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PEGAS NONWOVENS SA

annual report 2006

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PEGAS NONWOVENS SA
annual report 2006

PEGAS
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Table of Contents

1 About the Company .... page 4

2 2006 Key Figures .... page 8

3 2006 – A Year of Outstanding Performance .... page 10

4 Statement from the Chief Executive Officer .... page 14

5 Investor Information .... page 16

6 Board of Directors Report on Business Activity .... page 18

6.1 Description of the Company Business and Market | 6.1.1 Overview of the Nonwoven Market | 6.1.2 Description of Company's history and business | 6.1.3 Overview of Company's Products | 6.2 Technology and Production | 6.2.1 Technology | 6.2.2 Production Process | 6.3 Plants and Premises | 6.4 Customers | 6.5 Suppliers | 6.6 Quality Management and Environment | 6.6.1 Quality Management System | 6.6.2 Environmental Management System | 6.7 R&D | 6.7.1 Development and Technical Support | 6.7.2 Intellectual Property | 6.8 Strategy | 6.8.1 The Company's Strategy and Outlook | 6.9 Human Resources | 6.9.1 Employees | 6.10 Comments on Financial Results | 6.11 Czech Investment Incentives

7 Corporate Governance .... page 39

7.1 Organizational Structure and its Development | 7.2 Board of Directors | 7.3 Remuneration of directors and management | 7.4 Corporate Governance | 7.5 Risk Factors

8 Consolidated Financial Statements and Notes to the Financial Statements, Independent auditor's report .... page 68

8.1 Independent Auditor's Report | 8.2 Consolidated Statement of Income for the Year end December 31st | 8.3 Consolidated Balance Sheet as at December 31st | 8.4 Consolidated Cash Flow Statement for the Year end December 31st | 8.5 Consolidated Statement of Changes in Equity for the Year end December 31st, 2006 | 8.6 Notes to Consolidated the Financial Statements | 8.6.1 General Information and Definition of the Consolidated Entity | 8.6.2 Basis of Preparation | 8.6.3 Summary of Significant Accounting Policies | 8.6.4 Financial Risks | 8.6.5 Notes to the Consolidated Financial Statements | 8.6.6 Related Parties transactions | 8.6.7 Contingencies and Commitments | 8.6.8 Material Subsequent Events

9 Other information .... page 100

9.1 Basic Information on the Company

CD Presentation

1 About the Company

PEGAS NONWOVENS SA ("PEGAS" or the "Company" or "Group") is one of the leading European producers of nonwoven textiles for use primarily in the personal hygiene products market. PEGAS supplies its customers with spunbond and meltblown (together, "spunmelt") polypropylene and polypropylene/polyethylene ("PP" and "PP/PE") based textiles principally for use in disposable hygiene products (such as baby diapers, adult incontinence and feminine hygiene products) and, to a lesser extent, in construction, agricultural and medical applications.

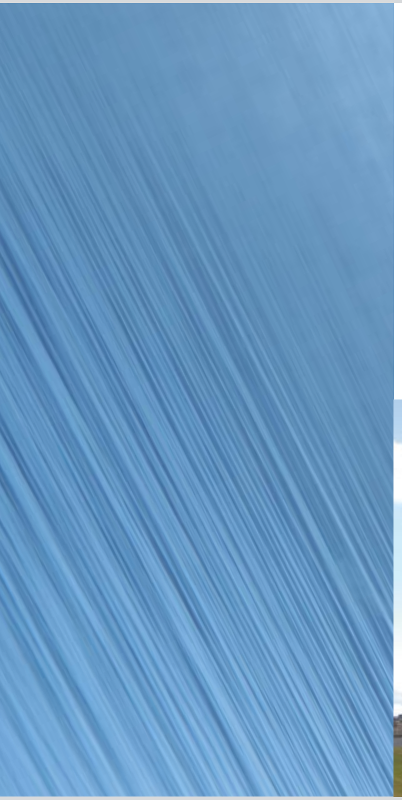
At the end of 2006, PEGAS was Europe's second largest producer, in terms of tonnage output, of PP and PP/PE based spunmelt nonwoven, with a market share of approximately 10.3% of European production capacity and a market share of approximately 19% by volume of nonwovens destined for European manufacturers of personal hygiene products.

PEGAS consists of a parent holding company in Luxembourg, a Czech holding company and four operating companies PEGAS NONWOVENS s.r.o., PEGAS - DS a.s., PEGAS-NT a.s. and PEGAS - NW a.s. all located in the Czech Republic. By the end of 2006, PEGAS employed 327 people.

