
| Cash in hand – Ukrainian Hryvnia | 188 | 196 |
| Bank current account – Roubles | 252,956 | 72,576 |
| Bank current account – Ukrainian Hryvnia | 13 | - |
| Bank current accounts and deposits – US Dollars | 5,286 | 45,598 |
| Cash in transit – Roubles | 70,477 | 63,397 |
| Cash in transit – Ukrainian Hryvnia | 632 | 554 |
| Short term deposits - Roubles | 54,820 | 72,000 |
| Other cash equivalents | 4,379 | 3,774 |
| | **411,681** | **276,837** |

The bank accounts represent current accounts. Interest income on overnights/term deposits is immaterial. Cash in transit is cash transferred from retail outlets to bank accounts and bank card payments being processed.

The Group assesses credit quality of outstanding cash and cash equivalents balances as high and considers that there is no significant individual exposure. Maximum exposure to credit risk at the reporting date is the carrying value of cash and bank balances.

Credit quality of cash and cash equivalents balances are summarized as follows (current ratings):

| Bank | Moody's | Fitch | S&P | 31 December 2009 | 31 December 2008 |
|---|---|---|---|---|---|
| Alfa-Bank | Ba1 | BB- | B+ | 208,610 | 17,237 |
| Raiffeisenbank | Baa3 | BBB+ | BBB- | 20,314 | 140,568 |
| Sberbank | Baa1 | BBB | - | 51,273 | 28,243 |
| VTB | Baa1 | BBB | BBB | 19,031 | 1,889 |
| Other banks | | | | 13,847 | 1,995 |
| Cash in transit and in hand | | | | 94,227 | 82,889 |
| Other monetary assets | | | | 4,379 | 4,016 |
| **Total** | | | | **411,681** | **276,837** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

# 10 PROPERTY, PLANT AND EQUIPMENT

| | Land and buildings | Machinery and equipment | Refrigerating equipment | Vehicles | Other | Construction in progress | Total |
|---|---|---|---|---|---|---|---|
| **Cost**: | | | | | | | |
| At 1 January 2008 | 1,532,179 | 186,974 | 125,169 | 30,396 | 129,923 | 233,997 | 2,238,638 |
| Additions | 175,310 | 7,875 | 1,800 | 263 | 4,627 | 705,989 | 895,864 |
| Transfers | 415,159 | 73,567 | 46,526 | (1,452) | (43,191) | (513,419) | (22,810) |
| Assets from acquisitions (Note 7) | 795,286 | 57,819 | 22,215 | 283 | 18,044 | 72,670 | 966,317 |
| Disposals | (4,233) | (2,340) | (737) | (501) | (2,393) | (179) | (10,383) |
| Translation movement | (495,517) | (53,843) | (32,562) | (4,756) | (18,543) | (83,282) | (688,503) |
| At 31 December 2008 | 2,418,184 | 270,052 | 162,411 | 24,233 | 88,467 | 415,776 | 3,379,123 |
| Additions | 26,784 | 10,840 | 1,901 | 5,086 | 3,546 | 112,866 | 161,023 |
| Transfers | 135,435 | 87,038 | 18,292 | 4,710 | 23,680 | (276,673) | (7,518) |
| Assets from acquisitions (Note 7) | 100,677 | 6,140 | 11,981 | 3 | 500 | 6,998 | 126,299 |
| Disposals | (3,251) | (3,748) | (1,167) | (32) | (642) | (410) | (9,250) |
| Translation movement | (60,682) | (6,561) | (3,863) | (245) | (2,258) | (20,807) | (94,416) |
| At 31 December 2009 | 2,617,147 | 363,761 | 189,555 | 33,755 | 113,293 | 237,750 | 3,555,261 |
| **Accumulated depreciation:** | | | | | | | |
| At 1 January 2008 | (99,217) | (68,084) | (33,488) | (2,923) | (44,368) | - | (248,080) |
| Charge for the year | (88,082) | (37,086) | (23,069) | (3,752) | (6,081) | - | (158,070) |
| Disposals | 629 | 620 | 512 | 306 | 660 | - | 2,727 |
| Translation movement | 26,388 | 16,621 | 9,024 | 336 | 10,975 | - | 63,344 |
| At 31 December 2008 | (160,282) | (87,929) | (47,021) | (6,033) | (38,814) | - | (340,079) |
| Charge for the year | (108,387) | (45,490) | (21,131) | (4,898) | (21,696) | (20,187) | (221,789) |
| Disposals | 222 | 1,600 | 449 | 16 | 560 | - | 2,847 |
| Translation movement | (1,540) | 807 | 420 | (35) | 428 | (991) | (911) |
| At 31 December 2009 | (269,987) | (131,012) | (67,283) | (10,950) | (59,522) | (21,178) | (559,932) |
| **Net book value at 31 December 2009** | **2,347,160** | **232,749** | **122,272** | **22,805** | **53,771** | **216,572** | **2,995,329** |
| **Net book value at 31 December 2008** | **2,257,902** | **182,123** | **115,390** | **18,200** | **49,653** | **415,776** | **3,039,044** |
| **Net book value at 1 January 2008** | **1,432,962** | **118,890** | **91,681** | **27,473** | **85,555** | **233,997** | **1,990,558** |

Construction in progress predominantly relates to the development of stores through the use of sub-contractors.

The buildings are mostly located on leased land. Land leases with periodic lease payments are disclosed as part of commitments under operating leases (Note 34). Certain land leases are prepaid for a 49 year term. Such prepayments are presented as prepaid leases in the consolidated statement of financial position and amount to USD 98,510 (31 December 2008: USD 90,831)

### *Impairment Test*

At the end of 2009 management performed a regular impairment test of land, buildings and construction in progress. The evaluation for long-lived assets is performed at the lowest level of identifiable cash flows, which is generally at the individual store level. The variability of these factors depends on a number of conditions, including uncertainty about future events and changes in demand.

An impairment review has been carried out by comparing recoverable amount of the individual store with their carrying values. The recoverable amount of store is determined as the higher of fair value less cost to sell or value in use.

*Fair value less costs to sell*

The Group defines fair value less costs to sell of the item of land and buildings and construction in progress by reference to current observable prices on an active market.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

*Value in use*
Discounted free cash flow approach is applied and covered a 10 year period from 2010. The free cash flows are based on the current budgets and forecasts approved by key management. For the subsequent years, the data of the strategic plan are extrapolated based on the consumer price indices as obtained from external resources and key performance indicators inherent to the strategic plan. The projections are made in the functional currency of the Group and discounted at the Group weighted average cost of capital (12%-16%). EBITDA growth rate used for projections was 8.1%, inflation rates are inline with consumer price index forecast published by Ministry of Economical Development of Russian Federation. The Group's management believes that all of its estimates are reasonable and consistent with the internal reporting and reflect management's best estimates.

The result of applying discounted cash flows model reflects expectations about possible variations in the amount and timing of future cash flows and is based on reasonable and supportable assumptions that represent management's best estimate of the range of uncertain economic conditions.

*Impairment Test*
The carrying amount of the stores exceeded their recoverable amount and impairment loss was recognised in amount of USD 48,253 included in depreciation expense.

| | Useful lives |
|---|---|
| Land and buildings | 28,066 |
| Construction in progress | 20,187 |
| **Total** | **48,253** |

## 11 INVESTMENT PROPERTY

The Group held the following investment properties at 31 December 2009 and 31 December 2008:

| Cost | 2009 | 2008 |
|---|---|---|
| Cost at 1 January | 130,997 | 132,595 |
| Additions | 8,574 | 3,034 |
| Transfer from fixed assets | 7,518 | 22,810 |
| Translation movement | (2,953) | (27,442) |
| Cost at 31 December | 144,136 | 130,997 |
| **Accumulated depreciation:** | | |
| Accumulated depreciation at 1 January | (5,304) | (3,589) |
| Charge for the year | (5,299) | (4,668) |
| Translation movement | (108) | 2,953 |
| Accumulated depreciation at 31 December | (10,711) | (5,304) |
| **Net book value at 31 December** | **133,425** | **125,693** |
| **Net book value at 1 January** | **125,693** | **129,006** |

Rental income from investment property amounted to USD 22,967 (2008: USD 22,141). Direct operating expenses incurred by the Group in relation to investment property amounted to USD 7,759 (2008: 6,271).

Management estimates that the fair value of investment property at 31 December 2009 amounted to USD 164,641 (31 December 2008: USD 130,844).

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

# 12 GOODWILL

Movements in goodwill arising on the acquisition of subsidiaries at 31 December 2009 and 31 December 2008 are:

| Cost | 2009 | 2008 |
|---|---|---|
| Gross book value at 1 January | 2,811,579 | 2,955,625 |
| Acquisition of subsidiaries (Note 7) | 236,999 | 425,294 |
| Translation to presentation currency | (88,498) | (569,340) |
| Gross book value at 31 December | 2,960,080 | 2,811,579 |
| **Accumulated impairment losses:** | | |
| Accumulated impairment losses at 1 January | (2,257,020) | - |
| Translation to presentation currency | 64,463 | - |
| Accumulated impairment losses at 31 December | (2,192,557) | (2,257,020) |
| **Carrying amount at 31 December** | **767,523** | **554,559** |
| **Carrying amount at 1 January** | **554,559** | **2,955,625** |

### *Goodwill Impairment Test*

Goodwill is monitored for internal management purposes at the segment level being retail trading in Russia (CGU).

