AS BALTIKA

CORPORATE GOVERNANCE REPORT, 2010

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

Baltika adheres to all applicable laws and regulations. As a public company, Baltika also observes the rules of the Tallinn Stock Exchange and the requirement to treat investors and shareholders equally. Accordingly, Baltika complies, in all material respects, with the provisions of CGC. Explanations for departures from CGC are provided below. In addition, our corporate governance report contains information on the annual general meeting of 2010, the supervisory council, the management board and explains Baltika's governance structure and processes.

CGC Article 1.3.3.

An issuer shall make attendance and participation in the general meeting possible by means of communication equipment (e.g. the Internet) if the technical equipment is available and where doing so is not too cost prohibitive for the issuer

Since Baltika does not have the required technical equipment and acquisition of such equipment would be costly, currently attendance and participation in general meetings is not possible by means of communication equipment.

CGC Article 2.2.1.

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

Members of Baltika's management board are responsible for strategic areas and their duties are not limited to the ones provided in the Commercial Code and the company's Articles of Association (management and representation of the company). Therefore, four members of the management board serve the company under employment contracts and one member of the management board, Andrew Paterson, serves the company under a consulting services agreement entered into with his company Keel Consulting Associates Ltd. The Chairman of the Management Board Meelis Milder is the Group's CEO, Ülle Järv the CFO, Maire Milder the Director of the Retail Division, Boriss Loifenfeld the Director of Wholesale and CIS Projects and Andrew Paterson the Director of Merchandising, Sourcing and Supply Chain.

CGC Article 2.2.7.

The basic salary, performance pay, severance package, and other benefits and bonus schemes of a management board member as well as their essential features (incl. features based on comparison, incentives and risk) shall be published in clear and unambiguous form on the website of the issuer and in the corporate governance report. Information shall be deemed clear and unambiguous if it directly expresses the amount of expense to the issuer or the amount of foreseeable expense as of the day of disclosure.

The remuneration and other benefits provided to members of the management board are set out in their employment contracts. Owing to the confidentiality of the contracts, Baltika does not disclose the remuneration and benefits provided to each member of the management board. However, Baltika discloses the total amount of remuneration provided to members of the supervisory council and management board in the management report section of its interim and annual reports. In 2010, the figure amounted to 0.3 million euros. The contractual severance benefits of members of the management board range from 6- to 12-fold monthly remuneration.

Members of the management board, like other employees, are eligible to performance pay in accordance with the Group's bonus scheme, which is based on the performance of profit centres. The maximum bonus level for the chairman of the management board/CEO is 1.5% of the Group's net profit for the financial year although the actual disbursement may not exceed the chairman's one annual salary. The bonuses of other members of the management board/directors are linked to the performance of their respective profit centres but the actual disbursements may not exceed one half to two thirds of their annual salary. Annual bonuses are paid in three portions: two payments are made in advance and the final one is calculated and made after the financial statements have been audited. The bonus of the chairman of the management board/CEO is determined by the supervisory council. The bonuses of members of the management board are determined by the chairman of the supervisory council based on a proposal made by the chairman of the management board. Due to the loss incurred, members of the management board did not receive any performance pay in 2010.

Members of the management board, similarly to all executives working under a director's contract in the Group, are eligible to one funded pension contribution of up to one month's salary per year, provided they have worked in the director's position for at least three years. Members of the management board may use a company car and are eligible to other benefits provided for in the company's internal rules. Members of the management board have participated in the convertible bond (option) programs arranged for Group's employees and are eligible to do so in the future.

In 2010, members of the management board participated in a convertible bond program designed for the company's top and middle management, which was approved by the annual general meeting in 2009. The terms and conditions of the bonds are provided in the resolutions of the respective annual general meeting. Changes in management board members' interests in the company are disclosed in the company's share register, which is available on the website of the Estonian Central Securities Depository (www.e-register.ee), as well as in the Group's interim and annual reports.

CGC Article 2.3.2.

