Annual Report 2017

ADLER
ALLES PASST

MULTI-YEAR OVERVIEW

		2013	2014	2015	2016	2017	Change 2017 to 2016 absolute	Change 2017 to 2016 relative
Revenue	**€ million**	**528.6**	**535.3**	**566.1**	**544.6**	**525.8**	**−18.8**	**−3.5 %**
Material expenses	€ million	−234.9	−243.2	−261.2	−256.5	−244.1	12.4	−4.8 %
Gross profit	€ million	293.7	292.0	304.9	288.1	281.8	−6.3	−2.2 %
Gross profit margin		55.6 %	54.6 %	53.9 %	52.9 %	53.6 %	0.7	1.3 %
EBITDA	**€ million**	**42.9**	**41.5**	**33.3**	**23.3**	**32.0**	**8.7**	**37.3 %**
EBITDA margin		8.1 %	7.8 %	5.9 %	4.3 %	6.1 %	1.8	42.2 %
Depreciation	€ million	−14.0	−15.4	−16.3	−16.7	−16.5	0.2	−1.2 %
EBIT	**€ million**	**28.9**	**26.2**	**17.0**	**6.5**	**15.6**	**9.1**	**140.0 %**
EBIT margin		5.5 %	4.9 %	3.0 %	1.2 %	3.0 %	1.8	148.6 %
Net income from operations	**€ million**	**24.6**	**21.2**	**12.1**	**1.7**	**10.7**	**9.0**	**529.4 %**
Income taxes	€ million	−6.0	−7.1	−4.2	−1.3	−6.8	−5.5	423.1 %
Consolidated profit for the year	**€ million**	**18.6**	**14.1**	**7.9**	**0.4**	**3.9**	**3.5**	**875.0 %**
Earnings per share	€	1.05	0.77	0.43	0.02	0.21	0.2	950.0 %
Cash flows								
Net cash flows from operating activities	€ million	40.9	36.4	19.5	22.2	21.2	−1.0	−4.5 %
Net cash flows from investing activities	€ million	−9.2	−11.4	−16.6	−10.8	14.8	25.6	237.0 %
Free cash flow	€ million	31.8	25.0	2.9	11.4	35.9	24.6	215.8 %
Total assets	**€ million**	**228.4**	**244.3**	**243.4**	**222.6**	**241.1**	**18.5**	**8.3 %**
Non-current assets	€ million	89.1	93.1	99.7	95.5	88.6	−6.9	−7.2 %
Current assets	€ million	139.4	151.2	143.7	127.1	152.5	25.4	20.0 %
Inventories	€ million	77.5	75.6	81.3	75.4	73.7	−1.7	−2.3 %
Cash and cash equivalents	€ million	54.5	69.7	52.1	42.8	63.3	20.5	47.9 %
Equity	**€ million**	**92.0**	**105.6**	**104.9**	**95.8**	**100.0**	**4.2**	**4.4 %**
Equity ratio		40.3 %	43.3 %	43.1 %	43.1 %	41.5 %	−1.6	−3.8 %
Non-current liabilities	€ million	62.1	63.5	64.6	60.7	64.7	3.9	6.4 %
Current liabilities	€ million	74.3	75.1	74.0	66.0	76.5	10.6	16.1 %
Debt equity ratio		1.48	1.31	1.32	1.32	1.41		
Employees								
Number of employees as of December 31		4,301	4,154	4,203	3,984	3,866	−118.0	−3.0 %
Personnel expenses	€ million	−92.0	−95.2	−102.5	−102.3	−96.9	5.4	−5.3 %
Total number of stores		**171**	**170**	**177**	**183**	**182**	**−1**	
of which in Germany		143	145	153	156	155	−1	
of which in Austria		25	22	21	22	22	0	
of which in Luxembourg		2	2	2	3	3	0	
of which in Switzerland		1	1	1	2	2	0	

SIGHTS FIRMLY SET ON *profitable growth*

» Our analyses have shown that there is incredible potential in the 55+ target group. Therefore, we're going to concentrate all our energies on best serving precisely this age group. Those are our roots; that's what we have to return to. It's now time that we set the course for growth again. «

THOMAS FREUDE
CEO OF ADLER MODEMÄRKTE AG

INTERVIEW

» OUR MISSION: FASHION FOR PEOPLE IN THEIR PRIME «

Is it possible to achieve profitable long-term growth in a declining market? Thomas Freude, the new CEO of Adler Modemärkte AG since September 2017, and CFO Karsten Odemann see excellent opportunities for ADLER by going back to the company's roots. In this interview, they introduce their new corporate strategy.

Mr Freude, you've been the CEO of ADLER Modemärkte since September 2017. You most recently served as a senior executive in charge of the Technical Services division at Deutsche Telekom. The move to a fashion retailer seems a bit unusual.

FREUDE It may seem so at first glance. But I have spent most of my professional life in the traditional retail business, including at major department store chains such as Karstadt and Kaufhof, but also the OTTO Group. In that respect, the decision to move to ADLER was a return to my professional roots. I am confident that my ten years´ experience at Deutsche Telekom will be of great value to ADLER in view of the continuing trend toward digitalisation.

THOMAS FREUDE CEO
Thomas Freude has been CEO of Adler Modemärkte AG since 11 September 2017. He is responsible for strategy, sales and distribution, e-commerce, marketing, M&A, public relations, supply chain, and purchasing.

KARSTEN ODEMANN CFO
Since his appointment as CFO in 2011, Karsten Odemann has been responsible for finance, controlling, audits, legal, IT, investor relations, technical purchasing, sustainability, and human resources.

How did you approach your new task?
FREUDE Well, the expectation level is always high with every new CEO. But I'm not a big fan of hasty action and I deliberately took more time than the traditional 100 days to communicate our new strategy. From day one I was on the road a lot, visiting several stores every week, talking to the staff and customers and carefully inspecting the processes. That helped me get a good feel for how the business and its people tick. After all, no one knows better than our employees working in ADLER's more than 180 stores what our customers really want.

What were the most important things you learned?
FREUDE It's no secret when I say that the development at ADLER in recent years, while solid, has certainly not been optimal. That's due in part to general conditions overall, which are difficult – that's something we can't change. But there were also some negative developments that were clearly of our own making. We've identified those and now we have to address them. The good news is that we've discovered a great deal of upside potential at ADLER!

Mr Odemann, in the last quarterly reports you yourself said that the foundation for this has been laid. In 2016, ADLER had already introduced comprehensive measures to increase efficiency and reduce costs. How are you coming along with that?
ODEMANN Well, on that note I'd say our earnings performance speaks for itself. Even though revenue declined as expected, we were able to increase our EBITDA in 2017 by just under 7 % to € 25.4 million. That was the benefit reaped from our efficiency enhancement programme, which was not easy for all concerned. Unfortunately, the fourth quarter, which went very badly for the industry as a whole, thwarted our plans to achieve our targets, which were actually even higher. However, the improvement in the EBITDA margin from 4.4 % to 4.8 % demonstrates that we've made some real strides since 2016.

At € 32.0 million, reported EBITDA was actually a lot higher as a result of a non-recurring effect …
ODEMANN That's right. As a legacy of our past, we still had four buildings in Austria under a lease agreement that expired in April 2017. We sold those properties as well as another building in St. Pölten to strategic investors in a two-phase transaction. At the same time, we were able to secure more favourable lease conditions for the stores located in four of those five buildings. The transactions had a very positive impact on both cash flow and earnings and further boosted our already solid balance sheet.

What are the grounds for that last statement?
ODEMANN Thanks to higher profit and the proceeds from the real estate sales, we managed to increase free cash flow to € 35.6 million in 2017, a new record for ADLER, and in the current market environment, too. Our equity ratio compared to the industry is a very solid 41.5 %. This gives us financial leeway for the future, even if the investments for the strategic realignment are relatively modest. We're very glad that we can finance the growth targets for the coming years on our own.

Is there still room for further improvements in efficiency?
ODEMANN Absolutely! We've already initiated the necessary steps. For example, in 2017 we terminated the contract with our former logistics partner. In future we'll be cooperating with the firm Meyer&Meyer in this area. The transition will still result in ramp-up costs in 2018, because the warehouse has to be relocated, for example. But starting in 2019, this will lead to significant cost reductions. There's been a change in the area of purchasing, as well. With Hermes-Otto International we have found a new procurement agency as our future strategic partner.

Mr Freude, cost efficiency is important, but the capital market naturally also wants to see top-line growth again in the future. How do you intend to achieve this in view of the difficult market environment?

FREUDE We've been doing a great deal of analysis in the past months. We've commissioned market studies, conducted customer surveys. In the process, one thing became very clear – ADLER was trying to be something it isn't. The average age of ADLER's customers is 62. All attempts to lower the age of our target group have essentially failed and, what's worse, also resulted in our actually very loyal customer base no longer being able to identify with "their/our" brand. Why are we spending so much money and energy to become more youthful when we don't need to? Our analyses have also shown that there is incredible potential in the 55 + target group. Therefore, we're going to concentrate all our energies on best serving precisely this age group. Those are our roots; that's what we have to return to. After taking hits to our revenues year in year out, it's now time that we set the course for growth again.

What does that mean, specifically?

FREUDE We've formulated our mission: "Fashion for people in their prime". ADLER will be *the* platform for the 55 + target group, both "real" and digital. Our focus will be placed on four areas: first our products. Second, the distribution channels we want to serve. Third, the way we communicate with our customers and how we can increase footfall in the stores. And fourth, the things we can leverage to help us to be efficient and forward-looking, for example digitising all relevant business processes.

What was the problem with the products?

FREUDE Nothing, really. But in our attempt in the past to attract younger target groups we placed more emphasis on external brands, and our high-margin private label brands didn't always reflect the tastes of our regular customers. We're going to change that. Popular product lines will be expanded, and the number of external brands will be significantly reduced. The needs of our customers have to be taken seriously; they have to be able to once again clearly identify what the ADLER brand stands for and what distinguishes it from the competition. But beyond this, the agenda also includes streamlining our portfolio, optimising the distribution of merchandise among the individual stores and adjusting the pricing architecture.

Key word: channel strategy. ADLER's online shop records high growth rates but still represents only a fraction of overall revenues. What role do online sales play for ADLER?

FREUDE Our goal is to make ADLER *the* platform for customers – with products, information and content available anytime, anywhere. In the ADLER app, in the ADLER online shop and in ADLER stores. We'll continue to grow organically in the area of e-commerce, but not at all costs. Here, too, improving profitability is the primary objective. As part of our omnichannel strategy, our online channel is an important factor for attracting new customers and increasing footfall in our stores. We also want to leverage potential revenue sources on highly frequented online marketplaces for ADLER.

What about the stores? What changes can we expect to see with the strategic realignment?

ODEMANN ADLER stores are primarily located outside the bustling prime locations. That is both a blessing and a curse. The rents are lower but those locations naturally don't offer the traditional walk-in business you get in a major shopping district like central Frankfurt or Düsseldorf. Traditional advertising or customer promotions are no longer enough to increase footfall. Therefore, in line with our stated mission: "Fashion for people in their prime," we're currently considering adding complementary product ranges or services to encourage people to visit our stores. Our vision is one-stop-shopping for people over 55. In other words, we want to make ADLER stores a place where our target group can find much more of interest to them than just clothing. It might be a hair salon, a chemist's with products specifically for best agers or a telecommunications provider. We're considering a number of options at the moment. Of course, we're also going to continue building on the strength of our staff, namely their sales expertise. Going forward, the ADLER brand will stand even more strongly for trained, motivated personnel and optimum service.

» Our goal is to make ADLER *the* platform for the 55 + target group, both "real" and digital – with products, information and content available anytime, anywhere. «

THOMAS FREUDE

If the traditional advertising methods no longer produce the desired results, how do you intend to address your customers in the future?

FREUDE ADLER's marketing will become more customised and digitised. No more TV marketing, just individual advertising mailers. That means less widespread advertising and instead consistent use and digitisation of our CRM data pool. The aim is to convince our customers of the advantages of our ADLER app and to communicate with them individually and efficiently at any time. In addition, we also want to break new ground. ADLER customers typically come to us first and foremost when they need a specific item of clothing. Or, and this is the really exciting thing, if they are offered a specially organized event. This can involve many things, from the popular ADLER bus tours with breakfast and fashion show, music events or styling shows – because older people have time and are looking for social contact. Our aim must therefore be to create additional incentives to visit an ADLER store through attractive events, which will have a stronger effect than simply the prospect of finding the next bargain. We're also planning to develop and publish an "ADLER magazine" with entertaining articles for our customers on the topics of fashion, travel, cooking and puzzles. As you see, the common theme in our strategy is creating added value for our customers that goes beyond the range of clothing we offer. We want to turn the ADLER store into a meeting place, where customers come to attend regular events and spend time with us.

» Our equity ratio compared to the industry is a very solid 41.5 %. This gives us financial leeway for the future. We're very glad that we can finance the growth targets for the coming years on our own. «

KARSTEN ODEMANN

So there's a lot in motion. And when will that show an impact on sales?

FREUDE 2018 will be the year in which we'll implement our product, channel and communications strategy and therefore once again focus on consolidation. Many of the measures we plan to introduce will take time to implement or their impact will not be felt immediately. Irrespective of this, however, we have our sights firmly set on returning to a profitable growth path and are very confident that we will be able to show slight growth in sales starting in 2019. With an optimised organisational, digitisation and IT structure and a continuing high level of cost efficiency, we are also aiming for a significant and sustained improvement in profitability.

Mr Freude, Mr Odemann, thank you for talking with us.


WHEN CASUALTY
IS YOUR FAVOURITE
FASHION TREND
– IT FITS.
ADLER
ALLES PASST

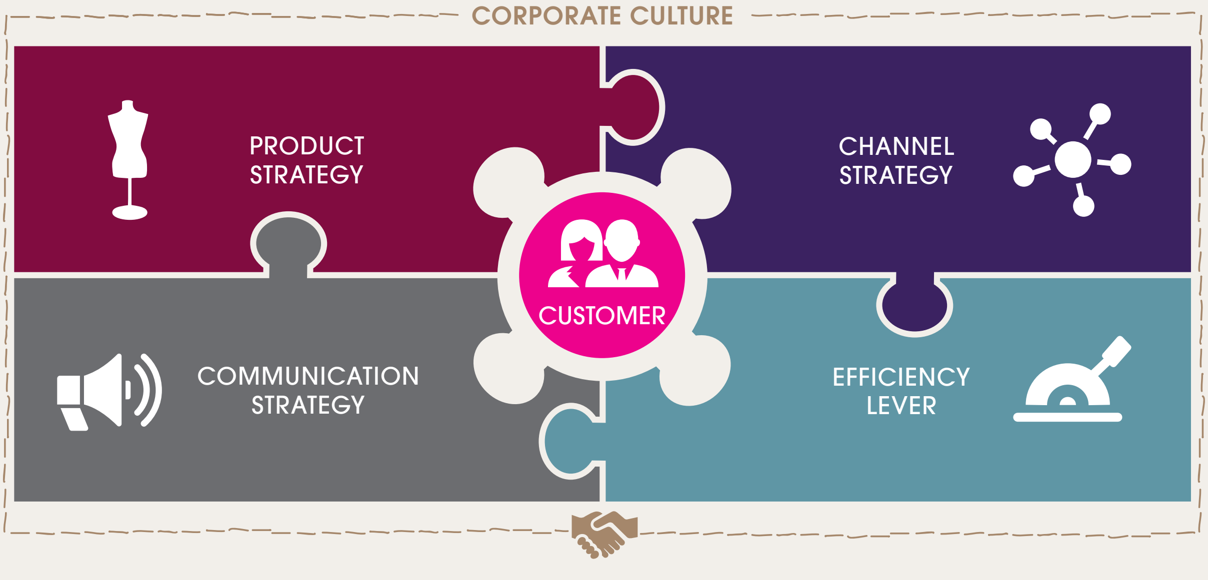
ADLER
ALLES PASST

ADLER 2020: » WE WANT TO BE THE DESTINATION FOR PEOPLE AGED 55 AND UP «

A fashion brand must convey a clear and consistent message, not only in its marketing strategy, but also in its product range. It is possible to strike a balance between continuing to offer existing customers the best possible service while at the same time winning over new, younger target groups. But over time, this can also diminish the brand's identity.

We have chosen to take a new, more mature approach to our strategy: gone are the days of chasing a younger audience! Our analyses indicate that we can generate profitable growth with our existing customer base and by setting a clear focus on people aged 55 and up. This is also based in part on demographic changes. It is projected that this age group will grow by approximately 10 % in the next 10 years to 32.8 million people and then stabilise at this high level.

We will continue to strengthen and expand ADLER's already excellent position among this target group: with a brand promise tailored to the needs and desires of our core target group – ensuring that people in the prime of their lives are impeccably dressed. And in doing so, we are striving to be more than just a fashion retailer. Our objective is to become the in-store and online destination for those 55 and up. The measures developed as part of our new strategic direction focus on this objective. The most important measures are presented in the following pages.



I go to ADLER because**...

The average ADLER customer*…	*… is 62 years old and retired.*	*… has time on their hands and is looking for social interaction.*	*… lives in a small town or more rural areas.*

** Source: October 2017 online survey // ** Source: Destatis*

PRODUCT STRATEGY

» WE FOCUS ON PRODUCTS THAT OUR CUSTOMERS LOVE AND VALUE «

ADLER generates approximately 75 % of its revenue from its high-margin own brands. Previous attempts to attract new customers to ADLER by offering well-known external brands did not have the desired success. But not just that: the product lines increasingly did not appeal to ADLER fans. This resulted in a decline in footfall and revenue. The trust our clients place in ADLER's own brands is one of our biggest strengths. We will re-gain and solidify this trust with our new product strategy.

We have come to understand what ADLER fans expect from us: a clear brand architecture that reflects their demand for high-quality fashion at fair prices. That is why we will place greater focus on our eleven own brands going forward. With fits specifically tailored to our customers these brands truly represent a unique selling point for ADLER and are vital to customer satisfaction.

Increasing own brands' share of revenue to 85 %

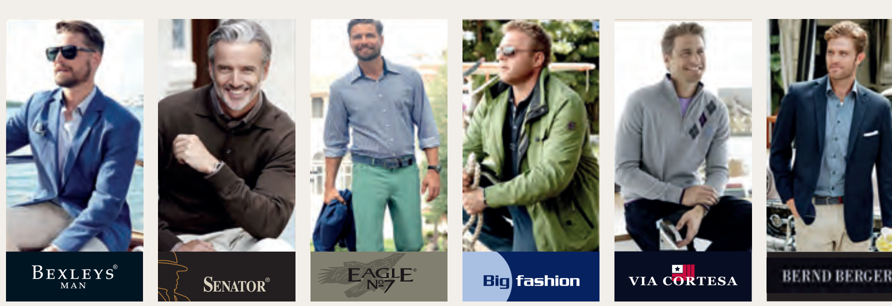
We will reduce our portfolio of currently more than 40 external brands by approximately half. In doing so, we aim to gradually increase the share of total revenue attributable to own brands from currently 75 % to 85 % by 2020. But we have also taken a close look at our own products and will phase out roughly 4,000 less popular items. By contrast, we will expand particularly popular product lines.

New IT systems will allow us to optimally manage our inventory according to demand at each of the 180 stores in order to reduce shortages and excess stock. This will help us reduce the revenue lost due to unavailable merchandise as well as mark-downs on unsold and discounted items.

We are confident that these measures will help us lift profitability per square metre and revenue.

> We have come to understand what ADLER fans expect from us: a clear brand architecture that reflects their demand for high-quality fashion at fair prices.

OWN BRANDS OF ADLER MODEMÄRKTE AG



PHASING OUT OF EXTERNAL BRANDS

External brand shops:

2017: 40

2020: 22

Share of revenue own brands:

2017: 75%

2020: 85%

CHANNEL STRATEGY

» WE'RE COMBINING THE BEST OF IN-STORE AND ONLINE SHOPPING «

Pursuing an omni-channel strategy – i.e., establishing a presence on as many sales channels and platforms as possible – is now par for the course in retail. But not everything that the digital and analogue worlds have to offer also makes economic sense. That's why we're fully focused on those things that our target group actually wants.

Whether in the stores, online or through the ADLER app: our aim is to offer a compelling brand experience, top-notch service and premium quality through every channel.

Sales excellence at brick-and-mortar shops

Our employees at the more than 180 ADLER stores play a key role. Their commitment and selling expertise have a vital influence on customer satisfaction, average ratio of revenue to sales receipts and – not least – on how likely customers are to come back and recommend ADLER to their friends. That is why we centre our brick-and-mortar channel strategy around outstanding sales expertise, which sets us apart from other fashion retailers. This strategy comprises five action areas:

- Firstly, we will use a footfall-based staffing plan to create the organisational conditions that enable us to ensure high employee availability even at peak hours.
- Secondly, we will offer sales staff regular in-depth training in order to further improve the quality of assistance and sales focus.
- Thirdly, we will introduce sensible incentives in order to reward staff with bonuses for going the extra mile.
- Fourthly, we will also make stores more attractive to help make shopping at ADLER a pleasant experience.
- And finally, we will cooperate with partners in the future to offer complementary services and products to our customers in the stores. This makes it possible for us to offer our customers true added value and achieve our objective of becoming the preferred destination for customers aged 55 and up.

> “We centre our brick-and-mortar channel strategy around outstanding sales expertise, which sets us apart from other fashion retailers.”

CORE ELEMENTS OF ADLER´S SALES EXCELLENCE

The pocked-sized ADLER store: download the ADLER app

Online sales growing increasingly important

While the brick-and-mortar stores remain crucial to the success of our business model, online sales are growing increasingly important for ADLER as a second pillar. ADLER's online shop helps attract new customers and increases footfall at the stores through the Click&Collect service. In addition, we aim to focus more strongly on popular online marketplaces in an effort to increase revenue and boost brand awareness.

One key tool of our digital sales strategy is the ADLER app, the functionality of which we intend to gradually expand in line with our objective of becoming the preferred retailer for our target group. The app is not only designed to enable users to conveniently shop via their mobile devices but also become a pocket-sized ADLER store: personalised advertising, event alerts and further content of relevance to our target group will help encourage regular use of the app and increase customer loyalty.

COMMUNICATIONS STRATEGY

» WE ARE TRANSFORMING ADLER INTO A MEETING PLACE «

Surveys tell us that existing ADLER customers are customers by conviction. Past customers largely tend to have a good image of the Company. And for those who didn't fall in love with the brand, advertising is not going to motivate them to visit an ADLER store.

We can't make everyone love ADLER. But we can increase ADLER fans' identification with the brand so that they visit us more often and win over neutral minds with our services.

The high share of revenue recorded using the ADLER customer loyalty card – accounting for more than 90 % of total revenue – offers impressive proof of how loyal our customers are. At the same time, thanks to the information provided by the card, we can understand their shopping patterns nearly as well as can a pure online retailer. We have neglected to leverage this trove of data thus far. And now that is going to change. That's because the unique combination of great loyalty and customer knowledge forms the basis for our new communications strategy.

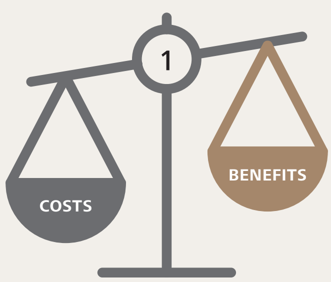
Digitalisation and individualisation of marketing measures

We will increase the efficiency of our marketing measures by digitising and individualising how we address customers based on the data supplied by their customer loyalty card. Specifically, that means no more expensive TV advertising with wasted coverage, and instead using more efficient, highly personalised communication through mailshots and via the ADLER app. We will gradually add new and relevant functionalities to the app, such as multimedia offerings that bring customers into contact with the ADLER brand more frequently.

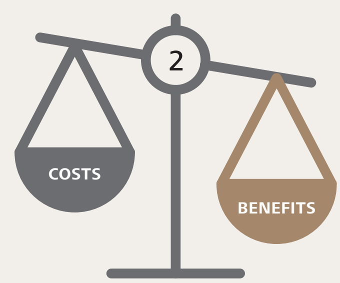
While we hope to leverage the advantages offered by digitisation, personal contact in the stores offers a vital brand promise, which we intend to keep in the future. Our objective is to become the preferred destination for those 55 and up. To achieve this, we aim to offer our customers true added value above and beyond shopping for clothes. A visit to an ADLER store should be a positive experience overall that offers our target group a wide range of events and activities. Recurring events such as travel presentations, concerts and styling workshops will make ADLER into a true meeting place – which offers us additional potential to communicate our expertise in fashion and bring our collections alive for our customers. In addition, we plan to introduce an ADLER magazine which will be available in the stores and offer fashion tips and other entertaining content such as travel, puzzles and health tips. In this way, ADLER customers bring their positive associations with the brand home with them.

> A visit to an ADLER store should be a positive experience overall that offers our target group a wide range of events and activities.

NEW MARKETING FOCUS ON EXISTING AND FORMER CUSTOMERS

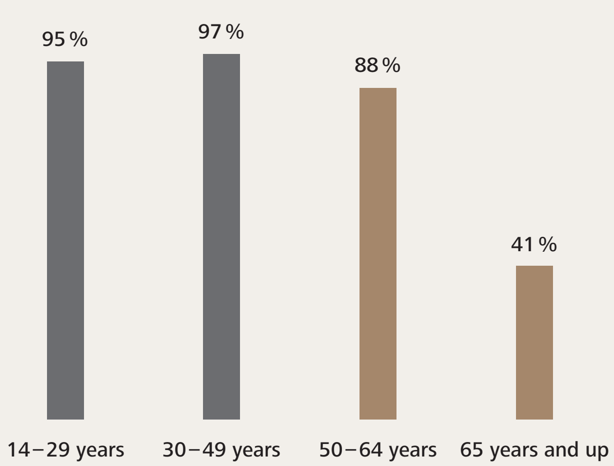


Individualised communication with existing and former customers via mailshots and ADLER app



Potential new customers addressed via TV marketing

USE OF SMARTPHONES HIGHLY POPULAR WITH ADLER TARGET GROUP*



* *Source: Bitkom Research*

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CONSOLIDATED FINANCIAL STATEMENTS

REPORT OF THE SUPERVISORY BOARD

Dear Shareholders,

Financial year 2017 was an eventful year that, in addition to the Supervisory Board's key decisions in connection with new appointments to the Executive Board, was marked by considerable challenges in the retail textiles sector. Thanks in part to the constructive collaboration between the Supervisory Board and the Executive Board, the measures to increase efficiency and profitability previously introduced in 2016 in response to the market environment contributed to further substantial cost savings during the year under review.

In 2017, the Supervisory Board performed the duties incumbent upon it by operation of law, the Articles of Association and its rules of procedure. The Supervisory Board regularly advised the Executive Board in managing the Company and assisted it in coordinating the Company's strategic objectives. The Executive Board fulfilled its duties with regard to the provision of information, notifying the Supervisory Board regularly, promptly and in detail, both in writing and orally, on the events and measures relevant for the Company. Based on these reports and during joint discussions with the members of the Executive Board, the Supervisory Board carefully and continually monitored the management. The full Supervisory Board voted on matters as required by operation of law or pursuant to the Articles of Association. In justified cases, resolutions were adopted outside of meetings. The Supervisory Board granted its consent to individual transactions to the extent this was required by law, the Articles of Association or the rules of procedure for the Executive Board. Above and beyond Supervisory Board meetings, the Chairman of the Supervisory Board and the Chairman of the Audit Committee maintained regular contact with the Executive Board and kept apprised of the current development of the business situation.

In preparation for the meetings of the full Supervisory Board, the shareholder and employee representatives addressed the agenda items in separate preliminary meetings. Overall, three regular meetings and two extraordinary meetings were held, with an average attendance rate of more than 83 %. The committees convened with an average attendance rate in excess of 87 %.

EFFECTIVE WORK IN THE COMMITTEES

In order to effectively perform its duties, the Supervisory Board formed four committees. The committees prepare issues and resolutions to be addressed by the full Supervisory Board. In appropriate individual cases, the full Supervisory Board may, to the extent permitted by law, assign powers to adopt resolutions to committees; the Supervisory Board exercised this right in 2017. The committee chairmen provided each subsequent Supervisory Board meeting with a detailed report of the matters discussed and resolved at the individual committee meetings. With the exception of the Audit Committee, the Chairman of the Supervisory Board chairs all committees. The composition of the committees can be found in the chapter entitled "Corporate Governance, Supervisory Board".

The *Personnel Committee* met four times in the year under review. It addressed the structure of the Executive Board remuneration system, and reviewed and set the remuneration for new and existing members of the Executive Board. For further details, we refer to the remuneration report in the management report. Key issues included the discussions surrounding the long-term succession planning and the related decisions

MASSIMILIANO MONTI
Chairman

made in March and April 2017 to recommend the early, mutually agreed upon termination of Lothar Schäfer's term of office as Chief Executive Officer and that the new member of the Executive Board, Andrew Thorndike, be appointed as Chief Operating Officer as well as the decision made in August to recommend that Thomas Freude be appointed as the new Chief Executive Officer. In addition, in accordance with the rules of procedure and in connection with Executive Board member Lothar Schäfer's departure, the Supervisory Board authorised Lothar Schäfer to enter into a business transaction with the Company.

The *Audit Committee* held four meetings in the year under review. In the presence of the auditor, the Chairman of the Executive Board, and the CFO, it discussed the annual and consolidated financial statements and management reports for Adler Modemärkte AG and the Group. It also issued its recommendation to the full Supervisory Board regarding the Supervisory Board's nomination for the election of the auditor for financial year 2017 by the Annual General Meeting. The interim reports were each discussed in detail prior to their publication. The auditor reported on all events material to the duties of the Supervisory Board that had arisen during the conduct of the audit and the auditor's review of the semi-annual financial report. The independence and qualifications of the auditor and additional services rendered by it were the subject of extensive discussions. On the basis of these discussions and the statement of independence by the auditor, it engaged it as auditor for financial year 2017 and specified the focal points of the audit, taking into account the recommendations of the full Supervisory Board. The Committee also addressed the new requirements under Regulation (EU) 537/2014 of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities as well as the German Audit Reform Act (*Abschlussprüfungsreformgesetz*, "AReG"). In this connection, the Committee passed a resolution in July 2017 on the ad hoc approval of a non-audit service for financial year 2017 and also passed a resolution in November 2017 on the approval of non-audit services by the auditor for financial year 2018. Moreover, the Audit Committee addressed the Company's accounting process and risk management system, as well as the effectiveness of internal audits and the internal control system. In line with its supervisory duties, the Audit Committee obtained reports from the Risk Management Officer and the head of the Internal Audit department regarding the focal points and findings of the audits conducted and the organisation and audit requirements. In addition, the Compliance Officer reported on the Company's compliance regime.

The *Nomination Committee* did not meet in the year under review.

The *Conciliation Committee* to be formed as required by law (§ 27 (3) of the German Co-determination Act (*Mitbestimmungsgesetz*, "MitbestG")) did not have to convene in the year under review.

MEETINGS AND RESOLUTIONS OF THE FULL SUPERVISORY BOARD

The regular discussions in the full Supervisory Board focused on issues such as the revenue development, earnings situation and employment trends of Adler Modemärkte AG and the Group, the financial position, the procurement of goods and the status of market expansion. The Supervisory Board received regular reports on corporate planning, strategic and business developments, and the current position of the Group.

The meeting on 14 March 2017 to discuss the annual accounts was centred around the annual and consolidated financial statements as at 31 December 2016, the management report, the Group management report and the dependent company report. In addition, the Supervisory Board discussed the agenda for the 2017 Annual General Meeting, including resolution proposals and the 2016 Annual Report and the corporate governance report contained therein. The full Supervisory Board also discussed the current financial indicators and a planned real estate transaction requiring approval.

The extraordinary meeting on 10 April 2017 focused on Executive Board personnel matters. On the basis of the Personnel Committee's resolutions, the Supervisory Board reached decisions on the appointment of the new Executive Board member and Labour Director, Andrew Thorndike, and on the early, mutually agreed upon termination of Lothar Schäfer's appointment as Chief Executive Officer. The Supervisory Board also discussed the Executive Board's areas of responsibility, the amendments to the Supervisory Board's rules of procedure and the implementation of the recommendations of German Corporate Governance Code, as amended.

Following a review of the implementation of the recommendations of the German Corporate Governance Code, the full Supervisory Board resolved in early May by way of a resolution outside of a meeting to issue a new Declaration of Conformity by the Executive Board and the Supervisory Board in accordance with § 161 of the German Stock Corporation Act (*Aktiengesetz*, "AktG").

The meeting of the Supervisory Board on 23 May 2017 focused on the Company's current financial indicators, the ADLER online shop and the Company's subsidiaries. The Supervisory Board also discussed the measures introduced in collaboration with the Executive Board to increase efficiency and profitability as well as to optimise the Company's cash flows. The full Supervisory Board also granted its consent for various transactions and measures that were presented by the Executive Board and required approval in accordance with the rules of procedure.

Another meeting of the Supervisory Board was held on 1 August 2017. In addition to the report by the Chairman of the Audit Committee on the semi-annual financial report and the audit review findings in this regard, the full Supervisory Board addressed the audit findings and results of the Committee concerning the effectiveness of the internal control system and internal audits. Another key agenda item was the decision, reached on the basis of the Personnel Committee's resolutions, to appoint Thomas Freude as the new Chief Executive Officer. The Supervisory Board also discussed setting a target for the proportion of women on the Executive Board pursuant to § 111 (5) sentence 1 AktG, the Company's performance during the current financial on the basis of an in-depth Executive Board report, the status of the measures designed to increase efficiency and profitability, the Company's existing portfolio of stores and potentially executing a business transaction requiring approval in accordance with the rules of procedure.

Strategic considerations and Purchasing and Supply Chain Management measures were the primary items discussed at the extraordinary meeting on 12 October 2017. In this connection and following an in-depth discussion, the Supervisory Board granted the Executive Board its consent for various measures and transactions. Further topics of intense discussion for the full Supervisory Board were the Company's current business performance and the status of the measures introduced to increase efficiency and their impact on the Company's performance going forward.

In November 2017, the Supervisory Board conducted its annual efficiency audit of the Supervisory Board.

CORPORATE GOVERNANCE AND DECLARATION OF CONFORMITY

The Supervisory Board discussed in detail the contents of the German Corporate Governance Code. Although the Executive Board and the Supervisory Board had issued a Declaration of Conformity on 9 May 2016, the Executive Board, in its meeting on 10 May 2017, and the Supervisory Board, outside the context of a meeting on the same date, both resolved to issue an updated Declaration of Conformity pursuant to § 161 AktG. This was made permanently available on the Company's website. According to that declaration, the Company has been in conformity with the Code's recommendations since 10 May 2017, with five exceptions, and will continue to be in future.

As previously reported, the work of the Supervisory Board during the year under review stood out by virtue of its high attendance rate in excess of 85 % for Committee meetings and the meetings of the full Supervisory Board. With the exception of Cosimo Carbonelli D'Angelo and Corinna Groß, no member of the Supervisory Board attended only half or fewer of the meetings of the Supervisory Board or the meetings of the committees on which they served. Apart from their role as board members and the transactions and legal relationships with related parties referred to in the notes to the annual and consolidated financial statements, the Supervisory Board members have no other legal relationships with the Company. Supervisory Board members Dott. Michele Puller and Paola Viscardi-Giazzi have contractual and professional ties to companies that are affiliates of S&E Kapital GmbH, Munich. Mr Cosimo Carbonelli D'Angelo is a member of the governing body/proprietor of one of the Company's suppliers. Therefore, these three Supervisory Board members also have obligations towards the interests of these companies. The interests of these companies might not be identical to the interests of Adler Modemärkte AG, meaning that there is potential for conflicts to arise in individual cases. Apart from this, there was no basis for conflicts of interest on the part of Supervisory Board and Executive Board members in terms of their obligations towards Adler Modemärkte AG.

Apart from this report, the corporate governance of the company is also presented in the Annual Report under the chapter entitled "Corporate Governance Report". That report was submitted jointly by the Executive Board and Supervisory Board and also contains the full text of the Declaration of Conformity dated 10 May 2017, including the notes on the five deviations from the recommendations of the German Corporate Governance Code.