Goodwill is tested for impairment at the CGU level by comparing carrying values of CGU assets to their recoverable amounts. The recoverable amount of CGU is determined as the higher of fair value less cost to sell or value in use.

*Fair value less costs to sell*

The Group defines fair value less costs to sell of the CGU by reference to an active market, i.e. as a market capitalization of the Group on the London Stock Exchange, since the Group's activities other than retail trade in Russia do not have a significant effect on the fair value. For indication purposes fair value less costs to sell of the CGU will be lower than its carrying amount if the share price falls below the level of USD 26.14 per share. The market capitalization of the Group at 31 December 2009 amounted to USD 8,653,060 significantly exceeded the carrying amount of the CGU.

*Value in use*

Discounted free cash flow approach was utilized. For the 10 year period from 2010 the free cash flows are based on the current budgets and forecasts approved by key management. For the subsequent years, the data of the strategic plan are extrapolated based on the consumer price indices as obtained from external resources and based on key performance indicators inherent to the strategic plan. The projections are made in the functional currency of the Group and discounted at the Group weighted average cost of capital (12%-16%). EBITDA growth rate used for projections was 8.1%, inflation rates are inline with consumer price index forecast published by Ministry of Economical Development of Russian Federation. The Group's management believes that all of its estimates are reasonable and consistent with the internal reporting and reflect management's best estimates.

Model applied for impairment testing is not sensitive to assumptions used by management because fair value less cost to sell and value in use are significantly greater than carrying values of cash generating unit assets.

The result of applying discounted cash flows model reflects expectations about possible variations in the amount and timing of future cash flows and is based on reasonable and supportable assumptions that represent management's best estimate of the range of uncertain economic conditions.

*Impairment Test*

The recoverable amount of CGU exceeded its carrying amount therefore no impairment was recognised.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 13 INTANGIBLE ASSETS

Intangible assets comprise the following:

| | Brand and private labels | Franchise agreements | Software and other | Lease rights | Total |
|---|---|---|---|---|---|
| **Cost:** | | | | | |
| At 1 January 2008 | 358,849 | 76,727 | 6,580 | 139,518 | 581,674 |
| Additions | - | - | 8,361 | - | 8,361 |
| Acquisition of subsidiaries (Note 7) | 124,196 | - | 437 | 8,137 | 132,770 |
| Disposals | (1,294) | (271) | - | - | (1,565) |
| Translation movement | (83,186) | (12,583) | (2,456) | (24,632) | (122,857) |
| At 31 December 2008 | 398,565 | 63,873 | 12,922 | 123,023 | 598,383 |
| Additions | - | - | 31,022 | - | 31,022 |
| Acquisition of subsidiaries (Note 7) | 2,176 | 670 | 926 | 18,909 | 22,681 |
| Disposals | (780) | (1,431) | - | - | (2,211) |
| Translation movement | (11,508) | (1,920) | 1,147 | (4,271) | (16,552) |
| At 31 December 2009 | 388,453 | 61,192 | 46,017 | 137,661 | 633,323 |
| **Accumulated amortisation:** | | | | | |
| At 1 January 2008 | (30,125) | (12,910) | (5,881) | (8,513) | (57,429) |
| Charge for the year | (23,077) | (20,982) | (4,526) | (13,914) | (62,499) |
| Disposals | 1,293 | - | - | - | 1,293 |
| Translation movement | 7,677 | 5,356 | 2,953 | 3,590 | 19,576 |
| At 31 December 2008 | (44,232) | (28,536) | (7,454) | (18,837) | (99,059) |
| Charge for the year | (21,196) | (8,775) | (1,887) | (9,297) | (41,155) |
| Disposals | 780 | 1,431 | - | - | 2,211 |
| Translation movement | 266 | 455 | (40) | 110 | 791 |
| At 31 December 2009 | (64,382) | (35,425) | (9,381) | (28,024) | (137,212) |
| **Net book value at 31 December 2009** | **324,071** | **25,767** | **36,636** | **109,637** | **496,111** |
| **Net book value at 31 December 2008** | **354,333** | **35,337** | **5,468** | **104,186** | **499,324** |
| **Net book value at 1 January 2008** | **328,724** | **63,817** | **699** | **131,005** | **524,245** |

## 14 INVENTORIES OF GOODS FOR RESALE

Inventories of goods for resale as of 31 December 2009 and 31 December 2008 comprise the following:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Inventories of goods for resale | 675,886 | 502,350 |
| Less: provision for shrinkage and slow moving stock | (63,164) | (25,875) |
| | **612,722** | **476,475** |

Provision for inventory shrinkage and slow moving stock recognised as cost of sales in the consolidated income statement amounted to USD 191,287 (2008: USD 134,292).

## 15 FINANCIAL INSTRUMENTS BY CATEGORY

| | Loans and receivables | Financial assets at fair value through profit and loss | Total |
|---|---|---|---|
| **31 December 2009** | | | |
| **Assets as per consolidated statement of financial position** | | | |
| Trade and other receivables excluding prepayments | 214,713 | - | 214,713 |
| Loans originated | 2,848 | - | 2,848 |
| Cash and cash equivalents | 411,681 | - | 411,681 |
| **Total** | 629,242 | - | 629,242 |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

| | Derivatives used for hedging | Financial liabilities at amortised cost | Total |
|---|---|---|---|
| **31 December 2009** | | | |
| **Liabilities as per consolidated statement of financial position** | | | |
| Borrowings (excluding finance lease liabilities) | - | 1,944,000 | 1,944,000 |
| Interest accrued | - | 8,863 | 8,863 |
| Finance lease liabilities | - | 6,536 | 6,536 |
| Derivative financial instruments | 10,108 | - | 10,108 |
| Trade and other payables excluding statutory liabilities and advances | - | 1,840,822 | 1,840,822 |
| **Total** | **10,108** | **3,800,221** | **3,810,329** |

| | Loans and receivables | Financial assets at fair value through profit and loss | Total |
|---|---|---|---|
| **31 December 2008** | | | |
| **Assets as per consolidated statement of financial position** | | | |
| Derivative financial instruments | - | 765 | 765 |
| Trade and other receivables excluding prepayments | 79,592 | - | 79,592 |
| Loans originated | 350 | - | 350 |
| Cash and cash equivalents | 276,837 | - | 276,837 |
| **Total** | **356,779** | **765** | **357,544** |

| | Derivatives used for hedging | Financial liabilities at amortised cost | Total |
|---|---|---|---|
| **31 December 2008** | | | |
| **Liabilities as per consolidated statement of financial position** | | | |
| Borrowings (excluding finance lease liabilities) | - | 2,059,401 | 2,059,401 |
| Interest accrued | | 8,384 | 8,384 |
| Finance lease liabilities | - | 4,040 | 4,040 |
| Derivative financial instruments | 18,180 | - | 18,180 |
| Trade and other payables excluding statutory liabilities and advances | - | 1,433,735 | 1,433,735 |
| **Total** | **18,180** | **3,505,560** | **3,523,740** |

## 16 TRADE AND OTHER ACCOUNTS RECEIVABLE

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Trade accounts receivable | 214,403 | 69,921 |
| Advances made to trade suppliers | 25,752 | 22,150 |
| Other receivables | 19,320 | 12,785 |
| Prepayments | 69,106 | 74,571 |
| Accounts receivable for franchise services | 1,814 | 61 |
| Receivables from related parties (Note 8) | 5,290 | 9,719 |
| Provision for impairment of trade and other receivables | (26,114) | (12,894) |
| | **309,571** | **176,313** |

All classes of receivables are categorized as loans and receivables under IAS 39 classification.

The carrying amounts of the Group's trade and other receivables are primarily denominated in Russian Roubles.

*Trade receivables*

There are balances of USD 27,715 that in accordance with accounting policies are past due but not impaired as at 31 December 2009 (31 December 2008: USD 12,997).

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The ageing of these receivables based on days outstanding is as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| 2-6 months | 23,313 | 10,840 |
| Over 6 months | 4,402 | 2,157 |
| | **27,715** | **12,997** |

Movements on the provision for impairment of trade receivables are as follows:

| | 2009 | 2008 |
|---|---|---|
| **At 1 January** | (11,233) | (5,787) |
| Accrual of provision for receivables impairment | (12,020) | (10,014) |
| Release of provision for receivables impairment | 9,821 | 2,861 |
| Translation movement | 313 | 1,707 |
| **At 31 December** | **(13,119)** | **(11,233)** |

The creation and release of the provision for impaired receivables have been included in general and administrative costs in the consolidated income statement.

The individually impaired trade receivables mainly relate to debtors that expect financial difficulties or there is likelihood of the debtor's insolvency. It was assessed that a portion of the receivables is expected to be recovered.

The ageing of amounts receivable that are individually impaired based on days outstanding is as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| 3-6 months | 643 | 1,843 |
| Over 6 months | 12,476 | 9,390 |
| | **13,119** | **11,233** |

For those receivables that are neither past due nor impaired the Group considers the credit quality as high. Trade receivables are mainly bonuses from suppliers of goods for resale receivable on quarterly basis with a low historic default rate. The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivable mentioned above. The Group does not hold any collateral as security.

*Other receivables and receivables for franchise services*

There are balances of USD 4,961 that in accordance with accounting policies are past due but not impaired as at 31 December 2009 (31 December 2008: USD 6,945).