Shares in PEGAS are listed on the Prague Stock Exchange and on the Warsaw Stock Exchange, following an Initial Public Offering in December 2006. The Company's largest shareholder is a private equity fund, Pamplona Capital Partners I, LP which holds a 43.4% stake. The Company's senior management holds together 2.0% of the shares. Other institutional and retail investors hold 54.6% of PEGAS's shares.

01

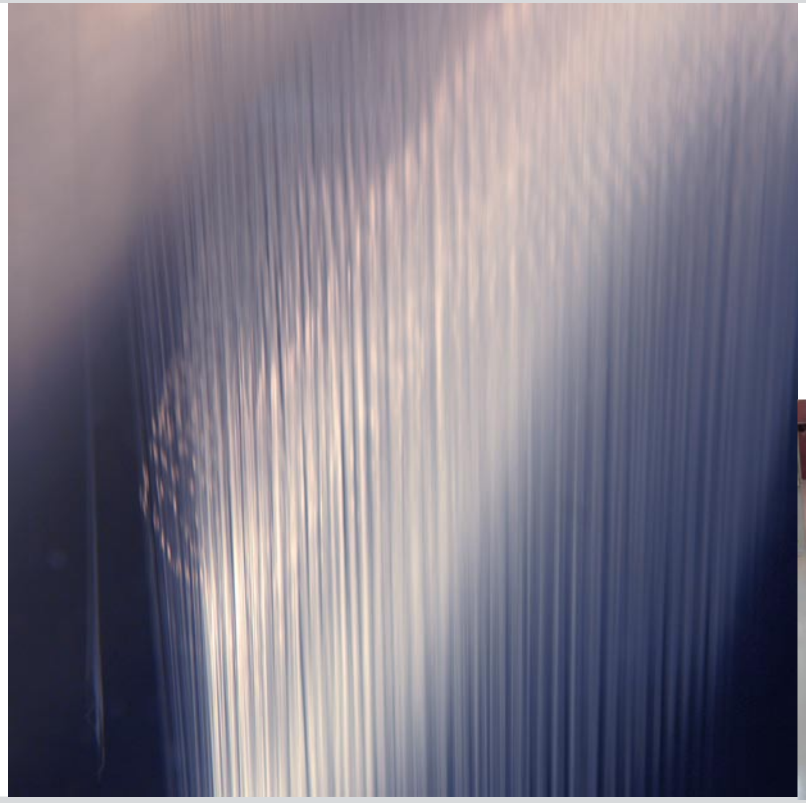
Production



The main raw materials used for spunmelt nonwoven are polymers, most importantly polypropylene followed by polyethylene, which are petroleum derivatives.

PEGAS owns and operates technologically advanced equipment necessary to produce high-quality spunmelt nonwoven textiles.

Nonwoven textiles are fiber-based textiles which are neither woven nor knitted, but are made from polymer fibers which are bonded together with pressure and heat.



Nonwoven materials are used in a wide range of applications, including: disposable hygiene, medical, home, leisure and travel, clothing, agriculture, automotive, construction and furniture.

Approximately 15 fully loaded trucks carry the goods to customers every day.

In 2002, the Company introduced BiCo production technology, reinforcing its strong European market position in manufacturing specialized nonwoven textiles.

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2 2006 Key Figures

Financials (Euro thousands)	*2004*[1]	*2005*[1]	*2006*
Total Revenues	72,819	109,491	120,941
EBITDA	29,317	40,680	53,263
Adjusted EBITDA	29,317	40,680	42,060[2]
Adjusted Profit from Operations	21,771	30,770	29,908[2]
Net Profit for the Period	18,021	26,637	20,705
No. of Shares	na	100,806	9,229,400
Total Assets	na	250,569	249,025
Total Equity	na	3,186	76,950
Total Borrowings	na	173,518	136,171
Net debt/ (Net cash balance)	na	183,200	114,157
CAPEX	16,150	11,042	5,265
Ratios			
Adjusted EBITDA Margin	40.3%	37.2%	34.8%[2]
Adjusted Operating Profit Margin	29.9%	28.1%	24.7%[2]
Net Profit Margin	24.7%	24.3%	17.1%
CAPEX as % of Revenues	22.2%	10.1%	4.4%
Operations			
Total Production Output (in tonnes net of scrap)	37,142	51,267	54,159
Number of Employees - End of Period (EOP)	311	312	327
Exchange Rates			
CZK/ Euro average	31.904	29.784	28.343
CZK/ Euro EOP	30.400	29.005	27.495