AUDIT OF ANNUAL AND CONSOLIDATED FINANCIAL STATEMENTS

PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft (formerly PricewaterhouseCoopers AG Wirtschaftsprüfungsgesellschaft), Stuttgart, audited the annual financial statements and the consolidated financial statements of Adler Modemärkte AG as at 31 December 2017 prepared by the Executive Board in accordance with German commercial law provisions and the Group management report combined with the management report and issued them all an unqualified auditors' report. The consolidated financial statements were prepared in accordance with the International Financial Reporting Standards (IFRSs) as adopted by the European Union (EU) and the supplemental commercial law provisions pursuant to § 315e (1) of the German Commercial Code (*Handelsgesetzbuch*, "HGB").

The dependent company report submitted by the Executive Board for financial year 2017, concerning relationships with affiliated companies, was also audited by the auditor. The dependent company report of the Executive Board was issued the following unqualified auditors' report: "After our due audit and assessment, we confirm that 1. the factual statements of the report are correct, 2. the consideration paid by the Company was not unreasonably high for the legal transactions set forth in the report."

The aforementioned documents and the Executive Board's recommendation for the appropriation of net retained profits have been provided to the Supervisory Board in good time. At its meeting on 6 March 2018 the Audit Committee first addressed the aforementioned documents in detail. At the meeting on 13 March 2018, the full Supervisory Board then discussed in detail and audited the aforementioned submissions by the Executive Board after the Committee Chairman had reported on the meeting of the Audit Committee. Both meetings were attended by representatives of the auditor, who reported on the key findings of the audit. It was also found that there are no material weaknesses in the internal control system and the risk early warning system related to the accounting process. In addition, the representatives of the auditor answered questions by the members of the Supervisory Board and confirmed that the risk early warning system established by the Executive Board is suitable for detecting at an early stage developments that may jeopardise the Company as a going concern. The auditor also examined the scope, costs and the focal points of the audit stipulated by the Audit Committee. There are no objections to be raised after audit and discussion of the annual financial statements, the consolidated financial statements, the management report, the Group management report as well as the Executive Board's dependent company report in the Audit Committee and our own audit in the Supervisory Board. The Supervisory Board has approved the findings of the audit by the auditor and unanimously approved the annual financial statements and consolidated financial statements. The annual financial statements are therefore adopted. After reviewing and considering all arguments, we have approved the Executive Board's profit appropriation proposal to use net retained profits to pay a dividend of €0.05 per no-par value share carrying dividend rights.

CHANGES TO COMPOSITION OF THE EXECUTIVE BOARD

In its extraordinary meeting on 10 April 2017, the Supervisory Board unanimously approved of the early, mutually agreed upon departure of the previous Chief Executive Officer Lothar Schäfer with effect from 30 April 2017 and also unanimously approved the appointment of Andrew Thorndike to the Executive Board and as the Company's Labour Director with effect from 1 May 2017 for a term of five years until the end of April 2022. The appointment of Mr Thorndike has been revoked with immediate effect by unanimously resolution of the Supervisory Board in its extraordinary meeting on 30 January 2018.

In its meeting on 1 August 2017, the Supervisory Board unanimously appointed Thomas Freude to the Executive Board of the Company with effect from 11 September 2017 for a term of five years until the beginning of September 2022 and appointed him Chairman of the Executive Board.

In its meeting on 13 March 2018, the Supervisory Board unanimously appointed Carmine Petraglia to the Executive Board of the Company with effect from 1 June 2018 for a term of four years and seven months until the end of December 2022.

The Supervisory Board would like to thank the members of the Executive Board, all employees and the employee representatives of Adler Modemärkte AG for their hard work over the past year in the face of a once again very challenging market environment.

Haibach, 13 March 2018
For the Supervisory Board

Massimiliano Monti
Chairman

SUPERVISORY BOARD

The members of the Supervisory Board of Adler Modemärkte AG in financial year 2017 were as follows:

Massimiliano Monti [1*, 2, 3*, 4*], *Lugano, Switzerland*, Chairman of the Supervisory Board, partner at Equinox S.A.

Majed Abu-Zarur [1, 2, 4], *Viernheim, Germany*, Deputy Chairman of the Supervisory Board, Chairman of the Joint Works Council at Adler Modemärkte AG

Wolfgang Burgard [1, 2*, 3], *Dortmund, Germany*, Managing Director of Bund Getränkeverpackungen der Zukunft GbR

Cosimo Carbonelli D'Angelo [1, 4], *Naples, Italy*, Chairman of the Managing Board of G.&C. Holding S.r.l.

Corinna Groß, *Neuss, Germany*, Deputy Head at ver.di, North-Rhine Westphalia District

Frank König, *Berlin, Germany*, Staff Member Information Desk and Cash Desk at Adler Modemärkte AG

Peter König [1, 2], *Rottendorf, Germany*, secretary of the national executive board of the ver.di union

Georg Linder [1, 2, 4], *Hösbach, Germany*, Divisional Head of Procurement Planning and Merchandise Management at Adler Modemärkte AG

Giorgio Mercogliano [3], *Montagnola – Lugano, Switzerland*, partner at Equinox S.A.

Dott. Michele Puller, *Bergkamen, Germany*, Chairman of the Executive Board of Steilmann Holding AG i.l.

Paola Viscardi-Giazzi [2], *Dortmund, Germany*, Executive Board member of Steilmann Holding AG i.l.

Beate Wimmer, *Nettetal, Germany*, Specialist Consultant Information Desk, Cash Desk and Sales at Adler Modemärkte AG

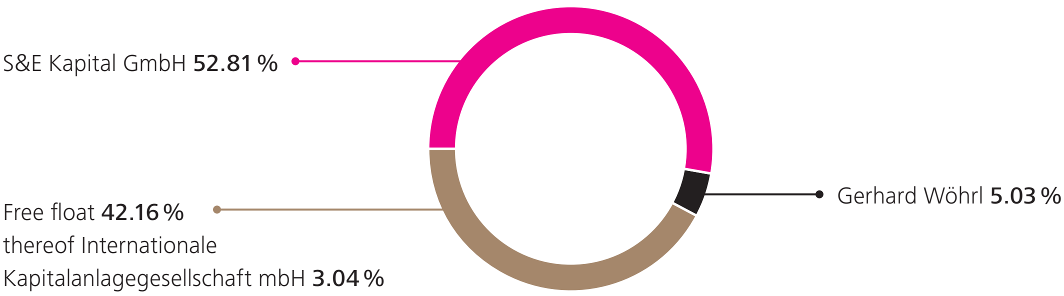
(Last amended: 31 Dec. 2017) Memberships in:
1) Personnel Committee, 2) Audit Committee, 3) Nomination Committee, 4) Conciliation Committee
** Chairman of the Committee*

ADLER SHARES

ADLER shares have been traded on the regulated market of the Frankfurt Stock Exchange since 22 June 2011. The share capital of Adler Modemärkte AG is divided into 18,510,000 no-par value bearer shares, each representing a notional interest in the share capital of € 1.00.

ADLER shares are admitted to trading on the regulated market (regulierter Markt) and the regulated market sub-segment with additional post-admission listing obligations (Prime Standard) of the Frankfurt Stock Exchange. The shares are included in several Deutsche Börse AG indices, including the CDAX, the Classic All Share, the DAXsector Consumer and the DAX Subsector Clothing & Footwear. ADLER's exchange ticker symbol is ADD; its Reuters instrument code is ADDG.DE.

SHAREHOLDER STRUCTURE*



** reportable shareholdings, as of 31 December 2017*

ADLER'S SHARE PRICE PERFORMANCE

Even though conditions continued to be difficult in the textile industry – the industry magazine "TextilWirtschaft" reported a decline of 2 % in revenues of brick-and-mortar fashion retailers for 2017 – the ADLER share price recorded very healthy growth in the year under review: with an increase of almost 24 %, it far outperformed the MAI fashion share index (Modeaktienindex) calculated by "TextilWirtschaft". By comparison, the MAI, which comprised 31 fashion stocks at the end of the year, was up by only 11 % in the same period.

Following the losses that ADLER's shares suffered in the 2016 financial year, prices recovered significantly in 2017, recording considerably stronger growth than the DAX stock index, which also performed robustly.

Starting at € 4.71 at the close of the last trading day of 2016, the performance of the ADLER share price was initially affected by volatility. Following a buoyant start to the year, with price gains in the double-digit percentage range, the shares lost ground again, falling back to their starting price by the middle of March. The publication of the forecast for 2017, in which ADLER anticipated an increase in EBITDA to € 27 – 30 million, marked a turning point: boosted by the announcement of positive non-recurring effects from a real estate transaction and the publication of good quarterly figures, the share price started an upwards trend lasting several weeks. On 24 May, the share price reached its year high of € 6.23, an increase of 34 % compared with 30 December 2016.

In a generally bearish market, the share price relinquished some of its gains, retreating to € 5.26 by the beginning of October. After another upwards move, which ended in the share price reaching € 6.21 and almost touching its high for the year, it lost some ground again until the end of the year. ADLER's share price ended the year at € 5.83, thus improving by 23.9 % overall and significantly outperforming the DAX, which was up by 12.5 %.

ADLER SHARE PRICE VERSUS DAX AND SDAX

Against a backdrop of strong economic recovery, the performance of the DAX was also better than many analysts had predicted at the beginning of the year. From a level of 11,481 points on the last trading day of 2016, the index almost exclusively maintained levels above the 12,000 points mark from as early as March. In the middle of June, the DAX reached its initial all-time high of more than 12,900 points, although it subsequently declined again, at times sharply. A short-lived fall to below 12,000 points on 30 August preceded another turning point: positive economic data from the eurozone and a weaker euro against the dollar triggered a rally that pushed the DAX above the 13,000 points mark on 12 October for the first time in its 30-year history. It reached its all-time high of 13,479 points on 3 November (+17.4%). For the remainder of the year, the DAX stayed mostly around the 13,000 points level, ending the 2017 trading year up 12.5% at 12,918 points.

The performance of the SDAX was extremely steady in 2017. Amid low volatility, the index rose from 9,519 points on 30 December 2016 to 11,887 points on 29 December 2017, reflecting an increase of 24.9%.

ADLER SHARE VERSUS DAX AND SDAX (INDEX AT 30 DECEMBER 2016 = 100)

DIVIDEND DISTRIBUTION

The Executive Board and Supervisory Board of Adler Modemärkte AG aim to let the shareholders of Adler Modemärkte AG participate commensurately in the Company's profits. Net profit for the year had declined to €0.4 million in the 2016 financial year (previous year: €7.9 million). The Executive Board and Supervisory Board therefore proposed to the Company's Annual General Meeting on 24 May 2017 that it resolve not to distribute a dividend for the 2016 financial year (previous year: €0.50). This decision was supported by the shareholders present, so that no dividend was paid in 2017 for the 2016 financial year.

INVESTOR RELATIONS

ADLER continued its intensive investor relations activities in the year under review and actively sought dialogue with the relevant target groups. In particular, these include institutional and private investors, analysts, the media, employees and the interested public.

Investor relations activities are performed by the Executive Board together with the IR department and are designed to increase public awareness of ADLER and to inform the various target groups about business performance, business policies and the management's strategies and objectives. The Executive Board aims to help achieve an appropriate valuation for the shares and to ensure sufficient market liquidity by providing the required transparency.

In order to achieve this objective, the Executive Board once again participated in capital market conferences and roadshows, including the Oddo Forum in Lyon, the German Corporate Conference in Frankfurt, the Baader Investment Conference in Munich and the German Equity Forum in Frankfurt. In addition, a large number of one-on-one meetings were again held with analysts and investors in 2017.

DESIGNATED SPONSORS

In financial year 2017, M.M. Warburg and Oddo Seydler were the designated sponsors of ADLER's shares.

In addition to these two institutions, five other investment firms monitored and prepared analyses on Adler Modemärkte AG and regularly reported on the Company's performance: Baader Bank, Bankhaus Lampe, Equinet, Montega and Sphene Capital.

CORPORATE GOVERNANCE REPORT

Effective corporate governance that reflects ADLER's high values and standards goes without saying. Corporate governance stands for responsible and transparent management aimed at adding value sustainably and steering and monitoring the Company. However, since the initial public offering in June 2011, it also stands for efficient collaboration between the Executive Board and the Supervisory Board, attention to shareholder and employee interests and respect for the Company's fundamental values and objectives. Openness and transparency in corporate communication are also aspects of good corporate governance and apply to all parts of the Company. In pursuing and refining these principles, ADLER wishes to continually reinforce the trust of employees, shareholders, investors and the public in the Company. Together, the Executive Board and the Supervisory Board provide the following information on governance measures and implementation in accordance with Section 3.10 of the German Corporate Governance Code.

IMPLEMENTATION OF THE GERMAN CORPORATE GOVERNANCE CODE

As a German stock corporation listed on the Prime Standard sub-segment of the regulated market (regulierter Markt) of the Frankfurt Stock Exchange, ADLER mainly bases its corporate governance on the laws applicable in Germany and the recommendations and suggestions of the German Corporate Governance Code. In financial year 2017, the Executive Board and the Supervisory Board discussed in detail the stipulations of the amended Code in the version adopted on 7 February 2017 and published on 24 April 2017. In 2017, the Supervisory Board focussed on the recommendations concerning Executive Board remuneration, the composition of the Supervisory Board and diversity at the Company during its in-depth deliberations. After the Executive Board and the Supervisory Board issued a declaration of conformity on 09 May 2016, the declaration of conformity was updated on 10 May 2017; it is published on ADLER's website and included at the end of this report. Since 10 May 2017, Adler Modemärkte AG complies with all but five recommendations of the Code (see Declaration of Conformity). As already indicated in the Declaration of Conformity dated 10 May 2017, in the meantime the Supervisory Board appointed an additional member of the Executive Board with effect of 11 September 2017 and, at the same time, nominated such member as Chairman of the Executive Board. Since then, Adler Modemärkte AG complies with all but four recommendations of the Code.

EXECUTIVE BOARD AND SUPERVISORY BOARD

The Executive Board and the Supervisory Board of ADLER work closely together for the benefit of the Company and are in regular contact. An intensive dialogue between the two boards forms the basis for efficient corporate governance. The Executive Board regularly and promptly provides the Supervisory Board with detailed information on any and all issues relevant to the Company. This includes business development, budgeting, the risk situation, risk management, adherence to compliance guidelines and any variances between the business development and the original budget. The Supervisory Board has specified reporting duties of the Executive Board that go above and beyond the statutory obligations. Moreover, there is a regular exchange of information between the CEO and the Chairman of the Supervisory Board.

The German Corporate Governance Code recommends that attention be paid to diversity and reasonable inclusion of women in the Supervisory Board and the Executive Board and when filling management positions.

The Executive Board of Adler Modemärkte AG currently has two members, both male. However, the Supervisory Board appointed in its meeting on 13 March 2018 a third male member of the Executive Board with effect of 1 June 2018. In its decisions to date, the Supervisory Board has always taken into account the recommendations of the German Corporate Governance Code. Taking into account the Company's best interests and circumstances as well as the target and deadline for meeting it set for the second time pursuant to § 111 (5) AktG and laid out in the corporate governance statement pursuant to § 289f (2) no. 4 HGB, the Supervisory Board will also continue to pay attention to the greatest possible diversity and reasonable inclusion of women in the work of the Personnel Committee.

When filling management positions in the Company, it has always been the ADLER Executive Board's fundamental approach to not only factor in professional qualifications but also to strive for the greatest possible level of diversity and reasonable inclusion of women. Personnel decisions in financial year 2017 were also made on the basis of this fundamental approach. Because diversity translates into opportunity, the ADLER Executive Board will take this principle into account going forward as well in the context of the targets and deadlines set again pursuant to § 76 (4) AktG and laid out in the corporate governance statement pursuant to § 289f (2) no. 4 HGB.

The Supervisory Board has a total of twelve members and, pursuant to the German Co-determination Act, has an equal number of shareholder and employee representatives. According to its own estimation, the Supervisory Board has a reasonable number of independent members. Its members should have complementary professional experience and skills in order to duly perform their duties. The members as a whole are also familiar with the sector in which the Company operates. However, the Supervisory Board continues to not specify any targets in terms of its constitution since this would too greatly limit its flexibility in searching for candidates with the necessary expertise and experience. For the same reason, the Company has also opted not to set an age limit for members of the Supervisory Board or any term limit for members of the Supervisory Board and, when making nominations, will not take into account specific targets, but rather stated intentions. However, the Supervisory Board in its current composition meets the requirements of the law and the Articles of Association. Only the percentage of women, which is currently 25 %, is slightly below that which is required under § 96 (2) AktG. In future, women are to be reasonably represented on the Supervisory Board and in compliance with the statutory minimum of 30 %.

Information about the board members' areas of responsibility and their CVs are available online on the Company's website under the heading Investor Relations/The Company/Management. For information on the remuneration of members of the Executive Board and Supervisory Board, see the "Remuneration report", which constitutes a component of the management report.

AVOIDANCE OF CONFLICTS OF INTEREST

In performing their board work, members of both the Executive Board and the Supervisory Board have an obligation towards ADLER's corporate interest. On this basis, personal interests may not be pursued nor may benefits be granted to third parties when decisions are taken. In financial year 2017 there were no conflicts of interest requiring disclosure to the Supervisory Board without undue delay. Transactions involving the Company, its executive bodies and related parties were always executed at arm's length received the approval of the Supervisory Board if they exceeded the materiality threshold. No member of the Supervisory Board performed special consultancy or other services for the Company in financial year 2017.

We refer to the notes to the consolidated financial statements for information on the memberships held by Executive Board and Supervisory Board members in statutory supervisory boards and comparable domestic and foreign boards of commercial enterprises. On this basis, one Executive Board member presently holds a supervisory board position in listed non-Group companies or on the supervisory bodies of non-Group companies. The notes to the consolidated financial statements include related party disclosures.

D&O INSURANCE DEDUCTIBLE

In accordance with the statutory requirements under § 93 (2) sentence 3 of the German Stock Corporation Act (Aktiengesetz, "AktG") the Company has taken out financial losses and liability insurance ("D&O insurance") for its executive bodies. The reasonable deductible provided for therein has been agreed for members of the Executive Board as well as for members of the Supervisory Board.

REPORTABLE SECURITIES TRANSACTIONS AND SHAREHOLDINGS

Persons discharging managerial responsibilities and persons closely associated with them within the meaning of the Market Abuse Regulation (MAR), which specifically includes members of the Executive Board and the Supervisory Board, are required under article 19 MAR to disclose reportable transactions relating to the shares or debt instruments of Adler Modemärkte AG or to derivatives or other financial instruments linked thereto if the total value of the transactions reaches or exceeds €5,000 in a calendar year. No such transactions were reported to the Company in financial year 2017. Detailed information in this regard is published on the ADLER website.

Apart from the share-based remuneration components of Executive Board compensation reported in detail in the remuneration report, the Company currently does not provide any other securities-based incentive systems.

SHAREHOLDERS AND ANNUAL GENERAL MEETING

The shareholders of Adler Modemärkte AG exercise their rights at the Company's Annual General Meeting, at which each ADLER share is granted one vote. The Annual General Meeting is held once annually for purposes of providing the shareholders with detailed information. The shareholders may exercise their voting right at the Annual General Meeting either themselves or through a proxy of their choice or a Company proxy subject to instruction. In addition, the shareholders may vote in writing through a postal ballot without appointing a proxy. Moreover, all key information and documents relating to the Annual General Meeting shall be made available on ADLER's website in good time.

CONTROL AND RISK MANAGEMENT

At ADLER, professional corporate management based on sound corporate governance also includes the continual and systematic management of corporate opportunities and risks. Risk management and risk controlling to be effected by the Executive Board make a material contribution to the detection and evaluation of risks early on. This makes it possible to effectively reduce and manage risk exposures. The Audit Committee set up by the Supervisory Board not only supervises the accounting, the accounting process and auditing, but also regularly monitors the effectiveness of the internal control, risk management and internal auditing systems as well as compliance. The systems are continually updated and modified in line with changing framework conditions. Interested shareholders will find details in the risk report.

CORPORATE COMPLIANCE AS A MANAGEMENT DUTY OF THE EXECUTIVE BOARD

ADLER considers corporate compliance – a measure aimed at ensuring adherence to statutory and official provisions, as well as to internal company guidelines – to be a management and supervisory duty. In 2016, the Company published its first sustainability report, underscoring its commitment to social and ecological sustainability. Corporate compliance also includes compliance with capital market, anti-corruption and antitrust law. ADLER has consolidated the understanding of corporate compliance in its code of conduct. This code of conduct, which has been implemented Group-wide, can be accessed on the ADLER website. However, these principles for avoiding violations of anti-corruption, competition and antitrust law also address how to deal with employees, clients, suppliers and company property properly and respectfully. Using the existing principles as a foundation, the objective is to continue to promote the understanding of corporate compliance within the Company through regular employee training. Audits, risk analyses and the lasting implementation of solutions to address issues identified during the course thereof will further improve corporate compliance. The programme will be supported by a whistleblower system that will encourage employees to openly address any concerns they have and report circumstances that may indicate a violation of law or internal guidelines.

ACCOUNTING AND AUDITING

ADLER's consolidated financial statements and quarterly reports are prepared in accordance with the International Financial Reporting Standards (IFRSs) as adopted by the European Union. The mandatory separate financial statements of Adler Modemärkte AG are prepared in accordance with the provisions of the German Commercial Code (Handelsgesetzbuch, "HGB"). For the year under review, the Supervisory Board arranged with the auditor, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Stuttgart, that the Chairman of the Audit Committee be advised immediately of any potential grounds for disqualification or partiality arising during the audit if these cannot be rectified without undue delay. The auditor shall report without undue delay on any and all key findings and events relevant to the duties of the Supervisory Board that it becomes aware of during performance of the audit. Moreover, the auditor shall inform the Supervisory Board or note in the audit report if it discovers facts in performing the audit that reveal an inaccuracy in the declaration of conformity issued by the Executive Board and the Supervisory Board in accordance with § 161 AktG. Furthermore, the Supervisory Board has obtained a declaration of auditor independence in accordance with Section 7.2.1 of the German Corporate Governance Code. The statutory requirements and rotation obligations under §§ 319 and 319a HGB are met.

TRANSPARENT CORPORATE GOVERNANCE

ADLER is committed to ensuring the greatest possible transparency by providing prompt, detailed and regular information on the Company's position and key business changes. Only in this way can the trust investors, capital providers, the media, and the interested public placed in ADLER be ensured long-term. The investor relations work was once again intensified in financial year 2017, so that ADLER is in even closer contact with the capital market. Moreover, there is an in-depth dialogue at analyst and investor conferences and during teleconferences and roadshows. These are presented regularly to discuss the annual financial statements, the publication of interim reports and current affairs. In addition, the Company publishes the accompanying presentations on ADLER's website.

Information on current developments for the ADLER Group and all publications are available to the shareholders and potential investors online at *www.adlermode-unternehmen.com*. All press releases and ad hoc disclosures by Adler Modemärkte AG are published in German and English under the heading "Investor Relations", under "News & Releases". Apart from ad hoc disclosures pursuant to article 17 MAR, ADLER has a policy of providing transparent and prompt information through press releases, notices on voting rights changes and reportable proprietary trades by senior executives. The Company's Articles of Association and information on implementation of the recommendations of the German Corporate Governance Code may be found in the "Corporate Governance" section, and the consolidated financial statements, interim financial reports and presentations may be found under "Reports & Publications".

In addition, the ADLER website offers extensive, up-to-date information on recurring dates, the date of the Annual General Meeting, publication dates for the financial reports and Company appearances at capital market forums under the heading "Financial Calendar".

DECLARATION OF CONFORMITY

The Executive Board and the Supervisory Board of Adler Modemärkte AG have issued the following declaration:

"Declaration of the Executive Board and Supervisory Board of Adler Modemärkte Aktiengesellschaft relating to the recommendations of the "German Corporate Governance Code Government Committee" as per Section 161 of the German Stock Corporation Act (Aktiengesetz, "AktG"):

The Executive Board and Supervisory Board of Adler Modemärkte AG declare that the recommendations of the German Corporate Governance Code ("Code") as amended on May 5, 2015, published by the Federal Ministry of Justice on June 12, 2015 in the official section of the Federal Gazette, were complied with during the time period since the last Declaration of Conformity from May 11, 2016 until April 23, 2017 with the subsequent exceptions:

Fixed amount as cap for the overall Executive Board remuneration (Section 4.2.3 para. 2 sent. 6 of the Code)
All current employment contracts of the Executive Board include caps for the fixed as well as the variable remuneration components. A fixed amount as cap for the overall amount of remuneration is not included in all current employment contracts of the Executive Board. The Supervisory Board sees no necessity for the explicit definition of a fixed amount as cap for the overall remuneration, since all employment contracts of the Executive Board contain a fixed monetary cap for all key remuneration components and thus implicitly the amount of total remuneration is limited accordingly.

Disclosure of Executive Board remuneration (Section 4.2.5 para. 3 of the Code)
The Company's Annual General Meeting on May 30, 2011, and May 4, 2016 passed a resolution that there would be no individualized disclosure of Executive Board remuneration. Therefore, the Company will also not implement the recommendations in Section 4.2.5 para. 3 of the Code which relate to the disclosure of the remuneration of each member of the Executive Board and the use of according model tables.

Re-appointment of Members of the Executive Board (Section 5.1.2 para. 2 sent. 2 of the Code)
In its decision dated July 17, 2012 (Az. II ZR 55/11), the Federal Court of Justice (Bundesgerichtshof, "BGH") generally permitted the early re-appointment after the consensual resignation of a member of the Executive Board prior to one year before the end of the original appointment period. In the opinion of the BGH, this generally also applies if there are no special circumstances for this course of action. Based on this decision and the requirement of a resolution by the Supervisory Board, which must act in the interest of the company, we do not consider necessary additional preconditions ("special circumstances") and we declare, as a precautionary measure, a deviation from the recommendation in Section 5.1.2 para. 2 sent. 2 of the Code.

Composition of Supervisory Board (Section 5.4.1 para. 2 and 3 of the Code)
The Company's Supervisory Board has not named any specific targets relating to the composition of the Board; for that reason, there is also no publication of the target and status of implementation in the Corporate Governance report. It is true that the Supervisory Board aims to have members with different and complementary professional experience and skills. Nevertheless, the Supervisory Board believes that the stipulation of specific targets would restrict the flexibility of the Supervisory Board too greatly in its search for candidates with the necessary ability and experience. For the same reason, the Company does not stipulate neither an age limit for members of the Supervisory Board nor a control limit for the term of membership in the Supervisory Board. With regard to nominations of the Supervisory Board, therefore, no specific targets are taken into consideration, but rather the intentions mentioned above.

Furthermore, the Executive Board and Supervisory Board declare that the recommendations of the German Corporate Governance Code ("Code") as amended on February 7, 2017, published by the Federal Ministry of Justice on April 24, 2017 in the official section of the Federal Gazette, were complied with since their publication and will be complied with in the future with the following exceptions:

Appointment of the Chairman of the Executive Board (Section 4.2.1 sent. 1 sub-clause 2 of the Code)
Due to the leave of the former Chairman of the Executive Board from May 1, 2017, the Executive Board has no Chairman or spokesperson. The Supervisory Board intends to appoint another member of the Executive Board and Chairman and thus will follow the recommendation in Section 4.2.1 sent. 1 sub-clause 2 of the Code in the future again. Until then, the acting members of the Executive Board shall lead the company jointly.

Fixed amount as cap for the overall Executive Board remuneration (Section 4.2.3 para. 2 sent. 6 of the Code)
All current employment contracts of the Executive Board include caps for the fixed as well as the variable remuneration components. Until April 30, 2017, a fixed amount as cap for the overall amount of remuneration was not included in all employment contracts of the Executive Board up to that date. Although the Supervisory Board sees no necessity for the explicit definition of a fixed amount as cap for the overall remuneration, since all employment contracts of the Executive Board contain a fixed monetary cap for all key remuneration components and thus implicitly the amount of total remuneration is limited accordingly. However, since May 1, 2017, all current employment contracts of the Executive Board also include caps for the overall amount of remuneration. The Supervisory Board also intends to comply with the recommendation in Section 4.2.3 para. 2 sent. 6 of the Code in the future.

Disclosure of Executive Board remuneration (Section 4.2.5 para. 3 of the Code)
The Company's Annual General Meeting on May 30, 2011, and May 4, 2016 passed a resolution that there would be no individualized disclosure of Executive Board remuneration. Therefore, the Company will also not implement the recommendations in Section 4.2.5 para. 3 of the Code which relate to the disclosure of the remuneration of each member of the Executive Board and the use of according model tables.

Re-appointment of Members of the Executive Board (Section 5.1.2 para. 2 sent. 2 of the Code)
In its decision dated July 17, 2012 (Az. II ZR 55/11), the Federal Court of Justice (Bundesgerichtshof, "BGH") generally permitted the early re-appointment after the consensual resignation of a member of the Executive Board prior to one year before the end of the original appointment period. In the opinion of the BGH, this generally also applies if there are no special circumstances for this course of action. Based on this decision and the requirement of a resolution by the Supervisory Board, which must act in the interest of the company, we do not consider necessary additional preconditions ("special circumstances") and we declare, as a precautionary measure, a deviation from the recommendation in Section 5.1.2 para. 2 sent. 2 of the Code.

Composition of Supervisory Board (Section 5.4.1 para. 2 and 4 of the Code)
The Company's Supervisory Board has not named any specific targets relating to the composition of the Board and not compiled a competence profile for the plenum; for that reason, there is also no publication of the target and status of implementation as well as the numbers and names of the independent members of the shareholder representatives according to the assessment of the Supervisory Board in the Corporate Governance report. It is true that the Supervisory Board aims to have members with different and complementary professional experience and skills. Nevertheless, the Supervisory Board believes that the stipulation of specific targets would restrict the flexibility of the Supervisory Board too greatly in its search for candidates with the necessary ability and experience. For the same reason, the Company does not stipulate neither an age limit for members of the Supervisory Board nor a control limit for the term of membership in the Supervisory Board. However, the Supervisory Board intends to compile a competence profile for the plenum. With regard to nominations of the Supervisory Board, therefore, no specific targets or a competence profile are taken into consideration, but rather the intentions mentioned above.

Consideration of ownership structure (Section 5.4.2 sent. 1 sub-clause 2 of the Code)
The Supervisory Board of the company is to co-determination on a parity. Therefore the Supervisory Board consists of in each case six shareholder and employee representatives. In the assessment of the Supervisory Board the Supervisory Board has a sufficient number of independent members and therefore considers its composition as appropriate and serving all interests. In the present circumstances the Supervisory Board sees no necessity to further consider the ownership structure in its composition.

Haibach, May 10, 2017

Adler Modemärkte Aktiengesellschaft

The Executive Board The Supervisory Board"

This English version of the Declaration of Conformity is a translation of the original German version. Sole authoritative and universally valid version is the original German language document.

CORPORATE GOVERNANCE STATEMENT

Further information on the Company's Corporate Governance, particularly the working method of the Executive Board and the Supervisory Board, the targets set pursuant to § 76 (4) and § 111 (5) AktG and on key corporate governance practices is contained in the Corporate Governance Statement under § 289f and § 315d HGB, which is published on ADLER's website (*www.adlermode-unternehmen.com*) under the heading Investor Relations/Corporate Governance.

GROUP MANAGEMENT REPORT

SIGNIFICANT EVENTS DURING THE FINANCIAL YEAR

CEO Lothar Schäfer left the Executive Board of Adler Modemärkte AG as at 30 April 2017.

Andrew Thorndike was appointed to serve on the Executive Board and as Labour Director for a five-year term with effect from 1 May 2017. In his position as Chief Operating Officer, he was responsible for Purchasing, Logistics, Human Resources and Technical Purchasing. Andrew Thorndike left the Company's Executive Board on 30 January 2018.

The new CEO of Adler Modemärkte AG is Thomas Freude, who was also appointed for a five-year term with effect from 11 September 2017. In addition to the Company's strategic orientation, he is responsible for the Sales and Distribution, e-Commerce, Marketing, M&A, Expansion and Public Relations departments.

Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria, sold two buildings in Klagenfurt and St. Pölten with effect from 1 April 2017. The transaction is in line with ADLER's strategy, announced at the beginning of 2017, of placing continued focus on investment restraint and cash flow management. While the building in St. Pölten had been owned by the Company since 2015, the building in Klagenfurt was prematurely bought out from the real estate portfolio which was under a lease that is set to expire on 30 April 2017, and then sold off directly. The proceeds of the sale of the two buildings totalled approximately € 10 million. As part of the transaction, a 10-year lease agreement with favourable terms for ADLER was entered into; this enables the Company to continue to operate the part of the building in St. Pölten used as an ADLER store as before. The building sold in Klagenfurt had not been used as an ADLER store. Rather, the existing shop will continue to be operated in a different building in Klagenfurt, independently of the transaction.

The liquidity generated through that sale enabled ADLER to acquire 100 % of the shares of GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria, which held the three remaining buildings (in Ansfelden, Salzburg and Vösendorf) contained in the expired lease. As at 29 November 2017, these three buildings were sold on under a contract entered into with a strategic investor, which will allow ADLER to keep the stores, which are successfully in operation at the respective locations, under a long-term lease.

In October 2017, ADLER appointed Meyer & Meyer, Osnabrück, as its new service provider for fashion logistics. Effective 1 January 2019, Meyer & Meyer will be responsible for warehousing, supplies to all ADLER stores and an extensive range of e-commerce services. The cooperation is the result of a programme to increase efficiency and profitability launched in 2016. Under this programme, ADLER examined all areas of the Company to determine the potential for improvement. In view of the challenging conditions in the textile industry, the optimisation of logistics was the focus of particular attention in this process.

BUSINESS & GENERAL CONDITIONS

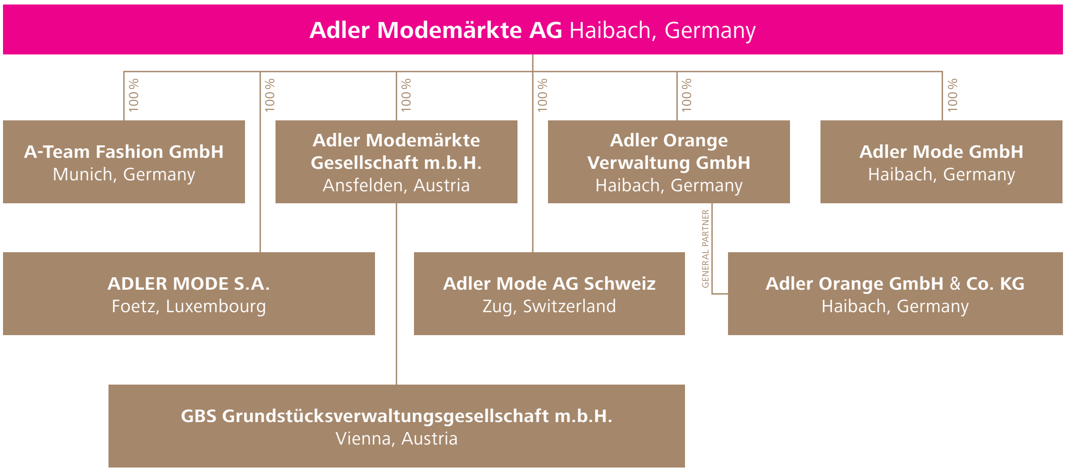
GROUP STRUCTURE AND CORPORATE ORGANISATION

Adler Modemärkte AG, having its registered office in Haibach near Aschaffenburg, is the strategic and operating holding company of the ADLER Group. In Germany, ADLER operates its own stores itself and via its wholly owned subsidiaries Adler Mode GmbH, Haibach, and Adler Orange GmbH & Co. KG, Haibach. In Luxembourg, Austria and Switzerland, ADLER operates its stores via the wholly owned subsidiaries ADLER MODE S.A., Foetz, Luxembourg, Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria, and Adler Mode AG Schweiz, Zug, Switzerland, respectively. A-Team Fashion GmbH, Munich, is primarily responsible for vertical product refinement, in particular the design of and production processing of the Steilmann product range.

GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria, was acquired on 3 May 2017.

In its function as the Group parent, Adler Modemärkte AG oversees the areas of responsibility affecting all companies within the Group. These include procurement and marketing, IT infrastructure management, finance and accounting, internal audit and controlling, and legal issues.