The ageing of these receivables based on days outstanding is as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| 2-6 months | 3,522 | 3,058 |
| Over 6 months | 1,439 | 3,887 |
| | **4,961** | **6,945** |

Movements on the provision for impairment of other receivables are as follows:

| | 2009 | 2008 |
|---|---|---|
| **At 1 January** | (1,661) | (1,789) |
| Accrual of provision for receivables impairment | (11,639) | (276) |
| Release of provision for receivables impairment | 883 | 79 |
| Translation movement | (578) | 325 |
| **At 31 December** | **(12,995)** | **(1,661)** |

The creation and release of the provision for impaired receivables has been included in general and administrative costs in the consolidated income statement.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The individually impaired other receivables mainly relate to debtors that expect financial difficulties or there is likelihood of the debtor's insolvency. It was assessed that a portion of the receivables are expected to be recovered.

The ageing of amounts receivable that are individually impaired based on days outstanding is as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| 3-6 months | 461 | 344 |
| Over 6 months | 12,534 | 1,317 |
| | **12,995** | **1,661** |

For those receivables that are neither past due nor impaired the Group considers the credit quality as high. The maximum exposure to credit risk at the reporting date is the carrying amount of each class of receivable mentioned above. The Group does not hold any collateral as security.

## 17 VAT AND OTHER TAXES RECOVERABLE

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| VAT recoverable | 161,397 | 234,339 |
| Other taxes recoverable | 13,365 | 5,079 |
| | **174,762** | **239,418** |

VAT recoverable related to property, plant and equipment of USD 20,542 (31 December 2008: USD 59,868) is recorded within current assets because management expects it will be recovered within 12 months after the balance sheet date. Timing of the VAT refund depends on the registration of certain property, plant and equipment, therefore there are risks that recovering the balance may take longer than twelve months.

## 18 DERIVATIVES

As at 31 December 2008 call option for a 25% share in subsidiaries in the amount of USD 765 was recognized. The option was utilized in 2009 (Note 7).

The Group applied hedge accounting to interest rate swaps initiated in 2008 and in 2009 (Note 30). As at 31 December 2009 the negative fair value of the interest rate swaps of USD 10,108 was recognised in Equity (31 December 2008: USD 18,180).

## 19 PROVISIONS AND OTHER LIABILITIES

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Taxes other than income tax | 61,961 | 51,012 |
| Provisions and liabilities for tax uncertainties (Note 34) | 147,087 | 110,619 |
| Accrued salaries and bonuses | 102,653 | 99,600 |
| Payables to landlords | 6,462 | 4,747 |
| Other accounts payable and accruals | 141,004 | 115,128 |
| Accounts payable for services received | 16,244 | 17,701 |
| Accounts payable for property, plant and equipment | 18,134 | 21,280 |
| Advances received | 40,161 | 37,403 |
| | **533,706** | **457,490** |

There are no significant amounts of payables to foreign counterparties as at 31 December 2009 and 31 December 2008.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

# 20 BORROWINGS

| | | 31 December 2009 | | |
|---|---|---|---|---|
| | Interest rate, % p.a. | Current During 1 year | Non-current In 1 to 3 years | Total |
| USD Syndicated loan | USD Libor+1.5% | 1,093,135 | - | 1,093,135 |
| USD Bilateral Loans | 3.6%-3.86% | 75,000 | - | 75,000 |
| RUR Bonds | 7.6% - 18.46% | 297,390 | 262,403 | 559,793 |
| RUR Bilateral Loans | Mosprime +3.1% - +4.25% | 57,874 | 24,972 | 82,846 |
| RUR Bilateral Loans | 15.25%-19% | 133,223 | 3 | 133,226 |
| **Total borrowings** | | **1,656,622** | **287,378** | **1,944,000** |

| | | 31 December 2008 | | |
|---|---|---|---|---|
| | Interest rate, % p.a. | Current During 1 year | Non-current In 1 to 3 years | Total |
| USD Syndicated loan | USD Libor+1.5% | - | 1,087,617 | 1,087,617 |
| USD Bilateral Loans | USD Libor + 1,4% - 4% | 200,000 | - | 200,000 |
| RUR Bonds | 7,6% - 12% | 5,919 | 304,986 | 310,905 |
| RUR Bilateral Loans | Mosprime +3,1% | 9,494 | 35,201 | 44,695 |
| RUR Bilateral Loans | 7.57%-19.6% | 363,020 | 53,164 | 416,184 |
| **Total borrowings** | | **578,433** | **1,480,968** | **2,059,401** |

In December 2007 the Group raised a 3 year syndicated loan facility of USD 1,100,000 from a consortium of banks. The margin for the first year was 2.25% per annum over USD LIBOR. In December 2008 the margin changed from 2.25% to 1.5% in accordance with an agreed the Net Debt/EBITDA grid. LIBOR is fixed from a one to six month period. The Group has pledged as collateral for the syndicated loan 100% of the voting shares in its subsidiaries, including OOO “Agrotorg”, OOO “Agroaspekt”, Perekrestok Holdings Ltd., Alpegru Retail Properties Ltd., ZAO “TH “Perekrestok”, OOO “Perekrestok-2000” and ZAO “X5 Nedvizhimost”. In November 2009 X5 Retail Group and Sberbank reached agreement on a “forward-start” committed credit facility for refinancing of USD 1,100,000 syndicated loan with December 2010 maturity. In January 2010 X5 Retail Group and Sberbank finalized documentation of this credit facility. Refinancing will be in the form of 5-year rouble denominated committed credit facility up to USD 1,100,000 (in RUR equivalent, based on the exchange rate of the CBR as at the draw down date). The credit facility may be utilized in several tranches with varying maturities.

In July 2007 the Group placed RUR 9 bn (USD 297,578) corporate bonds with a maturity of 7 years including a put option exercisable at the option of the bond holder, in 3 years. Coupons 1 to 6 were fixed at the level of 7.60% per annum, with the remaining coupon level to be defined by the Group later.

In June 2009 the Group placed RUR 8 bn (USD 264,463) corporate bonds with a maturity of 7 years including a put option exercisable at the option of the bond holder, in 2 years. Coupon rates for 5-14 coupon payments are defined by the Issuer, according to issue documents.

All borrowings at 31 December 2009 are shown net of related transaction costs of USD 10,056 which are amortised over the term of loans using the effective interest method (31 December 2008: USD 13,726).

In accordance with the syndicated loan facility agreement the Group maintains an optimal capital structure by tracking certain capital requirements: the maximum level of Debt/EBITDA (4.25), minimum level of EBITDA/Interest expense (3), minimum level of EBITDAR/Fixed costs (2.25) and required level of capital expenditure.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 21 SHARE CAPITAL

As at 1 January 2008 the Group had 942,278 ordinary shares held as treasury stock. The nominal par value of each ordinary share is EUR 1.

In May 2008 the Group completed an offering of rights to acquire Global Depositary Receipts, following the decision of the Supervisory Board authorized by the Extraordinary General Meeting of Shareholders. As part of the Public Offering the Company issued an additional 12,026,675 ordinary shares for USD 999,454 and sold 942,278 treasury shares (total cash inflow of USD 143,336 comprised of USD 131,919 cash receipt for the sale of treasury shares and a make-whole payment of USD 11,417 received by the Group as compensation related to the Public Offering). Transaction costs relating to issue of share capital deducted from shareholder's equity amounted to USD 26,164.

As part of the acquisition of Karusel in June 2008 the Group issued an additional 1,746,505 ordinary shares which were transferred to Karusel shareholders in exchange for 25% shares of Formata.

As at 31 December 2009 the Group had 190,000,000 authorized ordinary shares of which 67,813,947 ordinary shares are outstanding and 79,271 ordinary shares held as treasury stock.

No dividends were paid or declared during the year ended 31 December 2009 and the year ended 31 December 2008.

## 22 EARNINGS PER SHARE

Basic earnings per share are calculated by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of ordinary shares in issue during the year, excluding treasury shares.

Earnings per share are calculated as follows:

| | 2009 | 2008 |
|---|---|---|
| Profit/(Loss) attributable to equity holders of the Parent | 165,351 | (2,138,287) |
| Weighted average number of ordinary shares in issue | 67,813,947 | 63,928,885 |
| Effect of share options granted to employees | 149,281 | - |
| Weighted average number of ordinary shares for the purposes of diluted earnings per share | 67,963,228 | 63,928,885 |
| **Basic earnings/(losses) per share for profit from continuing operations (expressed in USD per share)** | **2.44** | **(33.45)** |
| **Diluted earnings/(losses) per share for profit from continuing operations (expressed in USD per share)** | **2.43** | **(33.45)** |

## 23 REVENUE

| | 2009 | 2008 |
|---|---|---|
| Revenue from sale of goods | 8,683,821 | 8,319,821 |
| Revenue from franchise services | 8,060 | 11,029 |
| Revenue from other services | 25,518 | 22,400 |
| | **8,717,399** | **8,353,250** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 24 EXPENSES BY NATURE

| | 2009 | 2008 |
|---|---|---|
| Cost of goods sold | 6,409,199 | 6,044,109 |
| Staff costs (Note 27) | 855,189 | 858,813 |
| Operating lease expenses | 267,857 | 260,161 |
| Depreciation, amortisation and impairment | 268,243 | 225,238 |
| Other store costs | 150,760 | 165,114 |
| Utilities | 159,577 | 134,789 |
| Other | 239,301 | 216,624 |
| Before Goodwill Impairment | **8,350,126** | **7,904,848** |
| Goodwill Impairment | - | 2,257,020 |
| **After Goodwill Impairment** | **8,350,126** | **10,161,868** |

Operating lease expenses include USD 248,379 (2008: USD 243,030) of minimum lease payments and contingent rents of USD 19,478 (2008: USD 17,131).