1 Audited Income Statement under IFRS of Pegas a.s. and audited Balance Sheet under IFRS of PEGAS NONWOVENS SA
2 Adjusted by Foreign Exchange (FX) diff erences and Mark-to-Market revaluation of Interest Rate Swaps for 2006 only

3 2006 – A Year of Outstanding Performance

The year to December 31st, 2006 was a very successful one for PEGAS in terms of both operational and financial performance. Its main highlights are summarised below:

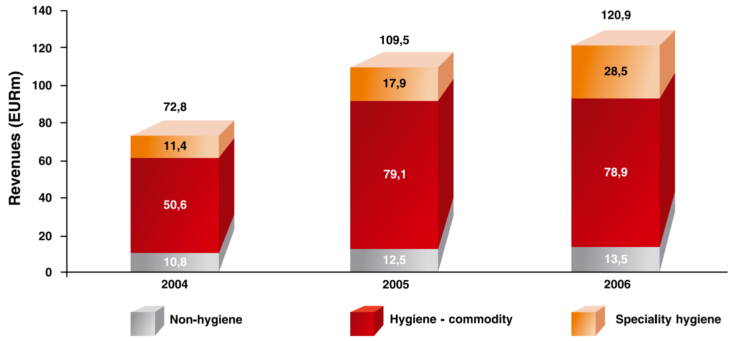
Financials

PEGAS's principal focus was on growing revenues from specialty products where margins are typically higher. Specialty products[3] accounted for 23.6% of revenues in 2006 compared with 16.3% in 2005. Revenues from sales of nonwoven textiles for the hygiene industry were 88.8% of total revenues in 2006. This was similar to the proportion of hygiene revenues in 2005 which was 88.6%.

Revenues from sales of specialty products in the hygiene segment amounted to Euro 28.5 million, up by 59% yoy. Revenues from sales of standard textiles for hygiene products reached Euro 78.9 million, a reduction of 0.3% in comparison with 2005. Revenues from sales of non-hygiene products (for construction, agriculture and medical applications) amounted to Euro 13.5 million in 2006, an increase of 8.0% over 2005.

Specialty Hygiene as a % of Revenues (2004 – 2006)

PEGAS increased its adjusted EBITDA[4] by 3.4% from Euro 40.7 million in 2005 to Euro 42.1 million in 2006. This increase was due to higher proportion of specialties sales and higher production output.



TOTAL REVENUES 2004 – 2006 CAGR: 28.9 %

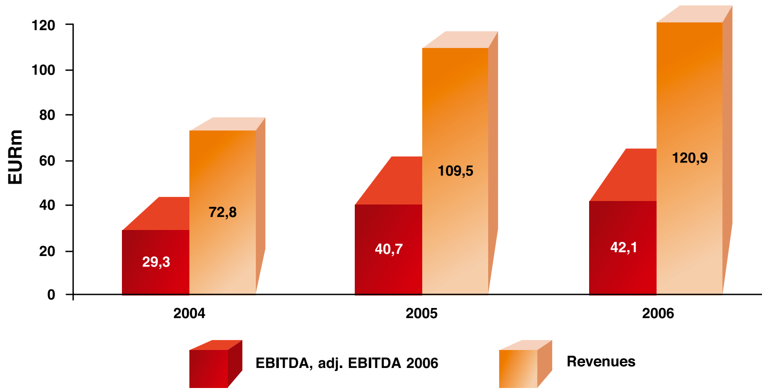
3 The Company defines speciality products as bi-component nonwovens and lightweight materials. Specialty products offer higher margins than standard textiles.

4 Adjusted EBITDA includes revenues for sold products, raw material and consumables used /incl. R&D expense, staff costs and other net operating income/(expense), excluding realized and unrealized FX changes as of December 31st, 2006 and mark-to-market revaluation of the interest rate swaps.

Net profit in 2006 amounted to Euro 20.7 million, down by 22.3% yoy, due to higher finance costs (Euro 18.8 million in 2006 compared with Euro 0.2 million in 2005).

PEGAS substantially reduced its consolidated financial debt at December 31st, 2006, down by 35.2% compared with December 31st, 2005[5]. In addition, the Company repaid all of its most expensive debt (shareholder debt and mezzanine debt) and part of its amortising senior debt, using proceeds from the Initial Public Offering (IPO) in December 2006 and its own generated cash. Net debt at December 31st, 2006 was therefore Euro 114.2 million, down by 37.7% compared with 2005. The ratio of Net Debt / Adjusted EBITDA was 2.7 times at December 31st, 2006.