As at the end of the reporting period the structure of the ADLER Group was as follows:



GENERAL DESCRIPTION OF BUSINESS ACTIVITIES

Adler Modemärkte AG is one of the leading textile retail chains in Germany. The industry magazine Textil-Wirtschaft ranks the Company 22nd in its Top 100 Ranking for 2016, maintaining the same position as in 2015. At the end of 2017, the Group operated a total of 182 stores (2016: 183), 155 (156) of which were in Germany, with a further 22 in Austria, three in Luxembourg and two in Switzerland as in the previous year. The Company also operates an online shop at *www.adlermode.com*.

In terms of fit, fashionability, functionality and quality, ADLER's product range is primarily tailored to the age group of over 55-year-olds, whose share of the population is set to grow by around 10 % to 33 million over the next ten years. ADLER offers this target group high-quality products that represent attractive value for money in the lower mid-range price segment. The product range includes a broad selection of womenswear, menswear and underwear. With a supplementary range consisting of accessories, footwear, kidswear and babywear, traditional dress and durable goods, ADLER offers a well-rounded product portfolio, thus harnessing the cross-selling potential in its stores.

The Group's own brands are ADLER's main revenue drivers. At the end of the 2017 financial year, these included Bexleys, Malva, Thea, My Own, Via Cortesa, Viventy by Bernd Berger and Steilmann for women, as well as Bexleys, Senator, Eagle No.7, Big Fashion, Via Cortesa and Bernd Berger for men. These represent approximately 75% of the Group's revenue and the majority of its earnings.

ADLER also offers nationally and internationally recognised external brands for womenswear, menswear and kidswear at many of its stores.

As part of its strategic realignment, ADLER will in future focus more strongly on its high-margin own brands and gradually reduce its external product range by 2020. This will allow ADLER to ensure that the products offered meet the needs of its target group and prevent the cannibalisation of its own brands.

CORPORATE GOVERNANCE

The ADLER Group is managed by the Executive Board, which in particular sets the Group's strategic course. Group strategy is implemented on an operational level in close co-operation with the sales managers and the heads of central Group departments. The organisational and managerial structure clearly assigns internal authorities and responsibilities within the Company and defines reporting lines. The structure aligns all Company resources with the goal of sustainably increasing enterprise value.

REVENUE AND EBITDA AS KEY PERFORMANCE INDICATORS

As a growth-oriented company, ADLER attaches particular importance to profitably increasing revenue. All activities undertaken to boost revenue are measured against their potential to sustainably increase EBITDA and the EBITDA margin. EBITDA was selected because it provides the best information on the profitability of the actual operating activities while excluding any non-recurring factors. The gross profit margin is the primary EBITDA driver. The most important measures in this context are improvements in procurement as well as the optimisation of merchandise management and the rebates policy. Moreover, other operating expenses are strictly monitored.

CORE ELEMENTS OF THE INTERNAL CONTROL SYSTEM

The Group's planning, controlling and monitoring activities are geared towards optimising the aforementioned key performance indicators. The Group financial planning, the Group-wide computerised reporting system and investment financial control make up the core elements of the Company's internal control system.

The Executive Board and the Financial Control and Purchasing departments are responsible for managing inventories and trade payables. Since merchandise is sold directly to end consumers against cash, EC card or credit card payments, trade receivables are of marginal importance to ADLER.

The Group's investing activities focus on the expansion and modernisation of its retail sales activities. The investment financial control process first estimates the investment volume and then calculates the return on investment (ROI) as part of a profitability analysis. On this basis, cross-divisional investment meetings are held regularly to decide which investments to make.

REGULAR UPDATES OF GROUP FINANCIAL PLANNING AND PROJECTIONS

The Group financial planning is developed for a three-year period and uses regular projections for the current financial year. The three-year budget is prepared annually as part of the Group-wide budget process and takes the current business situation into account. During the planning process, the Executive Board sets planning and business objectives for the operating units on the basis of Group targets. The units prepare an earnings forecast and determine the necessary investment levels on the basis of these objectives.

In order to extrapolate the expected consolidated profit or loss for the current year, the annual budget is revised at regular intervals taking into account actual business performance and the existing opportunities and risks. The Financial Control department also prepares weekly projections regarding liquidity developments on the basis of the Group's expected performance. This allows financial risks to be identified early on and appropriate measures to be taken to address financing requirements.

Details regarding the management of financial risks can be found in the risk report.

GENERAL ECONOMIC ENVIRONMENT

Driven by strong domestic demand, the European economy staged a recovery in 2017 that was more robust than many experts had initially anticipated. According to the International Monetary Fund (IMF), real gross domestic product increased by 2.4%, thus significantly exceeding the previous year's positive performance (+1.6%). The strong upturn also had an effect on the global economy, contributing considerably to global economic growth of 3.6% (previous year: 3.1%).

There were also continued signs of growth in Germany – Adler Modemärkte's most important market. Similar to the European Economic Area as a whole, the growth rate was much higher than expected at the beginning of the year, so that experts were required to adjust their forecasts upwards in the course of the year. Gross domestic product increased by 2.0%, and thus rose significantly faster than in 2016 (1.6%). In Austria, where ADLER had 22 stores in the year under review, gross domestic product improved by 2.3% (previous year: 1.5%). Luxembourg and Switzerland are thus far of minor importance for ADLER, because the Group only has three stores in Luxembourg and two in Switzerland. These markets registered economic growth of 3.9% and 1.0% respectively.

FURTHER RISE IN CONSUMER SPENDING IN GERMANY

Against a backdrop of strong economic growth and rising employment numbers, Germany's consumers were in the best of buying moods for long periods of 2017. Boosted by income expectations at record levels, the consumer climate, which is determined monthly by the market and consumer research institute GfK, Nuremberg, was robust in the face of various risk factors in Germany and abroad. Minor setbacks did little to buck the generally positive trend. In total, GfK predicts that private consumer spending will increase by 1.5% in 2017, of which around 30% is attributable to retail. The rest is spent, for example, on rent, (health) services or travel.

The situation was similar in Austria, where the economic expectations of the consumers surveyed reached their highest levels since 2011. Although income expectations and the propensity to spend were subject to fluctuations, the country's sustained economic recovery meant that the consumer climate remained at a high level overall.

BRICK-AND-MORTAR FASHION RETAILERS

The brick-and-mortar fashion retail industry as a whole failed once again to benefit from the positive consumer sentiment. In 2017, declining revenues and news of further insolvencies dampened the mood in the industry. The companies regularly surveyed by the industry magazine TextilWirtschaft ("TW-Testclub") were only able to report an increase in revenues in three months. These were offset by nine months of declines, in some cases by high single-digit or even double-digit percentages. For the full year, the panel members had to deal with a decrease in revenues of 2%, the same as in the previous year.

Following a sombre start to the year, which brought sharp declines in January (–7%) and February (–9%), the warm and sunny month of March made consumers keen on new spring fashion and boosted revenues for retailers by 9%. However, the good performance must be seen in the context of the previous year's poor showing (–6%). The following four months gave no cause for optimism. April, which had three fewer sales days than the previous year on account of the Easter holiday, ended down 7%, while May (–6%), June (–2%) and the unusually rainy July (–8%) also recorded significant falls in revenue. After a modest improvement of 3% in August, September's 20% increase was a record jump in the TW-Testclub's 20-year history – although this was mainly attributable to the fact that the hot weather in the same month in 2016 had led to a collapse in revenues by 16%. Disillusionment followed swiftly: in October, the revenues of panel members were 13% down year-on-year. A small increase in November (+2%) was followed by another decrease of likewise 2% in December.

DEVELOPMENT AND ANALYSIS OF REVENUE

DEVELOPMENT OF REVENUE

In financial year 2017, consolidated revenue decreased by 3.5 % to € 525.8 million (2016: € 544.6 million). ADLER was unable to buck the decline in sales affecting the textile retail industry and much like the rest of the industry suffered under the accompanying pricing pressure and difficult weather conditions.

On a like-for-like basis, revenue for the past financial year declined by 4.5 %, representing a significant year-on-year deterioration.

SEASONAL, QUARTERLY PERFORMANCE

Over the course of a financial year, the ADLER Group's net revenue and EBITDA fluctuate from quarter to quarter in line with the nature of the industry. In the second and fourth quarters, it is generally possible to sell merchandise at the calculated sale price. This is true in particular for the first weeks of those quarters, and has a positive influence on revenue and earnings. The fourth quarter is ADLER's highest-margin quarter by far due to higher-priced winter merchandise and the stimulating effect of the holiday business. By contrast, the first and third quarters of the calendar year are each marked by clearance sales of seasonal merchandise. This impacts not only the Group's revenue potential, but also its earnings.

DEVELOPMENT OF REVENUE BY QUARTER

A quarterly analysis reveals the following: In 2017, ADLER was unable to buck the negative trend in the textile retail industry. In the traditionally weak first quarter, revenue rose by 3.2 % to € 108.7 million (Q1 2016: € 105.3 million). In the second quarter, revenue decreased by 4.2 % to € 145.3 million (Q2 2016: € 151.8 million). In the third quarter, revenue increased by 1.9 % to € 120.2 million (Q3 2016: € 117.9 million). In the fourth quarter 2017, revenue fell by 10.6 % to € 151.6 million (Q4 2016: € 169.6 million).

On a like-for-like basis, revenue rose in the first (1.5 %) and third (0.3 %) quarters, but declined in the second (– 6.0 %) and fourth quarters (– 10.7 %).

ANALYSIS OF REVENUE BY COUNTRY

In financial year 2017, ADLER generated € 435.4 million (82.8 %) of its consolidated revenue in its traditional core market, Germany (2016: € 453.7 million). In Austria, the Company generated revenue of € 68.9 million (2016: € 71.2 million), corresponding to 13.1 % of ADLER's total revenue. Revenue in Luxembourg rose to € 18.2 million (2016: € 16.7 million). Accordingly, the share of total revenue amounted to 3.5 % (2016: 3.1 %). In 2017, ADLER's two stores in Switzerland increased revenue, generating € 3.2 million as compared with € 3.0 million in 2016.

FINANCIAL PERFORMANCE

GROSS PROFIT MARGIN RISES

Due to an adjustment in purchasing volumes, the 4.8 % decline to € 244.1 million (2016: € 256.5 million) in the ADLER Group's cost of materials was more pronounced than the decrease in revenue. Gross profit (revenue less cost of materials) decreased from € 288.1 million to € 281.8 million in financial year 2017. However, the gross profit margin increased from 52.9 % to 53.6 %.

ADLER will continue its policy of avoiding excessive price markdowns. The Company will work to further optimise its inventory management system and continuously increase the share of merchandise in its product range that is directly sourced.

Other operating income primarily includes rental income, reversals of provisions, construction subsidies, income from special projects and income from the hanger recycling project. The figure was € 18.8 million compared with € 8.7 million in financial year 2016, largely due to the sale of buildings in Austria. Adjusted for this non-recurring effect, other operating income amounted to € 6.9 million and was thus € 1.8 million lower than in the previous year. The year-on-year decline is primarily attributable to a reduction in rental income due to the sale of buildings and lower construction subsidies. The figure for the previous year also included income from damages claims for water and fire damage.

PERSONNEL EXPENSES

Despite the voluntary wage and salary increases for 2017 under the collective bargaining agreement and the restructuring expenses, personnel expenses fell significantly by 5.3 % to € 96.9 million (2016: € 102.3 million). The figure includes severance payments for personnel changes, primarily in the purchasing and distribution departments, as part of the restructuring and strategic realignment measures introduced in 2017. Excluding the restructuring effect of € 2.3 million (2016: € 0.2 million), the decline would have been 7.6 % to € 94.6 million. The reduction in personnel expenses at an operational level was primarily due to the decline in the number of employees and the waiver of employee holiday pay and bonuses. The personnel expenses ratio (personnel expenses in relation to revenue) declined to 18.4 % or 18.0 % on an adjusted basis (2016: 18.8 %).

OTHER OPERATING EXPENSES

In 2017, other operating expenses increased by 0.3 % to € 171.7 million (adjusted: € 168.8 million) as compared with € 171.2 million in 2016, corresponding to 32.7 % of consolidated revenue (2016: 31.4 %). This item includes in particular building management expenditures, marketing and advertising outlays, freight and transport expenses, costs for technical facilities, and closure costs. Consulting fees increased by € 1.0 million due to the restructuring and strategic realignment. In sum, consulting fees include expenses for these measures of € 1.5 million. At around € 1.1 million, strategy consulting services represented the most significant item in this area. Furthermore, costs of € 0.6 million incurred which largely relate to fees associated with the sale of the buildings as well as costs of € 0.9 million due to losses from disposals of assets and closure costs.

Adjusted for these effects, other operating expenses would have declined by € 2.4 million.

EARNINGS

In total, EBITDA of €32.0 million was generated in financial year 2017 (2016: €23.3 million). The sale of two buildings in Austria by Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria, in the first quarter of 2017 and the sale of GBS Grundstücksverwaltungsgesellschaft m.b.H.'s, Wien, Austria, buildings in the fourth quarter of 2017 generated non-recurring income for ADLER. This was offset by additional costs relating to ADLER's strategic realignment, primarily restructuring expenses and consulting fees. Taking into account the non-recurring income generated from these transactions and adjusting for non-recurring expenses from restructuring measures, the positive effect on the Company's earnings totalled approximately €6.6 million. Accordingly, adjusted EBITDA amounted to €25.4 million (2016 adjusted for comparable restructuring expenses: €23.8 million).

In financial year 2017, depreciation, amortisation and write-downs decreased by €0.2 million (adjusted: €0.4 million) from €16.7 million in 2016 to €16.5 million (adjusted: €16.3 million). The decrease was due primarily to the expiry of several finance leases for Austrian stores expired during the reporting period. These buildings were either sold or transferred to operating leases. The non-recurring effect of €0.2 million on depreciation, amortisation and write-downs resulted from impairment losses on the property, plant and equipment of stores that were closed in the year under review.

EBIT rose to €15.6 million (adjusted: €9.1 million) from €6.6 million in 2016 (adjusted: €7.1 million). The EBIT margin rose accordingly from 1.2% to 3.0% (adjusted: 1.7%).

Net finance costs amounted to €4.9 million (2016: €4.9 million). EBT amounted to €10.7 million during the year under review (adjusted: €3.9 million) compared with €1.7 million in financial year 2016.

In financial year 2017, income taxes increased year on year, amounting to €−6.8 million (adjusted: €−1.9 million) as compared with €−1.3 million in 2016. The higher earnings before taxes and the decision not to recognise loss carryforwards led to a sharp rise in the tax expense, which was however partially offset by deferred tax reversal effects. The consolidated net profit for the year rose from €0.4 million in 2016 to €3.9 million in 2017 (adjusted: €2.3 million).

EARNINGS PER SHARE

The net earnings per share amounted to €0.21 or €0.11 on an adjusted basis (based on 18,510,000 no-par value shares). Earnings per share had amounted to €0.02 in the previous year or €0.05 on an adjusted basis (based on 18,510,000 no-par value shares).

FINANCIAL POSITION AND CASH FLOWS

FINANCIAL POSITION

The ADLER Group's total assets as at 31 December 2017 increased year on year to €241.1 million (2016: €222.6 million). However, property, plant and equipment decreased to €75.0 million (2016: €78.1 million). This included expenditures for the modernisation of existing stores, including the associated procurement of other office equipment for store construction, as well as new or renewed finance leases. The lease agreements relate to leased store buildings, whereby the Group is deemed the beneficial owner for the purpose of the underlying lease agreements.

Inventories at the end of the reporting period decreased by € 1.7 million to € 73.7 million (2016: € 75.4 million) thanks to the improved marketing of old merchandise and merchandise allocation.

The ADLER Group's cash and cash equivalents rose sharply from € 42.8 million to € 63.3 million, primarily due to the cash inflow from the sale of the buildings in Austria and the waiver of dividends for financial year 2016.

Group equity rose to € 100.0 million (2016: € 95.8 million). The equity ratio (41.5 %) was below the prior-year figure (2016: 43.1 %). No dividends were paid to shareholders of Adler Modemärkte AG (2016: € 9.3 million).

DEBT/EQUITY RATIO

As at 31 December 2017, ADLER's liabilities increased by € 14.5 million to € 141.2 million (2016: € 126.7 million). As at the end of the reporting period, ADLER no longer had any liabilities to banks. Liabilities related in particular to finance lease liabilities (€ 56.0 million; 2016: € 52.2 million), liabilities from the customer loyalty card programme (€ 10.4 million; 2016 adjusted: € 10.6 million), and current and non-current financial liabilities (€ 2.6 million; 2016 adjusted: € 2.9 million). Since the year under review, liabilities from the customer loyalty card are presented as a separate item "Liabilities from the customer loyalty card programme".

The provisions for pensions and similar obligations declined slightly by € 0.3 million to € 5.5 million (2016: € 5.8 million), and income tax liabilities amounted to € 3.8 million (2016: € 0.1 million). The debt/equity ratio (1.41) was up on the previous year's ratio (2016: 1.32).

DECREASE IN WORKING CAPITAL

Working capital (inventories plus trade receivables, less trade payables) decreased by € 4.0 million to € 46.7 million as at the end of the reporting period (2016: € 50.7 million). The working capital ratio (working capital in relation to revenue) decreased to 8.9 % (2016: 9.3 %).

CASH FLOW MANAGEMENT

Cash flows from operating activities (net cash flow) are one key indicator of ADLER's operating earnings power. Net cash flow decreased during the year under review by € 1.0 million from € 22.2 million to € 21.2 million. Cash flows used in investing activities rose by € 25.6 million to € 14.8 million (2016: € – 10.8 million). Of this amount, around € 14.0 million was attributable to the sale of the buildings in Austria. This item also includes the costs for modernising existing stores.

Free cash flow increased in 2017 by € 24.5 million to € 35.9 million (2016: € 11.4 million). The increase was primarily due to the sale of the buildings and the higher consolidated net profit.

At € 15.4 million, cash flows used in financing activities were down on the prior-year figure of € 20.7 million. This is primarily attributable to the waiver of dividend payments. The repayment of a loan in connection with the acquisition of GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria had an offsetting effect.

As at the end of the reporting period, the ADLER Group's cash and cash equivalents amounted to € 63.3 million, representing an increase of € 20.5 million from € 42.8 million as at 31 December 2016.

INVESTMENT

The ADLER Group's investments during financial year 2017 totalled € 15.8 million (2016: € 13.3 million). Of that amount, € 4.1 million (2016: € 8.8 million) was invested in property, plant and equipment (real estate property, buildings and operating and office equipment) and € 9.7 million (2016: € 2.4 million) was attributable to new finance lease agreements and the renewal of existing finance lease agreements. Investments in intangible assets amounted to € 1.6 million (2016: € 2.2 million). This figure mainly relates to IT investments. Capital expenditure commitments include investments that had already been authorised as at the reporting date. Investments during the year under review included new store openings as well as the modernisation of existing stores.

PROCUREMENT

The ADLER Group does not currently operate its own production facilities. The Company has a lean organisation and focuses on its core competencies, which is why its products are imported directly from Asia, India, Turkey, Greece, northern Africa and eastern Europe as well as indirectly through importers and brand manufactures at cost-effective prices. Purchasing high-quality products at low prices, securing delivery of the merchandise and optimally showcasing the articles to the customers at the Company's own stores are the main priorities of procurement and logistics.

ADLER has many years of experience in procuring textiles in Asia. The production of textiles is outsourced to strategic partners. ADLER works mainly with a core group of suppliers, which represented 46 % of the purchasing volume in financial year 2017.

ADLER sells products from its own-brand range and brand-name items (external brands). ADLER's primary direct suppliers of own brands in Asia are the procurement agents METRO Sourcing International Limited, Hong Kong (MSI, formely MGB) and NTS Holding Limited, Hong Kong (NTS). MSI bundles the procurement activities of the METRO Group in Asia. ADLER is one of MSIs most important customers for textiles. NTS in China is the Steilmann Group's former procurement company.

ADLER's purchasing department directly manages individual producers in Morocco, Greece and Turkey.

In financial year 2017, ADLER purchased merchandise valued at a total of € 228 million. Of this amount, 23 % or € 53 million was used to purchase external brands and € 175 million to purchase own brands. Of the own brands, € 99 million was purchased from the procurement agents MSI and NTS in Asia and € 10 million was purchased directly from producers. In financial year 2017, the share purchased from EU-based suppliers amounted to 29 % or € 66 million.

ADLER intends to further optimise its procurement sources and internal processes over the medium term since increasing gross profit is one of the Company's strategic objectives. In this vein, in financial year 2017, ADLER arranged shorter delivery times with its Asian suppliers and strengthened its partnerships with its European suppliers in order to ensure that its procurement activities are even more demand-driven. It also intends to push forward the concentration of suppliers already initiated and intensify its strategic partnerships. ADLER also gained extensive know-how about manufacturing in eastern Europe by acquiring the Steilmann brand and team in 2016.

DIVERSIFIED SUPPLIER RELATIONSHIPS

ADLER makes sure that it distributes its purchase volumes evenly across a worldwide network of suppliers in order to spread the risk and to minimise its dependency on any one procurement market or manufacturing site. ADLER has therefore entered into a large number of agreements with importers, each of which accounted for considerably less than 5 % of the total volume delivered to ADLER in financial year 2017. Some importers also guarantee rapid responses to changes in demand since their production facilities are close to Europe. Most of the agreements with importers pertain to NOS items ("never-out-of-stock"), which are automatically replenished when they sell out. ADLER maintains additional supplier relationships with the manufacturers of the external brands it offers in its stores.

DISTRIBUTION, SALES & MARKETING

ADLER announced its strategic realignment in the first quarter of 2018. The implementation of the new strategy will allow ADLER to more consistently tailor its full range of products and services to its target group. ADLER defines this group as women and men aged 55 and above who want high-quality clothing at attractive prices, without wishing to follow the latest fashions. ADLER already enjoys a leading market position with this demographic group in the DACH region (Germany, Austria, Switzerland), which the company intends to further strengthen and expand. The aim is to create a brick-and-mortar and digital platform for "best agers" and become the number one choice to meet their fashion needs with regard to style, fit, quality and service.

According to estimates by the German Federal Statistical Office, the number of people over the age of 55 in Germany will grow by 10 % over the next ten years to around 33 million people. ADLER´s strategy, which focuses on profitable growth, aims to achieve even better penetration of this growth market in future. With this in mind, the primary objective is to create greater loyalty to the ADLER brand among existing customers in order to increase ADLER´s share of wallet (proportion of a customer's total spending on a specific product group).

ADLER pursues a multi-channel strategy through which we aim to ensure a consistently positive brand experience across all sales channels.

BRICK-AND-MORTAR SALES STRATEGY

For its brick-and-mortar business, ADLER focuses on large-space retail concepts, meaning that the space occupied by the stores it operates is usually between 1,500 m² and 4,000 m². Large sales floors with wide aisles, spacious fitting rooms and rest areas exemplify the Company's customer-oriented approach. At the end of 2017, the Company had an extensive brick-and-mortar sales network spanning 182 stores in Germany (155), Austria (22), Luxembourg (3) and Switzerland (2).

The majority of ADLER stores are located in shopping centres and retail parks. Free-standing stores located at greenfield sites or in downtown locations are the exception. In addition to economic factors, the key criteria for selecting a store location are easy accessibility for customers, the size of the catchment area and the proximity to the nearest ADLER store.

ADLER conducted extensive analyses and surveys of customers, former customers and non-customers in 2017 to identify growth potential. Based on the findings, ADLER believes that the greatest potential for short- and medium-term footfall and revenue growth lies in directly addressing existing customers (increasing the share of wallet), in particular, as well as winning back former customers. In order to generate economies of scale and to strengthen its market position, ADLER also plans to expand the network of stores organically as well as through acquisitions over the long term. Outside of this long-term planning, new store openings are also possible in the near term if opportunities arise in attractive locations.

Surveys have shown that ADLER customers highly value service and personal advice. Well-trained, motivated and approachable sales staff play a key role in ADLER's brick-and-mortar stores. Continuously improving the sales skills of our employees and optimised planning of personnel resources to deal with peak periods are therefore a core focus of our strategy.

To enhance the customer benefits of visiting a store, the new strategy also includes plans to cooperate with partners that offer the target group relevant additional non-textile services and products, thus potentially generating additional footfall at the stores.

ADLER wants to generate additional cost benefits and optimise internal processes by employing innovative technology. After the Company-wide introduction of RFID (radio frequency identification), ADLER is reviewing how the technology can be used to further automate processes. The prerequisite for the use of the technology is an appropriate cost-benefit ratio. RFID uses electromagnetic waves to automatically detect and identify merchandise, which has already had a clear positive impact on the efficiency of checkout and stocktaking processes.

ONLINE SALES STRATEGY

As part of the omni-channel strategy, ADLER operates an online shop in Germany, Austria and Luxembourg at *www.adlermode.com*.

In financial year 2017, ADLER's online shop had 10.8 million visitors, around 15 % more than in the previous year. Revenue generated through the online shop was up 19 % in 2017 at € 10.6 million, which represents 2.0 % of the Group's total revenue (2016: 1.6 %).

The online shop serves as ADLER's display window and mainly offers rapidly changing ranges in traditional women's fashions for blouses, jackets and dresses. It also caters to market niches such as plus-sizes and traditional dress. During the year under review, the average age of online customers was 55, while customers at physical stores were on average 62 years old. The online shop is therefore becoming increasingly important in terms of reaching and gaining younger customers. The Click&Collect service, which allows customers to order online and pick up or return the merchandise at a store, is also helping to drive up footfall at stores.

Different approaches to leveraging various digital shopping mediums (e.g. mobile and desktop) to generate sales are also gaining in importance for ADLER. Mobile devices accounted for around 49 % of visits to the ADLER online shop in 2017, representing an increase of nine percentage points on 2016. Against this background, the digital sales offering was rounded out with the launch of the ADLER app in spring 2017. As part of the strategic realignment, the functionality of the app is to be considerably expanded to offer users additional benefits and further enhance brand loyalty.

Alongside its own online shop, ADLER plans to make greater use of third-party digital selling platforms for its own brands in future, with the aim of improving brand recognition and increasing revenue.

The e-commerce strategy is bolstered by an online marketing budget structured for growth and increased efforts to digitally interact with ADLER's existing customer base. The online marketing measures include a mix of performance-oriented marketing instruments, including a broad e-mail and mobile marketing campaign.

MARKETING

As an operator of large-space retail stores, mainly in peripheral locations, ADLER uses extensive brand and product advertisements to generate footfall. In financial year 2017, advertising expenditure amounted to €46.0 million, up 1.4% on the prior-year figure.

THE ADLER LOYALTY CARD

The ADLER loyalty card is a key marketing tool. The programme was first launched in 1974 and is thus one of the oldest and most successful loyalty card programmes in Germany. Cardholders receive a rebate credit amounting to 3% of their respective shopping basket, which can be used against their next purchase. In financial year 2017, the loyalty card programme had some 3.4 million members and registered a total of approximately 92% of the Company's revenue. In addition to enhancing customer loyalty, the card also means that ADLER's knowledge of its customers is comparable to that of an online or mail-order retailer. In future, the Company plans to make far greater use of the enormous potential offered by the loyalty card data to accurately target the content, design and timing of its advertising and marketing measures.

ADVERTISING

As part of the strategic realignment, ADLER has modified its communications strategy and will in future primarily focus on targeting existing and selected former customers. Against this background, the formats used to date have undergone a new, detailed cost-benefit analysis. Based on the results, ADLER is to stop using TV advertising from the second half of 2018 and instead allocate the budget to other advertising channels on a performance-oriented basis.

During the year under review, ADLER used inserts, mailshots, TV and radio advertising, as well as online advertising in the form of banners and search engine optimisation as the main means of promoting its products and image. In 2017, ADLER sent a total of 46 million advertising mailshots to customers. During the same period the total number of all newspaper and magazine inserts was approximately 131 million. ADLER also invested €2.6 million in TV advertising and €2.0 million in radio spots.

In the third quarter of 2017, ADLER launched a new integrated image campaign that ties in with the "Fashion is for people" campaign launched in 2014 and interprets the "ADLER – A perfect fit" brand message for the target group. The focus is less on the products than the models: real women who live life to the full and wear their supposed imperfections such as grey hair, curves and wrinkles confidently and unselfconsciously. The aim of this approach is to convey the high regard in which ADLER holds its customers.

ELECTRONIC TERMINALS FOR CUSTOMER SATISFACTION SURVEYS

ADLER gleans additional information from targeted, in-store customer surveys, and then uses this data to improve the quality of its services and products. To this end, the Company installed electronic terminals at all of its stores in order to better collect customer feedback. The surveys allow customers to anonymously rate their shopping experience and provide open-ended comments, which may be added in a textbox. In addition, the "Consumer Heartbeat" survey was launched in 2016 in an effort to obtain regular, independent feedback from ADLER and other customers. It collects information about, among other things, why customers did or did not purchase certain products.

"GERMANY'S CUSTOMER CHAMPIONS" AWARD

For the tenth consecutive year, ADLER was a recipient of the "Germany's Customer Champions" prize awarded by the market research institute forum! Marktforschung and the German Society for Quality (Deutsche Gesellschaft für Qualität e.V., "DGQ") in 2017. ADLER also received an honorary award for this special achievement.

Recipients of the title are companies that are particularly successful in appealing to consumers on a service and on an emotional level, thus gaining them as customers and turning them into fans. The key factor driving customer loyalty at ADLER is how the Company dovetails customised marketing efforts, attractive product ranges and one-on-one customer services at its stores.

EMPLOYEES

As at the end of the 2017 financial year, ADLER had a total of 3,866 employees (31 December 2016: 3,984). In addition to efficiently accomplishing the tasks at the Company headquarters, ADLER places particular importance on direct contact with its customers through the sales staff. Having a keen eye for the wishes and needs of the target group is especially important. An important objective of the Company's HR development is therefore to provide its employees with training in order to continually heighten their sensitivity to the needs of individual customers. At the same, the objective is also to strengthen and steadily foster the employees' self-motivation and customer service skills as well as the team spirit at ADLER. To this end, the Company regularly provides local training seminars with internal and external instructors.

CORPORATE CULTURE

ADLER is a company with almost 70 years of tradition and a well-established corporate culture, which rests on the pillars of excellent service orientation, team spirit, creativity, openness and transparency. Great importance is placed on fostering a work environment that enables each employee to optimally apply themselves and their unique set of skills. For ADLER, this type of work environment is an important starting point to continue improving our customer focus and the quality of the service we provide.

In 2017, ADLER successfully completed the INQA audit "Future-oriented corporate culture" developed by the Initiative New Quality of Work (Initiative Neue Qualität der Arbeit, "INQA"). As the first step in the audit process, employees were asked to put forward their ideas, wishes and criticisms as part of an anonymous, Group-wide employee survey. Extensive measures to improve the quality of work at stores and Company headquarters, as well as to leverage additional potential were developed based on the survey findings. These measures cover the areas of personnel management, equal opportunities and diversity, health, and knowledge and expertise.

EXPERIENCED LOCAL MANAGEMENT TEAMS

ADLER's management makes the organisational and personnel decisions necessary to ensure that the individual stores are led by locally based, experienced employees. These employees are present on the sales floors and are given appropriate discretion to make decisions based on their duties. The store managers are familiar with the local conditions and the characteristic features of the region. ADLER has been able to continually attract qualified and experienced employees from within the Company as well as from its competitors when expanding upon its number of stores or recruiting local managers.

EMPLOYEE TURNOVER

Compared to other companies in the retail industry, employee turnover at the Company headquarters and at ADLER's stores is low. The turnover rate was approximately 13 % in the reporting year (previous year: 13 %). This moderate rate is a good indication on the one hand that ADLER adheres to high social standards and on the other hand that the employees hold the Company in high regard. A large number of employees have been with the ADLER Group for many years. The average ADLER employee has been with the Company for more than 11 years. As they have worked for the Company for many years, many employees have built up personal relationships with customers, which has contributed to the high proportion of regular customers.

DIVERSITY AT ADLER

ADLER is an employer that does not take nationality, gender, background, religion, age, disabilities or sexual preferences into account when considering and evaluating employees and applicants. Given current demographic changes, ADLER wants to fully tap the potential that a diverse applicant pool has to offer. The professional qualifications, personal integrity and commitment of the applicants are the only attributes given priority during the Company's selection process. ADLER considers a diverse staff a competitive advantage, as this allows employees with skills and talents that complement one another to successfully work together in the Company. At the end of 2017, ADLER employed people from 43 different countries.

Women have made up an extremely high share of ADLER's workforce since the Company's founding. Approximately half of the positions at executive level are held by women. One-fourth of the Supervisory Board seats are currently held by women. Overall, 90 % of ADLER's workforce are women. Recognising that many mothers carry the dual burden of balancing both their professional and family lives, ADLER will continue to make their professional and family lives more compatible by accommodating work conditions. ADLER is also committed to affording people with severe disabilities the opportunity to participate in the workforce with the same rights as other employees.

ADLER GROUP EMPLOYEES AS AT THE END OF THE FINANCIAL YEAR (31 DECEMBER 2017):

	31 Dec. 2017	31 Dec. 2016
Total employees	**3,866**	**3,984**
of which managers	215	219
of which full-time employees	671	715
of which part-time employees	2,704	2,714
of which trainees/interns	276	336
Average age in years	46.7	46.4
Men	10.0 %	9.8 %
Women	90.0 %	90.2 %

Personnel expenses (adjusted) at the ADLER Group amounted to € 94.6 million in 2017, a decrease of € 7.5 over the previous year (adjusted: € 102.1 million).

VOCATIONAL TRAINING AND CONTINUING EDUCATION

ADLER will continue to rely on qualified and service-oriented employees going forward. The Company therefore promotes young talent from within its own ranks. In principle, ADLER offers vocational training positions based on which positions it needs to fill. Currently, ADLER offers vocational training for the following positions: office management assistant in retail sales, office management assistant, wholesale and export merchants, software engineer and visual marketing designer.

As at 31 December 2017, ADLER employed 276 trainees and interns. Of these, 162 were trainees, 62 were trainees from joint vocational programmes (überbetriebliche Auszubildende), six were trainees with entry-level qualifications and 44 were interns. ADLER also employed two students as part of the dual education programme with LDT Nagold.

ADLER provides its employees with continuing education opportunities which are matched to their individual abilities. Employees may also be transferred to other departments or positions as part of the employee training programme (cross-functional work model). Moreover, ADLER offers opportunities for advancement within the Group as well as options for its employees to expand their areas of responsibility and gain new skills. Sales employees attend regular training sessions to improve their customer focus and increase their motivation when providing customer service. An established monitoring system based on regular sales analyses allows management to provide sales staff with targeted training and encouragement.

SUSTAINABILITY AND THE ENVIRONMENT

The procurement and sale of textile clothing are at the core of Adler Modemärkte AG’s business. Corporate social responsibility, sustainability objectives and environmental awareness are important preconditions for ADLER’s long-term success. Sustainability concerns are taken into account when making any strategic or operating decisions and also when working together with business partners.

INTEGRATED SUSTAINABILITY MANAGEMENT

The objective of ADLER’s sustainability management function is to offer customers ecologically and socially sound products and at the same time, act in the best interests – socially and economically – of employees, suppliers and other stakeholders.

ADLER follows an integrated sustainability management approach. The underlying aim is to create and foster a corporate culture that is anchored in sustainable business principles and embodied by every single employee. Against this background, ADLER develops and implements certification measures and management processes for the departments, and also supports the departments at an operational level with these tools.

COMPLIANCE WITH BSCI STANDARDS BY SUPPLIERS AND PRODUCERS

ADLER sells products from its own-brand range and external brands (brand-name items). ADLER is directly responsible for its own-brand products. It is essential to know and document not only which raw materials are used to make the products, but also the social and ecological conditions under which they are made. ADLER's procurement policy forbids the sourcing of products made under conditions which are exploitative, harmful to health or which otherwise violate human dignity, such as child or forced labour.

All suppliers who supply ADLER via METRO Sourcing International Limited and NTS Holding Limited or who have products made in "risky" countries are audited in accordance with the criteria of the Business Social Compliance Initiative (BSCI). Audits are carried out at the production facilities.

Of the 286 production facilities at 31 December 2017, 21 % were rated "good". Room for improvement was identified at 72 % of the facilities and 7 % were undergoing a re-audit process. None of the production facilities were deemed "non-compliant". As part of process improvement efforts, suppliers and producers receive support from the purchasers in planning improvement measures.

Since 2013, ADLER has required European suppliers, which have one of ADLER's own brands made in countries deemed risky by the BSCI, demonstrate that the relevant producer has passed a BSCI audit.