Provision for impairment of trade and other receivables amounted to USD 12,955 for the year ended 31 December 2009 (2008: USD 7,350).

## 25 OPERATING LEASE INCOME

The Group leases part of its store space to companies selling supplementary goods and services to customers. The lease arrangements are operating leases, the majority of which are short-term. The future minimum lease payments receivable under non-cancellable operating leases are as follows:

| | 2009 | 2008 |
|---|---|---|
| Not later than 1 year | 40,072 | 44,692 |
| Later than 1 year and no later than 5 years | 17,726 | 18,544 |
| Later than 5 years | 7,965 | 5,343 |
| | **65,763** | **68,579** |

The rental income from operating leases recognised in the consolidated income statement amounted to USD 92,391 (2008: USD 89,918). There were no contingent rents recognised in the consolidated income statement in the year ended 31 December 2009 (2008: nil).

## 26 FINANCE INCOME AND COSTS

| | 2009 | 2008 |
|---|---|---|
| Interest expense | 148,275 | 149,723 |
| Interest income | (3,817) | (10,511) |
| Other finance costs, net | 9,689 | 9,293 |
| | **154,147** | **148,505** |

Other finance costs include transaction costs of USD 6,950 written-off to the consolidated income statement (2008: USD 5,158) (Note 20).

## 27 STAFF COSTS

| | 2009 | 2008 |
|---|---|---|
| Wages and salaries | 662,947 | 729,556 |
| Social security costs | 132,926 | 131,708 |
| Share-based payments expense | 59,316 | (2,451) |
| | **855,189** | **858,813** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

*Key executive management personnel*

X5's key management personnel consists of Management Board and Supervisory Board members, having authority and responsibility for planning, directing and controlling the activities of the Company as a whole. Members of the Management Board and Supervisory Board of the Group receive compensation in the form of a short-term compensation in cash (including, for Management Board members, a cash bonus) and share-based payments (Note 28). For the year ended 31 December 2009 members of the Management Board and Supervisory Board of the Group were entitled to total short-term compensation of USD 6,524 (2008: USD 6,793), including bonuses of USD 2,060 (2008: USD 2,871). The compensation is made up of annual remuneration and a performance bonus depending on, inter alia, operating results. As at 31 December 2009 the total amount of GDRs for which options were granted to members of the Management Board and Supervisory Board under the ESOP was 3,187,500 (31 December 2008: 2,814,375 GDRs). The total intrinsic value of vested share options amounted to USD 1,245 as at 31 December 2009 (31 December 2008: zero).

## 28 SHARE-BASED PAYMENTS

In 2007 the Group introduced an employee stock option program (ESOP) for its key executives and employees. Each option that may be granted under the ESOP carries the right to one GDR. The program ran in four tranches granted over the period to 19 May 2009. The vesting requirement of the program is the continued employment of participants.

The first and second tranches were approved for granting at 15 June 2007. The first tranche vested immediately and covered the period of service of option holders from 1 January 2007 to 15 June 2007. The second tranche vested on 18 May 2008. The exercise prices of the first and second tranches were USD 15.96 and USD 28.58 per GDR , respectively. In May 2008 the third tranche was granted at the exercise price of USD 33.43. The third tranche vested on 19 May 2009. In May 2009 the fourth tranche was granted at the exercise price of USD 13.91. The fourth tranche will vest on 19 May 2010. Participants of the ESOP can exercise their share options granted under first, second, third and fourth tranches over the period from vesting until 19 November 2010, 16 December 2011, 20 November 2012 and 20 November 2013 respectively, at any time except black-out periods defined by Group's Code of Conduct of Insider Dealing. The maximum number of GDRs under the ESOP was 11,261,264 GDRs.

In total, during the year ended 31 December 2009 the Group recognized an expense related to the ESOP in the amount of USD 59,316 (income during the year ended 31 December 2008: USD 2,451). At 31 December 2009 the share-based payments liability amounted to USD 85,545 (31 December 2008: USD 37,921). The equity component was effectively zero at 31 December 2009 (31 December 2008: zero).

Details of the share options outstanding during the year ended 31 December 2009 are as follows:

| | Number of share options | Weighted average exercise price, USD |
|---|---|---|
| Outstanding at the beginning of the period | 5,704,825 | 28.9 |
| Granted during the period | 3,203,875 | 13.9 |
| Exercised during the period | (830,000) | 16.3 |
| Cancelled during the period | (491,750) | 23.2 |
| **Outstanding at the end of the period** | **7,586,950** | **24.4** |
| Exercisable at 31 December 2009 | 4,484,325 | 31.6 |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

The total intrinsic value of vested share options amounted to USD 2,538 as at 31 December 2009 (31 December 2008: zero).

The fair value of services received in return for the share options granted to employees is measured by reference to the fair value of the share options granted which is determined at each reporting date. The estimate of the fair value of the services received is measured based on the Black-Scholes model. Expected volatility is determined by calculating the historical volatility of the Group's share price over the period since May 2006. Management assumes that holders will exercise the options on the expiry date of the options due to behavioural considerations. Other key inputs to the calculation of ESOP liability at 31 December 2009 were as follows:

| | |
|---|---|
| Expected GDR price | 30.06 |
| Expected volatility | 73% |
| Risk-free interest rate | 3% |
| Dividend yield | 0% |

## 29 INCOME TAX

| | Year ended 31 December 2009 | Year ended 31 December 2008 |
|---|---|---|
| Current income tax charge | 168,438 | 178,244 |
| Deferred income tax benefit | (69,823) | (129,196) |
| Deferred tax benefit resulting from reduction in tax rate** | - | (40,942) |
| **Income tax charge for the year** | **98,615** | **8,106** |

The theoretical and effective tax rates are reconciled as follows:

| | Year ended 31 December 2009 | Year ended 31 December 2008 |
|---|---|---|
| Profit/(Loss) before taxation | 263,966 | (2,130,181) |
| Theoretical tax at the effective statutory rates * | 52,793 | (511,243) |
| Tax effect of items which are not deductible or assessable for taxation purposes: | | |
| Goodwill impairment | - | 541,492 |
| Reduction in deferred taxes closing balance resulting from reduction in tax rate** | - | (40,942) |
| Share-based payments expenses | 2,561 | 517 |
| Effect of income taxable at rates different from standard statutory rates | 9,283 | 40,043 |
| Effect of different tax regime in parent company | (3,169) | (38,590) |
| Recognition of DT asset on prior losses for which no DT asset was previously recognised | (7,225) | (20,356) |
| Expenses on inventory shrinkage and surpluses | 37,409 | 42,530 |
| Other non-deductible expenses and non-taxable income | 6,963 | (5,345) |
| Income tax charge for the year | **98,615** | **8,106** |

* Profit before taxation on Russian operations is assessed based on the statutory rate of 20% (2008: 24%), profit before taxation on Ukrainian operations is assessed based on the statutory rate of 25%.
** An income tax rate of 20% has been enacted in November 2008 which becomes effective starting from 1 January 2009.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## Deferred income tax

Deferred tax assets and liabilities and the deferred tax charge in the consolidated income statement are attributable to the following items for the year ended 31 December 2009:

| | 31 December 2008 | Credited to profit and loss | Deferred tax on business combinations (Note 7) | Recognised in equity for translation differences | 31 December 2009 |
|---|---|---|---|---|---|
| **Tax effects of deductible temporary differences and tax loss carryforwards:** | | | | | |
| Tax losses available for carry forward | 51,155 | (6,555) | 14 | (1,782) | 42,832 |
| Property, plant and equipment | 16,273 | 30,379 | - | 1,021 | 47,673 |
| Intangible assets | 396 | (294) | - | (26) | 76 |
| Inventories of goods for resale | 14,832 | 21,156 | 641 | 586 | 37,215 |
| Accounts receivable | 36,896 | (24,773) | 13,100 | (2,780) | 22,443 |
| Accounts payable | 10,810 | 56,346 | 1,020 | 2,407 | 70,583 |
| Other | 11,550 | (636) | 110 | (400) | 10,624 |
| **Gross deferred tax asset** | **141,912** | **75,623** | **14,885** | **(974)** | **231,446** |
| Less offsetting with deferred tax liabilities | (47,354) | (32,306) | - | - | (79,660) |
| **Recognised deferred tax asset** | **94,558** | **43,317** | **14,885** | **(974)** | **151,786** |
| **Tax effects of taxable temporary differences:** | | | | | |
| Property, plant and equipment | (158,698) | 13,139 | (18,742) | 5,911 | (158,390) |
| Intangible assets | (93,118) | (3,745) | (4,533) | 2,655 | (98,741) |
| Inventories of goods for resale | - | (4,025) | - | (197) | (4,222) |
| Accounts receivable | (4,660) | (8,877) | - | (301) | (13,838) |
| Accounts payable | (618) | (531) | | (8) | (1,157) |
| Other | (9,421) | (1,761) | (63) | 244 | (11,001) |
| **Gross deferred tax liability** | **(266,515)** | **(5,800)** | **(23,338)** | **8,304** | **(287,349)** |
| Less offsetting with deferred tax assets | 47,354 | 32,306 | - | - | 79,660 |
| **Recognised deferred tax liability** | **(219,161)** | **26,506** | **(23,338)** | **8,304** | **(207,689)** |