The supervisory council shall approve transactions that are significant to the issuer and are entered into between the issuer and a member of its management board, or another person connected or close to them, and shall determine the terms of such transactions. Transactions approved by the supervisory council between the issuer and a member of the management board, or a person connected or close to them, shall be published in the issuer's Corporate Governance Report.

In 2010 nor 2009 no significant transactions were performed.

CGC Article 3.2.5.

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

The annual general meeting of 2009 passed the motion that the emoluments of members of the supervisory council should remain the same as decided by the extraordinary general meeting of 8 December 2004. The remuneration of the chairman of the supervisory council amounts to 639 euros per month and the remuneration of a member of the supervisory council to 383 euros per month. A member of the supervisory council is not eligible to severance compensation or any other monetary benefits.

CGC Article 3.3.2.

A member of the supervisory council shall promptly inform the chairman of the supervisory council and the management board of any business offer related to the business activity of the issuer made to the member of the supervisory council or a person close or connected to the member of the supervisory council. All conflicts of interests that have arisen during the reporting year shall be disclosed in the Corporate Governance Report along with their resolutions.

In 2010 nor 2009 no conflicts of interests occurred.

CGC Article 5.6.

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

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

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

CGC Article 6.2.

Election of the auditor and auditing of the annual accounts

In accordance with the Baltika's Articles of Association, the auditor(s) is (are) appointed by the general meeting for the performance of a single audit or for a specific term. The annual general meeting which convened on 21 June 2010, appointed the auditor of the annual financial statements for 2010. According to the audit agreement, the engagement partner is Ago Vilu and the engagement manager Eva Jansen. Baltika ensures the auditor's independence by rotating the engagement partner and engagement manager in accordance with the rules of Financial Supervision Authority.

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

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

GOVERNANCE PRINCIPLES AND ADDITIONAL INFORMATION

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

General meeting

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

The annual general meeting of 2010 was held on 21 June at 24 Veerenni in Tallinn, Estonia. A total of 9,379,077 shares were represented (50.3% of the voting stock). The meeting approved the company's annual report and profit allocation proposal for 2009 and appointed AS PricewaterhouseCoopers as the company's auditor. The general meeting elected two additional supervisory council members: Edoardo Miroglio and Jaakko Sakari Mikael Salmelin. In addition, the general meeting decided to increase share capital by issuing additional 8,850,000 ordinary shares. As a result of this decision, the share capital of Baltika increased by 5,656,181 euros to 20,128,878 euros. The chairman of the management board informed shareholders about Baltika Group's strategy for 2010-2014 created in co-operation with the international consulting firm Roland Berger.

Supervisory council

The supervisory council plans the activities of the Baltika, organises the management and supervises the activities of the management board. The supervisory council meets according to need but not less frequently than once every three months. A meeting of the supervisory council has a quorum when more than half of the members participate. A resolution of the supervisory council is adopted when more than half of the members of the supervisory council who participate in the meeting vote in favour. Each member of the supervisory council has one vote. In 2010, the supervisory council met six times. All members of the supervisory council attended all or most of the meetings of the supervisory council.

According to the Articles of Association, Baltika's supervisory council has three to seven members. The members are elected by the general meeting for a period of three years. Five members of the current council were elected by the annual general meeting in 2009. The annual general meeting of 2010 elected two additional supervisory council members.