In addition to BSCI audits, certifications of compliance with standards such as SA 8000, WRAP and GOTS, which are based on the relevant standards set by the United Nations and the International Labour Organisation (ILO), are also acceptable.

COTTON

Cotton is currently sourced from certified organic producers (Global Organic Textile Standard (GOTS) or Organic Cotton Standard (OCS)), the Better Cotton Initiative (BCI) and from Fairtrade. These standards cover the reduction of water and energy consumption, acceptable nutrient levels in the soil and the moderate to prohibited use of toxic and persistent pesticides.

ADLER works together with these various initiatives so that suppliers are always able to offer buyers products made of sustainable cotton. This enables buyers to increase the share of sustainable items in the product range and thus meet their sustainability targets.

FAIRTRADE AT ADLER

ADLER has offered Fairtrade products as part of its range since 2010. Fairtrade sows the seeds for social progress for small-scale farmers and workers in countries that are usually designated as non-industrialised countries. By buying Fairtrade cotton, ADLER pays farmers both a fair price and a Fairtrade premium. The premium is used, for example, to build hospitals, schools, or kindergartens, for adult education or infrastructure such as the construction of roads and bridges.

RECYCLING OF USED CLOTHING

ADLER's vision of sustainability also includes supporting sustainable consumption. ADLER works together with the I:CO take back-system, allowing customers to return used textiles and shoes to stores so that these products can be repurposed in a way that benefits the environment. Customers returning used textiles are rewarded with coupons for ADLER products. By employing I:CO's solution, ADLER fulfils its product responsibility and actively contributes to the conservation of valuable resources.

A total of 3.9 million kilogrammes of used clothing have been collected since ADLER became the first clothing company in Germany to enter into a partnership with I:CO in 2009. In 2017 alone, 733 tonnes of used clothing were recycled. By recycling used merchandise, ADLER has made a significant contribution to reducing CO_2 emissions and to conserving water.

For every kilogramme of clothing and shoes returned, ADLER donates two cents to the CharityStar donation platform, where any customer or interested individual can decide which charitable project to support with the money collected. You can find more information about the CharityStar donation platform under *www.charitystar.com* (only available in German).

PARTNERSHIP FOR SUSTAINABLE TEXTILES

Established in 2014, the Partnership for Sustainable Textiles is an initiative of representatives from companies, non-profit organisations and trade unions. Initiated by the German Federal Ministry for Economic Cooperation and Development, the partnership aims to bundle the strength and expertise of its members in order to bring about social, ecological and economic improvements along the textile supply chain. The Partnership for Sustainable Textiles sees itself as a platform where participants jointly review the implementation of the partnership's objectives, share experiences and best practices and learn from each other in order to improve conditions in the producer countries.

ADLER has followed the Partnership from the very beginning and has helped shape the broad-based initiative. ADLER joined the Partnership for Sustainable Textiles in June 2015 together with leading trade and producer associations and other companies. In doing so, ADLER also signed a voluntary agreement to no longer offer plastic carrier bags free of charge, and since July 2016 now charges 10 or 20 cents for carrier bags at all of its stores in Germany. For the latest information, please visit *www.textilbuendnis.com*.

OPPORTUNITIES AND RISK REPORT

REPORT ON OPPORTUNITIES

General economic opportunities

The ADLER Group is the only major vendor in the fashion industry consistently focused on the fashion needs of the growing group of customers aged 55 and up. ADLER's market position is thus not only clearly established, the Company is also reaping the benefits of demographic changes in Germany and Europe: the target group – and with it, revenue potential – will continue to grow going forward. This solid foundation will be further bolstered through the judicious expansion of the product range. ADLER will leverage its product range to appeal to potential new customers, who will flow into the primary target group, thus lending additional momentum to the business.

Sector-specific opportunities

Given the dynamic environment and the structural changes in the textile retail industry, ADLER slowed the pace of its short-term organic and inorganic growth. In addition to increasing profitability by lowering costs and improving efficiency, ADLER's management is focusing on realigning the Company and reviewing its corporate strategy. In the course of this realignment, the target customer group and their market potential have been examined, and the product strategy, channel strategy and communication strategy have been redefined.

These and other measures are important steps that were taken to create a stable and sustainable basis on which the planned growth course can continue to be pursued in the medium term.

Corporate strategy opportunities

As part of the channel strategy, the online shop will in future be a key component of ADLER's multi-channel approach. ADLER successfully launched its online shop in 2010 in response to the increasing importance of online retail and the changing buying patterns of its customers. The online shop is continuously being expanded and optimised to meet the rising expectations of consumers and to further improve their shopping experience. By coupling its in-store and online retail activities, ADLER is leveraging cross-selling effects on the one hand by using the Click&Collect system, which allows customers to order online and pick up or return the merchandise at an ADLER store, and on the other via ROPO effects. An analysis of the behaviour of the 10-million-plus online visitors demonstrated that products are selected online and then purchased in stores. In both cases customers are encouraged to purchase additional products by visiting a store, thus creating the potential for additional revenue.

By taking advantage of its longstanding experience, a large network of manufacturers in Asia, India, Turkey, northern Africa and eastern Europe, and increasing globalisation, ADLER can leverage procurement-related opportunities and continuously improve its procurement structures and purchasing conditions. The contracts with the procurement agencies MSI in Hong Kong and NTS in Hong Kong were terminated at the end of 2017. At the same time, a new procurement agency, Hermes-Otto International (HOI) in Hong Kong, was engaged as a future strategic partner. ADLER has thus ensured the improvement of the supplier structure and product range from 2019 onwards.

To improve efficiency, the Supply Chain Management division was established in 2017 to optimise processes, merchandise allocation and markdown management. In connection with this, the existing contract with the former logistics service provider BLG was terminated at the end of 2017 and a new contract was entered into with Meyer & Meyer. ADLER expects this change in logistics partner to make the delivery and distribution of goods easier to plan and more cost effective starting from 2019.

RISK AND OPPORTUNITY MANAGEMENT SYSTEM

ADLER is exposed to a large number of risks and opportunities in the course of its business activities. There is always a risk that targets will not be met or will be only partly met due to unforeseen events or negative market developments. Conversely, unexpected opportunities may lead to these targets being exceeded.

Opportunity and risk management is a management tool used by ADLER to identify, classify and manage opportunities and risks at an early stage in order to ensure that the Company's short-, medium- and long-term targets are met, thus securing its continued existence and profitability, as well as increasing its enterprise value.

The risk management system (RMS) is generally valid for all of the Company's divisions and subsidiaries. Strategic and operational factors, events and actions having a significant impact on the existence and economic position of the Company are considered risks. External factors, such as the competitive environment, demographic changes, etc., that might prevent the Company from achieving its objectives, are also taken into account and evaluated. The risk management system covers strategic decisions made by the Executive Board as well as day-to-day business operations.

The executive bodies of the Group have laid down basic rules for risk assumption. These include that ADLER may assume specific corporate risks, provided that opportunities associated with those risks are likely to increase the value of the Company.

ADLER's Executive Board holds overall responsibility for ensuring the efficient management of opportunities and risks within the ADLER Group. The risk management officer coordinates and defines responsibilities and processes, and draws up binding guidelines and formal rules. The risk management officer reports directly to the Executive Board, as well as to the Audit Committee of the Supervisory Board once per year.

Risks are generally managed where they arise. Each department head is therefore also a risk owner since their management responsibilities in their day-to-day function require them to weigh risks and opportunities when taking decisions and undertaking actions, and to decide on an appropriate course of action.

The primary medium for the RMS is the risk manual, which lays out the core issues of the Company's risk management regime. It defines risk areas, how risks are assessed and the organisational approach to risk. Defining the process chain for handling risks ensures that risk areas are identified rapidly and that systematic countermeasures can be implemented at any time.

In terms of day-to-day business operations, risk management means weighing the identified opportunities and the efforts involved in managing the associated risks, as well as continuously monitoring the risks entered into and the measures introduced for their management. A coordinated set of measures to mitigate risks requires clearly delineated responsibilities and a suitable framework. In this respect, risk management is among the most important management duties and is regularly reviewed.

RISK RECOGNITION AND ANALYSIS

The legal requirement of a functioning risk management system is that it must record as fully as possible all material risks, namely all strategic and operational factors that could impact the Company's financial position, cash flows and financial performance. In order to meet this requirement, there are two key tools for recognising and assessing risk.

The purpose of the risk inventory is to record all of the risks within the departments as fully as possible. In the initial risk inventory, a questionnaire is used to determine potential and already identified risks. Together with the department heads, these risks added to as necessary and analysed, before responsibilities are defined. In addition to comprehensively identifying the potential risks, the aim of the initial inventory is to raise the management's risk awareness, clearly define responsibilities and provide guidance on how to eliminate or manage risks, e.g. through the implementation of risk monitoring tools. Any measures taken to manage risk are documented in an appropriate form during the process and their effectiveness is monitored by the risk management officer.

Following the initial risk inventory, an inventory is carried out on a regular half-yearly basis in each department, documented using the questionnaire provided by the risk management officer, and recorded centrally in the risk inventory document.

The risk inventory document is a centralised document which contains the Company's entire risk portfolio resulting from the risk inventory. The risk inventory document is therefore also used for the purpose of reporting to the Executive Board and the parent company. Since the risk situation must be able to be quickly, clearly and comprehensively determined, a brief description of the risks is provided, ensuring that they can be allocated to a risk field and risk owner in a clear format. The risk inventory document is updated annually.

The risk analysis assesses the significance of the identified risks with regard to influencing factors and impact. The assessment system must be simple and practical. The aim of the risk inventory is not to accurately estimate the potential monetary cost of the risk, but to clarify the relevance of the risk in question.

RISK REPORTING

Risk reporting serves to monitor risks on an ongoing basis. It ensures that existing risks are identified, analysed and evaluated and that risk-related information is systematically forwarded on to the responsible decision-makers. Risks are monitored with the aid of indicators and management is notified of any pertinent developments if thresholds are exceeded. The risk reports summarise the findings of the risk inventories and are prepared individually for each operating company and for the Group as a whole.

As part of the monthly reporting under the German Commercial Code (Handelsgesetzbuch, "HGB") and IFRSs, any deviations from the budget are reviewed and their impact on target achievement are forecasted. The key indicators here are revenue, expense items and, as a result, EBITDA. Further KPIs, including customer footfall, sales closing ratio, average shopping basket, liquidity development, and the change in inventories and their valuation are used to assess the Company's position.

MACROECONOMIC AND POLITICAL RISKS

Although there are presently no indications of such, the economic situation can worsen at any time. Both in theory and in practice there are numerous causes and triggers that would lead consumers to spend less or to maintain lower spending levels. A significant deterioration of the global economic climate would also negatively impact the European Union and the situation in ADLER's sales markets. The occurrence of the aforementioned risks could have an adverse effect on the ADLER Group's financial position, cash flows and financial performance.

MARKET RISKS

The ADLER Group's business performance and growth depend on general demand trends in the retail clothing industry and ADLER's target customer group in particular. Demand trends are of key significance in the ADLER Group's home market of Germany, where the Group generates the predominant share of its revenue. However, the remaining sales markets – Austria, Luxembourg and Switzerland – are also of economic consequence for ADLER. Demand depends significantly on the economic climate and consumer behaviour.

Any phase of weak economic performance in the ADLER Group's sales markets or decline in disposable income for clothing in ADLER's target customer group increases the risk of a negative sales trend. On the one hand, this could result in greater pricing pressure on the merchandise sold by ADLER and in lower margins. On the other hand, shifts in income levels for entire demographic groups could mean that consumers who in the past purchased high-end merchandise might turn to ADLER for their clothing needs in the future.

Changes in buyer behaviour, for example from brick-and-mortar to online retail, increase the risk of a negative sales trend and shrinking margins.

Fluctuations in supply and demand among suppliers or on commodities markets may lead to supply shortages, quality defects or higher logistics and manufacturing costs. It may not be (entirely) possible to offset these costs with higher prices. ADLER counters such risks by following a rather broadly diversified procurement policy while at the same time focussing on reliable partners. The simultaneous expansion of its retail business ensures higher margin flexibility and allows for the possibility of offsetting price fluctuations on supplier markets.

Country risks are primarily attributable to international purchasing activities. For ADLER, these include potential macroeconomic, political and other entrepreneurial risks abroad. The Company counters these risks through the aforementioned diversification of its supplier structure. Country risks are offset on the sales side by selling ADLER products exclusively in neighbouring, German-speaking countries with stable economic and political environments. As is the case for all companies, there is the risk that potential acts of terrorism or environmental disasters could jeopardise the financial position, cash flows and financial performance of the Company.

ADLER's economic success depends in large part on the brand image of the ADLER umbrella brand and its long-term strong positioning among the customer segment aged 55 and up. Therefore, the utmost priority is placed on protecting and maintaining ADLER's brand image. By the same token, this theoretically gives rise to the risk that ADLER could damage the umbrella brand through poor decisions or incorrect actions. Such decisions or actions may adversely affect the Company's growth prospects.

ADLER identifies current trends in its target customer group early on and adapts its design, procurement, distribution and sales processes to reflect them. The Group's competitive position, growth prospects and profitability may be adversely affected in the event ADLER fails to identify important trends or cater to the tastes of its customers. This also applies to the Company's pricing and product development.

FINANCIAL AND LIQUIDITY RISKS

ADLER's long-term corporate financing is secured through the availability of the Company's own cash and cash equivalents and sufficient invoice terms for accounts payable. At the same time, the Company has access to sufficient lines of credit to rule out liquidity squeezes. Corporate financial planning, together with weekly rolling liquidity planning, ensures that liquidity reserves are always available. As a result of the available cash and cash equivalents and the expected positive business development, ADLER avoids exposure to any risk of insufficient financing.

The Company is primarily financed through equity, which is why ADLER is only partly affected by interest rate changes. No interest hedges have been concluded.

CURRENCY RISKS

ADLER is only marginally exposed to currency risks since it realises revenue and procures merchandise primarily in euros. However, the procurement markets for the textiles industry, which are primarily located in Asia, generally deal in US dollars. There are indirect currency risks insofar as importers might pass on the currency fluctuations resulting from the current weakness of the euro via the price at which they sell goods to ADLER. This results in a margin risk which affects ADLER as well as any other textiles company with a high share of imported goods.

However, ADLER normally purchases the delivered merchandise at fixed prices that are agreed upon in advance on which it can base its sales price calculation.

ADLER procures merchandise from Europe as well as the Far East. The procurement sources in Europe include more than 80 suppliers for various fashion segments. ADLER is not dependent on any single supplier to the extent that this might have a noticeable adverse effect on revenue development. If problems with a given supplier arise, alternative procurement sources are available. Merchandise procurement from the Far East is conducted largely via METRO Sourcing International Limited, which operates as an intermediary procurement agent. ADLER also procures merchandise from a large number of manufacturers bundled through MSI. There are no dependencies or major risks in the event of problems with MSI suppliers. ADLER uses NTS Holding Limited to conduct a portion of its business with Chinese suppliers.

RISKS ASSOCIATED WITH THE PROCUREMENT OF MERCHANDISE

Aside from general geographical and political risks, rising wages in emerging regions and increasing prices for raw materials mean that there is always a risk of increasing production costs and hence lower margins. The ADLER Group counteracts this risk through margin-based collection planning in order to ensure an early response to rising production costs. Negative effects on the gross profit margin are reduced through the expansion and continued professionalisation of the operating business, Group-wide efficiency enhancement measures, improved material use and the consistent implementation of pricing policy.

ASSESSMENT OF RISKS BY THE EXECUTIVE BOARD

Based on the information currently available, no individual or aggregated risks have been identified which might jeopardise the Company as a going concern.

INTERNAL CONTROL & RISK MANAGEMENT SYSTEM

Internal control and risk management system (ICS) related to the (Group) accounting process (report in accordance with §§ 289 (4), 315 (2) no. 5 of the German Commercial Code (Handelsgesetzbuch, “HGB”))

The internal control and risk management system features suitable structures and defined processes that are integrated within the organisation. It is designed in such a way to ensure the timely, consistent and correct recording of all business processes and transactions. To consolidate the companies included in the consolidated financial statements, ADLER’s ICS ensures compliance with mandatory statutory norms, accounting requirements and internal accounting instructions. Changes are continually analysed with regard to their relevancy and impact on the consolidated financial statements and, where necessary, are integrated into the intra-Group guidelines and systems.

ADLER’s Group Finance department is responsible not only for actively supporting all business divisions and Group companies but also for developing and updating standard guidelines and work instructions for accounting-related processes. Aside from established control mechanisms, the principles of the ICS consist of technical system-based and manual reconciliation processes, the separation of management and control functions and the adherence to guidelines and work instructions.

The financial statements of the Group companies outside of Germany are drawn up by Group Accounting. The Group companies are responsible for adhering to Group-wide guidelines and procedures and the proper and timely operation of their accounting-related processes and systems. Local companies are supported by points of contact at the Group level throughout the entire accounting process. Appropriate measures are implemented as part of the accounting process to ensure that the consolidated financial statements are in compliance with the regulations. The measures serve in particular to identify and evaluate risks and to mitigate and monitor known risks.

In principle, it should be taken into account that an internal control system, regardless of its design, cannot provide absolute certainty that material accounting misstatements will not be made or discovered. However, it can be used with sufficient certainty to prevent business risks from having a material impact.

REMUNERATION REPORT

The remuneration report describes the principles applied in setting the Executive Board members' total remuneration, explains the structure and specifies the amount of the remuneration paid to Executive Board members. The report also provides a summary of the principles underlying the Supervisory Board members' remuneration and the amount thereof. The report contains the disclosures required under the German Commercial Code (Handelsgesetzbuch, "HGB"), International Financial Reporting Standards (IFRSs), and the declaration of conformity in accordance with the recommendations of the German Corporate Governance Code.

PERFORMANCE-BASED REMUNERATION SCHEME FOR THE EXECUTIVE BOARD

Since ADLER's founding, Executive Board remuneration has been based on a scheme aimed at creating an appropriate incentive for successful and forward-thinking corporate management. Executive Board remuneration, which is in line with that of comparable organisations, is based on the Company's size and financial situation and aims to appropriately reward exceptional performance as well as to tangibly reflect failures to meet performance targets. Executive Board members are expected to demonstrate their long-term commitment to ADLER. This expectation, which is part and parcel of the shareholders' interest in an attractive investment, is met by making the remuneration contingent on the long-term and thus sustainable increase in the Company's value as reflected in ADLER's share price.

Based on applicable law, specifically the German Act on the Appropriateness of Executive Board Remuneration (Gesetz zur Angemessenheit der Vorstandsvergütung, "VorstAG") as well as a corresponding provision in the rules of procedure for the Supervisory Board, the full Supervisory Board is responsible, following preparation by the Personnel Committee, for setting and periodically reviewing the remuneration of the individual Executive Board members. The remuneration scheme for the Executive Board – the underlying principles of which remained unchanged in 2017 – was approved most recently by the Annual General Meeting held on 13 May 2015 in accordance with § 120 (4) of the German Stock Corporation Act (Aktiengesetz, "AktG").

The Executive Board members' remuneration consists of a base salary plus performance-based components. The performance-based components are the "short-term incentive" (STI) bonus and the "long-term incentive" (LTI) bonus, the calculation of which takes several years into account.

Base remuneration

The base remuneration for Executive Board members consists of an annual fixed amount paid out in 12 equal instalments as a monthly salary. Executive Board members also receive ancillary benefits in the form of non-cash benefits consisting primarily of the use of a company car, telephone and insurance premiums. The Company reimburses the Executive Board members 50 % of their documented expenses for health and long-term care insurance, albeit not more than the total of the Company's share of the health and long-term care insurance premiums owed in the event an employment relationship is deemed to exist under social security insurance law.

Short-term incentive bonus (STI)

The STI is the first remuneration component, and continues to be based on the Company's performance for the past financial year. In financial year 2017, the STI for current members of the Executive Board will be calculated based on earnings before interest, tax, depreciation and amortisation (EBITDA) as reported in the audited IFRS consolidated financial statements for the financial year ended and based on targets and further financial ratios to be defined at the beginning of the year which operate to either increase or decrease the STI depending on the degree to which such targets and ratios are met. Each member's STI is capped at € 750 thousand annually.

The Supervisory Board may reasonably reduce the STI if it is based on circumstances which are not adequately attributable to the performance of Executive Board members; or are attributable to extraordinary developments. The STI for the past financial year is due and payable two weeks after the conclusion of the Annual General Meeting. If a member's appointment to the Company's Executive Board was only for part of the financial year, the STI will be paid on a pro rata temporis basis.

Long-term incentive bonus (LTI)

The LTI bonus, the calculation of which takes several years into account, is intended as monetary recognition of the Executive Board member's contribution toward increasing the Company's value. The LTI bonus is based on EBITDA as reported in the audited and approved IFRS consolidated financial statements for the financial year ended. The amount of the bonus depends on the performance of ADLER shares (weighted average share price for the Company during the financial year for which the LTI bonus is calculated as compared to the prior-year weighted average share price). The new LTI bonus, the calculation of which takes several years into account, is currently limited to a total amount of € 1,500 thousand and is not paid out if ADLER shares do not perform accordingly. The LTI bonus for each financial year ended is due and payable two weeks after the conclusion of the Annual General Meeting. If a member's appointment to the Company's Executive Board was only for part of the financial year, the new LTI bonus will be paid on a pro rata temporis basis.

The previous LTI bonus, which was based on stock appreciation rights (SARs), expired at the end of the 2016 financial year.

Commitments in connection with the termination of executive board membership

In the event an Executive Board membership or service agreement is terminated early without good cause, the current service agreements provide for the payment of severance benefits. The payments, including ancillary benefits, may not exceed the equivalent of two annual salaries ("Severance Cap") and may not amount to more than the remaining term of the service agreement. The Severance Cap is determined based on either an individual amount or on the total remuneration for the past financial year and the expected total remuneration for the current financial year. No commitments have been made to pay benefits to members of the Executive Board for early termination of the Executive Board membership as a result of a change of control.

Pensions

There are no contractual pension claims in existence for active members of the Executive Board.

TOTAL REMUNERATION FOR FINANCIAL YEAR 2017

The Company's Annual General Meeting on 4 May 2016 resolved that individual Executive Board members' remuneration would not be disclosed separately. For financial year 2017, remuneration for the Executive Board totalled €2,327 thousand (previous year: €1,313 thousand). The breakdown of the remuneration is as follows:

€'000	2017	2016
Fixed remuneration	1,073	1,009
Non-cash benefits	26	22
Bonuses	228	210
Short-term employee benefits payable to Executive Board members	**1,327**	**1,241**
Long-term incentive bonus (LTI)	0	72
Benefits payable to Executive Board members from long-term bonus (LTI)	**0**	**72**
Severance payments	1,000	0
Benefits due to termination of the Executive Board position	**1,000**	**0**
Total	**2,327**	**1,313**

SUPERVISORY BOARD REMUNERATION

The remuneration system for the Supervisory Board has recently been modified by resolution of the Annual General Meeting on 13 June 2013. The remuneration system is set forth under article 14 of Adler Modemärkte AG's Articles of Association. At ADLER, the remuneration of the Supervisory Board is structured in the form of fixed remuneration only. As with the remuneration for the Executive Board, the remuneration for the Supervisory Board is contingent on the size of the organisation and should reflect the level of activity and responsibility assumed.

Accordingly, the members of the Supervisory Board receive annual remuneration in the amount of €20 thousand for their activities, payable following the conclusion of a given financial year. The chairman of the Supervisory Board receives double this amount and the deputy chairman receives 1.5 times this amount. For each Supervisory Board committee of which they are a member, members receive an additional 10% to the amount set out above, provided that the respective committee has met at least twice in the respective financial year. Excepted from this provision is the membership in the Conciliation Committee pursuant to §27 (3) MitbestG. Supervisory Board members who have not been a member or chairman of the Supervisory Board or a committee for an entire financial year shall be remunerated on a pro rata temporis basis. Remuneration is due and payable at the end of the Annual General Meeting resolving on the ratification of the acts of the Supervisory Board. Supervisory Board members also receive €300 for each Supervisory Board meeting attended. The chairman receives double this amount and the deputy chairman receives 1.5 times this amount. Members of the Supervisory Board are also reimbursed for all expenses as well as VAT payable on their remuneration and out-of-pocket expenses. The Annual General Meeting shall decide by resolution on other methods of remuneration for the members of the Supervisory Board and benefits of a remunerative nature.

In financial year 2017, the total remuneration for members of the Supervisory Board was € 317 thousand (previous year: € 322 thousand). The breakdown of the remuneration is as follows:

	2017				2016			
€'000	Fixed remuneration	Committee membership	Meeting attendance	Total remuneration	Fixed remuneration	Committee membership	Meeting attendance	Total remuneration
Supervisory Board members in office as at 31 December 2017								
Massimiliano Monti, Chairman [1]	40.0	8.0	3.0	51.0	33.3	6.0	3.3	42.6
Majed Abu-Zarur [1], Deputy Chairman	30.0	6.0	1.8	37.8	22.0	1.2	2.4	25.6
Wolfgang Burgard [1]	20.0	4.0	1.5	25.5	20.0	4.0	1.8	25.8
Cosimo Carbonelli D'Angelo [1]	20.0	2.0	0.3	22.3	20.0	2.0	2.1	24.1
Corinna Groß	20.0	–	0.6	20.6	20.0	–	1.2	21.2
Frank König [1, 2]	20.0	–	1.5	21.5	8.4	–	0.9	9.3
Peter König [1]	20.0	4.0	1.2	25.2	20.0	4.0	2.1	26.1
Georg Linder [1]	20.0	4.0	1.5	25.5	20.0	4.0	2.1	26.1
Giorgio Mercogliano	20.0	–	1.5	21.5	20.0	–	2.1	22.1
Dott. Michele Puller [1]	20.0	–	1.5	21.5	26.8	1.4	3.3	31.4
Paola Viscardi-Giazzi [1]	20.0	2.0	1.2	23.2	20.0	2.0	0.9	22.9
Beate Wimmer	20.0	–	1.5	21.5	20.0	–	2.1	22.1
Former members of the Supervisory Board								
Martina Zimlich, Deputy Chairwoman [1, 2]	–	–	–	–	17.4	3.5	1.8	22.7
Total	**270.0**	**30.0**	**17.1**	**317.1**	**267.8**	**28.0**	**26.1**	**322.0**

[1] *The Chairman and the Deputy Chairman of the Supervisory Board receive a higher fixed remuneration and a higher remuneration for attending meetings. In accordance with the Articles of Association of Adler Modemärkte AG, Supervisory Board members receive an additional 10 % for each Supervisory Board committee of which they are a member; this remuneration is reported separately from the remuneration for committee activities.*

[2] *Frank König was elected with immediate effect to replace Martina Zimlich, who passed away on 30 July 2016 and was thus no longer on the Supervisory Board.*

MISCELLANEOUS

The Company has taken out D&O liability insurance, in particular for the members of its governing bodies. The insurance includes a deductible for members of the Executive Board and the Supervisory Board in compliance with § 93 (2) sentence 3 AktG and the German Corporate Governance Code.

LEGAL DISCLOSURES

The following section primarily contains disclosures and explanations pursuant to § 289a, § 289b, § 289f, § 315a, § 315b and § 315d of the German Commercial Code (Handelsgesetzbuch, "HGB"). These disclosures concern corporate legal structures and other legal relationships and serve to provide a better overview of the Company and any obstacles that may exist with respect to an acquisition.

CORPORATE GOVERNANCE STATEMENT

The corporate governance statement under § 289f and § 315d of the German Commercial Code (Handelsgesetzbuch, "HGB") constitutes a component of the management report. Pursuant to § 317 (2) sentence 6 HGB, the audit of the disclosures provided under § 289f and §315d HGB is limited to whether the relevant disclosures have been made. The statement published on the ADLER website at *www.adlermode-unternehmen.com* under the heading Investor Relations/Corporate Governance pursuant to § 289f (2) sentence 2 and §315d sentence 2 in conjunction with § 289f (2) sentence 2 HGB contains the declaration of conformity, information on corporate governance practices, a description of the procedures applied by the Executive Board and the Supervisory Board and information on targets set pursuant to § 76 (4) and § 111 (5) AktG.

SEPARATE NON-FINANCIAL REPORT IN ACCORDANCE WITH § 289B (3) HGB AND §315B (3) HGB

Adler Modemärkte AG prepared a separate non-financial report in accordance with § 289b (3) HGB and §315b (3) HGB for financial year 2017 that is not contained in the management report. This report will be published as a separate sustainability report on the Company's website (*www.adlermode-unternehmen.com*) under the heading "Sustainability" by 30 April 2018, where it will be available for inspection and download for a minimum of ten years.

REPORT ON RELATIONSHIPS WITH AFFILIATES

S&E Kapital GmbH, Munich, held a majority interest in the Company throughout the year under review. No control or profit and loss transfer agreement exists between Adler Modemärkte AG and S&E Kapital GmbH.

Therefore, the Executive Board of Adler Modemärkte AG prepared a dependent companies report on relationships with affiliates pursuant to § 312 of the German Stock Corporation Act (Aktiengesetz, "AktG"). At the conclusion of that report, the Executive Board declared "[…] that Adler Modemärkte AG and its subsidiaries, based on the circumstances which were known to the Executive Board at the time and under which the legal transactions were effected received reasonable consideration for each such legal transaction. No measures were taken or omitted in the interest or at the behest of the controlling entity or any entities affiliated with it".

DISCLOSURES UNDER TAKEOVER LAW PURSUANT TO § 289A AND § 315A HGB AS AT 31 DECEMBER 2017 AND EXPLANATORY REPORT

Composition of subscribed capital

Adler Modemärkte AG's share capital is currently still € 18,510,000 and is divided into 18,510,000 no-par value ordinary bearer shares, each representing a notional interest in the share capital of € 1.00. All shares carry the same rights and each share carries one vote at the Annual General Meeting.

Restrictions on voting rights or the transferability of shares, even if these could arise from agreements between shareholders, to the extent these are known to the Executive Board of the parent company

There were no restrictions on voting rights or the transferability of shares.

Equity interests in excess of 10% of the voting rights

As at 31 December 2017, to the best of ADLER's knowledge, direct and indirect equity interests held in the Company in excess of 10% of the voting rights as disclosed pursuant to the German Securities Trading Act (Wertpapierhandelsgesetz, "WpHG") exist as follows:

Direct equity interest held by S&E Kapital GmbH, Munich, representing 52.81% of the voting interest in the Company.

Indirect equity interests by virtue of the attribution of the 52.81% voting interest in the Company held by S&E Kapital GmbH, Munich, under the WpHG: STB Fashion Holding GmbH i.l., Herne; Steilmann SE i.l., Bergkamen; Miro Radici Hometextile GmbH i.l., Bergkamen; Steilmann Holding AG i.l., Bergkamen; Excalibur I S.A., Luxembourg; Equinox Two S.C.A., Luxembourg; and Equinox S.A., Luxembourg. Changes may have arisen after the reporting date which were not required to be disclosed to the Company. The complete notifications are contained in the notes ("Voting rights notifications"). In addition, all notifications received by the Company pertaining to voting rights may be viewed on ADLER's website (*www.adlermode-unternehmen.com*) under the heading Investor Relations / News & Releases / Voting Rights Announcements.

Shares with special rights granting control powers

No shares with special rights granting control powers exist.

Type of voting rights control where employees hold equity interests and do not directly exercise their control rights

The Company has not currently issued any shares to employees under any employee stock option plan.

Appointment and dismissal of members of the Executive Board, amendments to the Articles of Association

The appointment and dismissal of members of the Executive Board of Adler Modemärkte AG is governed by § 84 and § 85 AktG and by § 31 of the German Co-determination Act (Mitbestimmungsgesetz, "MitbestG") in conjunction with article 6 of the Articles of Association. According to the provisions thereunder, members of the Executive Board are appointed by the Supervisory Board for a maximum term of five years. Re-appointment or an extension of the term of office for up to an additional five years is permissible. Under § 31 (2) MitbestG, a majority of at least two thirds of the members of the Supervisory Board is required to appoint members of the Executive Board. If this does not result in an appointment being made, the Conciliation Committee of the Supervisory Board must propose a candidate for appointment within one month of voting. The Supervisory Board will then appoint the members of the Executive Board by majority vote of its members. If this does not result in an appointment being made either, a new vote will be held in which the chairman of the Supervisory Board's vote counts twice. Pursuant to article 6 (1) of the Articles of Association, the Executive Board is composed of at least two members; the Supervisory Board stipulates the number of members on the Executive Board. Pursuant to § 84 AktG and article 6 (1) of the Articles of Association, the Supervisory Board may appoint a chairman of the Executive Board (CEO) as well as a deputy chairman. If the Executive Board is lacking a required member, the member will be judicially appointed in urgent cases by application of one of the parties pursuant to § 85 AktG. Pursuant to § 84 (3) AktG, the Supervisory Board may revoke the appointment as a member of the Executive Board and the appointment as CEO for good cause.

Amendments to the Articles of Association are passed with a majority of at least three quarters of the share capital represented at the adoption of the resolution; §§ 179 et seq. AktG apply. Pursuant to article 16 of the Articles of Association, the Supervisory Board is authorised to pass editorial amendments to the Articles of Association. The Supervisory Board is further authorised to update the language of article 4 of the Articles of Association (Share capital amount and division) to reflect the utilisation of authorised and/or contingent capital in each case.

Executive Board's authority to issue shares

The Executive Board's authorisation under article 5 (5) of the Articles of Association currently in force, subject to the consent of the Supervisory Board, to increase the Company's share capital against cash and/or in-kind contributions, on one or several occasions, by a total of up to € 7,930,000 by issuing new no-par value bearer shares (Authorised Capital), expired on 10 February 2016.

The Executive Board's authorisation, granted by resolution of the Company's extraordinary General Meeting held on 30 May 2011, subject to the Supervisory Board's consent, to issue, on one more occasions on or before 30 April 2016, warrant-linked and/or convertible bonds with a total nominal amount of up to € 250,000,000 with a maximum term to maturity of 20 years and, subject to the specific stipulations of the respective terms and conditions of the warrant-linked and/or convertible bonds, to grant option rights to the holders of warrant-linked bonds and conversion rights to the holders of convertible bonds in respect of up to € 7,930,000 no-par value ordinary bearer shares of the Company, expired on 30 April 2016. In connection with this, the contingent increase of € 7,930,000 in the Company's share capital through the issue of up to 7,930,000 new no-par value ordinary bearer shares (Contingent Capital 2011), resolved by the extraordinary General Meeting held on 30 May 2011 and pursuant to article 5 (6) of the Company's current Articles of Association, lapsed on the same date.

Executive Board's authority to buy back shares

The Annual General Meeting on 13 June 2013 authorised the Company pursuant to § 71 (1) no. 8 AktG to acquire treasury shares representing a total of up to 10 % of the share capital existing at the time the resolution is adopted until 12 June 2018. At no time may the shares acquired under this authorisation together with other shares of the Company which the Company had acquired at the time of acquisition and still holds or which are attributable to it pursuant to § 71d or § 71e AktG represent more than 10 % of the share capital. The Company may not exercise the authorisation for the purpose of trading in treasury shares. The authorisation may be exercised in whole or in partial amounts on one or more occasions by the Company, or by dependent companies or entities in which the Company has a majority shareholding, or by third parties acting for the account of the Company or that of dependent companies or entities in which the Company has a majority shareholding. At the Executive Board's option, treasury shares may be acquired over the stock exchange or by way of a public purchase offer directed to all shareholders. If the shares are acquired over the stock exchange, the consideration paid per share (excluding ancillary acquisition costs) may not be more than 10 % above or below the price determined for the share on the relevant trading day in the opening auction of the XETRA trading system (or a comparable successor system). If the shares are acquired by way of a public purchase offer, the purchase price offered or the minimum and maximum amounts of the purchase price range per share (excluding ancillary acquisition costs) may not be more than 10 % above or below the closing price in the XETRA trading system (or a comparable successor system) on the third stock exchange trading day preceding the day of the public announcement of the purchase offer. If, following publication of a public purchase offer, there are significant deviations from the relevant price, the purchase offer may be adjusted. In this case, the price on the third stock exchange trading day preceding the public announcement of any such adjustment shall be relevant. The volume of the offer may be restricted. If the offer is over-subscribed, acceptance of the offer must take place on a pro rata basis. A preferential acceptance of smaller units of up to 100 tendered shares per shareholder may be stipulated.