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

### Deferred income tax

Deferred tax assets and liabilities and the deferred tax charge in the consolidated income statement are attributable to the following items for the year ended 31 December 2008:

| | 31 December 2007 | Credited to profit and loss | Deferred tax on business combinations (Note 7) | Recognised in equity for translation differences | 31 December 2008 |
|---|---|---|---|---|---|
| **Tax effects of deductible temporary differences and tax loss carryforwards:** | | | | | |
| Tax losses available for carry forward | 16,713 | 43,968 | - | (9,526) | 51,155 |
| Property, plant and equipment | 7,529 | 13,606 | 656 | (5,518) | 16,273 |
| Intangible assets | 53 | 1,213 | - | (870) | 396 |
| Inventories of goods for resale | 9,206 | 8,441 | - | (2,815) | 14,832 |
| Accounts receivable | 15,157 | 29,012 | 273 | (7,546) | 36,896 |
| Accounts payable | 9,698 | 3,201 | - | (2,089) | 10,810 |
| Liability for share based expenses | 573 | (566) | - | (7) | - |
| Other | 2,615 | 6,192 | 5,184 | (2,441) | 11,550 |
| **Gross deferred tax asset** | **61,544** | **105,067** | **6,113** | **(30,812)** | **141,912** |
| Less offsetting with deferred tax liabilities | (29,923) | (26,000) | (477) | 9,046 | (47,354) |
| **Recognised deferred tax asset** | **31,621** | **79,067** | **5,636** | **(21,766)** | **94,558** |
| **Tax effects of taxable temporary differences:** | | | | | |
| Property, plant and equipment | (125,212) | 46,178 | (115,849) | 36,185 | (158,698) |
| Intangible assets | (108,299) | 21,758 | (26,232) | 19,655 | (93,118) |
| Accounts receivable | (3,298) | (3,853) | 1,718 | 773 | (4,660) |
| Accounts payable | (3,500) | 2,785 | (62) | 159 | (618) |
| Other | (2,936) | (1,797) | (7,868) | 3,180 | (9,421) |
| **Gross deferred tax liability** | **(243,245)** | **65,071** | **(148,293)** | **59,952** | **(266,515)** |
| Less offsetting with deferred tax assets | 29,923 | 26,000 | 477 | (9,046) | 47,354 |
| **Recognised deferred tax liability** | **(213,322)** | **91,071** | **(147,816)** | **50,906** | **(219,161)** |

Temporary differences on unremitted earnings of certain subsidiaries amounted to USD 570,943 (2008: USD 571,164) for which the deferred tax liability was not recognised as such amounts are being reinvested for the foreseeable future.

The current portion of the deferred tax liability amounted to USD 16,730 (31 December 2008: USD 26,369), the current portion of the deferred tax asset amounted to USD 25,280 (31 December 2008: USD 32,650).

Management believes that the future taxable profits in tax jurisdictions that suffered a loss in the current or preceding years will be available to utilise the deferred tax asset of USD 42,832 recognised at 31 December 2009 for the carryforward of unused tax losses (31 December 2008: USD 51,155). Unused tax losses are available for carry forward for a period of 10 years.

## 30 FINANCIAL RISKS MANAGEMENT

The risk management function within the Group is carried out in respect of financial risks (credit, market, geographical and liquidity risks), operational risks and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

Risk management is carried out by a central treasury department (Group Treasury). Group Treasury monitors and measures financial risks and undertakes steps to limit their influence on the Group's performance. In this connection the Group uses certain derivative financial instruments to mitigate financial risk exposures. These instruments are intended to cap foreign currency and interest rate risks associated with the most significant long-term borrowings.

**(a) Market risk**

***Currency risk***

The Group is exposed to foreign exchange risk arising from currency exposure with respect to the US Dollar borrowings. From an operational perspective the Group does not have any substantial currency exposures due to the nature of its operations having all revenues and expenses fixed in the local currency (RUR). All other transactions in foreign currency except for financing arrangements are insignificant.

The Group has a substantial amount of foreign currency denominated long-term borrowings, and is thus exposed to foreign exchange risk (Note 20). In March 2009 as a part of FX risk mitigation policy the Group started using USD/RUB call spreads with leading banking institutions to hedge its short-term cash flows exposed to foreign currency risk. The effect on the consolidated financial statements at 31 December 2009 was immaterial.

As a part of its currency risk mitigation policy the Group attracts new loans and refinances existing ones primarily in the local currency (RUR).

At 31 December 2009, if the Russian Rouble had weakened/strengthened by 20% against the US dollar with all other variables held constant, post-tax profit for the year would have been USD 166,725 (31 December 2008: USD 231,350) lower/higher as a result of foreign exchange losses/gains on USD denominated borrowings and USD 13,614 lower/higher (31 December 2008: USD 623 higher/lower) as a result of foreign exchange losses/gains on share-based payments liability and cash and cash equivalents.

***Interest rates risk***

As the Group has no significant interest-bearing assets, the Group's income and operating cash inflows are substantially independent of changes in market interest rates.

The syndicated loan for USD 1,100,000 was hedged against interest rate risk in 2008 and 2009 (Note 20). The Group regarded the interest rate swaps initiated in 2008 and in 2009 as a hedging instruments and applied hedge accounting (Note 18). The fair value of the interest rate swap of USD 10,108 was recorded through equity.

If LIBOR had been 200 basis points lower/higher in 2009 with all other variables held constant, post-tax profit for the year would have been USD 16,288 (2008: USD 16,532) higher/lower without taking into account effect of interest rate hedge.

**(b) Credit risk**

Financial assets, which are potentially subject to credit risk, consist principally of cash and cash equivalents held in banks, trade and other receivables (Note 9 and Note 16). Due to the nature of its main activities (retail sales to individual customers) the Group has no significant concentration of credit risk. Cash is placed in financial institutions which are considered at the time of deposit to have minimal risk of default. The Group has policies in place to ensure that in case of credit sales of products and services to wholesale customers only those with an appropriate credit history are selected. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded. In accordance with the Group treasury policies and exposure management practices, counterparty credit exposure limits are continually monitored and no individual exposure is considered significant.

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

**(c) Liquidity risk**

Liquidity risk is defined as the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. Liquidity risk is managed by the Group Treasury.

The following is an analysis of the contractual undiscounted cash flows payable under financial liabilities and as at the balance sheet date at spot foreign exchange rates:

| Year ended 31 December 2009 | During 1 year | In 1 to 3 years |
|---|---|---|
| Borrowings | 1,761,560 | 312,283 |
| Trade payables | 1,556,325 | - |
| Gross finance lease liabilities | 1,950 | 4,586 |
| Derivative financial liabilities | 10,108 | - |
| Other finance liabilities | 284,498 | - |
| | **3,614,441** | **316,869** |

| Year ended 31 December 2008 | During 1 year | In 1 to 3 years |
|---|---|---|
| Borrowings | 593,485 | 1,643,696 |
| Trade payables | 1,175,279 | - |
| Gross finance lease liabilities | 2,197 | 1,843 |
| Derivative financial liabilities | 18,180 | - |
| Other finance liabilities | 258,456 | - |
| | **2,047,597** | **1,645,539** |

At 31 December 2009 the Group has negative working capital of USD 2,335,950 (31 December 2008: USD 1,031,800) including short-term borrowings of USD 1,656,622 (31 December 2008: USD 578,433).

At 31 December 2009 the Group had available bank credit lines of USD 555,170 (31 December 2008: USD 367,383).

At 31 December 2009 the Group short-term borrowings mainly comprised of a syndicated loan of USD 1,093,135 . In January 2010 X5 Retail Group and Sberbank finalized documentation with respect to a “forward-start” committed credit facility for refinancing of USD 1,100,000 syndicated loan with December 2010 maturity.

Sberbank’s facility takes the form of a 5-year ruble-denominated committed credit line of up to USD 1,100,000 in RUR equivalent (based on the exchange rate of the Central Bank of Russia as at draw-down date). The credit facility can be utilized in several tranches with varying maturities. Interest rate will be based on the maturity of each particular tranche.

Although at 31 December 2009 syndicated loan is presented as short-term it will be replaced by the long term committed facility provided by Sberbank. No liquidity risk exists at 31 December 2009 as the Group has a guaranteed source of refinancing.

Management regularly monitors the Group’s operating cash flows and available credit lines to ensure that these are adequate to meet the Group’s ongoing obligations and its expansion programs. Part of the short term liquidity risk is seasonal, with the highest peak in the 1st quarter and strong cash generation in 4th quarter, therefore the Group negotiates the maturity of short-term credit lines for the 4th quarter, when the free cash flow allows for the repayment of short-term debts. Part of the existing lines in the local currency (RUR) are provided on a rolling basis which is closely monitored by detailed cash flow forecasts and managed by the Group Treasury.

The Group's capital expenditure program is highly discretionary. The Group optimizes its cash outflows by managing the speed of execution of current capex projects and by delaying future capital extensive programs, if required.

The Group is carefully monitoring its liquidity profile by maximizing the drawdown periods within revolving credit facilities as well as extending existing credit facilities or obtaining new credit lines. The Group manages liquidity requirements by the use of both short-term and long-term projections and maintaining the availability of funding. Based on the review of the current liquidity position of the Group management considers that the available credit lines and expected cash flows are sufficient to finance the Group's current operations.