EBITDA and Revenues (2004 – 2006)



EBITDA 2004 – 2006 CAGR: 19.8 %

5 Year on year comparison 2006 vs. 2005 for PEGAS NONWOVENS SA

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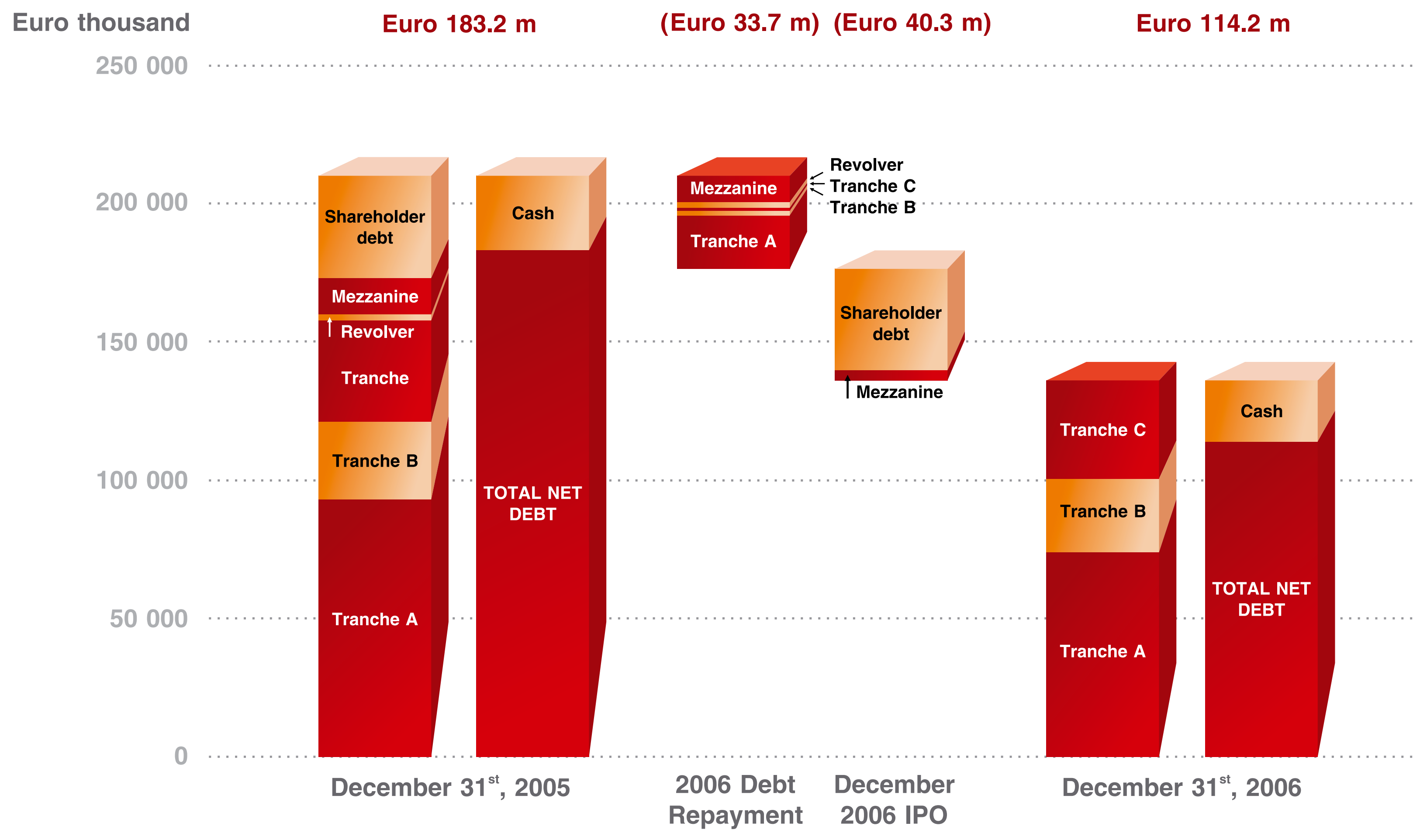
Development of Company's Indebtedness in 2006



Initial Public Offering

On November 27th, PEGAS launched an Initial Public Offering of its shares at a price of Euro 27 per share. The IPO consisted of the offer of 5,042,750 shares in total, including a Primary Offering of 1,810,000 shares and a Secondary Offering of 3,232,750 shares which were offered by the selling shareholder Pamplona Capital Partners I, LP. The IPO was highly successful and PEGAS received strong market support, which was demonstrated by the significant oversubscription for shares and pricing at the top of the offer range.