The Executive Board shall be authorised to use shares of the Company, which have been acquired pursuant to this authorisation or any prior issued authorisation, for any purpose permitted by law. Specifically, the Executive Board's authorisation shall cover the following: (i) The Executive Board shall be authorised, subject to the Supervisory Board's consent, to dispose of treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, over the stock exchange or by tender offer to all the shareholders. Shares sold over the stock exchange shall not carry any shareholders' pre-emptive subscription rights. In the event shares are sold by way of a public tender, the Executive Board shall be authorised, subject to the Supervisory Board's consent, to exclude shareholders' pre-emptive subscription rights on fractional shares. (ii) The Executive Board shall furthermore be authorised, subject to the Supervisory Board's consent, to dispose of treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, in a manner other than over the stock exchange or by tender offer to all the shareholders, provided the treasury shares acquired are sold at a price that is not substantially lower than the stock exchange price of the Company's shares with the same features at the time of any such sale. Shareholders' pre-emptive subscription rights shall be excluded in this context. This authorisation shall be limited to a total of 10% of the share capital existing at the time the resolution is adopted by the Annual General Meeting or to the Company's share capital existing at the time this authorisation is exercised, whichever is lower. The proportionate amount of the share capital represented by the shares which pursuant to this authorisation may be sold in a manner other than over the stock exchange or by tender offer to all the shareholders shall be reduced by the proportionate amount of the share capital represented by those shares which were issued since the grant of this authorisation based on the authorisation under article 5 (5) of the Articles of Association (Authorised Capital), and by those shares for which the holders or creditors of warrant-linked and/or convertible bonds issued since the grant of this authorisation are or were eligible to subscribe, in each case to the extent that, when shares were issued from authorised capital or when warrant-linked and/or convertible bonds were issued, pre-emptive subscription rights under §186 (3) sentence 4 AktG were excluded. (iii) The Executive Board shall furthermore be authorised, subject to the Supervisory Board's consent, to use treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, as (partial) consideration in the context of corporate mergers or to acquire companies, equity investments in companies, parts of companies or other assets. (iv) The Executive Board shall furthermore be authorised, subject to the Supervisory Board's consent, to offer for purchase or to transfer treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, to employees of the Company or its Group companies. The Supervisory Board shall be authorised to offer for purchase or to transfer treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, to members of the Company's Executive Board. (v) The Executive Board shall furthermore be authorised, subject to the Supervisory Board's consent, to offer for purchase or to transfer treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, to third parties who, as business partners of the Company or its Group companies, play a significant role in assisting the Company in achieving its corporate goals. (vi) The Executive Board shall furthermore be authorised to use treasury shares, which were acquired pursuant to this or any prior issued authorisation, to satisfy conversion or subscription rights arising under convertible or warrant-linked bonds granted by the Company or its Group companies. (vii) The Executive Board shall furthermore be authorised, subject to the Supervisory Board's consent, to cancel treasury shares, which were acquired pursuant to this authorisation or any prior issued authorisation, without the need for a separate resolution by the Annual General Meeting. The authorisation to cancel shares may be exercised in whole or in part. The cancellation of shares would result in a capital reduction. Alternatively, the Executive Board may determine that the share capital will not be reduced and that the cancellation will instead result in the proportionate interest in the share capital held by the other shareholders being increased pursuant to §8 (3) AktG. In this case, the Supervisory Board is authorised to amend the number of shares set out in the Articles of Association. (viii) Shareholders' pre-emptive subscription rights shall be excluded in effecting the measures under ii. to vi.

The aforementioned authorisations may be exercised on one or several occasions, in whole or in part, individually or jointly.

In January 2014, the Company sold 888,803 treasury shares that had been previously acquired.

Material agreements of the parent company which are contingent upon a change of control as a result of a takeover offer

Adler Modemärkte AG has three credit facility agreements for a total of €15 million and three guarantee facilities for a total of €7 million, four of which provide for a right of termination for good cause in the event of a change of control. The agreements essentially give the lender a right of termination in those cases where the lender has reason to believe that its legitimate concerns will be impaired by the acquisition of direct or indirect control over the Company by one or several legal entities or that such an acquisition would have a negative impact on the performance of Adler Modemärkte AG. The lender may also terminate where a change of control occurs and the parties are unable to agree on continuing the agreement on new terms where applicable, e.g. with respect to the interest rate, collateral or other arrangements, within an appropriate period or in due time before the change of control occurs.

Compensation agreements entered into by the Company with members of the Executive Board or employees in the event of a takeover offer

No commitments have been made to pay benefits to members of the Executive Board or employees for premature termination of the Executive Board position as a result of a change of control.

REPORT ON EXPECTED DEVELOPMENTS

GLOBAL ECONOMIC UPTURN CONTINUES

According estimates by the International Monetary Fund (IMF), the global economy will continue to grow in 2018. Based on the positive economic performance in 2017, which was more dynamic than originally expected, the experts increased their forecast by 0.2 % to 3.9 % in January 2018. The short-term risk/opportunity profile for the global economy is set to be balanced, but risks are likely to outweigh opportunities over the medium term. In particular, the IMF considers geopolitical tensions, an increased tendency towards protectionism in individual countries and a potential correction of the financial markets to pose potential risks.

The IMF anticipates a slight economic slowdown in the eurozone, with GDP growth of 2.2 % in 2018 compared with 2.4 % in 2017. Growth of 2.3 % (2017: 2.5 %) is forecast for the German economy, while the Austrian economy is expected to grow by 1.8 %.

Buoyed by positive impetus from the approved tax reforms, the US economy is predicted to grow by 2.7 % (2017: 2.3 %). The IMF expects Chinese economic growth to match the previous year's level of 6.5 %.

CONSUMER DEMAND SUSTAINED AMID RISING PURCHASING POWER

According to a study conducted by GfK, a market research institute based in Nuremberg, nominal disposable income in Germany is set to rise by €633 or 2.8 % per capita in 2018. Given the strong economic upturn in 2017, the still healthy labour market situation and the prospects for further growth, consumers have an optimistic outlook for 2018. Propensity to spend therefore also rose again at the beginning of the year. Overall, GfK believes that the conditions for a successful consumer year in 2018 are very good. However, a more isolationist trade policy from the US and dragging Brexit negotiations could have a dampening effect.

In Austria, the good economic growth, which is expected to initially continue in 2018, also led to positive business and consumer sentiment at the beginning of the year. The Austrian Institute of Economic Research expects economic growth to gradually slow down in the further course of 2018, which will also impact consumer sentiment. As a result, private consumption, which will have initially benefited from the favourable development in income levels, will likely only add limited impetus to the late phase of the upswing.

According to a survey conducted by Switzerland's State Secretariat for Economic Affairs (SECO), Swiss consumer sentiment improved at the beginning of the year. The corresponding index thus reached a seven-year high in January 2018. However, the optimism regarding economic growth and the labour market situation was only reflected to a limited extent in consumers' expectations for their personal finances, which remained largely unchanged at average levels.

ONGOING PESSIMISM AMONG BRICK-AND-MORTAR FASHION RETAILERS

After brick-and-mortar fashion retailers were again unable to benefit from the consumer demand in 2017, retailers surveyed by industry magazine Textilwirtschaft had a pessimistic outlook for 2018. Almost half of those surveyed believe that the consumer climate for textiles and clothing will continue to deteriorate. In particular, they were concerned by declining customer footfall, increasingly fierce competition, and the potential deterioration of political conditions.

FORECAST AND OVERALL ASSERTION

ADLER's Executive Board had predicted that the environment in the textile retail industry would remain challenging in the 2017 financial year and therefore forecast a slight decline in revenue as compared to the 2016 financial year (€544.6 million). Revenue was not expected to reach the prior-year figure; however, revenue generated by the online shop was expected to once again significantly exceed the 2016 figure. These expectations were only partially met, with revenue of €525.8 million in 2017, since the decline in revenue from brick-and-mortar stores was more significant than predicted.

The effects of the measures introduced to increase efficiency had an impact, particularly in the area of personnel expenses. EBITDA was expected to significantly exceed the figure generated in 2016 and amount to between €27–30 million. Although this figure was reached due to the non-recurring effects of the real estate transactions, at an operational level the target was not met with adjusted EBITDA of €25.4 million. The primary reason for this was the steeper than expected decline in revenue.

ADLER's Executive Board expects the environment in the textile retail industry to remain challenging in the 2018 financial year and therefore expects revenue to remain approximately level with the prior-year figure (€525.8 million). EBITDA is expected to exceed the adjusted 2017 figure (€25.4 million) and amount to between €26–29 million. This forecast takes into consideration the slight uptick in personnel expenses, due to the increase in wages, salaries and benefits, as well as a temporary rise in transport and logistics costs due to the change in logistics provider. By contrast, the measures to increase efficiency are expected to have a positive impact, particularly in the purchasing and distribution departments. ADLER expects only minor changes as it pertains to the EUR/USD exchange rate. The same applies to the development of key commodity prices. The positive effects of the change in logistics provider will only start to be felt in financial year 2019.

FORWARD-LOOKING STATEMENTS

This management report contains forward-looking statements regarding Adler Modemärkte AG, its subsidiaries and affiliates, and the economic environment. All of these statements are based on assumptions that the management made on the basis of the knowledge and information available to it at the time this report was prepared. If these assumptions do not or only partially hold true, or if additional risks arise, actual business performance may deviate from the expected business performance. Therefore, no specific responsibility is taken for any forward-looking statements made in this management report.

CONSOLIDATED FINANCIAL STATEMENTS AS AT 31 DECEMBER 2017

CONSOLIDATED INCOME STATEMENT

FOR THE FINANCIAL YEAR FROM 1 JANUARY TO 31 DECEMBER 2017

€'000	Note	2017	2016
Revenue	1	**525,814**	**544,553**
Other operating income	2	18,812	8,734
Cost of materials	3	−244,060	−256,467
Personnel expenses	4	−96,849	−102,333
Other operating expenses	5	−171,712	−171,187
EBITDA		**32,005**	**23,300**
Depreciation, amortisation and write-downs	6	−16,454	−16,660
EBIT		**15,551**	**6,640**
Other interest and similar income	7	318	19
Interest and similar expenses	7	−5,173	−4,948
Net finance costs	7	**−4,855**	**−4,929**
Consolidated net profit for the year before tax		**10,696**	**1,711**
Income taxes	8	−6,838	−1,301
Consolidated net profit for the year		**3,858**	**410**
of which attributable to shareholders of Adler Modemärkte AG		3,858	410
Basic in €	35	0.21	0.02
Diluted in €	35	0.21	0.02

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE FINANCIAL YEAR FROM 1 JANUARY TO 31 DECEMBER 2017

€'000	Note	2017	2016
Consolidated net profit for the year		**3,858**	**410**
Currency translation gains from foreign subsidiaries		231	−24
Remeasurement of defined benefit pension entitlements and similar obligations	19	18	−209
Deferred taxes		−7	65
Items that will not be recycled to the income statement going forward		**242**	**−168**
Change in fair value of available-for-sale financial instruments		8	−5
Items subsequently recycled to the income statement		**8**	**−5**
Other comprehensive income		**250**	**−173**
Consolidated total comprehensive income		**4,108**	**237**
of which attributable to shareholders of Adler Modemärkte AG		4,108	237

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

ASSETS (€'000)	Note	31 Dec. 2017	31 Dec. 2016
Non-current assets			
Intangible assets	9	5,581	6,476
Property, plant and equipment	10	74,975	78,136
Investment property	11	413	413
Other non-current receivables and assets	12	277	439
Deferred tax assets	14	7,398	10,046
Total non-current assets		**88,644**	**95,510**
Current assets			
Inventories	15	73,676	75,399
Trade receivables	16	635	582
Other current receivables and assets	12	14,550	8,034
Available-for-sale financial assets	13	286	277
Cash and cash equivalents	17	63,342	42,773
Total current assets		**152,489**	**127,065**
TOTAL ASSETS		**241,133**	**222,575**

EQUITY AND LIABILITIES (€'000)	Note	31 DEC. 2017	31 DEC. 2016
Capital and reserves			
Subscribed capital	18	18,510	18,510
Capital reserves	18	127,408	127,408
Accumulated other comprehensive income	18	−2,085	−2,336
Negative retained earnings	18	−43,886	−47,743
Total equity	18	**99,947**	**95,839**
LIABILITIES			
Non-current liabilities			
Provisions for pensions and similar obligations	19	5,493	5,816
Other non-current provisions	20	1,309	1,236
Non-current financial liabilities	22	2,267	2,581
Liabilities from finance leases	23	50,233	46,331
Other non-current liabilities	25	5,359	4,654
Deferred tax liabilities	14	75	91
Total non-current liabilities		**64,737**	**60,709**
Current liabilities			
Other current provisions	20	4,366	4,463
Liabilities from the customer loyalty card programme (adjusted)[1]	21	10,380	10,624
Current financial liabilities (adjusted)	22	316	314
Liabilities from finance leases	23	5,718	5,823
Trade payables	24	27,608	25,261
Other current liabilities	25	24,250	19,479
Current income tax liabilities	26	3,810	63
Total current liabilities		**76,449**	**66,027**
Total liabilities		**141,185**	**126,736**
TOTAL EQUITY and LIABILITIES		**241,133**	**222,575**

[1] *Prior-year item adjusted in accordance with IAS 8. Please refer to Note 22.*

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FROM 1 JANUARY TO 31 DECEMBER 2017

	Subscribed capital	Capital reserves	Accumulated other comprehensive income			Negative retained earnings	Total equity
€'000			Securities	Currency translation	Other changes[2]		
As at 1 Jan. 2016	**18,510**	**127,408**	**19**	**−134**	**−2,048**	**−38,899**	**104,856**
Dividend payment	0	0	0	0	0	−9,255[1]	−9,255
Transactions with shareholders	**0**	**0**	**0**	**0**	**0**	**−9,255**	**−9,255**
Consolidated net profit for the year	0	0	0	0	0	410	410
Other comprehensive income	0	0	−5	−24	−143	0	−173
Consolidated total comprehensive income	0	0	−5	−24	−143	410	237
As at 31 Dec. 2016	**18,510**	**127,408**	**14**	**−159**	**−2,191**	**−47,743**	**95,839**
As at 1 Jan. 2017	**18,510**	**127,408**	**14**	**−159**	**−2,191**	**-47,743**	**95,839**
Dividend payment	0	0	0	0	0	0[1]	0
Transactions with shareholders	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Consolidated net profit for the year	0	0	0	0	0	3,858	3,858
Other comprehensive income	0	0	8	231	11	0	250
Consolidated total comprehensive income	0	0	8	231	11	3,858	4,108
As at 31 Dec. 2017	**18,510**	**127,408**	**22**	**72**	**−2,180**	**−43,886**	**99,947**

[1] *No dividend was distributed in the financial year (previous year: €0.50 per share).*
[2] *Other changes relate to actuarial gains and losses less deferred taxes.*

CONSOLIDATED STATEMENT OF CASH FLOWS

FROM 1 JANUARY TO 31 DECEMBER 2017

€'000	Note	2017	2016
Consolidated net profit for the period before tax		**10,696**	**1,711**
Depreciation of property, plant and equipment and amortisation of intangible assets		16,300	16,660
Impairment		154	0
Increase (+)/decrease (–) in pension provisions		–304	–263
Gains (–)/losses (+) from the sale of non-current assets		–7,138	25
Gains (–)/losses (+) from currency translation		307	–38
Other non-cash expenses (+)/income (–)		–8,945	2,246
Net interest income		4,855	4,929
Interest income		311	10
Interest expense		–319	–344
Income taxes paid		–2,005	–2,270
Increase (–)/decrease (+) in inventories		3,930	4,200
Increase (–)/ decrease (+) of trade receivables and other receivables		–8,016	485
Increase (+)/decrease (–) of trade payables, other liabilities and other provisions		11,305	–7,289
Increase (+)/decrease (–) in other items of the statement of financial position		25	2,129
Cash from (+)/used (–) in operating activities (net cash flow)	27	**21,157**	**22,191**
Proceeds from disposals of non-current assets		10,393	183
Proceeds from disposals of non-current assets (property) held for sale		17,250	0
Payments for investments in non-current assets		–6,184	–11,013
Payments for acquisitions of subsidiaries		–6,671	0
Cash from (+)/used (–) in investing activities	27	**14,789**	**–10,830**
Free cash flow	27	**35,946**	**11,361**
Payments in connection with the repayment of loan liabilities		–4,773	–314
Dividend distribution		0	–9,255
Payments in connection with finance lease liabilities		–10,604	–11,095
Cash from (+)/used (–) in financing activities	27	**–15,377**	**–20,664**
Net decrease (–)/increase (+) in cash and cash equivalents	27	**20,569**	**–9,303**
Cash and cash equivalents at beginning of period		42,773	52,076
Cash and cash equivalents at end of period		63,342	42,773
Net decrease (–)/increase (+) in cash	27	**20,569**	**–9,303**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS AS AT 31 DECEMBER 2017

I. PRELIMINARY REMARKS

Adler Modemärkte AG is a corporation (Kapitalgesellschaft) in accordance with German law and its registered office is at Industriestraße Ost 1–7, Haibach, Federal Republic of Germany. The relevant registration court is located in Aschaffenburg (registered under Number HRB 11581).

Its financial year is the calendar year. The financial years of all the companies included in the consolidated financial statements also end on 31 December of the calendar year.

The consolidated financial statements were prepared by the Executive Board on 5 March 2018 for publication.

The ADLER Group (Adler Modemärkte AG and its subsidiaries) is engaged in apparel retailing and operates specialist clothing stores in Germany, Luxembourg, Austria and Switzerland. Under the trade name "ADLER", the Group operates specialist clothing stores either on a stand-alone basis or as part of specialist store or shopping centres. It also operates specialist clothing stores together with other retailers at locations operated jointly. The range of goods offered by the ADLER stores includes womenswear, menswear and kidswear.

The euro (EUR) is both the reporting currency and the functional currency of the ADLER Group. The figures in the notes to the consolidated financial statements are quoted in thousands of euros (€'000).

S&E Kapital GmbH, Munich, prepares the consolidated financial statements for the largest group of companies. These financial statements can be obtained at the company's registered office in Munich. Adler Modemärkte AG, Haibach, prepares the consolidated financial statements for the smallest group of companies. These financial statements can be obtained at the Company's registered office in Haibach.

II. NOTES ON THE BASES AND METHODS EMPLOYED IN THE CONSOLIDATED FINANCIAL STATEMENTS

ACCOUNTING POLICIES

The consolidated financial statements of Adler Modemärkte AG were prepared in accordance with the requirements of the International Accounting Standards Board (IASB), London, in conformity with International Financial Reporting Standards (IFRSs), as adopted by the EU. The interpretations issued by the IFRS Interpretations Committee (the International Financial Reporting Interpretations Committee and the Standing Interpretations Committee) were also applied. The consolidated financial statements conform to the directives relating to consolidated accounts issued by the European Union (Directive 83/349/EEC). In order to ensure equivalence with consolidated financial statements prepared in accordance with the German Commercial Code (Handelsgesetzbuch, "HGB"), all of the disclosures and explanations required by § 315e HGB over and above the requirements of the IASB have also been provided. The consolidated financial statements in the form in which they are presented here comply with the provisions of § 315e HGB; those provisions constitute the legal basis for the preparation of consolidated accounts in accordance with international accounting standards in Germany in conjunction with Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

Those International Financial Reporting Standards (IFRSs) were applied that had become mandatory by the end of the reporting period on 31 December 2017. There was no early adoption of standards whose application had not yet become mandatory as at 31 December 2017.

STANDARDS AND INTERPRETATIONS APPLICABLE FOR THE FIRST TIME

The application of the following standards and interpretations revised or newly issued by the IASB was mandatory for the first time from the start of financial year 2017:

Standards	
Amendments to IAS 7	Disclosures about changes in financial liabilities – "Statement of Cash Flows"
Amendments to IAS 12	Recognition of deferred tax assets for unrealised losses

IAS 7 Statement of Cash Flows

The IASB published amendments to IAS 7 "Statement of Cash Flows" on 29 January 2016. The amendments require that changes in liabilities arising from financing activities, whose payments are recognised under cash flows from financing activities, are disclosed in the form of a reconciliation in the notes to the financial statements. No reconciliation in the notes to the financial statements was necessary since liabilities from the customer loyalty card programme were reported separately from financial liabilities during the reporting period. The amendments to IAS 7 thus do not have any effect on Adler Modemärkte AG's disclosures in the notes.

The first-time application of the following new or amended financial reporting standard did not have a material effect on the presentation of the assets, liabilities, financial position and profit or loss of Adler Modemärkte AG:

IAS 12 Income Taxes

On 19 January 2016, the IASB published the amendments to IAS 12 "Income Taxes". The amendments clarify the recognition of deferred tax assets for unrealised losses related to debt instruments measured at fair value and recognised in other comprehensive income.

STANDARDS, INTERPRETATIONS AND AMENDMENTS TO PUBLISHED STANDARDS THAT ARE NOT YET MANDATORY

The following standards are not yet mandatory. These will be applied by the ADLER Group from the prescribed date and the Group has estimated the expected effects of the individual standards, amendments to standards and interpretations on its financial position, cash flows and financial performance, to the extent that it was possible to make such an estimate at this stage.

Mandated by IASB from/expected to be mandatory for financial years beginning on or after*	Standards		Adopted by EU Commission
2018	IFRS 15	Revenue Recognition Revenue from Contracts with Customers	Yes
	Amendments to IFRS 15	Clarifications to IFRS 15 (Application mandated by IASB from 1 January 2018)	Yes
	IFRS 9	Financial Instruments	Yes
	Amendments to IFRS 2	Classification and Measurement of Share-based Payment Transactions	No
	Amendment to IFRS 4	Amendments in relation to the interaction of IFRS 4 and IFRS 9 – Insurance Contracts	Yes
	IFRIC 22	Foreign Currency Transactions and Advance Consideration	No
	Amendment to IAS 40	Transfers of Investment Property	No
	Annual Improvements 2014–2016	Amendments and clarifications to various IFRSs/Effective (EU) as from 1 January 2017/1 January 2018	No
	IFRIC 23	Uncertainty over Income Tax Treatments	No
2019	IFRS 16	Leasing	Yes
	Amendment to IFRS 9	Financial Instruments – Prepayment Features with Negative Compensation	No
	Amendments to IAS 28	Investments in Associates – Applying IFRS 9 to Long-term Interests in Associates and Joint Ventures	No
	Annual Improvements 2015–2017	Amendments and clarifications to various IFRSs/Effective (EU) as from 1 January 2019	No
2021	IFRS 17	Insurance Contracts	No
unknown	Amendments to IFRS 10/IAS 28	Sale of contributions assets between an investor and its associate or joint venture	No

** Date of first-time mandatory application stipulated by the IASB. Where the standard, interpretation or amendment has already been adopted by the EU Commission, the date is the date for mandatory application stipulated by the EU.*

IFRS 15 Revenue from Contracts with Customers

The new IFRS 15 replaces IAS 18 "Revenue" and IAS 11 "Construction Contracts" as well as any related interpretations. On 28 May 2014, the IASB together with the FASB adopted the new IFRS 15 "Revenue from Contracts with Customers". IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. This standard combines all previous standards and interpretations that contained guidance on revenue recognition. The scope applies to all contracts with customers, unless these fall under the scope of IAS 17, IFRS 9, IFRS 10, IFRS 11, IAS 27 or IAS 28. A five-step model will govern revenue transactions going forward:

- Step 1: Identify the contract with the customer
- Step 2: Identify the performance obligations in the contract
- Step 3: Determine the transaction price
- Step 4: Allocate the transaction price to the performance obligations in the contract
- Step 5: Recognise revenue when (or as) the entity satisfies a performance obligation

Furthermore, IFRS 15 contains explicit guidance on multi-component transactions. Going forward, revenue will be recognised once control in goods or services has been transferred. The transfer of opportunities and risks will serve only as an indicator. Moreover, the standard provides new guidance on deciding when revenue must be recognised either over time or at a point in time. IFRS 15 replaces IAS 11 "Construction Contracts", IAS 18 "Revenue", IFRIC 13 "Customer Loyalty Programmes", IFRIC 15 "Agreements for the Construction of Real Estate", IFRIC 18 "Transfers of Assets from Customers" and SIC–31 "Revenue - Barter Transactions Involving Advertising Services". IFRS 15 is mandatory for all IFRS users and applies to nearly all types of contracts with customers; the main exceptions are leases, financial instruments and insurance contracts.

ADLER will apply the simplified transition option, i.e. the cumulative effect of contracts that were not completed as at the beginning of the period will be recognised in equity.

The analyses of existing revenue streams conducted to date leading up to the introduction of IFRS 15 show that the standard will apply to the following:

Customer loyalty card programme: Customers are given the option to purchase merchandise at a later time at discounted price. Revenue is deferred by means of liabilities from the customer loyalty card programme. Under IFRS 15, the time at which revenue is recognised – either when the customer loyalty points are acquired or the claim expires – will not change.

Customer's right of return: The right of return is recognised as liabilities for returns and deducted from revenue in financial year 2017. IFRS 15 did not give rise to any other effects.

Further analyses will be conducted in financial year 2018 in order to identify and quantify any other areas of application such as vouchers for third parties. The processes and systems will be adjusted on the basis of those results in order to ensure that the presentation in the financial statements is in compliance with IFRS 15. It is expected that the amendments to IFRS 15 will lead to a decrease of approximately €400 thousand in both revenue and cost of materials and an increase in the same amount for liabilities for refunds and inventories.

IFRS 9 Financial Instruments

On 24 July 2014, the IASB published the final version of IFRS 9 "Financial Instruments". This version added guidance on the impairment of Financial Instruments and guidance on a new fair value through other comprehensive income (FVTOCI) measurement category.

Under the standard, financial instruments are impaired on the basis of the expected loss model. As at the first-time application, the 12-month expected credit losses are generally recognised. All appropriate and reliable information available as at the reporting date and relevant for estimating the expected credit losses must be taken into account. If the credit risk deteriorates significantly, a loss allowance for full lifetime expected credit losses must be recognised from this point forward.

This version also introduces a third measurement category of fair value through other comprehensive income for certain debt instruments on the assets side of the balance sheet. To be classified as such, the instruments must (1) fulfil the cash flow criterion and (2) the business model must allow for both the holding and selling of the instruments.

The amendments to IFRS 9 "Financial Instruments" cover the changes in the classification requirements for financial assets. Under certain circumstances, financial assets with negative compensation may be measured at amortised cost or at fair value through other comprehensive income instead of at fair value through profit or loss.

ADLER analysed the changes arising from the first-time application of IFRS 9 on the accounting of financial instruments. The changes relate primarily to receivables from credit card institutions and lease receivables, which will need to be written down in individual cases. The analysis of the receivables did not give rise to any material 12-month expected credit losses. In light of the short terms and credit quality of the financial assets, the standard is not expected to have any further effects on Adler Modemärkte AG's accounting.

IFRS 2 Share-based Payment

The amendments to IFRS 2 clarify the accounting of certain cash-settled share-based payment transactions. The most significant amendment is that the standard now contains guidance relating to the fair value calculation of liabilities resulting from share-based payment transactions. The amendments do not have any effect on Adler Modemärkte AG's accounting.

IFRS 4 Insurance Contracts

The amendments to IFRS 4 in relation to the interaction of IFRS 4 and IFRS 9 "Insurance Contracts" do not have any effect on Adler Modemärkte AG's accounting.

IAS 40 Investment Property

IAS 40 clarifies the transfer of property to "investment property" after a change in use. The deciding factor is not whether a change in use is intended, but if there is evidence of the change in use. This amendment to IAS 40 does not have any effect on Adler Modemärkte AG's accounting.

IFRIC 23 Uncertainty over Income Tax Treatments

IFRIC 23 clarifies the accounting for uncertainties in income taxes and is to be applied to the determination of taxable profit and losses, tax bases, unused tax losses, unused tax credits and tax rates, when there is uncertainty over income tax treatments under IAS 12. To date, there is nothing to indicate that this may have any effect on Adler Modemärkte AG's accounting.

IFRS 16 Leases

The new IFRS 16 replaces the currently applicable IAS 17 "Leases" and IFRIC 4 "Determining whether an Arrangement contains a Lease". The standard applies to all leases of right-of-use assets, lease agreements, subleases and sale and leaseback transactions. This standard may be applied to certain types of intangible assets. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

IFRS 16 "Leases" requires that lessees recognise all leases as lease liabilities in the statement of financial position. Lessees must recognise the right to use an underlying asset by recognising the present value of future lease payments plus directly attributable costs. A distinction will no longer be drawn between operating and finance leases.

These new provisions will materially affect Adler Modemärkte AG's accounting and will apply from financial year 2019 onwards. The amendment will primarily affect the accounting of lease agreements and motor vehicle and IT leases. A portion of the lease agreements are currently already recognised as finance leases. A project team was deployed to prepare the changes to the operating processes and the accounting. Supported accounting software and contract management tools have by and large been implemented. The key agreements were remeasured taking into account IFRS 16.

Recognising all lease agreements will significantly increase assets and liabilities. ADLER expects non-current assets, in particular property, plant and equipment, and liabilities from finance leases to increase between €100–150 million. The increase will primarily be attributable to the leases for the stores. Lease obligations from IT and motor vehicle leases amount to approximately €3,000–5,000 thousand.

Recognising all lease agreements will improve EBITDA by €25,000–35,000 thousand due to the fact that other operating expenses (lease/rent expenses) will be reclassified to depreciation, amortisation and write-downs and net finance costs (interest expense).

This will lead to a significant shift in the financial indicators. For instance, the increase in total assets will significantly impact indicators such as the debt/equity ratio and the equity ratio.

Adler Modemärkte AG has not yet decided on which transition method it will apply. Adler Modemärkte AG will exercise its option to not apply the right-of-use approach to low-value assets and short-term leases (terms of less than one year), nor does it expect to apply the option to separate leasing and non-leasing components in a contract.

IFRIC 22 Foreign Currency Transactions and Advance Consideration

IFRIC 22 "Foreign Currency Transactions and Advance Consideration" does not have any effect on ADLER's accounting.

IAS 28 Investments in Associates and Joint Ventures

The amendments to IAS 28 clarify that entities must apply IFRS 9 to long-term interests in an associate or joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied. The amendments do not have any effect on Adler Modemärkte AG's accounting.

IFRS 17 Insurance Contracts

IFRS 17 establishes uniform principles for the presentation and measurement of insurance contracts and requires insurance liabilities to be measured at the current settlement amount. IFRS 17 replaces IFRS 4 "Insurance Contracts". The amendments do not have any effect on Adler Modemärkte AG's accounting.

These consolidated financial statements are based on the historical cost principle. Available-for-sale financial assets and investment property are accounted for at fair value. The income statement was prepared using the nature of expense method. Items in the consolidated statement of financial position are classified according to their maturities. Assets and liabilities falling due within one year are reported as current. Assets and liabilities are classified as non-current if they remain within the Group for longer than one year. Trade receivables and payables and also inventories are of an exclusively short-term nature and are therefore reported under the current items.

GROUP OF CONSOLIDATED COMPANIES/SHAREHOLDINGS

The consolidated financial statements include Adler Modemärkte AG as well as four German and four foreign subsidiaries. These subsidiaries are listed in the table below.

Name, registered office	Shareholding in %	Currency	Subscribed capital/ limited partnership capital in local currency (in '000)
Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria	100	€	1,500
ADLER MODE S.A., Foetz, Luxembourg	100	€	31
Adler Mode GmbH, Haibach	100	€	25
Adler Mode AG Schweiz, Zug, Switzerland	100	CHF	100
Adler Orange GmbH & Co. KG, Haibach	100	€	4,000
Adler Orange Verwaltung GmbH, Haibach	100	€	1,040
A-Team Fashion GmbH, Munich	100	€	25
GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria	100	€	37

Due to the fact that the Group holds 100 % of shares in the subsidiaries, there are no minority (non-controlling) interests.

ALASKA GmbH & Co. KG, Pullach/Isartal, in which the Group holds no interest, has also been included in the consolidated financial statements as a structured entity in accordance with IFRS 10 on the basis of a rental agreement with Adler Modemärkte AG, Haibach (relating to an administration building).

Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria, acquired GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria, on 3 May 2017, effective end of 30 April 2017.

CONSOLIDATION PRINCIPLES

Subsidiaries are all companies (including structured entities) in which the Group has the power to govern the financial and operating policies and generally holds more than 50 % of the voting rights. Subsidiaries are included in the consolidated financial statements from the date on which control is obtained by the Group (full consolidation). They are no longer consolidated from the date on which control is lost.

The financial statements of the German and foreign subsidiaries included in the consolidated financial statements are prepared using uniform accounting policies in accordance with IFRS 10.

Intra-Group profits and losses, revenue and income and expenses are eliminated, together with receivables and liabilities existing between subsidiaries consolidated. Receivables and liabilities to the same third-party company are offset where the relevant conditions are met. Intercompany profits are eliminated. Deferred tax assets and liabilities are recognised in respect of temporary differences arising from consolidation adjustments in accordance with IAS 12 "Income Taxes".

In addition to Adler Modemärkte AG, the consolidated financial statements include all material German and foreign subsidiaries, including structured entities, over which Adler Modemärkte AG has direct or indirect control. This is the case if Adler Modemärkte AG has direct or indirect power over the potential subsidiary on account of voting rights or other rights, is exposed to positive or negative variable returns from its involvement in the potential subsidiary and can affect these returns. There were no significant restrictions.

CONSOLIDATION OF SUBSIDIARIES

Subsidiaries acquired are accounted for using the acquisition method. The cost of the acquisition is the fair value of the assets given, the equity instruments issued and the liabilities incurred or assumed at the date of the transaction. The acquiree's identifiable assets, liabilities and contingent liabilities in a business combination are measured on initial consolidation at their fair values at the date of the transaction, irrespective of the extent of any non-controlling interests.

Any excess of the cost of acquisition over the Group's share of the net assets measured at fair value is recognised as goodwill; if the cost of the acquisition is lower than the net assets of the subsidiary acquired measured at fair value, the difference is recognised immediately in profit or loss.

COMPANY ACQUISITIONS

The ADLER Group uses the purchase method for the purpose of accounting for business combinations. The consideration paid is equal to the fair value at the date of the acquisition of the assets given, the liabilities assumed and the equity instruments issued. Incidental costs of the acquisition are expensed. The acquiree's identifiable assets, liabilities and contingent liabilities in a business combination are measured on initial consolidation at their fair values at the date of the transaction. The excess of the consideration paid, the amount of all non-controlling interests and the fair value of the share of the acquiree's equity held prior to the acquisition over the fair value of the net assets at the date of acquisition is recognised as goodwill. If the consideration paid is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in profit or loss as income, once the identification and measurement of the net assets and the measurement of the cost of the acquisition have been reassessed.

Adler Modemärkte Gesellschaft m.b.H., Ansfelden, Austria, acquired GBS Grundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria, on 3 May 2017, effective end of 30 April 2017. In accordance with IFRS 3, the purchase was classified as acquisition of assets pursuant to IFRS 3.2 (b), and not as a business combination. For further details and information on the accounting treatment, please see Note "Purchase and disposal of assets".

CURRENCY TRANSLATION

Business transactions in foreign currencies in the separate financial statements of subsidiaries prepared in euros are measured at the rate of exchange at the date of the transaction. Exchange rate gains and losses arising up to the end of the reporting period from the translation of receivables and liabilities are reflected in the financial statements; gains and losses resulting from movements in exchange rates are reported in profit or loss. The annual financial statements of the foreign Group company are translated into the ADLER Group's reporting currency. The functional currency is the local currency. The functional currency and the reporting currency of the parent, and hence of the consolidated financial statements, is the euro.

ADLER translates the assets and liabilities of foreign Group companies for which the euro is not the functional currency using the spot rate at the end of the period. By contrast, expenses, income and results are translated using average exchange rates. Any resulting translation differences are recognised separately in equity.

The exchange rates used in currency translation were as follows:

Currency	Spot rates per €		Average rates per €	
	31 Dec. 2017	31 Dec. 2016	2017	2016
Swiss franc (CHF)	1.1702	1.0739	1.112	1.0902

ACCOUNTING POLICIES

The accounting policies set out below were applied for the purpose of preparing the consolidated financial statements.

The accounting policies are applied in principle on a consistent basis.