## 31 OPERATING ENVIRONMENT OF THE GROUP

***Russian Federation.*** The Russian Federation displays certain characteristics of an emerging market, including relatively high inflation and high interest rates. Despite strong economic growth in recent years, the financial situation in the Russian market significantly deteriorated during 2008, particularly in the fourth quarter. As a result of global volatility in financial and commodity markets, among other factors, there has been a significant decline in the Russian stock market since mid-2008. Since September 2008, there has been increased volatility in currency markets and the Russian Rouble (RR) has depreciated significantly against some major currencies. The official US Dollar (USD) exchange rate of the Central Bank of the Russian Federation ("CBRF") increased from RR 25.37 at 1 October 2008 to RR 29.38 at 31 December 2008 and RR 30.24 at 31 December 2009.

A number of measures have been undertaken to support the Russian financial markets, including the following:

In October 2008 the CBRF reduced the mandatory reserves ratio to 0.5% and raised the guarantee repayment of individual deposits under the state deposit insurance scheme to RR 700 thousand per individual in case of the withdrawal of a licence of a bank or a CBRF-imposed moratorium on payments.

The list of assets which can be pledged under repurchase agreements with the CBRF was significantly extended.

As part of preventive steps to ease the effects of the situation in financial markets on the economy, the Government incurred a large fiscal deficit in 2009

The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations and frequent changes, and other legal and fiscal impediments contribute to the challenges faced by entities currently operating in the Russian Federation. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

Management is unable to predict all developments in the economic environment which could have an impact on the Group's operations and consequently what effect, if any, they could have on the financial position of the Group.

***Impact of the ongoing global financial and economic crisis.*** The ongoing global liquidity crisis which commenced in the middle of 2008 has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector, and, at times, higher interbank lending rates and very high volatility in stock markets. The uncertainties in the global financial markets have also led to bank failures and bank rescues in the United States of America, Western Europe, Russia and elsewhere. Indeed the full extent of the impact of the ongoing financial crisis is proving to be impossible to anticipate or completely guard against.

The volume of wholesale financing has significantly reduced since August 2008. Such circumstances may affect the ability of the Group to obtain new borrowings and re-finance its existing borrowings at terms and conditions similar to those applied to earlier transactions.

Debtors of the Group may be affected by the lower liquidity situation which could in turn impact their ability to repay the amounts owed. Deteriorating operating conditions for debtors may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets.

Management is unable to reliably estimate the effects on the Group's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and growth of the Group's business in the current circumstances.

## 32 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. The Group manages total equity attributable to equity holders recognized under IFRS requirements.

Simultaneously, the Group maintains optimal capital structure by tracing certain capital requirements based on ratios. The ratios are maximum level of Debt/EBITDA, minimum level of EBITDA/Interest expense, minimum level of EBITDAR/Fixed costs and maximum level of capital expenditure. These ratios are included as covenants into loan agreements (Note 20). The Group is in compliance with externally imposed capital requirements.

## 33 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Russian Federation continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments.

***Financial assets carried at amortised cost.*** The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on credit risk of the counterparty.

Carrying amounts of trade and other financial receivables approximate fair values.

***Liabilities carried at amortised cost.*** The fair value of bonds is based on quoted market prices. Fair values of other liabilities are determined using valuation techniques. Carrying amounts of trade and other payables approximate fair values.

The fair value of X5 Finance bonds traded on the MICEX is determined based on active market quotations and amounted to USD 586,450 at 31 December 2009

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

(31 December 2008: 261,052). The carrying value of these bonds amounted to USD 558,899 at 31 December 2009 (31 December 2008: 304,986) (Note 20). The fair value of long-term borrowings amounted to USD 327,241 (31 December 2008: 1,210,484). Fair value was calculated by estimating future cash flows in nominal terms and discounting them at appropriate market rate. Market rates used for calculation vary from 9.4% to 10.2% depending on the amount and currency of particular loan. The fair value of short-term borrowings was not materially different from their carrying amounts.

***Derivative financial instruments.*** All derivative financial instruments are carried at fair value as assets when the fair value is positive and as liabilities when the fair value is negative. The fair value is determined based on quoted market prices or valuation techniques (Note 18).

## 34 COMMITMENTS AND CONTINGENCIES

### Commitments under operating leases

At 31 December 2009, the Group operated 802 stores through rented premises (31 December 2008: 589). There are two types of fees in respect of operating leases payable by the Group: fixed and variable. For each store fixed rent payments are defined in the lease contracts. The variable part of rent payments is predominantly denominated in RR and normally calculated as a percentage of turnover. Fixed rent payments constitute the main part of operating lease expenses of the Group as compared to the variable rent payments. Substantially all of the lease agreements have an option that enables the Group to cancel the agreement with the mutual concord of the parties involved.

The present value of future minimum lease payments and their nominal amounts under non-cancellable operating leases of property are as follows (net of VAT):

| | 31 December 2009 (present value) | 31 December 2008 (present value) | 31 December 2009 (nominal value) | 31 December 2008 (nominal value) |
|---|---|---|---|---|
| During 1 year | 199,983 | 131,800 | 215,389 | 144,380 |
| In 2 to 5 years | 351,996 | 238,369 | 525,354 | 368,568 |
| Thereafter | 139,307 | 92,559 | 474,981 | 310,358 |
| | **691,286** | **462,728** | **1,215,724** | **823,306** |

A discount rate applied in determining the present value of future minimum lease payments is based on the Group weighted average cost of capital (12-16%).

### Capital expenditure commitments

At 31 December 2009 the Group contracted for capital expenditure of USD 100,068 (net of VAT), (2008: USD 173,343).

### Legal contingencies

In the normal course of business the Group is involved in periodic legal cases. Management does not anticipate any material negative impact on the resolution of these cases.

### Taxation environment

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged as not having been in compliance with Russian tax laws applicable at the relevant time. In particular, the Supreme Arbitration Court issued guidance to lower courts on reviewing tax cases providing a systematic roadmap for anti-avoidance claims, and it is possible that this will significantly increase the level and frequency of tax authorities scrutiny. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Russian transfer pricing legislation introduced on 1 January 1999 provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controllable transactions, provided that the transaction price differs from the market price by more than 20%. Controllable transactions include transactions with interdependent parties, as determined under the Russian Tax Code, and all cross-border transactions (irrespective of whether performed between related or unrelated parties), transactions where the price applied by a taxpayer differs by more than 20% from the price applied in similar transactions by the same taxpayer within a short period of time, and barter transactions. There is no formal guidance as to how these rules should be applied in practice. The arbitration court practice in this respect is contradictory.

Tax liabilities arising from inter-company transactions are determined using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Russian Federation and the changes in the approach of the Russian tax authorities, that such transfer prices could potentially be challenged in the future. Given the brief nature of the current Russian transfer pricing rules, the impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial condition and operations of the entity.

Russian tax legislation does not provide definitive guidance in many areas. From time to time, the Group adopts interpretations of such uncertain areas that reduce the overall tax rate of the Group. As noted above, such tax positions may come under heightened scrutiny as a result of recent developments in administrative and court practices; the impact of any challenge by the tax authorities cannot be reliably estimated; however, it may be significant to the financial condition and operations of the entity.

Management regularly reviews the Group's taxation compliance with applicable legislation, laws and decrees and current interpretations published by the authorities in the jurisdictions in which the Group has operations. Furthermore, management regularly assesses the potential financial exposure relating to tax contingencies for which the three years tax inspection right has expired but which, under certain circumstances, may be challenged by the regulatory bodies. From time to time potential exposures and contingencies are identified and at any point in time a number of open matters may exist. Management estimates that possible exposure in relation to profit tax and other non-profit tax risks such as inter-company transactions, VAT and employee related taxes, that are more than remote, but for which no liability is required to be recognised under IFRS, could be several times the additional accrued liabilities and provisions reflected on the statement of financial position at that date (and potentially in excess of the Group's profit before tax for the year). This estimation is provided for the IFRS requirement for disclosure of possible taxes and should not be considered as an estimate of the Group's future tax liability. At the same time management has recorded liabilities for income taxes and provisions for taxes other than income taxes in the amount of USD 147,087 at 31 December 2009 (31 December 2008: USD 110,619) in these consolidated financial statements as their best estimate of the Group's liability related to tax uncertainties as follows:

Notes to Consolidated Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

| | |
|---|---|
| **Balance at 1 January 2008** | **76,708** |
| Increases due to acquisitions during the year recorded as part of the purchase price allocation (Note 7) | 57,694 |
| Translation movement | (23,783) |
| **Balance at 31 December 2008** | **110,619** |
| Increases due to acquisitions during the year recorded as part of the purchase price allocation (Note 7) | 41,253 |
| Translation movement | (4,785) |
| **Balance at 31 December 2009** | **147,087** |

# X5 Retail Group
# Company's Statement of Financial Position at 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | Note | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| **ASSETS** | | | |
| **Non-current assets** | | | |
| Financial assets | 36 | 2,474,217 | 3,138,016 |
| | | 2,474,217 | 3,138,016 |
| **Current assets** | | | |
| Financial assets | 36 | 770,833 | - |
| Deferred tax assets | | - | 14,980 |
| Amounts due from subsidiaries | | 349,713 | 130,871 |
| Accounts receivable | | 988 | 16 |
| Cash | | 1,513 | 226 |
| | | 1,123,047 | 146,093 |
| **Total assets** | | **3,597,264** | **3,284,109** |
| **EQUITY AND LIABILITIES** | | | |
| Paid up and called up share capital | 37 | 97,400 | 95,764 |
| Share premium account | | 1,936,452 | 1,993,385 |
| Other reserves | | 111,480 | (34,906) |
| Profit of the year | | 92,757 | 149,664 |
| Currency translation reserve | | (35,394) | (36,537) |
| **Total equity** | | **2,202,695** | **2,167,370** |
| **Non-current liabilities** | | | |
| Bank loans | 38 | - | 1,087,617 |
| Share based payment liability | 40 | 25,986 | - |
| | | 25,986 | 1,087,617 |
| **Current liabilities** | | | |
| Bank loans | 38 | 1,093,135 | - |
| Amounts due to subsidiaries | | 189,500 | - |
| Financial liabilities | 39 | 10,108 | 18,180 |
| Accrued expenses | 39 | 10,415 | 10,942 |
| Share based payment liability | 40 | 59,559 | - |
| Corporate income tax | 42 | 5,866 | - |
| | | 1,368,583 | 29,122 |
| **Total equity and liabilities** | | **3,597,264** | **3,284,109** |

# X5 Retail Group
# Company's Income Statement for the year ended 31 December 2009

(expressed in thousands of US Dollars, unless otherwise stated)

| | Note | 31 December 2009 | 31 December 2008 |
|---|---|---|---|
| Other income and expenses after tax | 41 | 92,757 | 149,664 |
| **Profit after taxation** | | **92,757** | **149,664** |

## 35 ACCOUNTING PRINCIPLES

**General**
The Company was incorporated as a limited liability Company under the laws of The Netherlands on 13 August 1975 and has its statutory seat in Amsterdam. The Company is publicly owned. The principal activity of the Company is to act as a retail chain.