New Production Line

The new production line is currently under construction and is due to enter service in the fourth quarter of 2007. The construction of the building which will house the new line started in October 2006, in March 2007 installation of the line itself began. It will be the Company's eighth line and will enable a rapid increase in production capacity from the current 54.2 thousand tonnes per annum to approximately 69 thousand tonnes per annum in 2008 (based on current production basis weights). The line will also allow the Company to increase the proportion of its sales which are specialty products.

Production

Although the Company did not install any new production equipment in 2006, the Group was able to increase total output by 5.7% from 51.3 thousand tonnes in 2005 to 54.2 thousand tonnes in 2006 owing to improved production efficiencies.

TOTAL OUTPUT YEAR END 2004 – 2006 CAGR: 20.8%

4 Statement from the Chief Executive Officer

Dear Shareholders

It is my great pleasure to introduce PEGAS to you for the first time as a publicly listed company. I appreciate and would like to thank you for the confidence you have shown in the Company in supporting its Initial Public Offering in December 2006.

I am very pleased with our achievements in 2006 in both operational and financial terms as well as with the changes we have made in corporate governance. In 2006 PEGAS was transformed from a private company, owned by a private equity fund and its management, to a publicly listed company which is actively traded on the two stock markets in Prague and Warsaw. Operationally, the Company continued its double digit revenue growth and remained at the leading edge of new technologies in the production of nonwoven spunmelt textiles.

In 2005, Pamplona Capital Partners I, LP ("Pamplona") acquired a 100% stake in the Group from its previous owners. Pamplona's international experience has contributed significantly to the further development of the Company, particularly in the area of financing, capital markets and corporate governance.

We made two changes to our corporate structure in 2006. The first was the merger of Pegas a.s. (the entity acquired by Pamplona) into PEGAS NONWOVENS s.r.o. (the special purpose vehicle established by Pamplona to effect the acquisition). The sole purpose for this merger was to effect the security for the acquisition loans and it had no impact on the Company's trading. The second significant corporate change we made was the strengthening of the board of directors of PEGAS NONWOVENS SA which now consists of four executive and four non-executive directors. The purpose of this move was to protect the interests of all shareholders and to achieve the best market standards of corporate governance of publicly listed companies.

In December 2006, PEGAS successfully completed its IPO on the Prague and Warsaw stock exchanges at a price of Euro 27 per share. The IPO was significantly oversubscribed confirming a strong interest from investors in PEGAS's success story. We currently have 54.6% of the Company's shares placed in the hands of institutional and retail investors as well as the 43.4% stake held by Pamplona and the 2.0% stake held by the management. I strongly believe that PEGAS is a fundamentally strong company with a superior production programme and, as such, will continue to deliver high returns to its shareholders in future years.

Our financial performance in 2006 confirmed our unique position as a market leader in technology and a top producer of spunmelt nonwovens in Europe. Our revenues increased because of increases in input prices and a better mix of sales. In addition, the actual production output went up owing to better utilisation of our current production capacity, although we did not add any new capacity last year. We have significantly reduced our total debt acquired in 2005 by almost 40% using both the IPO proceeds and our own generated cash. High revenue generation, strict cost control and our determination to reduce finance costs enabled us to remain profitable with a solid net profit margin despite some inevitable costs related to the IPO and to changes in our Company structure.

Our principal focus in 2006 was on growing revenues from specialty products with a higher added value for our customers and we have delivered our financial targets in this area beyond expectations. We managed to grow the share of specialty products to 23.6% of revenues (Euro 28.5 million) in 2006 from 16.3% (Euro 17.9 million) in 2005 - an increase of almost 60%.

We are strongly determined not only to increase our share of our current markets, but also to tap into new markets in upcoming years. In October 2006, we started with the installation of our new eighth production line which will enter service in the fourth quarter of 2007. This new capacity will enable a rapid increase in production capacity by more than 27% in 2008. The configuration and design of the new production line continues our track record of installing and commissioning world-leading technology at regular two to three year intervals. It is designed to keep us at the leading edge of nonwovens technology and to maintain our margins at a high level.

The eighth production line, which will again represent the most advanced technology available in the world, will enable PEGAS to produce ultra lightweight materials for the hygiene market and also to step into the medical market.

PEGAS's successful track record of world leading technology and operational excellence has been supported by its strong management team, by the expertise of its personnel, and by the team's commitment and professional attitude. In particular, the technical know-how of our managers and employees has been crucial in retaining our competitive edge in technology, our competitive advantage over our global market rivals, our improved production efficiencies and the top quality of our production in 2006.

Looking ahead, our future success will be based on a strategy of (1) increasing our production capacity, (2) increasing the proportion of sales from specialty products which offer higher margins, and (3) maintaining our low cost base.

