

2.6 Supplementary Management Report to the Separate Financial Statements of ZALANDO SE

The management report of ZALANDO SE as a separate entity and the group management report have been combined. The following notes are based on the annual financial statements of ZALANDO SE, which were prepared in accordance with the provisions of the German Commercial Code and the AktG ["Aktiengesetz": German Stock Corporation Act] in conjunction with Art. 61 EU CR 2157/2001.

2.6.1 Business Activity

ZALANDO SE is the parent company of the Zalando group. Its registered office is the corporate headquarters in Berlin. Its operating activities mainly include the development, sourcing, marketing and retail sale of various types of goods, in particular clothing and shoes. Other responsibilities include management of the online shops, HR management, IT, finance management and risk management. The country-specific websites of Zalando as well as the websites of Zalando Lounge are part of ZALANDO SE.

GRI 102-3

As the parent company of the group, ZALANDO SE is represented by its Management Board, which sets the direction of the group and defines the corporate strategy.

The financial statements of ZALANDO SE are prepared in accordance with the German Commercial Code. The consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted in the EU. This gives rise to differences in recognition and measurement policies. The differences primarily relate to provisions, fixed assets, financial instruments, deferred taxes.

In addition, ZALANDO SE has extensive supply and service relationships with its subsidiaries. The services purchased essentially encompass fulfillment and distribution services, content creation and customer service as well as procurement services.

The services ZALANDO SE provides to its subsidiaries comprise administrative and IT services.

2.6.2 Economic Situation of ZALANDO SE

The results of operations of ZALANDO SE presented in the following condensed income statement broken down by the type of expense reveal revenue growth with solid profitability in the reporting period.

GRI 103-1/-2/-3 MA
Economic Performance
GRI 201-1

Income Statement of ZALANDO SE According to German Commercial Code (Short Version)

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IN EUR M	Jan 1 – Dec 31, 2017	As % of sales	Jan 1 – Dec 31, 2016	As % of sales	Change in percentage points
Revenue	4,479.6	100.0%	3,650.7	100.0%	0.0pp
Own work capitalized	36.5	0.8%	45.2	1.2%	-0.4pp
Other operating income	48.9	1.1%	50.7	1.4%	-0.3pp
Cost of materials	-2,533.9	-56.6%	-2,043.3	-55.9%	-0.7pp
Gross profit	2,031.1	45.3%	1,703.3	46.7%	-1.3pp
Personnel expenses	-278.8	-6.2%	-227.4	-6.2%	0.0pp
Amortization and depreciation	-37.4	-0.8%	-27.0	-0.7%	-0.1pp
Other operating expenses	-1,545.6	-34.5%	-1,245.9	-34.2%	-0.3pp
Earnings before interest and taxes	169.4	3.8%	203.0	5.6%	-1.8pp
Financial result	0.2	0.0%	-4.4	-0.1%	0.1pp
Results from ordinary business activities	169.6	3.8%	198.6	5.4%	-1.7pp
Income taxes	-64.4	-1.4%	-65.7	-1.8%	0.4pp
Net income for the year	105.1	2.3%	132.9	3.6%	-1.3pp
EBIT margin	3.8%		5.6%		-1.8pp

In the reporting period, Zalando increased its revenue by EUR 829.0m to EUR 4,479.6m. The 22.7% increase in revenue is the result of the higher number of orders (30.8%) and a larger customer base. Zalando continued its positive development in all markets.

In the current fiscal year, the DACH countries generated more than half of the 24 total revenue. At the same time, revenue recorded in the other European countries climbed significantly, contributing substantially to overall growth.

Revenue of ZALANDO SE by Segment

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IN EUR M	2017		2016		Change	
DACH*	2,350.1	52.5%	1,952.0	53.5%	398.1	20.4%
Rest of Europe**	2,129.5	47.5%	1,698.7	46.5%	430.8	25.4%
Total	4,479.6	100.0%	3,650.7	100.0%	828.9	22.7%

*) As in fiscal 2016, DACH countries include Germany, Austria and Switzerland.

***) As in fiscal 2016, the Rest of Europe comprises the Netherlands, France, Italy, the United Kingdom, Poland, Belgium, Sweden, Finland, Denmark, Spain, Norway and Luxembourg.

Other operating income mainly results from income from foreign currency translation.

The cost of materials rose by EUR 490.6m to EUR 2,533.9m, in line with the expansion of business. The increase of 0.7 percentage points in the ratio of the cost of materials to revenue to 56.6% can be primarily attributed to a higher discount level in fiscal year 2017. Overall, the company generated a gross profit of EUR 2,031.1m in fiscal year 2017 (prior year: EUR 1,703.3m).

Personnel expenses rose by EUR 51.4m to EUR 278.8m, in line with the rise in the number of employees. As of December 31, 2017, the headcount increased by 365 on the prior year from 3,929 to 4,294 employees.

Other operating expenses primarily include marketing expenses as well as shipping and fulfillment costs. The cost ratio as a percentage of revenue (34.5%) is slightly below the previous year. The increase in the fulfillment cost ratio, which is mainly driven by the extension of the logistics network, was not fully compensated for by lower marketing costs resulting from efficiency gains in particular within performance marketing.