**Basis of presentation**
The Company financial statements of X5 Retail Group N.V. have been prepared in accordance with Part 9, of Book 2 of the Dutch Civil Code.

**Accounting principles**
The statutory financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the Netherlands, in accordance with Part 9 of Book 2 of the Dutch Civil Code. The Dutch GAAP accounting principles applied for the entity accounts are similar to those used in the IFRS Consolidated Financial Statements (refer to note 2 to the consolidated financial statements), unless stated otherwise below. The consolidated accounts of companies publicly listed in the European Union must be prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the IASB and adopted by the European Commission. Consequently the consolidated financial statements of the Group for the year ending 31 December 2009 have been prepared accordingly.

In accordance with Section 362 paragraph 7, Part 9 of Book 2 of the Dutch Civil Code, the presentation currency in the annual report is USD as a result of the international bifurcation of the Company. As the Company exploits Russian grocery stores in three formats (hypermarkets, supermarkets and discounters), the functional currency of the Company is the Russian Rouble as this is the currency of its primarily business environment and reflects the economic reality. Reference is made to section 2.5 (a) of the notes to the consolidated financial statements with regard to the accounting policy in regard of the translation from functional currency to presentation currency.

**Financial assets and Liabilities**
Due to the international structure of the Company, the participations in Group companies are valued at historical cost. Provisions for impairment are taken into account when necessary.

Derivative financial assets and liabilities are valued at cost or at fair value. Changes in the value of these derivative financial instruments are recognized in the income statement upon transfer of the instrument to another party or if the instrument is impaired.

**Deferred income tax asset**
Deferred income tax asset is valued at nominal value and recognized as a part of current/non-current assets/liabilities based on estimated recoverability timing.

Notes to Company's Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

**Shareholders' Equity**
Issued and paid up share capital, which is denominated in Euro, is restated into US Dollar at the exchange rate as of balance date in accordance with section 373 sub 5 of book 2 of the Dutch Civil Code. The difference is settled with the currency translation adjustment reserve.

## 36 FINANCIAL ASSETS

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| **a. Movements in the interests in Group companies:** | | |
| Opening balance | 1,547,170 | 1,635,439 |
| Acquisitions / capital contribution | 209,079 | 210,342 |
| Impairment of investments | - | (29,519) |
| Other movements/foreign exchange differences | (50,418) | (269,092) |
| **Closing balance** | **1,705,831** | **1,547,170** |

A complete list of Group companies has been disclosed in the consolidated financial statements. Acquisitions in 2009 are mainly related to OOO "Firma Omega-97" (refer to note 7 of the consolidated financial statements).

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| **b. Movements in the loans to Group companies:** | | |
| Opening balance | 1,590,846 | 649,865 |
| Disbursement / repayments | (55,199) | 940,981 |
| Other movements/foreign exchange differences | 3,572 | - |
| **Closing balance** | **1,539,219** | **1,590,846** |
| **Total Financial assets** | **3,245,050** | **3,138,016** |

| Long-term loans provided to following Group companies: | Currency | Date of maturity |
|---|---|---|
| Speak Global Ltd. | USD | March 2010 (extended until December 2012) |
| Alpegru Ltd. | USD | December 2012 |
| Grasswell Ltd. | USD | December 2010 |
| Grasswell Ltd. | USD | December 2012 |
| Grasswell Ltd. | RR | June 2011 |
| CJSC Tradehouse Perekrestok | USD | December 2011 |

The loans have not been secured and attract up to 10.5 % interest per annum. In the loans receivable there is an amount to Grasswell Ltd denominated in RUR, the amount of this loan is RUR 3,085,408,000. Furthermore an amount of USD 770,833 is classified as short term.

## 37 SHAREHOLDERS' EQUITY

| | Share capital | Share premium | Other Reserves | Profit/(Loss) | Translation adjustment | Total |
|---|---|---|---|---|---|---|
| **Balance as per 1 January 2008** | **79,226** | **1,217,341** | **1,985** | **(31,990)** | **(13,485)** | **1,253,077** |
| Paid in | 21,648 | 1,207,967 | - | - | - | 1,229,615 |
| Transfer | - | - | (31,990) | 31,990 | - | - |
| Currency translation adj. | (5,110) | (431,923) | (4,901) | - | (23,052) | (464,986) |
| Result for the period | - | - | - | 149,664 | - | 149,664 |
| **Balance as per 31 December 2008** | **95,764** | **1,993,385** | **(34,906)** | **149,664** | **(36,537)** | **2,167,370** |
| Paid in | - | - | - | - | - | - |
| Transfer | - | - | 149,664 | (149,664) | - | - |
| Currency translation | 1,636 | (56,933) | (3,278) | - | 1,143 | (57,432) |
| Result for the period | - | - | - | 92,757 | - | 92,757 |
| **Balance as per 31 December 2009** | **97,400** | **1,936,452** | **111,480** | **92,757** | **(35,394)** | **2,202,695** |

Notes to Company's Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

Statutory undistributable reserve is maintained for currency translation adjustment recorded as the result of translation between functional and presentation currencies.

A reconciliation of the differences between the Company and consolidated equity and profit/loss in the financial year is as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Equity per Company financial statements | 2,202,695 | 2,167,370 |
| Accumulated result of Group | (1,842,251) | 445,700 |
| Acquisition of treasury shares | (14,150) | (14,150) |
| Hedging instruments | (10,108) | (18,180) |
| Results from subsidiaries for the year | 72,594 | (2,287,951) |
| Sale of treasury shares | 144,217 | 144,217 |
| Currency exchange differences | (219,682) | (237,722) |
| Equity change as an effect of reverse acquisition transaction | 1,439,149 | 1,439,149 |
| **Equity per consolidated financial statements** | **1,772,464** | **1,638,433** |

| Difference in profit/loss | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Profit according to Company annual accounts | 92,757 | 149,664 |
| Profit/(Loss) from subsidiaries for the year | 72,594 | (2,287,951) |
| **Profit per consolidated financial statements** | **165,351** | **(2,138,287)** |

**Share capital issued**

The authorised share capital of the Company amounts to EUR 190,000,000 divided into 190,000,000 shares of EUR 1 each.

As at 31 December 2009, the issued and paid-up share capital amounts to EUR 67,893,218 and consists of 67,893,218 shares of EUR 1 each (2008: 67,893,218). This has been recalculated into USD with an exchange rate of 1 EUR = 1.4346 USD (2008: 1 EUR = 1.5717 USD).

## 38 BANK LOANS

Movement in the bank loans have been as follows:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Opening balance | 1,087,617 | 1,083,226 |
| Finance costs | 5,518 | 4,391 |
| **Closing balance** | **1,093,135** | **1,087,617** |

The margin for the first year was 2.25% per annum over USD LIBOR. In December 2008 the margin changed from 2.25% to 1.5% in accordance with an agreed the Net Debt/EBITDA grid. USD LIBOR is fixed from a one to six month period (Note 20) .

In November 2009 the Group and Sberbank reached agreement on a "forward-start" committed credit facility for refinancing of USD 1,100,000 syndicated loan with December 2010 maturity. In January 2010 the Group and Sberbank finalized documentation of this credit facility. Refinancing will be in the form of five-year rouble denominated committed credit facility up to USD 1,100,000 (in RUR equivalent, based on the exchange rate of the CBR as at the draw down date). The credit facility may be utilized in several tranches with varying maturities.

## 39 CURRENT LIABILITIES

The current liabilities contain accrued expenses and non-income tax payable as well as derivatives. Refer to note 18 of the consolidated financial statements.

Notes to Company's Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 40 SHARE BASED PAYMENT LIABILITY

In compliance with changes in the Dutch Guidelines for annual reporting on share-based payments, the company modified presentation for share-based payments per 31 December 2009. X5 Retail Group N.V. accounts for a receivable insofar the options granted to employees of the Group are recharged. For employees of the company an expense is recorded in the profit and loss account. The receivable or expense is accounted for at the fair value determined in accordance with the policy on share-based payments as included in the consolidated financial statements, including the related liability for cash settled plans or as equity increase for equity settled plans.