NON-CURRENT ASSETS AND DEPRECIATION AND AMORTISATION

Goodwill

Goodwill arising on consolidation represents the excess of the cost of a company acquisition over the Group's interest in the fair value of the identifiable assets, liabilities and contingent liabilities of a subsidiary. In accordance with IFRS 3 "Business Combinations", goodwill is not amortised. Instead, in accordance with IAS 36 "Impairment of Assets", it is tested for impairment annually and whenever there are indications of possible impairment and, where necessary, written down to the recoverable amount. The impairment charge is recognised immediately in profit or loss. Impairment losses recognised in respect of goodwill may not be reversed in subsequent periods. For the purpose of impairment testing, goodwill is allocated to cash-generating units. The allocation is made to those cash-generating units or groups of cash-generating units which are expected to benefit from the synergies of the underlying business combination.

Other intangible assets

Purchased and internally generated intangible assets are recognised at cost. All purchased intangible assets with finite useful lives are amortised on a straight-line basis. Amortisation is based on the following economic useful lives applied consistently across the Group:

- concessions, rights, licences: 3 to 7 years or the shorter contractual term where relevant
- software: 3 to 5 years

Internally generated intangible assets mostly comprise software. Costs associated with the operation or maintenance of software are expensed when incurred. Costs incurred directly in connection with the production of identifiable individual software products over which the Group has control are recognised as an intangible asset if it is regarded as probable that the intangible asset will generate future economic benefits, is technically feasible and if the costs can be reliably determined. The directly attributable costs include personnel costs for the employees involved in development and other costs directly attributable to the development of software. Capitalised development costs for computer software with a finite useful life are amortised on a straight-line basis over the period of its expected use but subject to a maximum of five years.

Intangible assets which are not yet available for use are tested for impairment at least once annually. If impairment in excess of the amortisation charged is identified, the asset is written down to the recoverable amount.

There were no other intangible assets with indefinite useful lives during the period under review.

Property, plant and equipment

Individual items of property, plant and equipment whose cost is less than € 150 are generally expensed directly. To the extent that non-current assets (e.g., mannequins and store fixtures and fittings) acquired during the year under review are material to the ADLER Group's operations and are used for a period exceeding one year, they are recognised and reported under property, plant and equipment regardless of their cost, and in particular regardless of the aforementioned cost threshold, and are depreciated over their economic useful lives. Significant components of an item of property, plant and equipment are recognised and depreciated separately. Subsequent costs are recognised as a component of the cost of the asset only if it is probable that future economic benefits will flow to the Group as a result and if the costs can be reliably determined. All other repair and maintenance expenses are recognised as expenses in the income statement in the financial year in which they are incurred. Depreciation is not charged on land. For all other assets depreciation is charged on a straight-line basis over the following expected useful lives of the assets:

- Buildings: 33 years
- Operating facilities: 3 to 10 years
- Operating and office equipment: 3 to 10 years
- Vehicles: 4 to 6 years
- Leasehold improvements: 10 years

The carrying amounts and useful economic lives are reviewed at a minimum at the end of each reporting period and adjusted where necessary. If the carrying amount of an asset is higher than its estimated recoverable amount, it is immediately written down to the latter. Gains and losses from disposals of items of property, plant and equipment are calculated as the difference between the proceeds of sale and the carrying amount, and are recorded in profit or loss.

INVESTMENT PROPERTY

Investment property comprises land and buildings held in order to generate rental income and/or for the purposes of capital appreciation and that are not used in the ordinary course of business. It is measured at fair value. The fair value was determined by a property expert.

LEASING

Leases are classified as finance leases if substantially all of the risks and rewards of ownership are transferred to the lessee under the terms of the lease. All other leases are classified as operating leases.

Non-current assets that are rented or leased and where the relevant Group company has economic ownership (finance leases) are recognised at the present value of the minimum lease payments or the lower fair value and depreciated over their useful lives in accordance with the requirements of IAS 17 "Leases". If it is not sufficiently certain at the start of the lease that ownership will transfer to the lessee, the asset must be depreciated over the shorter of the term of the lease and the useful life.

The corresponding liability to the lessor is reported in the statement of financial position as a finance lease obligation under liabilities from finance leases. The lease payments are apportioned between the finance charge and the reduction of the lease obligation so as to produce a constant periodic rate of interest on the remaining balance of the liability.

In the event existing finance leases are extended or modified, the additional finance lease liability resulting from the modified lease increases the additional potential value in use of the leased asset to be capitalised.

Lease payments made under the terms of an operating lease are reported as an expense in the income statement on a straight-line basis over the term of the lease.

IMPAIRMENT OF NON-FINANCIAL AND FINANCIAL ASSETS

Assets with indefinite useful lives are not depreciated or amortised; they are tested for impairment annually or whenever there are indications that an asset may be impaired. Assets subject to depreciation or amortisation are reviewed for impairment if relevant events or changes in circumstances indicate that the carrying amount may no longer be recoverable. Intangible assets which are not yet available for use are also tested for impairment annually. Any impairment loss recognised is equal to the excess of the carrying amount over the recoverable amount. The recoverable amount is the higher of the fair value of the asset less selling costs and the value in use. For the purposes of the impairment test, assets are combined at the lowest level for which cash flows can be separately identified (cash-generating units).

If an impairment charge is subsequently reversed, the carrying amount of the asset (of the cash-generating unit) is increased to the newly estimated recoverable amount. For this purpose, the higher carrying amount resulting from the increase may not exceed the amount that would have been determined, net of depreciation or amortisation, if no impairment charge had been recognised in respect of the asset (the cash-generating unit) in prior years. A reversal of an impairment charge is recognised immediately in profit or loss. Impairment charges recognised in respect of goodwill may not be reversed. The assets are derecognised once all rights to payments have expired.

GOVERNMENT GRANTS

Government grants are recorded at their fair value if it is reasonably certain that the grant will be made and that the Group will comply with the conditions necessary for receipt of the grant. Government grants in respect of costs are recorded over the period during which the related costs, for which the grant is intended to compensate, are incurred.

The Group received government grants, that are recorded as income, as compensation for costs arising in connection with partial retirement agreements. As a result of the conditions attached to the government grants, the Group is under an obligation to keep open the positions occupied by partially retired employees and to recruit new employees to fill them.

As an industry partner of the EU's SERAMIS (Sensor Enabled Real-World Awareness for Management Information Systems) project, the Group received EU grant money for the RFID project in the year under review.

BUILDING COST SUBSIDIES

Building cost subsidies are either paid to the lessor by the Group company for the purpose of upgrading the property or granted by the lessor for independent building work for the construction of the store. Building cost subsidies paid are accounted for as other assets and are expensed over the remaining minimum term of the contract. Building cost subsidies received are reported as other liabilities and reversed to income over the minimum term of the contract or pursuant to the contractual arrangements. See Note "Other operating income".

CURRENT INCOME TAXES

Current income taxes for the period under review and for prior periods are measured in the amount expected to be paid to or reimbursed by the tax authorities. They are calculated on the basis of the company-specific tax rates applicable as at the end of the reporting period. Uncertain tax assets and liabilities are recognised as soon as ADLER's management believes their probability of occurrence exceeds 50 %. Uncertain income tax positions are recognised at their most probable amount.

DEFERRED TAXES

In accordance with IAS 12, deferred taxes are recognised for all temporary differences between the tax bases of the assets and liabilities and their carrying amounts in the IFRS consolidated financial statements (liability method). Deferred taxes are measured on the basis of the tax rates and tax laws in force or substantively enacted at the end of the reporting period and which are expected to apply at the date of realisation of the deferred tax asset or settlement of the deferred tax liability. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the temporary difference can be utilised. If it is sufficiently certain that it will be possible to utilise the future tax benefit resulting from loss carryforwards in future periods (five years), a deferred tax asset is recognised.

IAS 12.39 provides that deferred taxes on temporary differences in connection with investments in subsidiaries ("outside basis differences") should be recognised in the consolidated financial statements only when the following criteria are not met:

- the parent company, shareholder or joint venture partner is in a position to control the timing of the reversal of the temporary difference; and
- it is probable that the temporary difference will not reverse in the foreseeable future.

This is not the case for the ADLER Group. The temporary difference generally reverses only when the company is sold. At the present time the ADLER Group is not planning to dispose of any subsidiaries but, on the other hand, it would be in a position to control the timing of any disposal. No deferred taxes are recognised in the consolidated financial statements of the ADLER Group in respect of temporary differences relating to investments in subsidiaries.

Deferred tax assets and liabilities are netted if there is a legally enforceable right to offset current tax assets against current tax liabilities and if the deferred taxes relate to the same tax authority.

INVENTORIES

Merchandise accounted for as inventories is generally carried at the lower of cost and net realisable value. Net realisable value is the amount of the estimated sale proceeds achievable in the normal course of business less the necessary variable costs of sale. The cost of production includes all directly attributable costs and appropriate portions of necessary overheads and depreciation in addition to direct materials and production costs. Cost is determined using the weighted average method.

RECEIVABLES AND OTHER ASSETS

Trade receivables

Trade receivables are recorded initially at fair value and measured in subsequent periods at amortised cost less any impairment losses. An impairment charge is recorded in respect of trade receivables if there are objective indications that the amounts of receivables due are not collectible in full. The amount of the impairment charge is measured as the difference between the carrying amount of the receivable and the present value of the estimated future cash flows from that receivable, determined using the effective interest rate method. The impairment charge is reported in profit or loss. Trade receivables are classified under the loans and receivables category. Once the item is no longer expected to generate cash flows, it is derecognised.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets that have either been allocated to this category or have not been allocated to any of the other measurement categories set out in IAS 39. They are measured at fair value. Unrealised gains and losses resulting from changes in fair value are recorded outside profit or loss in other comprehensive income. When securities within the available-for-sale financial assets category are disposed of or become impaired, the adjustments to fair value accumulated directly in equity are recorded in the income statement as gains or losses from financial assets. For example, ADLER classifies securities with a longer-term investment horizon under this category. Once the item is no longer expected to generate cash flows, it is derecognised.

Other receivables and other assets and loans

Other receivables and other assets and loans are recorded initially at fair value and measured in subsequent periods at amortised cost using the effective interest method – in the case of non-current receivables – less any impairment losses. Appropriate valuation allowances are recognised in respect of any risks existing. At the end of each reporting period the carrying amounts of financial assets not measured at fair value through profit or loss are reviewed for objective indications of impairment (such as significant financial difficulties on the part of the debtor, a high probability of insolvency proceedings against the debtor, a significant change in the technological, economic or legal environment, or in the market environment of the issuer or a permanent decline in the fair value of the financial asset to below amortised cost). Any impairment charge, based on a lower fair value in comparison with the carrying amount, is reported in the income statement. If it becomes clear at subsequent measurement dates that the fair value has risen objectively as a result of events that occurred after the date when the impairment charge was recognised, the impairment charge is reversed through profit or loss in the relevant amount. The fair value determined for the purpose of reviewing possible impairment losses in respect of loans and receivables measured at amortised cost is equal to the present value of the estimated future cash flows, discounted at the original effective rate of interest. Once the item is no longer expected to generate cash flows, it is derecognised.

Other receivables and other assets and loans are allocated to the "loans and receivables" category.

Financial assets are generally recorded at the trade date.

Assets held for sale

Assets classified as held for sale are measured that the lower of the carrying amount and the fair value less costs of disposal. These assets are not depreciated or amortised.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash, demand deposits and other short-term highly liquid financial assets with an original term of no more than three months. Overdrafts utilised are reported as liabilities to banks under current financial liabilities.

Financial assets are carried at fair value at the time of acquisition.

EQUITY

Equity consists of subscribed capital, capital reserves, accumulated other comprehensive income and negative retained earnings (previously: net accumulated losses). Subscribed capital represents the nominal capital of the parent, reduced, if necessary, by the share of own shares repurchased. The nominal value of the shares amounts to €18,510,000. Capital reserves comprise all capital amounts contributed to the Company from external sources that are not subscribed capital.

Accumulated other comprehensive income includes minor exchange rate effects arising from the consolidation of subsidiaries with functional currencies other than the Group's reporting currency, as well as changes in the value of available-for-sale financial assets and actuarial gains and losses from pension obligations as well as the associated deferred taxes.

PROVISIONS

Provisions are recognised when the Group has a present legal or constructive obligation arising as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and the amount of the provision can be reliably estimated. Where there are a number of similar obligations, the likelihood that an outflow of resources will be required is determined by considering that class of obligations as a whole. Provisions are stated at the expected settlement amount after taking into account all identifiable associated risks and are not offset against rights of recourse.

Where the effect of the time value of money is material, non-current provisions are carried at the settlement amount discounted to the end of the reporting period. The discount rate used for this purpose is a pre-tax rate of interest reflecting the current market assessment of the economic situation and the risks specific to the obligation.

EMPLOYEE BENEFITS

Pension obligations

The ADLER Group has a number of different pension plans. They include both defined benefit and defined contribution plans. Defined contribution plans are post-employment plans under which an enterprise pays fixed contributions into a separate entity (such as a fund or insurance arrangement) and has no legal or constructive obligation to pay further contributions, even if the fund or the entitlements from the insurance agreement entered into do not have sufficient assets to pay all employee benefits relating to employee service in the current reporting period and prior periods. A defined benefit plan is a plan other than a defined contribution plan.

The agreements underlying the defined benefit plans provide for different benefits within the Group depending on the particular subsidiary. The latter mainly comprise

- pension entitlements once the relevant pensionable age is reached,
- one-off payments on cessation of employment.

The provision relating to defined benefit plans carried in the consolidated statement of financial position is calculated as the present value of the pension obligation at the end of the reporting period less the fair value of any plan assets available and any past service cost not yet recognised.

The actuarial calculation of the pension provisions for the Company's old-age pension benefits is based on the projected unit credit method prescribed by IAS 19 "Employee Benefits". An actuarial valuation is carried out by independent actuarial experts for this purpose at the end of each reporting period. The projected unit credit method takes account of the known pensions and vested benefits at the end of the reporting period and includes increases in salaries and pensions expected in the future. The valuations are based on the legal, economic and tax environment of the individual country, as well as that country's specific demographic trends. The obligations, which exist solely in the European Economic Area, were measured using an actuarial rate of interest of 1.6 % (previous year: 1.6 %), projected annual wage and salary increases of 2.5 % (previous year: 2.5 %) and projected annual pension increases of 1.75 % (previous year: 2.0 %). Employee turnover is determined for each specific company and taken into account on the basis of age and length of service. The actuarial valuations are mostly based on specific mortality tables for each country. The provision is made up of the present value of the expected benefits less the fair value of the plan assets plus or minus any actuarial gains and losses. The expected return on the plan assets in accordance with the amendment to IAS 19 was adjusted in the previous year in line with the actuarial rate of interest.

The accumulated actuarial gains and losses were attributable to the differences arising over the years between the projected pension obligations and plan assets and the actual amounts at the year-end. Actuarial gains and losses are recognised directly in other comprehensive income. Furthermore, the return on plan assets is recognised in the amount of the discount rate.

In accordance with IAS 19.173, disclosures pursuant to IAS 19.145 on the financing strategy and risks of the pension plans and a sensitivity analysis required in the case of changes in material valuation assumptions are presented under Note 19.

The interest component of the addition to provisions (interest cost for pension obligations and expected income from plan assets) is reported as interest expense within net finance costs.

Payments out of a defined contribution benefits plan are included in profit or loss and reported within personnel expenses.

Obligations for severance payments

Employees who began their service in Austria on or after 1 January 2003 participate in a defined contribution benefits plan. Obligations arising from severance payments for employees whose service began prior to 1 January 2003 are covered by defined benefit plans. When service is ended by the company or pensionable age is reached, or in the case of invalidity or death, participating employees receive a severance payment which amounts to a multiple of their basic monthly salary – depending on their length of service – subject to a maximum of twelve months' salary. A maximum of three months' salary is paid immediately on cessation of service, while the payment of any further amounts is distributed over a period of several months. In the event of death, the heirs of participating employees are entitled to 50 % of the severance payment.

Termination benefits

Termination benefits are paid when an employee is dismissed prior to the normal retirement date or when an employee leaves employment voluntarily in return for a termination payment. The Group recognises termination benefits immediately when it is demonstrably and irrevocably committed to terminating the employment of current employees on the basis of a detailed formal plan which cannot be withdrawn, or when it is demonstrably required to pay termination benefits on the voluntary termination of employment by employees. Payments falling due more than twelve months after the end of the reporting period are discounted to their present value. The entitlements to termination benefits are reported under provisions for personnel expenses. This item also includes portions of the entitlements arising from the German provisions relating to partial retirement arrangements.

LIABILITIES

Financial liabilities

Financial liabilities are recorded at fair value on initial recognition and measured at amortised cost in subsequent periods. Differences between the historical cost and the repayment amount of non-current liabilities are reflected in the financial statements using the effective interest method. Financial liabilities measured at amortised cost are recognised initially at fair value, taking into account transaction costs.

Loan liabilities are classified as current if repayment is due within the following twelve months.

Liabilities from the customer loyalty card programme

Beginning in this financial year, discount entitlements not yet utilised by customers will no longer be reported as current financial liabilities but rather separately as liabilities from the customer loyalty card programme. The effects of the retrospective changes are described in Note 22. Customers are awarded discount entitlements whenever they make a purchase using the ADLER customer loyalty card. Within a specifically defined period of less than one year, customers can offset these discount entitlements against a subsequent purchase or have the amount paid out in cash. The amount included in liabilities represents customers' discount entitlements not yet utilised at the end of the reporting period.

Liabilities from finance leases

Lease liabilities are recognised if economic ownership of the leased or rented leased assets is attributable to companies of the ADLER Group and the assets are capitalised under property, plant and equipment (finance leases). On initial recognition, the lease obligations are recorded at the fair value of the leased asset or, if lower, the present value of the lease payments.

For this purpose, the finance charge is apportioned over the term of the lease in such a way that a constant periodic rate of interest over time is produced on the outstanding balance of the finance lease liability.

Trade payables and other liabilities

On initial recognition, trade payables and other liabilities are carried at fair value; subsequently, they are carried at amortised cost. Trade payables and other current liabilities are reported under other liabilities.

CONTINGENT LIABILITIES

Contingent liabilities are possible or present obligations resulting from past events but for which an outflow of resources is estimated to be not probable. Under IAS 37, obligations of this nature are not recorded in the statement of financial position but are disclosed in the notes to the financial statements.

RECOGNITION OF INCOME AND EXPENSES

Revenue represents the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of business. Revenue is reported net of VAT and after deducting rebates and discounts. Customers' entitlements to refunds relating to goods delivered are recorded in the income statement once the relevant invoices have been examined.

Where customers making purchases with the ADLER customer loyalty card acquire an entitlement to a particular discount, the discount is recorded as a reduction in revenue. The liability is reported under liabilities from the customer loyalty card programme. The liability is reversed when the discount is utilised.

Revenue and other operating income are generally recognised only when the services have been performed or the goods or products have been delivered and the risks of ownership have been transferred to the customer. In-store retail sales are settled in cash or using an EC or credit card. Purchases in the online shop are settled via invoice, credit card or online payment services. The card company's charges are recorded in other operating expenses. The Group's business policy is that the end user acquires its products with a statutory right of return.

Expenses are recognised when the goods or services are utilised or when the expense is incurred. This also applies to the recognition of advertising expenses. The latter are recorded in accordance with the provisions of IAS 38 when the service – in this case the provision of advertising services – has been performed for the ADLER Group and not at the later date when the ADLER Group is conducting the relevant advertising campaigns.

Rental income and expenses are recorded as revenue or expenditure on an accruals basis in the period to which they relate.

NET FINANCE COSTS

Interest income and interest expenses are recorded on an accruals basis in the period to which they relate using the effective interest method, based on the outstanding balance of the loan and the applicable interest rate. The applicable interest rate is the rate of interest that discounts the estimated future cash flows over the term of the financial asset to its net carrying amount.

In the case of a finance lease agreement, payments received are apportioned between the finance charge and the reduction of the outstanding liability using mathematical methods.

Interest income from the expected return on plan assets is also recorded in net finance costs, as are interest expenses from the compounding of interest on pension obligations. The interest rates which serve as a basis for this are discussed in the note relating to the accounting for pension obligations.

Borrowing costs are reported in the income statement in the period in which they are incurred, except for borrowing costs required to be capitalised in respect of qualifying assets.

OTHER COMPREHENSIVE INCOME

The items of other comprehensive income were adjusted accordingly pursuant to the amendments to IAS 1 "Presentation of Financial Statements". Depending on whether they are to be recorded in the income statement going forward, the items of other comprehensive income are presented separately.

SEGMENT REPORTING

Under the provisions of IFRS 8, operating segments are identified on the basis of the internal organisation and reporting structure. An operating segment is defined as a component of an entity which generates revenues and incurs expenses from its business activities, whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available. The chief operating decision maker is the Executive Board of Adler Modemärkte AG.

Segments are structured for the purpose of segment reporting according to the entity's principal activities. As in the previous year, there was only one reportable segment in financial year 2017: "Stores (Modemärkte)".

EARNINGS PER SHARE

Earnings per share is determined in accordance with IAS 33 "Earnings Per Share" by dividing consolidated profit or loss by the weighted average number of shares outstanding during the financial year. Earnings per share is diluted if the share capital consists of not only ordinary and preference shares, but also equity instruments which may lead to a future increase in the number of shares. However, there is no dilutive effect in these consolidated financial statements.

LITIGATION AND CLAIMS FOR DAMAGES

The companies in the ADLER Group are involved in a range of legal and administrative proceedings in the course of their general business operations or similar proceedings could be initiated or claims asserted in the future. Although the outcome of individual proceedings cannot be predicted with certainty given the imponderable factors involved in legal disputes, it is currently estimated that they will have no material adverse effect on the results of operations of the Group over and above the risks reflected in the financial statements in the form of liabilities or provisions.

USE OF ESTIMATES AND ASSUMPTIONS

The preparation of the consolidated financial statements has involved the making of assumptions and use of estimates that have affected the reporting and the amount of the assets, liabilities, income and expenses recognised and of the contingent liabilities. These estimates and assumptions relate principally to the establishment of uniform economic useful lives used across the Group, the assessment of whether impairment charges are required for inventories, the measurement of provisions, pensions and risks specific to individual locations, together with the recoverability of future tax benefits, in particular those arising from loss carryforwards. The actual amounts may differ in particular cases from the estimates and assumptions made. Revised amounts are reflected at the date when improved knowledge becomes available.

Estimates are based on historical amounts and other assumptions considered to be accurate in the particular circumstances. The actual amounts may differ from the estimates made. The estimates and assumptions are reviewed on an ongoing basis. The "true and fair view" principle is also applied to the use of estimates.

Useful lives of non-current assets

The determination and standardisation of economic useful lives applied across the Group is based on historical data relating to the actual expected useful lives of non-current assets. It is assumed that the assets are subjected to normal use.

Valuation allowances on inventories

Valuation allowances on inventories are determined in the light of conditions in the sales market and are based to some extent on historical amounts.

Income taxes

The Group has a liability to pay income taxes in various countries in accordance with different particular bases of assessment. The global provision for taxes is recognised on the basis of the profit determined in accordance with local tax regulations and the applicable local rates of tax.

The amount of the tax provisions and liabilities is based on estimates of whether and in what amount income taxes will become payable. Risks arising from the possibility of a different treatment for tax purposes are reflected, where necessary, in provisions for the appropriate amount.

In addition, it is necessary to make estimates in order to assess the recoverability of deferred tax assets. The key factor in assessing the recoverability of deferred tax assets is the estimation of the likelihood that future profits for tax purposes (taxable income) will be available. Uncertainties relating to the interpretation of complex tax regulations and the amount and timing of future taxable income must also be taken into account. Especially in view of the international structure of the Group, differences between actual events and assumptions, or future changes in those assumptions, may result in revised amounts for the tax charge or benefit in future periods.

The companies of the ADLER Group are subject to income tax in several countries. When assessing income tax assets and liabilities, interpretations of tax regulations in particular can be subject to uncertainty. Differences in opinions on the part of the respective financial authorities with regard to the correct interpretation of tax regulations (for example, due to a change in case law) are taken into consideration when accounting for uncertain tax assets and/or liabilities for the corresponding financial year.

Provisions

Assumptions about the likelihood of an outflow of resources occurring have to be made for the purpose of determining whether to recognise provisions. These assumptions represent the best possible assessment of the circumstances underlying the particular provision but are subject to an element of uncertainty given the inevitable use of assumptions. Assumptions also have to be made about the amount of any outflow of resources for the purpose of measuring the provisions. A change in the assumptions can therefore result in a revised amount for the provision. Accordingly, the use of assumptions can also give rise here to an element of uncertainty.

The determination of the present value of pension obligations depends primarily on the choice of the discount rate of interest and the other actuarial assumptions which must be formulated afresh at the end of each financial year. For this purpose, the underlying discount rate is the rate of interest on corporate bonds with high credit ratings, denominated in the currency in which the payments are made and with the same maturity structure as the pension obligations. Changes in these interest rates may result in material revisions to the amount of the pension obligations.

Impairment

Goodwill is tested annually for impairment in accordance with IAS 36 "Impairment of Assets" and IAS 38 "Intangible Assets". If events or changes in circumstances give rise to indications of possible impairment, impairment testing must also be carried out more frequently. The amortisation of goodwill is not permitted. For the purpose of testing goodwill for impairment, the carrying amount of the individual cash-generating unit to which the goodwill has been allocated is compared with the respective recoverable amount, i.e. the higher of the net selling price and the value in use. In those cases where the carrying amount of the cash-generating unit is higher than its recoverable amount, the difference represents an impairment loss. Impairment losses calculated in this manner are deducted initially from the carrying amount of the goodwill allocated to the strategic business unit in question. Any remaining amount is allocated to the other assets in the respective strategic business unit pro rata on the basis of their carrying amounts, to the extent that IAS 36 applies. The calculation of the recoverable amount is based on the future cash flows expected to be derived from the continuing use of the cash-generating unit. The cash flow projections were based on the Company's current business plans. The cost of capital is calculated as the weighted average of the cost of equity and the cost of debt, taking into account the proportions of total capital represented by equity and debt respectively. The cost of equity represents the expected return from the cash-generating unit and is derived from a suitable peer group. The cost of debt is based on the average cost of debt derived from bonds with an average remaining maturity of 20 years.

For the purpose of reflecting risks specific to individual locations in the financial statements (mainly the estimation of anticipated losses from operating lease agreements and the impairment of finance lease agreements relating to store rents), an adjusted EBIT for a particular planning horizon is estimated for locations with ongoing losses. This is then compared with objectively determined rents in order to calculate the extent of any failure to cover future rents and/or to adjust the carrying amounts to a recoverable amount determined under the assumption either that the location will continue in its present use or that it will be used for a different purpose.

The fair value of land and buildings being tested for impairment is normally based on a valuation by an independent expert. Expert opinions on the market values of property, plant and equipment are subject to an element of uncertainty as a result of the unavoidable use of assumptions.

All identifiable risks at the date of preparation of the consolidated financial statements were included in the context of the underlying estimates and assumptions.

III. NOTES TO THE INCOME STATEMENT

1. REVENUE

Revenue (net) is generated almost entirely from sales of goods and is distributed geographically as follows:

€'000	2017	2016
Germany	435,436	453,663
Austria	68,938	71,209
Luxembourg	18,239	16,699
Switzerland	3,201	2,982
	525,814	**544,553**

2. OTHER OPERATING INCOME

€'000	2017	2016
Income from the sale of real estate	11,899	0
Income from the reversal of other liabilities and provisions	1,931	1,155
Passthrough expenses/reimbursement of expenses	1,540	2,465
Rent	1,265	2,059
Personnel-related government grants	336	329
Income from damages claims	282	806
Income from the hanger recycling project	250	359
Royalties	231	256
Income from the derecognition of expired liabilities	217	503
Credits from suppliers	122	76
Income from recoveries on receivables written off	118	210
Commissions	93	87
Restaurant	58	65
Other	470	364
	18,812	**8,734**

Income from the sale of real estate includes the sales proceeds from the properties and buildings in Klagenfurt, St. Pölten, Ansfelden and Vösendorf as well as the share of the Salzburg finance lease recognised in profit or loss. Income from the reversal of other liabilities and provisions related to provisions for personnel expenses, primarily bonuses and rent and incidental rental expenses. Passthrough expenses and reimbursements primarily include income from construction subsidies. The rental income was generated from subletting to store concessionaires. Rental income from investment property amounted to € 36 thousand (previous year: € 36 thousand). The decrease in income from damages claims is attributable primarily to insurance claims for one insurance event related to water damage and one insurance event related to fire damage in the previous year. Income from the derecognition of expired liabilities includes primarily the derecognition of expired discounts.

3. COST OF MATERIALS

The cost of materials amounting to €244,060 thousand (previous year: €256,467 thousand) consists entirely of purchased merchandise. The decline in cost of materials is attributable primarily to volume but also an improved inventory age structure and thus fewer write-downs on existing merchandise.

4. PERSONNEL EXPENSES

€'000	2017	2016
Wages and salaries	80,195	84,658
Other social security contributions	8,568	9,229
Employer's contribution towards the statutory pension scheme	7,371	7,922
Expenditures for old-age pensions	417	490
Expenditures for partial retirement/death benefits/anniversaries	298	34
	96,849	**102,333**

Personnel expenses decreased despite the wage and salary increases for 2017 under the collective bargaining agreement. This was due primarily to the decline in the number of employees, the waiver of holiday pay and bonuses as well as lower provisions for severance payments at the stores.

The average number of people employed by the Group during the reporting period was:

Employees	2017	2016
Managers	216	223
Full-time employees	674	750
Part-time employees	2,652	2,773
Trainees	282	336
	3,824	**4,082**

5. OTHER OPERATING EXPENSES

€'000	2017	2016
Operating lease payments and building expenditures	69,454	70,024
Advertising expenses	46,034	45,410
Freight and transport costs	18,131	18,098
Technical equipment	13,172	13,382
Consultancy fees	4,881	3,909
External cleaning fees	4,654	4,576
Administrative expenses	4,226	4,384
Consumables	3,107	3,329
Office expenses	1,593	1,606
Incidental costs of monetary transactions	1,242	1,227
Low-value assets	581	659
Losses from disposals of assets	567	268
Other	4,069	4,315
	171,712	**171,187**

The decrease in operating lease payments and building expenditures was attributable primarily to improved lease terms and conditions.

The operating lease agreements relate primarily to leased buildings for stores. The lease agreements generally include renewal clauses as well as price adjustment clauses based on changes in the rental price index. In addition, variable components of rent are contingent depending on the sales achieved in the individual stores. In financial year 2017, the contingent rental payments under operating lease agreements amounted to €84 thousand (previous year: €35 thousand). The increase in contingent rental payments from operating lease agreements is due mainly to lease amendments.

The increase in advertising expenses is attributable to an increase in mailshots and the revamped marketing campaign.

The increase in freight and transport costs was due mainly to an increase in freight costs attributable to the online shop.

The decrease in expenses for technical facilities was attributable primarily to modernisation measures conducted at seven stores in 2016; this was offset by income from construction subsidies amounting to €610 thousand.

The increase in consulting fees is due mainly to the advice the Company received in relation to implementing its strategic realignment.

The disposal of a temporary building below its carrying amount was reported under losses from disposals of assets.

6. DEPRECIATION, AMORTISATION AND IMPAIRMENT

The amounts of depreciation and amortisation are presented in the consolidated statement of changes in non-current assets. During the financial year, impairment charges of €154 thousand were recognised in respect of non-current assets.

7. NET FINANCE COSTS

Net finance costs comprise the items below analysed by the items giving rise to them as follows:

€'000	2017	2016
Interest income		
Receivables from banks	0	5
Other	318	14
	318	**19**
Interest expense		
Finance leases	−4,750	−4,601
Interest effect on pension obligations and provisions for anniversaries	−105	−136
Liabilities to banks	−35	−10
Other	−281	−201
	−5,173	**−4,948**
Net finance costs	**−4,855**	**−4,92**

Interest income from banks relates to current account balances. The related items were allocated to the loans and receivables category. Interest income decreased sharply due to the negative interest rate policies of the banks. Other includes interest income from prior-year tax credits.

All interest income and interest expenses arising from financial assets and financial liabilities were calculated using the effective interest method. During the financial year they included negative interest charged by banks for deposits.

The interest included in net finance costs represents the total amount of interest income and expenses calculated using the effective interest method.

8. INCOME TAXES

The income tax expense was made up as follows:

€'000	2017	2016
Actual tax expense (–)/income (+)	−4,192	−836
Deferred tax expense (–)/income (+)	−2,647	−466
	−6,838	**−1,301**

Income taxes paid and payable in the individual countries together with deferred tax expenses and benefits are reported under income taxes.

The income tax rate of 29.571 % (previous year: 29.512 %) applied for the German company is made up of corporation tax amounting to 15.825 % (previous year: 15.825 %) (including the solidarity surcharge of 5.500 %) and the trade tax rate of 13.746 % (previous year: 13.687 %). Foreign income taxes are calculated on the basis of the laws and regulations in force in the particular countries. The overall income tax rate applicable for the ADLER Group amounts to 29.570 % (previous year: 29.510 %).

The calculation of deferred taxes is based on the tax rates expected to apply in the individual countries when the deferred tax asset is realised or the liability is settled; these generally reflect the tax laws in force or enacted at the end of the reporting period.

The differences between the income tax expense actually recorded and the expected income tax expense are shown in the following reconciliation. The expected income tax expense is calculated from the profit or loss before taxes multiplied by the applicable income tax rate.

€'000	2017	2016
Consolidated net profit before income taxes	10,696	1,711
Applicable income tax rate	29.57 %	29.51 %
Expected income tax expense	3,162	505
Effects of different foreign tax rates	−468	5
Effects of different domestic tax rates	−4	−4
Tax effects		
Taxation real estate transaction Austria	1,401	0
Addition/reduction of trade tax	895	881
Non-recognition of current tax losses	680	457
Impairment deferred tax assets for tax losses	1,118	
Non-deductible expenses for tax purposes	89	83
Initial recognition of deferred tax assets	−105	−452
Prior-period tax income (–)/expense (+)	81	−111
Effect of Group tax rate adjustment on deferred taxes	−3	−85
Tax-exempt income	−59	−65
Recognition of previously unused tax loss carryforwards	0	−4
Other deviations	49	91
Total tax effects	4,146	783
Actual tax expense (+)/income (–)	**6,838**	**1,301**
Actual tax rate	63.94 %	76.04 %

Available-for-sale financial assets are measured at fair value in accordance with both local tax law and IFRSs; accordingly, no temporary differences arise in other comprehensive income.

IV. NOTES TO THE STATEMENT OF FINANCIAL POSITION

9. INTANGIBLE ASSETS

Intangible assets comprise purchased software, rights and licences, and goodwill. The internally generated intangible assets represent capitalised development costs for logistics software. In the interest of improving the presentation, the intangible assets that in the previous year were reported separately under the column "licenses, finance leases" are now presented under the column "software, rights, licences". The prior-year item was adjusted accordingly.

The development of intangible assets in financial year 2017 was as follows:

€'000	Software, rights, licences	Goodwill	Internally-generated assets	Construction in progress	Total
Cost as at 1 Jan. 2017	37,218	900	2,258	75	40,451
Additions	1,555	0	0	39	1,594
Disposals	−3	0	0	0	−3
Reclassifications	75	0	0	−75	0
As at 31 Dec. 2017	**38,845**	**900**	**2,258**	**39**	**42,042**
Depreciation, amortisation and write downs as at 1 Jan. 2017	−31,269	0	−892	0	−32,161
Additions	−2,489	0	0	0	−2,489
Disposals	3	0	0	0	3
As at 31 Dec. 2017	**−33,755**	**0**	**−892**	**0**	**−34,647**
Impairments as at 1 Jan. 2017	−448	0	−1,367	0	−1,815
As at 31 Dec. 2017	**−448**	**0**	**−1,367**	**0**	**−1,815**
Net carrying amount as at 1 Jan. 2017	5,501	900	0	75	6,476
Net carrying amount as at 31 Dec. 2017	**4,641**	**900**	**0**	**39**	**5,581**

Additions to software, rights and licences relate primarily to software for the online shop, expanded RFID functions, and the document management system. Software, rights and licences include the line item licences, finance leases – which relates to trademark rights.