The EBIT for the year of EUR 169.4m decreased by 1.8 percentage points mainly due to a lower gross profit margin and a higher fulfillment cost ratio.

The financial result comprises income from profit transfers of EUR 6.6m (prior year: EUR 4.4m) mainly from the profits generated by the outlets in Berlin, Frankfurt and Cologne during the reporting period.

Income taxes include the deferred taxes and current income taxes paid or payable. They comprise trade tax, corporate income tax and the solidarity surcharge. As in the prior year, the statutory corporate income tax rate, including the solidarity surcharge, for the assessment period 2017 was 15.8%. The applicable trade tax rate was 14.8% as in the prior year.

Current and deferred taxes are presented in the following table.

Income Taxes

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IN EUR M	Jan 1 – Dec 31, 2017	Jan 1 – Dec 31, 2016
Deferred taxes	-21.1	-41.8
Current taxes in Germany	-43.3	-23.9
Total	-64.4	-65.7

In fiscal year 2017, deferred tax liabilities of EUR 16.5m were recognized mainly due to the capitalization of intangible assets.

Net Assets and Financial Position

The net assets of ZALANDO SE are shown in the following condensed statement of financial position.

Assets

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IN EUR M	Dec 31, 2017		Dec 31, 2016		Change
Non-current assets	620.3	21.2%	461.8	17.9%	158.5
Current assets	2,292.8	78.3%	2,091.8	81.3%	201.0
Prepaid expenses	14.3	0.5%	15.4	0.6%	-1.1
Deferred tax assets	0.0	0.0%	4.5	0.2%	-4.5
Total assets	2,927.4	100.0%	2,573.5	100.0%	353.9

Equity and Liabilities

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IN EUR M	Dec 31, 2017		Dec 31, 2016		Change
Equity	1,569.0	53.6%	1,444.0	56.1%	125.0
Special items for government grants	0.2	0.0%	0.1	0.0%	0.1
Provisions	250.9	8.6%	237.2	9.2%	13.7
Liabilities	1,087.1	37.1%	890.5	34.6%	196.6
Deferred income	3.7	0.1%	1.7	0.1%	2.0
Deferred tax liabilities	16.5	0.6%	0.0	0.0%	16.5
Total equity and liabilities	2,927.4	100.0%	2,573.5	100.0%	353.9

The total assets of ZALANDO SE rose by around 13.8% as a result of the further increase in business volume. The assets of the company primarily consist of current assets, specifically inventories and cash and cash equivalents. Equity and liabilities exclusively comprise equity and current liabilities and provisions.

In fiscal year 2017, investments focused on intangible assets (EUR 46.4m) and financial assets (EUR 135.2m). Investing activities were financed exclusively from the group's own funds.

In fiscal year 2017, inventories solely comprised merchandise used in the core operational business of ZALANDO SE.

As of December 31, 2017, ZALANDO SE's trade receivables were up EUR 84.0m to EUR 387.2m.

With regard to the liquidity and the financial development of ZALANDO SE, we refer to the financial development of the Zalando group. The financial development of Zalando group essentially reflects the financial development of ZALANDO SE. Furthermore, ZALANDO SE is responsible for the cash management of the Zalando group.

In the past fiscal year, Zalando generated positive cash flow from operating activities of EUR 200.3m (prior year: EUR 252.9m). The cash flow was influenced by lower cash inflow from working capital, cash outflows for VAT liabilities and receivables and lower cash inflows from recognizing reimbursement obligations towards customers.

The cash flow from investing activities in fiscal year 2017 was mainly driven by capital increases in subsidiaries that were used to invest in the fulfillment infrastructure as well as to further expand the respective business segments of the subsidiaries. Cash and cash equivalents consist of cash on hand and bank balances as well as fixed-term deposits due within three months at credit institutions and in disposable money market funds.

The equity ratio stood at 53.6% (prior year: 56.1%).

Provisions and liabilities increased by EUR 210.3m to EUR 1,338.0m, in line with the expansion of the business. As of December 31, 2017, this figure mainly pertains to provisions for expected returns, outstanding invoices for fulfillment and marketing expenses and trade payables.

Reverse factoring agreements are in place with various suppliers and with several financial institutions. Under these agreements, the factor purchases the respective supplier receivables due from Zalando. Supplier claims against Zalando based on these agreements totaling EUR 328.9m had been transferred to the factor as of December 31, 2017 (prior year: EUR 282.3m). This amount is recognized in the balance sheet under trade payables.

2.6.3 Risks and Opportunities

The business development of ZALANDO SE is subject to largely the same risks and opportunities as the group. ZALANDO SE fully participates in the risks of its subsidiaries. Statements made by the Management Board on the overall assessment of the group's risk situation thus also summarize the risk situation of ZALANDO SE. The description of ZALANDO SE's accounting-related internal control system and risk management system stipulated in Section 289 (5) HGB ["Handelsgesetzbuch": German Commercial Code] is provided in the Risk and Opportunity Report of the group.

2.6.4 Outlook

The statements made on market trends and the development of revenue and the results for the group also apply here by virtue of the close ties between ZALANDO SE and the group companies and its weight within the group. The statements also reflect the expectations for the parent company.

Berlin, February 26, 2018

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