Our eighth production line will be launched in late 2007 and will increase our production capacity by more than 27% in 2008. Further production capacity will be added in future years. We will continue to develop new, higher margin specialty products in close cooperation with our key customers, raw material suppliers and machinery suppliers. We will maintain our low cost base through further improvements in efficiency and through locating production capacity either in the Czech Republic or in lower cost economies. In addition, we will further simplify the Company's corporate structure which will reduce costs and bring increased transparency to the group.

I am confident that PEGAS' strengths and clear strategy will maintain the Company as a leader in the spunmelt nonwovens market, will allow us to increase market share and will enable us to generate attractive returns for our shareholders.

Miloš Bogdan

CEO of PEGAS NONWOVENS s.r.o. and
member of the Board of Directors of PEGAS NONWOVENS SA

5 Investor Information

Shareholders as of December 31st, 2006	
Pamplona Capital Partners I, LP	43.4%
Management	2.0%
Free Float	54.6%

IPO Overview	
Date of launch	November 27th, 2006
No. of shares offered	5,042,750
Of which newly issued shares	1,810,000
Of which shares offered by selling shareholder	3,232,750
Nominal value of each share (in Euro)	1.24
Issue share price (in Euro)	27.00
Total number of shares as at December 31st, 2006	9,229,400
Market capitalization as at issue date (Euro million)	249.2
Market capitalization as at December 31st, 2006 (Euro million)	252.9
Net profit/(loss) per share (Euro)	2.20
Share price EOP (Euro)[6]	27.4

In December 2006, PEGAS completed an IPO of its shares at a price of Euro 27.00 per share. The IPO consisted of the offer of 5,042,750 shares in total, including 1,810,000 shares newly issued in the Company's share capital and 3,232,750 shares offered by the selling shareholder Pamplona Capital Partners I, LP. Shares of PEGAS NONWOVENS SA were listed on the Prague Stock Exchange and on the Warsaw Stock Exchange on December 21st, 2006. The shares are in registered form. The nominal value of one share is Euro 1.24 each. The aggregate nominal value of the issued share capital is Euro 11,444,456. The shares are traded on the Prague Stock Exchange with ISIN LU0275164910 BAAPEGAS and on the Warsaw Stock Exchange under PGS. The shares of PEGAS NONWOVENS SA are as of March 19th, 2007 part of the PX index, which covers the shares of all major issuers on the Prague Stock Exchange.

[6] Based on ČNB rate CZK/Euro 27.495, December 29th, 2006

Changes in the Shareholders Structure in 2006

Prior to the IPO, Pamplona Capital Partners I, LP held 97.5% of the share capital of the Company and remaining 2.50% was held by the management of the Company. Following the IPO and exercise of the Overallotment Option, Pamplona Capital Partners I, LP owned 43.4% of the issued share capital while the combined management shareholding was 2.0%. The remaining 54.6% of the share capital offered through the IPO is currently held by institutional and retail investors (the “free float”).

PEGAS's Investor Relations Committment

In the period since the IPO, PEGAS has focused on developing research coverage for the Company, developing relationships with analysts and setting up investor relations communication according to best market standards. At present, the Company has 5 analysts who publish research on the Company and a number of other analysts from both international investment banks and local Czech financial institutions who comment from time to time. The Company considers this level of coverage very encouraging.

PEGAS is further dedicated to an open and pro-active communication with its shareholders and has implemented a schedule of investor communications events which is fully compliant with market standards for listed companies. After each financial results announcement, the Company organises either conference calls with analysts or analyst meetings to ensure that the investor community has adequate access to senior management. In addition, PEGAS plans to participate in investor conferences in key European financial centres as well as to visit investors regularly on roadshows.

Financial Results Calendar for 2007

May 30th, 2007

Q1 2007 unaudited consolidated financial results of PEGAS NONWOVENS SA in accordance with IFRS

August 30th, 2007

Q1 – Q2 2007 unaudited consolidated financial results of PEGAS NONWOVENS SA in accordance with IFRS

November 29th, 2007

Q1 – Q3 2007 unaudited consolidated financial results of PEGAS NONWOVENS SA in accordance with IFRS

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6 Board of Directors Report on Business Activity

6.1 Description of the Company Business and Market

6.1.1 Overview of the Nonwovens Market

The global nonwovens market has grown by 7.41% CAGR since 1994 and is valued at Euro 12.45 billion (4.43 million tonnes of production) at the end of 2005. The market is expected to continue this growth path as technological advances increase the material's application range and emerging markets continue to grow.

The relevant market for PEGAS is the European market (including Western Europe, Central and Eastern Europe and Russia) and this market reached 1.44 million tonnes of production or Euro 4.6 billion of value and represented approximately 30% of the global nonwovens market in 2005.