The development of intangible assets in financial year 2016 was as follows:

€'000 (adjusted)	Software, rights, licences	Goodwill	Internally-generated assets	Construction in progress	Total
Cost as at 1 Jan. 2016	35,131	900	2,258	0	38,289
Additions	2,082	0	0	75	2,157
Disposals	−5	0	0	0	−5
Reclassifications	10	0	0	0	10
As at 31 Dec. 2016	**37,218**	**900**	**2,258**	**75**	**40,451**
Depreciation, amortisation and write downs as at 1 Jan. 2016	−28,862	0	−892	0	−29,754
Additions	−2,412	0	0	0	−2,412
Disposals	5	0	0	0	5
As at 31 Dec. 2016	**−31,269**	**0**	**−892**	**0**	**−32,161**
Impairments as at 1 Jan. 2016	−448	0	−1,367	0	−1,815
As at 31 Dec. 2016	**−448**	**0**	**−1,367**	**0**	**−1,815**
Net carrying amount as at 1 Jan. 2016	5,821	900	0	0	6,721
Net carrying amount as at 31 Dec. 2016	**5,501**	**900**	**0**	**75**	**6,476**

Goodwill and intangible assets with indefinite useful lives are tested for impairment at least once annually. Assets in use and other intangible assets with finite useful lives are tested for impairment only if there are specific indications that the assets may be impaired. The higher of the value in use and the fair value less costs of disposal of the relevant cash-generating unit is generally used to test goodwill and intangible assets with indefinite useful lives for impairment. The value in use is measured on the basis of the management's current planning. This planning is based on expectations with regard to future macroeconomic developments and the resulting assumptions about the textile retail markets, market shares and profitability of the products. This takes into consideration appropriate assumptions regarding macroeconomic trends (currency, interest rate and commodity price developments) as well as historical developments. Please refer to the report on expected developments in the management report for information regarding assumptions in the detailed planning period. Plausible assumptions regarding future developments are made for subsequent years. The planning assumptions are adjusted in each case to the information currently available.

Goodwill at the level of the cash-generating unit (CGU) is regularly tested for impairment at the end of the year, or when there are indications of impairment, by determining the value in use using the discounted cash flow calculation based on the WACC after taxes, derived from the multi-year plan. The cost of capital is calculated on the basis of the interest rate for risk-free assets, the market risk premium and ADLER's interest rate on debt. Furthermore, specific peer group information for beta factors and debt/equity ratios are also taken into account.

For reasons of materiality, the Company did not disclose the information required by IAS 36.134.

During the year under review, the impairment tests of goodwill did not give rise to any impairments.

10. PROPERTY, PLANT AND EQUIPMENT

The development of property, plant and equipment in financial year 2017 was as follows:

€'000	Land and equivalent rights	Buildings (incl. buildings on land owned by third parties)	Finance lease buildings	Other operating and office equipment	Construction in progress	Total
Cost as at 1 Jan. 2017	795	74,141	153,179	65,523	30	293,668
Additions	474	1,924	9,651	2,060	99	14,208
Disposals	−579	−3,468	−17,499	−3,117	0	−24,663
Reclassifications	0	31	0	0	−31	0
Foreign exchange differences	0	−70	0	−40	0	−110
As at 31 Dec. 2017	**690**	**72,558**	**145,331**	**64,426**	**98**	**283,103**
Depreciation, amortisation and write downs as at 1 Jan. 2017	0	−49,664	−112,281	−52,283	0	−214,228
Additions	0	−3,380	−6,325	−4,106	0	−13,811
Disposals	0	1,428	17,499	2,406	0	21,334
Foreign exchange differences	0	17	0	17	0	34
As at 31 Dec. 2017	**0**	**−51,599**	**−101,107**	**−53,966**	**0**	**−206,671**
Impairments as at 1 Jan. 2017	−297	−813	0	−194	0	−1,303
Additions		−131		−23		−154
As at 31 Dec. 2017	**−297**	**−944**	**0**	**−217**	**0**	**−1,457**
Net carrying amount as at 1 Jan. 2017	498	23,664	40,898	13,046	30	78,136
Net carrying amount as at 31 Dec. 2017	**393**	**20,015**	**44,224**	**10,244**	**98**	**74,975**

The development of property, plant and equipment in financial year 2016 was as follows:

€'000	Land and equivalent rights	Buildings (incl. buildings on land owned by third parties)	Finance lease buildings	Other operating and office equipment	Construction in progress	Total
Cost as at 1 Jan. 2016	795	72,207	150,789	66,964	115	290,870
Additions	0	5,149	2,391	3,583	19	11,144
Disposals	0	−3,226	0	−5,125	0	−8,351
Reclassifications	0	0	0	94	−104	−10
Foreign exchange differences	0	11	0	6	0	17
As at 31 Dec. 2016	**795**	**74,141**	**153,179**	**65,523**	**30**	**293,668**
Depreciation, amortisation and write downs as at 1 Jan. 2016	0	−49,335	−105,840	−52,823	0	−207,998
Additions	0	−3,474	−6,441	−4,334	0	−14,249
Disposals	0	3,147	0	4,876	0	8,023
Foreign exchange differences	0	−2	0	−2	0	−4
As at 31 Dec. 2016	**0**	**−49,664**	**−112,281**	**−52,283**	**0**	**−214,228**
Impairments as at 1 Jan. 2016	−297	−813	0	−194	0	−1,303
As at 31 Dec. 2016	**−297**	**−813**	**0**	**−194**	**0**	**−1,303**
Net carrying amount as at 1 Jan. 2016	498	22,058	44,947	13,948	115	81,566
Net carrying amount as at 31 Dec. 2016	**498**	**23,664**	**40,898**	**13,046**	**30**	**78,136**

Property, plant and equipment include leased land and buildings attributable to the Group as economic owner as a result of the structure of the underlying lease agreements. In order to ensure that these lease agreements, capitalised as finance leases, are measured at the appropriate amount, they were reviewed with the aim of identifying any impairment write-downs that might be necessary due to a lack of earnings prospects. There are indications of impairment if internal reporting provides substantive evidence that a store is less profitable or will be less profitable than expected. The audit of individual stores with finance leases found no substantive evidence that a store is less profitable or will be less profitable than expected. Therefore, as in the previous year, no impairment losses were recognised in respect of assets from finance leases in financial year 2017.

The terms of the finance leases generally amount to between five and 20 years with renewal options. The renewal options must be exercised by the Company, depending on the particular lease agreement, at a specified time prior to expiry of the lease agreement. This period ranges between three and twelve months prior to expiry of the lease agreement. The renewal terms amount to between one year and five years.

The decline in finance leases can be explained by straight-line amortisation and the fact that the agreements were increasingly classified as operating leases.

Expenses for operating leases amounted to €66,459 thousand during the financial year (previous year: €67,454 thousand). The operating lease agreements contain similar renewal options.

The remaining items of property, plant and equipment consist mainly of the fixtures and fittings of the stores.

Individual assets whose cost is less than €150 are not recognised as described above. The total costs of the relevant assets in the financial year amounted to €581 thousand (previous year: €659 thousand).

In financial year 2017, impairment losses of €154 thousand were recognised in respect of assets of stores slated to be closed.

Property, plant and equipment amounting to €2,999 thousand (previous year: €3,130 thousand) serves as collateral for financial liabilities.

11. INVESTMENT PROPERTY

The investment property reported in the financial statements consists of land and a building held by the structured entity ALASKA GmbH & Co. KG included in the consolidation. The building is not used in its entirety by the ADLER Group; some portions are sublet. The sub-let portion is classified as an investment property and reported as such. The investment property is carried at fair value, which was determined by an expert valuer on the basis of market data. In financial year 2017, €36 thousand in rental income was generated (previous year: €36 thousand).

€'000	2017	2016
Carrying amount as at 1 Jan.	**413**	**413**
Reclassification to property, plant and equipment	0	0
As at 31 Dec.	**413**	**413**

As in the previous year, the full amount of investment property serves as collateral for financial liabilities. Expenses for maintenance and repairs amounting to €21 thousand (previous year: €37 thousand) were incurred during financial year 2017.

12. OTHER RECEIVABLES AND OTHER ASSETS

€'000	31 Dec. 2017	31 Dec. 2016
Non-current receivables and other assets		
Deposits	146	159
Prepaid expenses	131	162
Payments towards a money market fund to hedge commitments for time-off credits	0	119
	277	**439**
Current receivables and other assets		
Credit card receivables	2,630	1,972
Prepaid expenses	861	916
Income tax assets	4,451	3,249
Miscellaneous	6,608	1,896
	14,550	**8,034**

Other receivables and other assets include financial assets amounting to € 2,777 thousand (previous year: € 2,250 thousand).

Tax assets related to income tax prepayments for domestic and foreign subsidiaries.

The prepaid expenses relate primarily to advance payments of rent, deferred rent payments in connection with operating leases, and maintenance contracts.

The miscellaneous item relates mainly to creditors with debit balances of € 967 thousand (previous year: € 651 thousand) and a € 3,500 thousand VAT receivable from the purchaser of GBS Grundstücksverwaltungsgesellschaft m.b.H.'s properties.

13. AVAILABLE-FOR-SALE FINANCIAL ASSETS

Available-for-sale financial assets amounting to € 286 thousand (previous year: € 277 thousand) include securities that could not be allocated to any of the other measurement categories set out in IAS 39. The item consists entirely of fund units. They were initially recognised and subsequently measured at fair value. Changes in fair value are recognised in other comprehensive income.

14. DEFERRED TAX ASSETS AND LIABILITIES

Deferred tax assets and liabilities are netted if there is a legally enforceable right to offset current tax assets against current tax liabilities and if the deferred taxes relate to the same tax authority.

The deferred tax liabilities and deferred tax assets relate to the following items:

€'000	31 Dec. 2017	31 Dec. 2016
Deferred tax assets		
Intangible assets	291	309
Investment property	70	70
Property, plant and equipment	89	93
Inventories	500	418
Receivables and other current assets	109	97
Prepaid expenses	0	11
Provisions	1,376	1,498
Other liabilities	17,507	16,133
Tax loss carryforwards	735	3,900
Total deferred tax assets	**20,677**	**22,529**
of which current	3,016	6,123
of which non-current	17,661	16,405
Deferred tax liabilities		
Intangible assets	131	150
Investment property	70	70
Property, plant and equipment	13,007	12,106
Inventories	96	135
Prepaid expenses	45	54
Receivables and other current assets	4	5
Provisions	0	53
Other liabilities	1	1
Total deferred tax liabilities	**13,354**	**12,574**
of which current	1,526	1,579
of which non-current	11,828	10,995
Offsetting of deferred tax assets and deferred tax liabilities	– 13,279	– 12,483
Carrying amount of deferred tax assets	**7,398**	**10,046**
Carrying amount of deferred tax liabilities	**75**	**91**

The change in deferred taxes was attributable to the measurement of pension entitlements in the amount of €–7 thousand (previous year: €65 thousand) and was therefore recognised in other comprehensive income. Changes in other deferred taxes as compared to the previous year were recognised in profit or loss.

The corporation and trade tax loss carryforwards shown here relate to Adler Modemärkte AG, Haibach, Adler Mode GmbH, Haibach, and A-Team Fashion GmbH, Munich. No deferred tax assets were recognised in respect of additional existing corporation tax and trade tax loss carryforwards relating primarily to Adler Orange GmbH & Co. KG, Haibach, Adler Mode AG Schweiz, Zug, Switzerland, and a higher share of Adler Mode GmbH, Haibach, and amounting to €18,284 thousand (previous year: €8,280 thousand).

The calculation of deferred taxes resulted in a surplus of deferred tax assets. Where there was doubt about the recoverability of the deferred tax assets due to insufficient projected earnings in the local tax budgets, the deferred tax assets in such cases were recognised only up to the amount of the deferred tax liabilities.

No deferred tax liabilities were recognised in respect of temporary differences in connection with investments in subsidiaries amounting to € 2,450 thousand (previous year: € 3,389 thousand).

Please refer also to the information under accounting policies and the details provided in Note 8.

15. INVENTORIES

€'000	31 Dec. 2017	31 Dec. 2016
Domestic	63,230	65,491
International	10,446	9,908
	73,676	**75,399**

Inventories are measured respectively at the lower of cost and the net realisable selling price as at the end of the reporting period. In accordance with IAS 2.36 (e), impairment allowances were recognised in financial year 2017 for the purpose of reducing risks.

In 2017, impairment allowances on inventories were € 8,984 thousand, or € 2,214 thousand lower compared with the previous year (€ 11,198 thousand). Impairment allowances are recognised primarily for merchandise from prior seasons and for slow-selling articles. The decrease is attributable primarily to the improvement in merchandise management. The carrying amount of the inventories measured at the net selling price amounts to € 66,656 thousand (previous year: € 68,530 thousand).

Inventories consist primarily of merchandise.

16. TRADE RECEIVABLES

All trade receivables have a remaining maturity of up to one year.

The ADLER Group did not receive any collateral or other credit enhancements as security for trade receivables or as security for outstanding invoices in the current or the previous financial year.

Trade receivables past due are reviewed and tested for impairment regularly. The impairment loss amounted to € 349 thousand (previous year: € 380 thousand). Nearly all of the receivables are denominated in euros. For those receivables that were not impaired, there were no indications at the end of the reporting period that the associated payments will not be made when they fall due.

17. CASH AND CASH EQUIVALENTS

Cash and cash equivalents were made up as follows:

€'000	31 Dec. 2017	31 Dec. 2016
Balances with banks	59,054	37,748
Cash-in-hand	4,288	5,026
	63,342	**42,773**

With the exception of € 100 thousand in bank balances pledged in line with industry practice for trade credit insurance policies, none of the cash was subject to restrictions on disposal at the end of the respective reporting periods.

As in the previous year, balances with banks were fully covered by the relevant deposit protection scheme of the individual financial institution.

18. EQUITY

Subscribed capital
As at the end of the reporting period, subscribed capital remained unchanged at € 18,510 thousand. It is divided into 18,510,000 no-par value shares, each with a nominal value of € 1.

The shares of the shareholders are fully paid in.

Accumulated other comprehensive income
For details relating to the changes in net retained profits/net accumulated losses, please refer to the information presented in the consolidated statement of changes in equity.

Dividend restrictions
The Articles of Association of Adler Modemärkte AG contain no provisions for dividend restrictions over and above the statutory minimum.

Capital management
The ADLER Group's objectives with respect to capital management are firstly to ensure that the business is able to continue operations on a long-term basis and to generate adequate returns for the shareholders, and secondly to maintain an optimal capital structure in order to reduce the cost of capital.

The capital structure is managed in such a way as to take account of changes in the general economic environment and the risks attaching to the underlying assets. As a result of its healthy operating cash flow over the course of the full year, the Company is in a position to deploy its own financial resources in the best possible way. For example, investments are regularly reviewed to see whether the Company's own available financial resources can be replaced by external (lease) financing in order to take advantage of improved purchasing prices for goods (e.g. discounts) or to exploit advantageous opportunities for sales arising at short notice. In this context, the raising of new debt is managed on the basis of a target debt structure. The choice of financial instruments is mainly influenced by the objective of matching the maturities of assets and liabilities which is achieved by managing the maturities of the instruments issued.

Capital is monitored on the basis of the indebtedness ratio, calculated as the relationship of debt to equity.

€'000	31 Dec. 2017	31 Dec. 2016
Equity	99,947	95,839
Debt	141,185	126,736
Debt/equity ratio	**1.41**	**1.32**

19. PROVISIONS FOR PENSIONS AND SIMILAR OBLIGATIONS

The provisions for pensions comprise firstly capital commitments to employees who began their employment with Adler Modemärkte AG prior to 1980 and also individual commitments to the founders of the firm and certain former members of management. The amount of the provision recognised in the statement of financial position is made up as follows:

€'000	31 Dec. 2017	31 Dec. 2016
Defined benefit obligations (unfunded)	5,188	5,472
Defined benefit obligations (wholly or partially funded)	2,059	2,166
Subtotal	**7,247**	**7,638**
Less fair value of plan assets	−1,754	−1,822
Provision for old-age pension benefits as at 31 Dec.	**5,493**	**5,816**

The development of the pension obligations (DBO) representing the present value of commitments granted under defined benefit plans in the ADLER Group companies was as follows:

€'000	31 Dec. 2017	31 Dec. 2016
As at 1 Jan.	**7,638**	**7,681**
Current service cost	103	116
Interest expense	118	149
Pensions paid	−582	−657
Actuarial gains (–)/losses (+)		
from changes to demographic assumptions	0	23
from changes to financial assumptions	−41	309
from experience adjustments	12	16
As at 31 Dec.	**7,247**	**7,638**

The associated plan assets developed as follows:

€'000	31 Dec. 2017	31 Dec. 2016
As at 1 Jan.	**1,822**	**1,811**
Contributions (employer)	156	163
Expected interest income	29	37
Pension payments (severance payments)	−238	−325
Administrative expenses for insurance	−4	−4
Experience adjustments (gains (+)/losses (−))	−11	140
Fair value of plan assets as at 31 Dec.	**1,754**	**1,822**

The plan assets consist of a direct insurance policy taken out to cover the obligations arising from severance payments. In accordance with IAS 19, the resulting claim against the insurance company is offset as plan assets against the provision for severance payments required to be recognised. The premiums are paid in the respective calendar year.

The expected return is calculated on the basis of the actuarial rate of interest in accordance with IAS 19 (rev. 2011). The actual gain on plan assets in financial year 2017 amounted to € 18 thousand (previous year: € 177 thousand).

Future cash flows (€'000)	31 Dec. 2017	31 Dec. 2016
Expected pension and severance payments in subsequent year	446	549
Total expected payments in subsequent years 2 to 5	2,163	2,111
Total expected payments in subsequent years 6 to 10	2,129	2,259
Expected contributions to plan assets in subsequent year	−156	−163

The weighted average maturity of the obligations is 10.4 years (previous year: 12.7 years).

Sensitivity analysis regarding the defined benefit obligation for pensions and severance payments:

Provided all other factors remain unchanged, an adjustment in each case of just one measurement parameter has the following effects: The sensitivity analysis takes into account the changes in an assumption, while the other assumptions remain unchanged. This means that potential correlation effects between the individual assumptions are not taken into account.

Measurement parameters	Starting value	Sensitivity	Effect on DBO (€'000)
Actuarial interest rate	1.50 %	+1.00 percentage point	−677
Actuarial interest rate	1.50 %	−1.00 percentage point	810
Projected annual pension increase/decrease	1.75 %	+0.25 percentage points	117
Projected annual pension increase/decrease	1.75 %	−0.25 percentage points	−112
Projected annual wage and salary increase/decrease	2.50 %	+0.50 percentage points	81
Projected annual wage and salary increase/decrease	2.50 %	−0.50 percentage points	−76

The current employers' contributions to the statutory pension scheme are included as an expense in the operating profit or loss for the relevant year and amounted to € 7,371 thousand for the Group as a whole in financial year 2017 (previous year: € 7,922 thousand).

20. OTHER PROVISIONS (NON-CURRENT AND CURRENT)

€'000	Restructuring/ severance payments	Rent and incidental rental expenses	Other provisions for personnel expenses	Other provisions	Total
As at 1 Jan. 2016	**1,224**	**1,586**	**1,358**	**764**	**4,932**
Utilisations	−1,001	−873	−209	−215	−2,298
Additions	1,848	1,474	119	497	3,938
Reversals	−223	−228	−194	−239	−884
Reclassifications	0	0	0	0	0
Accrued interest	0	0	11	0	11
As at 31 Dec. 2016	**1,848**	**1,959**	**1,084**	**808**	**5,699**
Non-current	0	0	1,066	170	1,236
Current	1,848	1,959	18	638	4,463
As at 1 Jan. 2017	**1,848**	**1,959**	**1,084**	**808**	**5,699**
Utilisations	−1,425	−611	−143	−354	−2,532
Additions	1,964	1,000	88	600	3,651
Reversals	−290	−701	−7	−154	−1,152
Accrued interest	0	0	9	0	9
As at 31 Dec. 2017	**2,097**	**1,647**	**1,031**	**900**	**5,675**
Non-current	113	0	1,026	170	1,309
Current	1,984	1,647	5	730	4,366

The obligations from restructuring activities comprise expenses associated with the closing of stores in addition to provisions for termination costs.

The provision for rent and incidental rental expenses relates to additional rent payable due to rent indexation provisions and possible additional payments arising from operating income and expenses statements.

The other provisions for personnel expenses relate to partial retirement commitments and provisions for anniversaries and death benefits, based on actuarial assumptions and discounted to reflect the expected maturities.

Other provisions include provisions for the costs of retaining documents with a non-current portion amounting to € 170 thousand (previous year: € 170 thousand).

21. LIABILITIES FROM THE CUSTOMER LOYALTY CARD PROGRAMME

The liabilities from the ADLER customer loyalty card represent discount entitlements not yet utilised due to customers who have settled their purchases using the ADLER customer loyalty card. The customers can offset the discount entitlement obtained from making a purchase against a subsequent purchase or can have the amount paid in cash. Since the entitlements expire at the latest on 31 December of the following year, the item is classified as current. The amounts credited to customers do not bear interest. The amount not yet utilised at the end of the reporting period is reported in full as a liability in accordance with the requirements of IAS 39. However, recent years' experience has shown that a significant number of customers do not claim their discount before they expire. The full amount is reported, however, since the discount entitlements classified as liabilities may be claimed in full. For presentation purposes, the adjustment is presented separately under Note 22.

€'000		31 Dec. 2017	31 Dec. 2016
Liabilities from the ADLER customer loyalty card programme	< 1 year	10,380	10,624

With the exception of liabilities amounting to CHF 77 thousand from the customer loyalty card programme of Adler Mode AG Schweiz, liabilities are repayable in euros.

22. FINANCIAL LIABILITIES

€'000		31 Dec. 2017	31 Dec. 2016
Financial liabilities pursuant to audited prior-year annual financial statements			13,519
Less reclassification of liabilities from the ADLER customer loyalty card programme			10,624
Financial liabilities (adjusted)			**2,895**
Liabilities to METRO Finance B.V.	< 1 year	316	314
Liabilities to METRO Finance B.V.	> 1 year	**2,267**	**2,581**
		2,583	**2,895**

The liability to METRO Finance B.V. comprises a loan at a current fixed rate of interest since 1 April 2017 of 0.900 % p.a. (until 31 March 2017: 0.936 % p.a.). The interest rate is fixed from 1 April 2017 until 31 March 2019. The loan has a maturity date of 31 July 2024 and is repaid in quarterly instalments.

As at 31 December 2017, the financial liabilities were secured by items of property, plant and equipment with a carrying amount of € 3,000 thousand (previous year: € 3,130 thousand) and by investment property with a carrying amount of € 413 thousand (previous year: € 413 thousand).

Financial liabilities are repayable in euros.

23. LIABILITIES FROM FINANCE LEASES

The ADLER Group's property, plant and equipment include assets classified under licences and land and buildings that are attributable to the Group as economic owner as a result of the structure of the underlying lease agreements. The Group's obligations arising from finance lease agreements of this nature can be seen from the following table:

€'000	31 Dec. 2017	31 Dec. 2016
Finance lease agreements		
Minimum finance lease payments payable		
up to 1 year	10,203	10,086
1 to 5 years	30,030	28,821
more than 5 years	43,308	38,673
	83,541	**77,580**
Discounts		
up to 1 year	−4,486	−4,263
1 to 5 years	−9,327	−9,517
more than 5 years	−13,778	−11,645
	−27,591	**−25,425**
Present value		
up to 1 year	5,718	5,823
1 to 5 years	20,703	19,303
more than 5 years	29,531	27,028
	55,952	**52,154**

The finance lease agreements relate primarily to leased buildings for stores. The lease agreements generally include renewal clauses as well as price adjustment clauses based on changes in the rental price index. In addition, variable components of rent are contingent depending on the sales achieved in the individual stores. In financial year 2017, the contingent rental payments under finance lease agreements amounted to € 967 thousand (previous year: € 1,088 thousand). The increase in finance leases is attributable primarily to new leases and lease amendments. The terms of the leases generally amount to between 5 and 20 years with renewal options. All of the liabilities from finance leases are repayable in euros.

Due to the renewal of the lease for the stores in Strassen, Luxembourg, and Salzburg, Austria, the operating leases for those stores will be reclassified as finances leases in financial year 2017.

24. TRADE PAYABLES

Trade payables at the end of the reporting period are due in their entirety, as in the previous year, to third parties unrelated to the Group. Also as in the previous year, all trade payables are due within one year.

Trade payables are primarily due in euros, as in previous years.

No collateral has been provided by the ADLER Group for the trade payables reported. Goods are delivered by suppliers subject to the retention of title provisions applying in the specific country.

25. OTHER LIABILITIES

€'000	31 Dec. 2017	31 Dec. 2016
Liabilities from value added tax	9,547	6,331
Wage and salary commitments	4,809	4,166
Liabilities to customers for gift vouchers sold	5,020	4,217
Deferred building cost subsidies	930	1,254
Liabilities from customs duties	869	966
Liabilities from wage tax	943	886
Workmen's compensation	501	551
Social security contributions	408	358
Deferred lease payments	289	288
Deferred income from sale and leaseback transactions	117	0
Payments received	136	0
Other	681	462
Other current liabilities	**24,250**	**19,479**
Deferred building cost subsidies	2,847	3,290
Deferred income from sale and leaseback transactions	1,408	
Deferred lease payments	1,104	1,364
Other non-current liabilities	**5,359**	**4,654**

Other current liabilities include financial liabilities amounting to € 5,547 thousand (previous year: € 3,636 thousand).

Other current liabilities include an amount of € 26 thousand (previous year: € 26 thousand) in respect of the compensation entitlement of the limited partners in ALASKA GmbH & Co. KG which is limited to this amount.

26. INCOME TAX LIABILITIES

Income tax liabilities of € 3,810 thousand (previous year: € 63 thousand) relate to corporation tax and trade tax liabilities.

27. STATEMENT OF CASH FLOWS

The statement of cash flows shows the development of the ADLER Group's cash and cash equivalents in the year under review and the prior year. Cash and cash equivalents are defined for this purpose as holdings of cash and cash equivalents less cash subject to restrictions on disposal.

In accordance with IAS 7, the cash flows are classified as cash from/used in operating activities, investing activities and financing activities.

€'000	2017	2016
Cash from (+)/used (–) in operating activities (net cash flow)	21,157	22,191
Cash from (+)/used (–) in investing activities	14,789	–10,830
Free cash flow	**35,946**	**11,361**
Cash from (+)/used (–) in financing activities	–15,377	–20,664
Net increase in cash and cash equivalents	**20,569**	**–9,303**

Cash and cash equivalents as at 31 December 2017 amounted to €63,342 thousand (previous year: €42,773 thousand) and include demand deposits with banks, current time deposits with terms of less than three months, cheques and cash-in-hand. As in the previous year, there was no cash subject to restrictions on disposal during the reporting period.

The following material non-cash transactions took place in financial year 2017: Other non-cash income and expenses amounting to €–8,945 thousand (previous year: €2,246 thousand) include in particular the change in inventories and trade receivables as well as effects from the real estate transactions in Austria.

Non-current assets and liabilities from finance leases both rose by €9,651 thousand (previous year: €2,391 thousand) with no effect on cash as a result of the addition of new finance leases or the renewal of existing leases.

Proceeds from disposals of property, plant and equipment includes in particular the proceeds from the sale of the St. Pölten and Klagenfurt properties. Proceeds from disposals of non-current assets (property) held for sale includes the disposal of the Vösendorf, Ansfelden and Salzburg properties.

Payments for investments in non-current assets include payments for the purchase of the Klagenfurt property and the non-current assets for the stores.

Payments for company acquisitions were attributable to the acquisition of GBS Gundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria.

Repayments of loan liabilities include the repayment of the loan for the Alaska property and the repayment of a loan granted by GBS Gundstücksverwaltungsgesellschaft m.b.H. as part of the company acquisition.

The breakdown of interest paid in the financial years under review was as follows:

€'000	2017	2016
Interest paid from finance leases	4,750	4,601
Interest paid from operating activities	319	344
Total	**5,069**	**4,945**

Liabilities from finance leases were made up as follows:

€'000	
Liabilities from finance lease liabilities 31. Dec. 2016	52.154
Cash changes	–10.604
Non-cash changes	+14.401
Liabilities from finance lease liabilities 31. Dec. 2017	**55.951**

Liabilities from finance leases 2016 were made up as follows:

€'000	
Liabilities from finance lease liabilities 31. Dec. 2015	56.257
Cash changes	–11.095
Non-cash changes	+6.992
Liabilities from finance lease liabilities 31. Dec. 2016	**52.154**

The change in financial liabilities is based exclusively on cash income.

28. SEGMENT REPORTING

2017 (€'000)	Stores segment	Reconciliation with IFRS	ADLER Group
Total revenue (net)	519,504	6,310	525,814
Other operating income	20,203	–1,391	18,812
Cost of materials	–266,769	22,708	–244,061
Personnel expenses	–98,604	1,755	–96,849
Other operating expenses	–157,779	–13,933	–171,712
EBITDA	**16,556**	**15,449**	**32,005**
Depreciation, amortisation and write-downs	–9,836	–6,618	–16,454
EBIT	**6,720**	**8,831**	**15,551**

2016 (€'000)	Stores segment	Reconciliation with IFRS	ADLER Group
Total revenue (net)	537,638	6,914	544,553
Other operating income	15,547	–6,813	8,734
Cost of materials	–278,641	22,174	–256,467
Personnel expenses	–105,383	3,051	–102,333
Other operating expenses	–156,827	–14,360	–171,187
EBITDA	**12,334**	**10,966**	**23,300**
Depreciation, amortisation and write-downs	–9,947	–6,714	–16,660
EBIT	**2,388**	**4,253**	**6,640**

The reconciliation contains differences from various account allocations for internal control purposes and differences arising between national accounting standards and IFRSs.

Where revenue and other operating income is concerned, these differences relate primarily to customer discounts, while the differences relating to cost of materials stem from logistics services and inventory measurements, and differences relating to personnel expenses and other operating expenses stem primarily from differences in account allocation and the accounting treatment for leases and pension provisions under HGB and IFRSs. Depreciation, amortisation and write-downs under IFRSs include amortisation and write-downs on finance leases and useful lives that in some cases deviate from the useful lives under HGB.

GBS Gundstücksverwaltungsgesellschaft m.b.H., Vienna, Austria, is not included in the segment report as it is not operational. Other operating income under IFRS would have been € 7,333 thousand higher had the company been included. This is partly due to the hidden reserves and partly due to the classification of the Salzburg lease as a finance lease. This results in the sales proceeds being reversed through profit or loss over a period of 13 years.

The segment report was prepared in accordance with IFRS 8 "Operating Segments". The segments were defined in accordance with the ADLER Group's internal management and reporting procedures. "Stores (Modemärkte)" was the only segment at the end of the reporting period. The Stores segment comprises the Company's entire activities relating to the stores operated by the ADLER Group. Due to the mass market in the Stores segment, there is no concentration risk with regard to key or significant customers.

Since the internal reporting system is based on the accounting requirements of the HGB, the information contained in the segment report has been prepared on the basis of the HGB. In accordance with the provisions of IFRS 8.28, a reconciliation has been provided to the accounting principles applied in the consolidated financial statements and therefore to the amounts presented in the consolidated income statement.

The principal performance indicator used by the ADLER Group's decision-makers for management purposes is the figure reported internally for EBITDA, which is defined as the profit or loss from operations before interest, taxes, depreciation and amortisation on property, plant and equipment and intangible assets, and impairment.

The breakdown of the non-current assets, defined as intangible assets, property, plant and equipment and investment property, by region is as follows:

	2017			2016		
€'000	Germany	International	Group	Germany	International	Group
Non-current assets	67,624	13,345	80,970	76,958	8,067	85,025

29. RISK MANAGEMENT

The finance department of Adler Modemärkte AG monitors and manages the financial risks of the entire ADLER Group. Specifically, those risks are

- Liquidity risks
- Market risks (interest rate and currency risks)
- Credit risks

The ADLER Group is exposed to a large number of financial risks as a result of its business activities. This is understood to mean unexpected events and possible developments that have a negative effect on achieving the objectives that have been set and the expectations. The risks that are relevant are those with a material effect on the Company's financial position, financial performance and cash flows. The Group's risk management system analyses a range of risks and attempts to minimise negative effects on the financial position of the Company. The risk management activities are carried out in the finance department on the basis of established guidelines.

For the purpose of measuring and managing material individual risks, the Group distinguishes between liquidity, credit and market risks.

Liquidity risks

Liquidity risks are understood in the narrow sense to mean the risk of being able to meet present or future payment obligations either not at all or only on unfavourable terms. The Company mainly generates financial resources through its operating activities.

Adler Modemärkte AG functions as the financial coordinator for the companies in the ADLER Group in order to ensure that the financial requirements for the operating business and for investments are covered on the most favourable terms possible in terms of cost and in amounts that are always sufficient. The necessary information is provided via a Group financial planning process with additional 14-day liquidity projections on a rolling weekly basis, and is analysed constantly.

The long-term corporate financing requirements of the ADLER Group are secured by the ongoing cash flows from operating activities and from leases entered into on a long-term basis.

The intra-Group cash management system enables short-term liquidity surpluses in individual Group companies to be used as internal financing to meet the cash requirements of other Group companies. This contributes to a reduction in the volume of external debt financing and to the best possible use of cash deposits and capital investments, and therefore has a positive effect on the net interest income and expenses of the Group.

At Group level, a consolidated and integrated liquidity plan is prepared using the latest business planning and financial projections together with additional special items that are identified at short notice.

The ADLER Group is mainly financed by its own liquid resources generated from its operating activities. The long-term leases of certain stores are reported as finance leases in accordance with IFRSs. The recognised long-term finance lease obligation amounted to €50,233 thousand at the end of the reporting period (previous year: €46,331 thousand). In addition, the Group has only one loan outstanding, to a company within the METRO AG group, which was used for a property financing transaction. The outstanding amount of the loan amounted to €2,583 thousand at the end of the reporting period (previous year: €2,895 thousand). Current loan liabilities at the end of the reporting period amounted to €316 thousand (previous year: €314 thousand). The remaining current financial liabilities/liabilities arising from the customer loyalty card programme at the end of the reporting period amounted to €10,380 thousand (previous year: €10,624 thousand).

Maturity analysis of financial liabilities

The table below shows the maturity structure of the contractual undiscounted cash flows from financial liabilities:

2017 (€'000)	up to 1 year	more than 1 year
Trade payables	27,608	0
Liabilities from the customer loyalty card programme	10,380	0
Financial liabilities	338	2,338
Liabilities from finance leases	10,203	73,338
Other financial liabilities	5,547	0

2016 (€'000) – (adjusted)[1]	**up to 1 year**	**more than 1 year**
Trade payables	25,261	0
Liabilities from the customer loyalty card programme	10,624	0
Financial liabilities	342	2,676
Liabilities from finance leases	10,086	67,494
Other financial liabilities	3,636	0

[1] *See Note 22.*

The undiscounted cash outflows are subject to the condition that the liabilities are repaid on the earliest due date. Other financial liabilities include primarily liabilities to customers for gift vouchers sold.

Based on the normal payment agreements with suppliers and other business partners, the maturities of the current trade payables and therefore the associated cash outflows are as follows:

€'000	**31 Dec. 2017**	**31 Dec. 2016**
Carrying amount	**27,608**	**25,261**
Thereof falling due within the following time bands:		
Less than 30 days	20,236	17,866
30–90 days	7,125	7,393
90–180 days	0	0
180 days–1 year	248	2

The liabilities from the customer loyalty card programme fall due immediately since the customers are entitled to redeem their credit at any time within twelve months. In accordance with IFRS 7, liabilities of this nature that are payable at any time are allocated to the earliest time band.

Based on the normal payment agreements with banks and other business partners, the maturities of the current financial liabilities and therefore the associated cash outflows, including interest, are as follows:

€'000	**31 Dec. 2017**	**31 Dec. 2016 (adjusted)**
	10,719	**340**
Thereof falling due within the following time bands:		
Less than 30 days	10,380	0
30–90 days	85	86
90–180 days	85	86
180 days–1 year	169	171

The maturities of the liabilities from finance leases “up to 1 year” and therefore the associated cash outflows are as follows:

€’000	31 Dec. 2017	31 Dec. 2016
Total falling due within one year	**10,203**	**10,086**
Thereof falling due within the following time bands:		
Less than 30 days	850	797
30–90 days	1,701	2,118
90–180 days	2,551	2,391
180 days–1 year	5,102	4,781

The maturities of the other current liabilities “up to 1 year” and therefore the associated cash outflows are as follows:

€’000	31 Dec. 2017	31 Dec. 2016
Total falling due within one year	**5,547**	**3,636**
Thereof falling due within the following time bands:		
Less than 30 days	5,046	3,085
30–90 days	0	0
90–180 days	501	551
180 days–1 year	0	0

Credit risks

Credit risks arise from the complete or partial default of a counterparty, for example through insolvency, and in connection with deposits. The maximum risk of default is equal to the carrying amounts of all the financial assets; default risks that deviate from the corresponding carrying amount are noted where relevant. Valuation allowances are recognised in respect of trade receivables and other receivables and assets in accordance with rules applied consistently across the Group and cover all identifiable credit risks.