The present members of the supervisory council are Tiina Mõis (chairman), Reet Saks, Allan Remmelkoor, Andres Erm, Lauri Kustaa Äimä, Jaakko Sakari Mikael Salmelin and Edoardo Miroglio. The two latter ones were elected by the annual general meeting in 2010. Tiina Mõis is the director of the investment firm AS Genteel and a member of the councils of several Estonian companies. Reet Saks is an attorney with Law Office Raidla Lejins & Norcous, a long-term partner of Baltika. Reet Saks has been a member of Baltika's supervisory council since 1997. Allan Remmelkoor, the chief executive of AS Kristiine Kaubanduskeskus which operates the Kristiine Centre in Tallinn, Estonia, contributes valuable retail expertise. Andres Erm has extensive experience with emerging markets in Eastern Europe which are also targeted by Group. Lauri Kustaa Äimä is a managing director of Kaima Capital Oy and a member of the councils of several Baltic companies. Mr Äimä has long-term experience in advising potential investors on matters related to investing in the companies of the Baltic countries. Jaakko Sakari Mikael Salmelin is a partner of KJK Capital Oy; he has managed various Eastern European funds focusing mainly on the Baltic and Balkan markets. Edoardo Miroglio is a Member of the Board of Directors of Miroglio S.P.A. and has long-term experience in international retail, fashion and textile industry.

One council member owns Baltika's shares: Tiina Mõis owns 977,837 preference shares or 3.10% of share capital through the company under her control as at the end of 2010.

Six of the seven members of Baltika's supervisory council are independent. The dependent member is Reet Saks who has been a member of Baltika's supervisory council for more than ten years.

Audit committee

To ensure conformance with the Auditors Activities Act, on 16 August 2010 the supervisory council of Baltika decided that an audit committee should be formed for the company and approved its rules of procedure. The audit committee is responsible for monitoring and analysing the processing of financial information, the effectiveness of risk management and internal controls, and the external audit of the consolidated financial statements. The committee is also responsible for making recommendations in relation to the above issues to prevent or eliminate problems and inefficiency.

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

In 2010 the audit committee had two meetings where the terms of the service contracts to be signed with members of the management board were discussed. At the beginning of 2011 the committee met with the representatives of the audit firm PricewaterhouseCoopers to obtain an overview of the audit of the consolidated financial statements for 2010.

Management board

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

According to the Articles of Association, Baltika's management board may have three to seven members who are elected by the supervisory council for a period of three years. The supervisory council may also remove a member of the management board.

Baltika's management board has five members: Meelis Milder (chairman), Ülle Järv, Maire Milder, Boriss Loifenfeld and Andrew Paterson. On 14 September 2009, the supervisory council decided to extend the board members' term of office for another three years.

The Chairman of the Management Board Meelis Milder is the company's CEO, Ülle Järv the CFO, Maire Milder the Director of the Retail Division and Boriss Loifenfeld the Director of Wholesale and CIS Projects. These members of the management board have been Baltika from 11 to 26 years. Andrew Paterson is the Director of Merchandising, Sourcing and Supply Chain. Mr Paterson advised Baltika on merchandise management during the period 2003-2006, when Baltika underwent a turnaround into a vertically integrated fashion retailer, and started working with Baltika again at the end of 2007.

Management board members are Baltika's largest shareholders through the holding company OÜ BMIG, which at the end of 2010 held 15.08% of Baltika's share capital (16.82% of listed ordinary shares). In addition, management board members have their individual shareholdings. Consequently, through their direct and indirect holdings, at the end of 2010 management board members controlled 19.11% of Baltika share capital (21.43% of listed ordinary shares).

Shareholdings of members of the management board at 31 December 2010

	Ordinary shares (listed)		Preference shares (not listed)		Total	
	No of shares	Holding	No of shares	Holding	No of shares	Holding
OÜ BMIG	4,624,860	16.82%	125,173	3.13%	4,750,033	15.08%
Meelis Milder	726,336	2.64%			726,336	2.31%
Maire Milder	316,083	1.15%			316,083	1.00%
Boriss Loifenfeld	200,366	0.73%			200,366	0.64%
Ülle Järv	13,850	0.05%			13,850	0.04%
Andrew Paterson	11,000	0.04%			11,000	0.03%
Total OÜ BMIG and management board members	**5,892,495**	**21.43%**	**125,173**	**3.13%**	**6,017,668**	**19.11%**
Baltika's share capital	**27,494,850**	**100%**	**4,000,000**	**100%**	**31,494,850**	**100%**

Baltika Group