If this guidance was applied for 2008, comparative information would be as follows.

| | 31 December 2008 | 31 December 2009 |
|---|---|---|
| Share based payments liability | (37,921) | (85,545) |
| Accounts receivable | 37,204 | 94,012 |
| Profit & loss | 236 | 1,378 |
| Retained earnings | 481 | 717 |

## 41 OTHER INCOME AND EXPENSES AFTER TAX

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Interest income from subsidiaries | 152,057 | 116,020 |
| Interest expenses | (43,508) | (53,966) |
| General and administrative expenses | (12,101) | (21,396) |
| Result of financial instruments | 7,201 | (21,490) |
| Share based payment | (2,096) | - |
| Currency exchange rate differences | 10,670 | 150,037 |
| Income tax charge | (19,466) | 9,977 |
| Provision for impairment of investments | - | (29,519) |
| | **92,757** | **149,664** |

In accordance with the Dutch legislation article 2:382a the total audit fees related to the accounting organisation PricewaterhouseCoopers Accountants N.V. amounted to USD 179 (2007: USD 223).

## 42 INCOME TAX EXPENSE

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Operating profit | 92,757 | 149,664 |
| Deferred income tax credit | (13,874) | (9,977) |
| Current income tax | (5,592) | |
| Effective tax rate | 21% | (7)% |
| Applicable tax rate | 25.5% | 25.5% |

The effective tax rate differs from the applicable tax rate due to tax losses for which no deferred income tax assets was recognized and currency exchange rate gains and share based expenses that are not taxable.

## 43 DIRECTORS

The Company has a Management Board and a Supervisory Board. The remuneration of all Board members paid through the Company and through Group companies is disclosed as follows below. Further reference is made to Notes 27 and 28 in the consolidated financial statements.

Notes to Company's Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

### Supervisory Board

Remuneration of the Supervisory Board members consists of cash salary which accrued evenly throughout the year in proportion to the period of service. Two members of the Supervisory Board are participating in the Share option programme of the Group. The number of options granted and outstanding to the members of the Supervisory Board is shown below. For calculation of intrinsic value refer to Note 27.

The Supervisory Board members received a remuneration of:

| | Base salary 2009 | Bonus 2009 | Option expenses | Other | |
|---|---|---|---|---|---|
| H. Defforey | 167 | - | | | |
| M. Fridman | 70 | - | | | |
| D. Gould | 104 | - | | | |
| A. Savin | 50 | - | | | Resigned 17 September 2009 |
| C. Criado-Pérez Trefault | 167 | - | 92 | 200 | Resigned 1 January 2010 |
| V. Ashurkov | 104 | - | | | |
| A. Tynkovan | 167 | - | | | |
| S. DuCharme | 167 | - | | | |
| | **997** | **-** | **92** | **200** | |

Number of Share options issued to Supervisory Board members:

| | No. of options granted in 2009 | No. of options granted prior 2009 | No. of options exercised in 2009/2008 | Cancellation | No. of options outstanding as at 31.12.2009 |
|---|---|---|---|---|---|
| H. Defforey | 70,000 | 72,500 | 30,000 | - | 112,500 |
| S.E. DuCharme | 32,500 | - | - | - | 32,500 |
| C. Criado-Pérez Trefault | 21,250 | 41,250 | 20,000 | 21,250 | 21,250 |
| | **123,750** | **113,750** | **50,000** | **21,250** | **166,250** |

### Management Board

Remuneration of the Management Board members consists of cash salary and annual bonus. All members of the Management Board are participating in the Share option programme of the Group. The number of options granted and outstanding to the members of the Management Board is shown below. For calculation of intrinsic value refer to Note 27.

| | Base salary 2009 | Bonus 2009 |
|---|---|---|
| L. Khasis | 2,122 | 1,456 |
| E. Kornilov | 866 | 520 |
| F. Lhoëst | 279 | 84 |
| | **3,267** | **2,060** |

Number of Share options issued to Management Board members:

| | No. of options granted in 2009 | No. of options granted prior 2009 | No. of options exercised in 2009/2008 | No. of options outstanding as at 31.12.2009 |
|---|---|---|---|---|
| L. Khasis | 860,625 | 2,480,625 | 810,000 | 2,531,250 |
| E. Kornilov | 220,000 | 250,000 | - | 470,000 |
| F.M. Lhoëst | 20,000 | - | - | 20,000 |
| | **1,100,625** | **2,730,625** | **810,000** | **3,021,250** |

Company standalone financial statements include salaries, and bonuses payable to statutory directors of USD 423 (2007: 357).

Notes to Company's Financial Statements for the year ended 31 December 2009 *(expressed in thousands of US Dollars, unless otherwise stated)*

## 44 STAFF NUMBERS AND EMPLOYMENT COSTS

The Company has no employees and hence incurred no wages, salaries or related social security charges during the reporting period, nor during the previous year, other than those for the Management and Supervisory Board.

## 45 COMMITMENTS AND CONTINGENCIES

Reference is made to the commitments and contingencies as disclosed in Note 34 in the consolidated financial statements. Guarantees are irrevocable assurances that the Company will make payments in the event that another party cannot meet its obligations. The Group has the following guarantees issued under obligations of its subsidiaries:

| | 31 December 2009 | 31 December 2008 |
|---|---|---|
| Guarantee issued to Commerzbank | - | 100,000 |
| Guarantee issued to Raiffeisenbank | - | 100,000 |
| Irrevocable offer to holders of X5 Finance bonds | 562,091 | 306,327 |
| Irrevocable offer to holders of Pyaterochka Finance bonds | 881 | 907 |

## 46 RELATED PARTY TRANSACTION

Refer to Note 8 of the consolidated financial statements, all Group companies are also considered related parties.

**Statutory Director's compensation**
Statutory director's compensation is disclosed in Note 43.

**Loans to Group companies**
For loans issued to and interest income from Group companies refer to Note 36.

Amsterdam, 08 April 2010

| **Managing Directors:** | **Supervisory Directors:** |
|---|---|
| L. Khasis | H. Defforey |
| | M. Fridman |
| | D. Gould |
| E. Kornilov | V. Ashurkov |
| | A. Tynkovan |
| | S. DuCharme |
| F. Lhoëst | C.P. Couvreux |

## 47 SUBSEQUENT EVENTS

In January 2010 X5 Retail Group and Sberbank finalized documentation of a credit facility. Refinancing will be in the form of 5-year rouble denominated committed credit facility up to USD 1,100,000 (in RUR equivalent, based on the exchange rate of the CBR as at the draw down date). The credit facility may be utilized in several tranches with varying maturities.

In March 2010 X5 Retail Group facilitated the deposit of 1,746,505 ordinary shares into Global Depositary Receipts ("GDR") facility. These shares were issued in 2008 as part of the consideration paid for the Karusel hypermarket chain. The increase in the size of listing on the Main Market of the London Stock Exchange will not affect the number of outstanding shares, which will remain unchanged at 67,893,218, while the number of GDRs will increase by 6,986,020.

# OTHER INFORMATION

**Auditor's report**
Auditor's report is included on the page 145.

**Statutory profit appropriation**
In Article 28 of the company statutory regulations the following has been stated concerning the appropriation of result.

On proposal of the Supervisory Board, the General meeting shall determine which part of the profits earned in a financial year shall be added to the reserves and the allocation of the remaining profits.

| Proposed appropriation of profit | 2009 |
|---|---|
| Profit for the year added to other reserves | 92,757 |

It will be proposed to transfer the profit to the other reserves.

For subsequent events refer to Note 47.

PricewaterhouseCoopers
Accountants N.V.
Thomas R. Malthusstraat 5
1066 JR Amsterdam
P.O. Box 90357
1006 B J Amsterdam
The Netherlands
Telephone +31 (0) 20 568 66 66
Facsimile +31 (0) 20 568 68 88
www.pwc.com/nl

To the General Meeting of Shareholders of X5 Retail Group N.V.:

# AUDITOR'S REPORT

## REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements 2009 of X5 Retail Group N.V., Amsterdam as set out on pages 79 until 143. The financial statements consist of the consolidated financial statements and the company financial statements. The consolidated financial statements comprise the consolidated statement of financial position as at 31 December 2009, the consolidated income statement, the statement of comprehensive income, the consolidated changes in equity and consolidated cash flows for the year then ended and the notes, comprising a summary of significant accounting policies and other explanatory information. The company financial statements comprise the company statement of financial position as at 31 December 2009, the company income statement for the year then ended and the notes.

**Management's responsibility**
Management of the company is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code, and for the preparation of the directors' report in accordance with Part 9 of Book 2 of the Netherlands Civil Code. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the 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 the financial statements based on our audit. We conducted our audit in accordance with Dutch law. This law requires 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 with respect to the consolidated financial statements**
In our opinion, the consolidated financial statements, set out in pages 79 until 134, give a true and fair view of the financial position of X5 Retail Group N.V. as at 31 December 2009, and of its result and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code.

**Opinion with respect to the company financial statements**
In our opinion, the company financial statements, set out in pages 135 until 143, give a true and fair view of the financial position of X5 Retail Group N.V. as at 31 December 2009, and of its result for the year then ended in accordance with Part 9 of Book 2 of the Netherlands Civil Code.

**Report on other legal and regulatory requirements**
Pursuant to the legal requirement under 2:393 sub 5 part f of the Netherlands Civil Code, we report, to the extent of our competence, that the directors' report is consistent with the financial statements as required by 2:391 sub 4 of the Netherlands Civil Code.

Amsterdam, 8 April 2010
PricewaterhouseCoopers Accountants N.V.
P.C. Dams RA