As part of the risk management system, minimum requirements for the credit rating and also specific upper limits for the exposure are laid down for all business partners of the ADLER Group. The level of the upper credit limit reflects the creditworthiness of a contractual counterparty and the typical size of the volume of transactions with that party. This is based on a systematic procedure for approving limits set down in the Treasury guidelines, which relies firstly on the classifications awarded by international ratings agencies and on internal credit assessments, and secondly on historical values experienced by the Group with the respective contractual parties. The ADLER Group therefore has a very low exposure to credit risks.

The loans and receivables reported in the consolidated financial statements amounting to €3,412 thousand (previous year: €3,189 thousand) are not secured. The maximum risk of default is therefore equal to the carrying amount of the loans and receivables reported.

Valuation allowances in appropriate amounts are generally recognised in order to take account of identifiable risks of default in respect of receivables.

None of the loans reported at the end of the reporting period were impaired or overdue.

Market risks (interest rate and currency risks)

Market risks are understood to mean the risk of loss that can arise due to a change in market parameters used for measurement (currency, interest rates, price).

Interest rate and currency risks are significantly reduced and limited by the principles laid down in the internal Treasury guidelines. These establish mandatory rules applied uniformly across the Group that all hedging transactions must be subject to predetermined limits and must never result in an increase in the risk position. At the same time, the ADLER Group is fully aware that the opportunities for increasing earnings by taking advantage of current or expected changes in interest rates or exchange rates are very limited.

The ADLER Group is essentially not exposed to currency risks since the consolidated revenue was generated almost exclusively in euros and all purchases of goods were also made in euros during the period under review. Receivables, loans and financial liabilities are primarily denominated in euros.

Risks due to changes in interest rates can arise mainly as a result of potential changes in the value of a financial instrument which is sensitive to interest rates, in response to changes in market rates of interest which lead to changes in the expected cash flows. In order to minimise the risk of changes in interest rates within the ADLER Group, where necessary, loans are taken out only on a long-term basis and leases are entered into at fixed rates of interest. With the exception of the liability to METRO Finance B.V. (see Note 21), the ADLER Group is not a party to any financial instruments bearing a variable rate of interest. If the level of interest rates had been 100 basis points higher at the date when the new rate of interest was determined for this liability in financial year 2017, the interest expense for financial year 2017 would have been € 5 thousand higher (previous year: € 8 thousand higher). If the level of interest rates had been 100 basis points lower at the date when the new rate of interest was determined for this liability in financial year 2017, the interest expense for financial year 2017 would have been € 10 thousand lower (previous year: € 7 thousand lower). Since the period for which the interest rate was fixed included the whole of financial year 2017, there was no sensitivity to interest rates in this period.

The ADLER Group is not exposed to any other material risks affecting the prices of financial instruments. At the end of the reporting period, the Group held no shares in quoted companies.

The sensitivity analysis of the available-for-sale financial assets resulted in the following potential changes as at 31 December 2017: In the event of an increase of 5 % in the market price, equity would have risen by € 11 thousand (previous year: € 10 thousand). In the event of a decrease of 5 % in the market price, equity would have fallen by € 11 thousand (previous year: € 10 thousand).

Carrying amounts and fair values of financial instruments

The table below shows the carrying amounts and fair values of the financial assets and liabilities for each measurement category in accordance with IAS 39. The fair value of a financial instrument is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm’s length transaction.

2017 (€'000)	At amortised cost Other liabilities	Loans and receivables	At fair value (no effect on profit/loss) Available-for-sale financial assets	Carrying amount pursuant to IAS 17	Total	Total
Item	Carrying amount	Carrying amount	Carrying amount	Carrying amount	Carrying amount	Fair Value
Available-for-sale financial assets	–	–	286	–	286	286
Cash and cash equivalents	–	63,342	–	–	63,342	63,342
Trade receivables	–	635	–	–	635	635
Other financial assets	–	2,777	–	–	2,777	2,777
Total financial assets	**0**	**66,754**	**286**	**0**	**67,040**	**67,040**
Trade payables	27,608	–	–	–	27,608	27,608
Liabilities from the customer loyalty card programme	10,380	–	–	–	10,380	10,380
Financial liabilities	2,583	–	–	–	2,583	3,970
Liabilities from finance leases	–	–	–	55,951	55,951	67,166
Other financial liabilities	5,547	–	–	–	5,547	5,547
Total financial liabilities	**46,119**	**–**	**–**	**55,951**	**102,070**	**114,672**

2016 (€'000) (adjusted)[1]	At amortised cost Other liabilities	Loans and receivables	At fair value (no effect on profit/loss) Available-for-sale financial assets	Carrying amount pursuant to IAS 17	Total	Total
Item	Carrying amount	Carrying amount	Carrying amount	Carrying amount	Carrying amount	Fair Value
Available-for-sale financial assets	–	–	277	–	277	277
Cash and cash equivalents	–	42,773	–	–	42,773	42,773
Trade receivables	–	582	–	–	582	582
Other financial assets	–	2,250	–	–	2,250	2,250
Total financial assets	**–**	**45,605**	**277**	**–**	**45,882**	**45,882**
Trade payables	25,261	–	–	–	25,261	25,261
Liabilities from the customer loyalty card programme	10,622				10,622	10,622
Financial liabilities	2,897	–	–	–	2,897	4,040
Liabilities from finance leases	–	–	–	52,154	52,154	59,301
Other financial liabilities	3,636	–	–	–	3,636	3,636
Total financial liabilities	**42,416**	**–**	**–**	**52,154**	**94,572**	**102,861**

[1] *See Note 22.*

The fair values of the available-for-sale financial assets are determined on the basis of the market price available in an active market. The determination of the fair value falls under Level 1 for the inputs used in the determination of fair values in accordance with IFRS 7.

The fair values of the other financial instruments were determined on the basis of the market information available at the end of the reporting period using the methods and assumptions described below.

In view of the short maturities of trade receivables and cash, it is assumed that the fair values are approximately equal to the carrying amounts.

In principle, the liabilities included in the statement of financial position under trade payables and liabilities from the customer loyalty card programme generally have short remaining maturities, so that the fair values are approximately equal to the carrying amounts reported, in line with the assumption made.

Other financial assets, financial liabilities, liabilities from finance leases and other financial liabilities reported in the statement of financial position comprise current and non-current financial assets and liabilities. The fair values of assets and liabilities with remaining maturities of more than 1 year are calculated by discounting the cash flows associated with those assets and liabilities using current interest rate parameters. For this purpose, the individual credit ratings used by ADLER are reflected in the form of normal market credit and liquidity spreads for the purpose of determining the present values.

Net gains and losses from financial instruments by measurement category

The table below shows the net gains and losses from financial instruments reported in the income statement by measurement category. Interest income and expenses were the only relevant items for the determination of the net gains and losses.

2017 (€'000)	Loans and receivables	Other liabilities	Total
From interest	0	−316	−316
Total	**0**	**−316**	**−316**

2016 (€'000)	Loans and receivables	Other liabilities	Total
From interest	5	−211	−206
Total	**5**	**−211**	**−206**

No interest income was received from impaired trade receivables during the period under review.

For information relating to the net gain or loss from available-for-sale financial assets, please see Note 13.

Other disclosures

At the end of the reporting period there were no financial assets or financial liabilities designated as at fair value through profit or loss. The Group had no holdings of derivative financial instruments.

30. PURCHASE AND DISPOSAL OF ASSETS

During the period under review, ADLER acquired a section of a building in Klagenfurt, which is not designated for own use, from the leasing company GBS Gundstücksverwaltungsgesellschaft m.b.H., which manages other buildings used by ADLER in Ansfelden, Salzburg and Vösendorf. In the previous year, ADLER acquired a building in St. Pölten that was partially designated for own use after the lease expired. As at 30 April 2017, the buildings in St. Pölten and Klagenfurt were sold to a strategic investor for a total sales price of € 10 million. The transaction generated € 7.6 million in other operating income.

In accordance with IFRS 3, the purchase of GBS Grundstücksverwaltungsgesellschaft m.b.H for € 6.7 million was classified as an acquisition of assets pursuant to IFRS 3.2 (b), and not as a business combination. The three buildings in Austria – Ansfelden, Salzburg and Vösendorf – were acquired as a part of the acquisition of the shares. The purchase price for the buildings and the liabilities assumed totalled € 11.0 million. Furthermore, as part of the acquisition, the financial liabilities of GBS Gundstücksverwaltungsgesellschaft m.b.H. amounting to € 4.3 million were repaid and replaced by intra-Group financing.

Since the Company planned to resell the buildings in the short-term, the assets were classified as assets held for sale pursuant to IFRS 5 and during the year were reported under the separate line item "non-current assets held for sale".

In the fourth quarter, the buildings in Ansfelden, Salzburg and Vösendorf were disposed as part of a sale and leaseback transaction. ADLER secured the use of the buildings at attractive terms via long-term leases. The Ansfelden and Vösendorf stores were classified as operating leases, the Salzburg store as a finance lease. The purchase price amounted to € 17.3 million and the IFRS disposal proceeds totalled € 5.8 million, of which € 4.3 million were recognised in profit or loss during the financial year. In accordance with IAS 17, the € 1.5 million in proceeds from the disposal of the Salzburg building were reversed over the term of the finance lease.

V. OTHER NOTES

31. OTHER FINANCIAL OBLIGATIONS

As at the end of the reporting period on 31 December 2017, there were other financial obligations arising from rental, lease and service agreements entered into by the Group in the ordinary course of business that cannot be terminated prior to maturity. The maturity analysis of the future payments arising from those agreements attributable to continuing operations is as follows:

2017 (€'000)	up to 1 year	1–5 years	more than 5 years	Total
Rental and lease obligations	48,067	153,183	116,330	317,580
Other obligations	18,014	0	0	18,014
Total	**66,081**	**153,183**	**116,330**	**335,594**

2016 (€'000)	up to 1 year	1–5 years	more than 5 years	Total
Rental and lease obligations	47,872	150,826	125,306	324,004
Other obligations	21,586	0	0	21,586
Total	**69,458**	**150,826**	**125,306**	**345,590**

The total rental and lease obligations from operating lease agreements amounting to €317,580 thousand (previous year: €324,004 thousand) relate to rental and lease agreements for land and buildings in an amount of €315,970 thousand (previous year: €321,128 thousand) and to operating lease agreements for other facilities and operating and office equipment in an amount of €1,611 thousand (previous year: €2,876 thousand).

Furthermore, there were capital expenditure commitments of €520 thousand (previous year: €768 thousand) at the end of the reporting period on 31 December 2017.

Capital expenditure commitments include investments planned for 2017 which had already been contractually agreed as at the end of the reporting period.

As at 31 December 2017, the total future minimum lease payments arising from subleases amounted to €2,615 thousand (previous year: €6,744 thousand). The decrease is attributable to the disposal of the Klagenfurt building.

2017 (€'000)	up to 1 year	1–5 years	more than 5 years	Total
Minimum lease payments arising from subleases	824	1,598	193	2,615
Total	**824**	**1,598**	**193**	**2,615**

2016 (€'000)	up to 1 year	1–5 years	more than 5 years	Total
Minimum lease payments arising from subleases	1,285	2,385	3,074	6,744
Total	**1,285**	**2,385**	**3,074**	**6,744**

32. CONTINGENT LIABILITIES

The Group has a guarantee facility in an amount of € 7,000 thousand (previous year: € 7,000 thousand) with various banks. As at 31 December 2017 the guarantee facility was being utilised in an amount of € 4,859 thousand (previous year: € 4,608 thousand). This includes rental guarantees for € 3,089 thousand (previous year: € 2,843 thousand), deliveries of goods amounting to € 270 thousand (previous year: € 270 thousand) and a customs guarantee in an amount of € 1,500 thousand (previous year: € 1,500 thousand).

33. REMUNERATION

The Company's Annual General Meeting on 4 May 2016 resolved that individual Executive Board members' remuneration would not be disclosed separately. For financial year 2017, remuneration for the Executive Board totalled € 2,327 thousand (previous year: € 1,313 thousand). The breakdown of the remuneration is as follows:

€'000	2017	2016
Fixed remuneration	1,073	1,009
Non-cash benefits	26	22
Bonuses	228	210
Total short-term benefits payable to Executive Board members	**1,327**	**1,241**
LTI bonus	0	72
Total benefits payable to Executive Board members from long-term bonus (LTI)	**0**	**72**
Severance payments	1,000	0
Benefits due to termination of the Executive Board position	**1,000**	**0**
Total	**2,327**	**1,313**

The STI is the first remuneration component based on the Company's performance for the past financial year. In financial year 2017, the STI for current members of the Executive Board will be calculated based on earnings before interest, tax, depreciation and amortisation (EBITDA) as reported in the audited IFRS consolidated financial statements for the financial year ended and based on targets and further financial ratios to be defined at the beginning of the year which operate to either increase or decrease the STI depending on the degree to which such targets and ratios are met. Each member's STI is capped at € 750 thousand annually.

The LTI bonus, the calculation of which takes several years into account, is intended as monetary recognition of the Executive Board member's contribution toward increasing the Company's value. The LTI bonus is based on EBITDA as reported in the audited and approved IFRS consolidated financial statements for the financial year ended. The amount of the bonus depends on the performance of ADLER shares (weighted average share price for the Company during the financial year for which the LTI bonus is calculated as compared to the prior-year weighted average share price). The new LTI bonus, the calculation of which takes several years into account, is currently limited to a total amount of € 1,500 thousand and is not paid out if ADLER shares do not perform accordingly.

The previous LTI bonus, which was based on stock appreciation rights (SARs), expired at the end of the 2016 financial year.

The total payments to former members of the executive bodies and their surviving dependants amounted to € 1,165 thousand (previous year: € 168 thousand). This includes remuneration to former managing directors of € 165 thousand (previous year: € 168 thousand). Pension provisions in the amount of € 1,830 thousand (previous year: € 1,881 thousand) have been recognised for former members of management and their surviving dependants.

The members of the Supervisory Board are also key management personnel of the ADLER Group in accordance with IAS 24. The total remuneration for members of the Supervisory Board during the financial year was €317 thousand (previous year: €322 thousand).

In financial year 2017 as well as in the previous year, no member of the Supervisory Board or an enterprise in which such member holds a key position provided the Company with any consultancy services.

34. RELATED PARTY DISCLOSURES

Adler Modemärkte AG has been an associated company of S&E Kapital GmbH, Munich, and indirectly an associated company of Steilmann Holding AG i.I., Bergkamen, since 25 April 2013. Steilmann Holding AG i.I. and its subsidiaries are thus to be considered related parties.

Transactions with related parties are contractually agreed and carried out at arm's length prices.

The following transactions were entered into with related parties:

€'000	2017	2016
Services purchased from related parties:		
Steilmann Group	25,392	30,012
Sale of goods, services and non-current assets to related parties		
Steilmann Group	4	328

The following balances with related parties were outstanding at the end of the reporting periods:

€'000	31 Dec. 2017	31 Dec. 2016
Trade receivables/services from related parties:		
Steilmann Group	0	0
Trade payables/services to related parties:		
Steilmann Group	2,221	656

Family members of key management personnel did not provide any services to the ADLER Group (previous year: €0 thousand). In the period under review, no property, plant or equipment was sold to or acquired from family members in key positions of controlled companies.

A member of the Executive Board was billed rent in the amount of €1 thousand per year (previous year: €2 thousand).

Goods amounting to €539 thousand were procured from Elan PVT Limited, Hong Kong, in the year under review. The company is associated with a member of the Supervisory Board and is therefore treated as a related party in accordance with IAS 24. There were no outstanding liabilities to Elan PVT Limited, Hong Kong, for deliveries of goods as at the reporting date.

Remuneration for members of the Supervisory Board in their function as employees amounted to €256 thousand (previous year: €264 thousand) during the year under review.

There are no obligations from finance or operating leases with related parties.

35. EARNINGS PER SHARE

The earnings per share figure is calculated by dividing the consolidated net profit or loss, classified as continuing operations or discontinued operations, by the weighted average of the existing shares.

In the reporting period, outstanding shares are weighted on a pro-rata basis for the period in which they are in circulation. The number of outstanding shares fluctuates as follows:

		2017	2016
Outstanding shares	as at 1 January	18,510,000	18,510,000
Shares sold during the year		0	0
Outstanding shares	as at 31 December	18,510,000	18,510,000
Consolidated net profit for the year (€'000)		3,858	410
Weighted average of outstanding shares	as at 31 December	18,510,000	18,510,000
Basic earnings per share	EUR	0.21	0.02
Diluted earnings per share	EUR	0.21	0.02

There were no dilutive effects in the reporting periods shown.

36. APPROPRIATION OF NET PROFIT – DIVIDEND

The dividend distribution is based on Adler Modemärkte AG's annual financial statements prepared under German commercial law. The Management Board of Adler Modemärkte AG proposes to the Annual General Meeting that the net profit of €926 thousand reported in the balance sheet as at 31 December 2017 be used to pay out a dividend of €0.05 per dividend-bearing share, i.e. in total an amount of €926 thousand.

37. LITIGATION AND CLAIMS FOR DAMAGES

The ADLER Group is not involved in any legal or arbitration proceedings with a significant effect on the position of the Group.

38. AUDITORS' FEES

Fees amounting in total to €407 thousand (prior year €383 thousand) were incurred in financial year 2017 for services provided by the auditor within the meaning of § 318 HGB:

€'000	2017	2016 (adjusted)*
Audit services (including half-yearly financial statements and FREP)	283	211
Other certification services	28	81
Tax advisory services	96	68
Other services	0	23
Total	**407**	**383**

* *Reclassification in accordance with the amendments to IDW AcP HFA 36 – Recording of interim financial statements and enforcement procedures for audit services.*

The audit services include primarily fees for the audit of the consolidated financial statements as well as the statutory audits of Adler Modemärkte AG and of the subsidiaries included in the consolidated financial statements. Also included are the fees for the review of the half-yearly financial statements and services provided by the Financial Reporting Enforcement Panel (FREP) in connection with enforcement procedures. The fees for other certification services include fees for revenue certificates (Umsatzbescheinigungen) and voluntary audits of IT systems. The fees for tax advisory services include in particular fees for preparing tax returns and general tax advisory services.

39. EVENTS AFTER THE END OF THE REPORTING PERIOD

There were no further matters arising after the end of the financial year up to the date of preparation of the consolidated financial statements that have a material effect on the financial position, cash flows and financial performance of the Company for financial year 2017.

40. DECLARATION OF CONFORMITY WITH THE GERMAN CORPORATE GOVERNANCE CODE

On 10 May 2017, the Executive Board and the Supervisory Board of Adler Modemärkte AG jointly issued the Declaration of Conformity with the recommendations of the German Corporate Governance Code as amended on 7 February 2017 in accordance with § 161 of the German Stock Corporation Act (Aktiengesetz, "AktG"). The form and content of the Declaration of Conformity is permanently available to shareholders on the Company's website at *www.adlermode-unternehmen.com/investor-relations/corporate-governance/entsprechenserklaerung*.

41. EXECUTIVE BODIES OF THE COMPANY

The following persons exercised an executive board function in financial year 2017 and up to the date of preparation of the financial statements:

Thomas Freude, *Wiesbaden, Germany*, Chairman of the Executive Board, Executive Board member for Strategy, Marketing, Sales, E-Commerce, Mergers & Acquisitions, Expansion and Public Relations (member and Chairman of the Executive Board since 11 September 2017), other supervisory board positions and comparable memberships: LSG Lufthansa Service Holding AG (since 29 August 2017)

Karsten Odemann, *Lenggries, Germany*, Executive Board, Executive Board member for Finance, Controlling, Audits, Legal, IT and Investor Relations (Labour Director until 30 April 2017)

Andrew Thorndike, *Cologne, Germany*, Executive Board and Labour Director, Executive Board member for Purchasing, Logistics, Human Resources and Technical Purchasing (Member of the Executive Board and Labour Director from 1 May 2017 to 30 January 2018)

Lothar Schäfer, *Villmar, Germany*, Chairman of the Executive Board, Executive Board member for Strategy, Mergers & Acquisitions, Purchasing, Marketing, Sales, E-Commerce, Store Expansion and Public Relations (member and Chairman of the Executive Board until 30 April 2017)

The members of the Supervisory Board of Adler Modemärkte AG in financial year 2017 were as follows:

Massimiliano Monti [1*, 2, 3*, 4*], *Lugano, Switzerland*, Chairman of the Supervisory Board, partner at Equinox S.A., other supervisory board positions and comparable memberships: Advisory Board of S&E Kapital GmbH

Majed Abu-Zarur [1, 2, 4], *Viernheim, Germany*, Deputy Chairman of the Supervisory Board, Chairman of the Joint Works Council at Adler Modemärkte AG

Wolfgang Burgard [1, 2*, 3], *Dortmund, Germany*, Managing Director of Bund Getränkeverpackungen der Zukunft GbR

Cosimo Carbonelli D'Angelo [1, 4], *Naples, Italy*, Chairman of the Managing Board of G.&C. Holding S.r.l., other supervisory board positions and comparable memberships: Member of the Advisory Board of S&E Kapital GmbH

Corinna Groß, *Neuss, Germany*, Deputy Head at ver.di, North-Rhine Westphalia District

Frank König, *Berlin, Germany*, Staff Member Information Desk and Cash Desk at Adler Modemärkte AG

Peter König [1, 2], *Rottendorf, Germany*, secretary of the national executive board of the ver.di union, other supervisory board positions and comparable memberships: Supervisory Board of BayWa AG

Georg Linder [1, 2, 4], *Hösbach, Germany*, Divisional Head of Procurement Planning and Merchandise Management at Adler Modemärkte AG

Giorgio Mercogliano [3], *Montagnola – Lugano, Switzerland*, partner at Equinox S.A., other supervisory board positions and comparable memberships: Advisory Board of S&E Kapital GmbH

Dott. Michele Puller, *Bergkamen, Germany*, Chairman of the Executive Board of Steilmann Holding AG i.I., Chairman of the Executive Board of Steilmann SE i.I., other supervisory board positions and comparable memberships: SLEEPZ AG (since 18 August 2017), Chairman of the Advisory Board of S&E Kapital GmbH, Member of the Advisory Board of Borussia Dortmund Geschäftsführungs-GmbH, Member of the Council of Economic Affairs of BV. Borussia 09 e.V. Dortmund

Paola Viscardi-Giazzi [2], *Dortmund, Germany*, Executive Board member of Steilmann Holding AG i.I., other supervisory board positions and comparable memberships: Advisory Board of S&E Kapital GmbH

Beate Wimmer, *Nettetal, Germany*, Specialist Consultant Information Desk, Cash Desk and Sales at Adler Modemärkte AG

(Last amended: 31 Dec. 2017) Memberships in: [1)] Personnel Committee, [2)] Audit Committee, [3)] Nomination Committee, [4)] Conciliation Committee

**Chairman of the Committee*

Haibach, 5 March 2018

Thomas Freude
Chairman of the Executive Board

Karsten Odemann
Member of the Executive Board

RESPONSIBILITY STATEMENT

To the best of our knowledge, and in accordance with the applicable reporting principles, the annual financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company, and the management report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the material opportunities and risks associated with the expected development of the Company.

Haibach, 5 March 2018

Thomas Freude
Chairman of the Executive Board

Karsten Odemann
Chairman of the Executive Board

INDEPENDENT AUDITOR'S REPORT

To Adler Modemärkte AG, Haibach

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS AND OF THE GROUP MANAGEMENT REPORT

Audit Opinions

We have audited the consolidated financial statements of Adler Modemärkte AG, Haibach, and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at December 31, 2017, and the consolidated statement of comprehensive income, consolidated statement of profit or loss, consolidated statement of changes in equity and consolidated statement of cash flows for the financial year from January 1 to December 31, 2017, and notes to the consolidated financial statements,] including a summary of significant accounting policies. In addition, we have audited the group management report of Adler Modemärkte AG for the financial year from January 1 to December 31, 2017. We have not audited the content of the statement on corporate governance pursuant to § [Article] 289f HGB [Handelsgesetzbuch: German Commercial Code] and § 315d HGB in accordance with the German legal requirements.

In our opinion, on the basis of the knowledge obtained in the audit,

- the accompanying consolidated financial statements comply, in all material respects, with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315e Abs. [paragraph] 1 HGB and, in compliance with these requirements, give a true and fair view of the assets, liabilities, and financial position of the Group as at December 31, 2017, and of its financial performance for the financial year from January 1 to December 31, 2017, and

- the accompanying group management report as a whole provides an appropriate view of the Group's position. In all material respects, this group management report is consistent with the consolidated financial statements, complies with German legal requirements and appropriately presents the opportunities and risks of future development. Our audit opinion on the group management report does not cover the content of the statement on corporate governance referred to above.

Pursuant to § 322 Abs. 3 Satz [sentence] 1 HGB, we declare that our audit has not led to any reservations relating to the legal compliance of the consolidated financial statements and of the group management report.

Basis for the Audit Opinions

We conducted our audit of the consolidated financial statements and of the group management report in accordance with § 317 HGB and the EU Audit Regulation (No. 537/2014, referred to subsequently as "EU Audit Regulation") and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Our responsibilities under those requirements and principles are further described in the "Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report" section of our auditor's report. We are independent of the group entities in accordance with the requirements of European law and German commercial and professional law, and we have fulfilled our other German professional responsibilities in accordance with these requirements. In addition, in accordance with Article 10 (2) point (f) of the EU Audit Regulation, we declare that we have not provided non-audit services prohibited under Article 5 (1) of the EU Audit Regulation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions on the consolidated financial statements and on the group management report.

Key Audit Matters in the Audit of the Consolidated Financial Statements

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the financial year from January 1 to December 31, 2017. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our audit opinion thereon; we do not provide a separate audit opinion on these matters.

In our view, the matters of most significance in our audit were as follows:

1 Acquisition and further sale of properties in Austria
2 Property leasing
3 Recoverability of deferred tax assets

Our presentation of these key audit matters has been structured in each case as follows:

1 Matter and issue
2 Audit approach and findings
3 Reference to further information

Hereinafter we present the key audit matters:

1 Acquisition and further sale of properties in Austria

1 During the financial year, the Company purchased various retail properties in Austria that it had previously used largely on the basis of finance lease agreements by exercising favorable purchase options. By the end of the 2017 financial year, the properties had been sold on to investors and long-term rental agreements had been concluded in this regard. The Company generated a total profit of EUR 13.4 million from these transactions. In preparing the consolidated financial statements, the Company's executive directors assessed whether the newly concluded rental agreements are to be classified and presented in the consolidated financial statements as finance leases or operating leases. This also involved assessing whether the leasing installments to be paid in accordance with the agreements approximated the market value of the properties and the associated financing costs on the whole. In one case, this led to classification as a finance lease. The corresponding profit from the further sale in the amount of EUR 1.5 million is recognized through profit and loss in line with the regulations governing sale-and-lease-back agreements over the term of the rental agreement. For the other rental agreements, which are classified as operating leases, the corresponding profit was recognized through profit and loss immediately in the full amount of EUR 11.9 million. In view of the material total impact that these property transactions, which were executed by the Company for the first time, have on the amounts of net assets, financial position, and results of operations of the Adler-Modemärkte Group and given the complexity of assessing the contractual agreements, this matter was of particular importance in the context of our audit.

2 For the purposes of our audit and in order to evaluate the proper accounting treatment of the property transactions, we first of all consulted the individual contractual agreements on the acquisitions and further sales, and the rental agreements concluded in this regard, as well as their impact on the financial statements. Within this context, we also assessed the market values and the transfer of benefits and encumbrances for the properties to the buyer in the 2017 financial year. In order to classify the rental agreements as finance leases/operating leases, we reviewed the estimates made by the executive directors based on the contractual agreements presented to us, and also reviewed the valuation assumptions used in this regard. We also verified and assessed the realization of the corresponding profits and the presentation of the property transactions in the Company's financial accounts. In our view, the accounting policies applied by the executive directors and the methodology for accounting for the leases are appropriate overall.

3 The Company's disclosures on the property transactions in Austria are contained in note 30 of the notes to the consolidated financial statements.

2 Property leasing

1 The Company operates its fashion stores in rented premises. In preparing the consolidated financial statements, the Company's executive directors assessed whether the rental agreements concluded by the Company are to be classified and – if necessary – presented in the consolidated financial statements as finance leases or operating leases. In cases involving finance leases, the leased asset is accounted for in a similar way to a loan-financed acquisition transaction, whereas operating leases are not presented in the consolidated statement of financial position and the rental payment is recognized in the consolidated income statement on a straight-line basis. The majority of the existing rental agreements were classified as operating leases by the Company based on the underlying contractual agreements. Buildings are reported as finance leases amounting in total to EUR 44 million (18.3% of total assets) under property, plant and equipment in the Company's consolidated financial statements. In view of the material total impact that the leases have on the amounts of net assets, financial position, and results of operations of the Adler-Modemärkte Group and given the complexity of assessing the contractual agreements, this matter was of particular importance in the context of our audit.

2 As part of our audit, we reviewed, among other things, whether the design and effectiveness of the internal processes and controls for classifying leases, as well as the methodology adopted by the Company for the classification and accounting treatment of leases were appropriate. In order to classify the leases as finance leases/operating leases, we reviewed the estimates made by the executive directors based on the contractual agreements presented to us, and also reviewed the valuation assumptions used in this regard. Based on our audit procedures, we were able to satisfy ourselves that the estimates and assumptions made by executive directors are justified and are suitable overall for the classification of leases and their accounting treatment.

3 The Company's disclosures on property leases are contained in note 10 to the consolidated financial statements.

3 Recoverability of deferred tax assets

1 Deferred tax assets amounting to EUR 10.0 million after netting are reported in the consolidated financial statements of the Company. Deferred tax assets amounting to EUR 22.5 million were recognized before netting with matching deferred tax liabilities. This item was recognized to the extent that the executive directors consider it probable that taxable profit will be available in the foreseeable future which will enable the deductible temporary differences and unused tax losses to be utilized. For this purpose, if insufficient deferred tax liabilities are available, future taxable profits are projected on the basis of the adopted business plan. No deferred tax assets were recognized in respect of deductible temporary differences and unused tax losses amounting in total to EUR 8.3 million since it is not probable that they will be utilized for tax purposes by means of offset against taxable profits. From our point of view, the accounting treatment of deferred taxes was of particular importance in the context of our audit, as it depends to a large extent on the estimates and assumptions made by the executive directors and is therefore subject to uncertainties.

2 As part of our audit, we reviewed, among other things, the internal processes and controls for recording tax matters as well as the methodology adopted for the determination, accounting treatment and measurement of deferred taxes. We also assessed the recoverability of the deferred tax assets relating to deductible temporary differences and unutilized tax losses on the basis of the Company's internal forecasts of its future earnings situation, and we evaluated the appropriateness of the underlying estimates and assumptions. Based on our audit procedures, we satisfied ourselves that the estimates and assumptions made by the executive directors are justified and adequately documented.

3 The Company's disclosures relating to deferred taxes are contained in note 14 of the notes to the consolidated financial statements.

Other Information

The executive directors are responsible for the other information. The other information comprises the statement on corporate governance pursuant to § 289f HGB and § 315d HGB.

The other information comprises further the remaining parts of the annual report – excluding cross-references to external information – with the exception of the audited consolidated financial statements, the audited group management report and our auditor's report.

The separate non-financial report pursuant to § 289b Abs. 3 HGB and § 315b Abs. 3 HGB is expected to be made available to us after the date of the auditor's report.

Our audit opinions on the consolidated financial statements and on the group management report do not cover the other information, and consequently we do not express an audit opinion or any other form of assurance conclusion thereon.

In connection with our audit, our responsibility is to read the other information and, in so doing, to consider whether the other information

- is materially inconsistent with the consolidated financial statements, with the group management report or our knowledge obtained in the audit, or

- otherwise appears to be materially misstated.

Responsibilities of the Executive Directors and the Supervisory Board for the Consolidated Financial Statements and the Group Management Report

The executive directors are responsible for the preparation of the consolidated financial statements that comply, in all material respects, with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB and that the consolidated financial statements, in compliance with these requirements, give a true and fair view of the assets, liabilities, financial position, and financial performance of the Group. In addition the executive directors are responsible for such internal control as they have determined necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the executive directors are responsible for assessing the Group's ability to continue as a going concern. They also have the responsibility for disclosing, as applicable, matters related to going concern. In addition, they are responsible for financial reporting based on the going concern basis of accounting unless there is an intention to liquidate the Group or to cease operations, or there is no realistic alternative but to do so.

Furthermore, the executive directors are responsible for the preparation of the group management report that, as a whole, provides an appropriate view of the Group's position and is, in all material respects, consistent with the consolidated financial statements, complies with German legal requirements, and appropriately presents the opportunities and risks of future development. In addition, the executive directors are responsible for such arrangements and measures (systems) as they have considered necessary to enable the preparation of a group management report that is in accordance with the applicable German legal requirements, and to be able to provide sufficient appropriate evidence for the assertions in the group management report.

The supervisory board is responsible for overseeing the Group's financial reporting process for the preparation of the consolidated financial statements and of the group management report.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements and of the Group Management Report

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and whether the group management report as a whole provides an appropriate view of the Group's position and, in all material respects, is consistent with the consolidated financial statements and the knowledge obtained in the audit, complies with the German legal requirements and appropriately presents the opportunities and risks of future development, as well as to issue an auditor's report that includes our audit opinions on the consolidated financial statements and on the group management report.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with § 317 HGB and the EU Audit Regulation and in compliance with German Generally Accepted Standards for Financial Statement Audits promulgated by the Institut der Wirtschaftsprüfer (IDW) will always detect a material misstatement. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements and this group management report.

We exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements and of the group management report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our audit opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit of the consolidated financial statements and of arrangements and measures (systems) relevant to the audit of the group management report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an audit opinion on the effectiveness of these systems.

- Evaluate the appropriateness of accounting policies used by the executive directors and the reasonableness of estimates made by the executive directors and related disclosures.

- Conclude on the appropriateness of the executive directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements and in the group management report or, if such disclosures are inadequate, to modify our respective audit opinions. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to be able to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements present the underlying transactions and events in a manner that the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and financial performance of the Group in compliance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315e Abs. 1 HGB.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express audit opinions on the consolidated financial statements and on the group management report. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinions.

- Evaluate the consistency of the group management report with the consolidated financial statements, its conformity with German law, and the view of the Group's position it provides.

- Perform audit procedures on the prospective information presented by the executive directors in the group management report. On the basis of sufficient appropriate audit evidence we evaluate, in particular, the significant assumptions used by the executive directors as a basis for the prospective information, and evaluate the proper derivation of the prospective information from these assumptions. We do not express a separate audit opinion on the prospective information and on the assumptions used as a basis. There is a substantial unavoidable risk that future events will differ materially from the prospective information.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the relevant independence requirements, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, the related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter.

OTHER LEGAL AND REGULATORY REQUIREMENTS

Further Information pursuant to Article 10 of the EU Audit Regulation

We were elected as group auditor by the annual general meeting on May 24, 2017. We were engaged by the chairman of the audit committee on July 4, 2017. We have been the group auditor of the Adler Modemärkte AG, Haibach, without interruption since the financial year 2009.

We declare that the audit opinions expressed in this auditor's report are consistent with the additional report to the audit committee pursuant to Article 11 of the EU Audit Regulation (long-form audit report).

GERMAN PUBLIC AUDITOR RESPONSIBLE FOR THE ENGAGEMENT

The German Public Auditor responsible for the engagement is Jürgen Schwehr.

FURTHER INFORMATION

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FINANCIAL CALENDAR

2017 Annual Report	15 March 2018
Report on the first quarter of 2018	8 May 2018
2018 Annual General Meeting	9 May 2018
Report on the first half of 2018	2 August 2018
Report on the first nine months of 2018	8 November 2018

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