Nonwoven textiles are fiber-based textiles which are neither woven nor knitted, but are made from polymer fibers which are bonded together with pressure and heat. They take on many different forms and can be produced using different technologies. The rapidly growing PP and PP/PE based personal hygiene segment in particular requires sophisticated technology to produce special properties in the products and to customize them for specific functional properties and applications.

Nonwoven materials are used in a wide range of applications, including: disposable hygiene, medical, home, leisure and travel, clothing, agriculture, automotive, construction and furniture.

The Company's core product market is the European personal hygiene sector, which was valued at Euro 1.38 billion per annum in 2005 and which represented approximately 33% in tonnage of the total European nonwovens market. This sector consists of three major products: disposable baby diapers (which in 2005 accounted for approximately 70% of the market by value), adult incontinence products (20%) and feminine hygiene (10%).

Substitution effect from carded to spunmelt technology

The nonwoven market is segmented into different process technologies which have historically focused on specific industries, based on their attributes. Carded nonwovens can be customized to combine different material fibers in multiple layers. Over time, the market has shifted away from carded nonwovens, since they are increasingly expensive owing to the higher weight per square meter required for equivalent mechanical strength. In addition, technologically advanced processes have simplified and quickened the production of spunmelt nonwovens.

The substitution has largely taken place already and leading hygiene product manufacturers have mostly adapted to the new technology. It is anticipated that the annual substitution from carded to spunmelt will be approximately 12 thousand tonnes by 2009.

As the carded-to-spunmelt substitution effect slows and polypropylene prices rise, the market focus is increasingly turning to reducing input costs through manufacturing lighter nonwovens. PEGAS has modern production machinery which is capable of manufacturing light-weight textiles. This creates additional cost benefits for customers.

Competition

The following table illustrates the main competitors of PEGAS and their estimated gross capacity levels of spunmelt PP- and PP/PE-based nonwovens in Europe in 2006.

In 2006, PEGAS ranked second in Europe in terms of spunmelt PP- and PP/PE-based production capacity, with an estimated 10.3% market share in terms of installed capacity.

PEGAS is a member of the European Disposables and Nonwovens Association (EDANA) with representatives on the Board and on various committees.

Producer	*Country*	*Annual Capacity (thousand tonnes)*	*Share*
BBA	United Kingdom	96.5	18%
PEGAS	Czech Republic	54.2	10%
Tesalca/Texnovo	Spain	46.0	9%
Avgol	Israel	34.0	7%
Union	Italy	32.5	6%
Fibertex	Denmark	29.0	6%
Gülsan	Turkey	29.0	6%
Radici	Italy	26.0	5%
Dounor	France	22.5	4%
Other		154.2	29%
Total		***523.9***	***100%***

6.1.2 Description of Company's history and business

PEGAS a.s., the predecessor of PEGAS NONWOVENS s.r.o, the main trading entity of the Group, was established in 1990. It soon developed into a producer of nonwoven textiles based on polypropylene, which has remained its core activity. In 1992, the Company installed its first production line for nonwoven textiles using spunmelt technology, supplying customers mainly in the agricultural industry. During this time, the Company began to develop its technological expertise in nonwoven textile production, benefiting in particular from its close cooperation with one of the leading suppliers of spunmelt manufacturing equipment, and with customers active in supplying personal hygiene products.

Following the installation of the second production line in 1996, the Company tripled its production capacity and began concentrating its operations in the hygiene market. From 1996 onwards, the Company continued to expand its capacity, by acquiring technologically advanced production equipment which combined spunmelt and meltblown technologies. In 2002, the Company introduced BiCo production technology, reinforcing its strong European market position in manufacturing specialized nonwoven textiles. In 2003, another of the production lines was equipped to enable the production of BiCo nonwovens.

In 2002 and 2003, the Company focused on further efficiency and quality improvements through the introduction of optical control equipment and an air management system on each of its production lines. In late 2004, the Company launched its seventh production line, a high-speed spunmelt line, to meet the increased customer demand. PEGAS has grown over the last 16 years since its foundation through the installation of a total of seven production lines. Each of the production lines, at the time of its installation, was among the most technologically advanced in commercial operation anywhere in the world. Of the current seven production lines, five lines (which account for approximately 90% of production capacity), remain among the most technologically competitive. In 2006, the Company's production of spunmelt nonwoven (net of scrap) reached 54,159 tonnes.

In the fourth quarter of 2007, PEGAS is planning to install its new eighth production line, which is expected to have an annual production capacity of approximately 15 thousand tonnes (based on current production basis weights) and will be able to produce ultra-lightweight nonwovens. This will also permit a more effective utilization of our bicomponent lines which currently produce both bicomponent and mono-component materials.

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6.1.3 Overview of Company's Products

In 2006, 88.8% of PEGAS's output was sold for final processing in the personal hygiene sector, which accounted for 88.8% of the Company's total sales in 2006. PEGAS's spunmelt nonwoven materials are used for various components of baby diapers and adult incontinence products, such as the core wrap, topsheet (in contact with the skin), backsheet (the waterproof containment component) and barrier cuffs (which seal the product against the legs), as well as for feminine hygiene products.

In 2006, approximately 26.5% of the Company's sales of hygiene products consisted of specialty products. The proportion of specialty hygiene products has increased in recent years, and the Company's strategy is to increase this still further in future years.

BiCo products are manufactured using both PP and PE, and are either pure spunmelt or SMS-type textiles ("S" indicates a spunbond layer, "M" indicates a meltblown layer). BiCo nonwoven are attractive to PEGAS's customers because of their comfort qualities when in contact with the most sensitive parts of human skin, and their higher extensibility compared with PP-based products. BiCo products are typically used in baby diapers and feminine hygiene products.

The Company's remaining production, approximately 11.2% of sales in 2006, is sold for use in non-hygiene applications. Although the percentage of total sales for these applications is relatively small, PEGAS intends to maintain production levels for these products, as they provide sufficient margins and product portfolio diversification. The Company's non-hygiene products are used in construction, agricultural and medical applications.

The table below provides a breakdown of the Company's sales and production by product type and geographical market:

For the year end December 31st (Euro thousands)						
	2006		*2005*		*2004*	
		% of total		% of total		% of total
Hygiene Sales						
Hygiene-specialty	28,498	23.6	17,886	16.3	11,398	15.7
Hygiene-other	78,870	65.2	79,142	72.3	50,601	69.5
Total hygiene	**107,368**	**88.8**	**97,028**	**88.6**	**61,999**	**85.1**
Non-hygiene	**13,573**	**11.2**	**12,463**	**11.4**	**10,820**	**14.9**
Total sales	**120,941**	**100.00**	**109,491**	**100.00**	**72,819**	**100.00**
Sales by region						
Western Europe	52,006	43.0	40,322	36.8	34,031	46.7
Central and Eastern Europe	31,853	26.3	43,416	39.7	28,594	39.3
Russia	4,099	3.4	3,014	2.8	510	0.7
Other	32,983	27.3	22,739	20.7	9,684	13.3
Total	**120,941**	**100.00**	**109,491**	**100.00**	**72,819**	**100.00**

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6.2 Technology and Production

6.2.1 Technology

PEGAS Group owns and operates technologically advanced equipment necessary to produce high-quality spunmelt nonwoven textiles. The production management is focused on continuous maintenance and modernization of its equipment and machinery, ensuring that the Company continues to rank among the leading European producers of nonwoven textiles.

All production lines are manufactured by Reicofil, a leading German global supplier of spunmelt nonwoven production equipment. Reicofil achieved world leadership in spunmelt technology machinery in the late 1980 s owing to the quality of its production lines which are capable of making multilayer nonwovens in a single process, thus significantly reducing the production cost of nonwoven materials. Reicofil currently dominates the market for PP and PP/PE based spunmelt nonwoven machines worldwide. The table below provides additional details on each of current seven production lines:

Machine	Year of Installation	Technology Configuration[7]	Plant Location
Reicofil 2	1992	S	Bučovice
Reicofil 2	1996	SMS	Bučovice
Reicofil meltblown	1996	M	Přímětice
Reicofil 3	1998	SMS	Bučovice
Reicofil 3 BiCo	2000	SSMMS	Přímětice
Reicofil 3 BiCo	2001	SSS	Přímětice
Reicofil 4	2004	SSS	Přímětice
TOTAL Annual Production Output in 2006 (tonnes)			*54,159*

[7] "S" indicates a spunbond layer, "M" indicates a meltblown layer

Since PEGAS began the production of spunmelt nonwovens in 1992, it has kept pace with the latest technological developments in this field. In 1998 PEGAS was the first spunmelt manufacturer to install Reicofil technology with a microfilament option which, at that time, was a substantial technological advance. In 2002, a Reicofil 3 production line was capable of producing BiCo materials, the first such production line in Europe (PEGAS remains the only BiCo manufacturer in Europe). The installation in 2004 of the Reicofil 4 line, which employs the world's most advanced spunmelt technology currently in commercial operation, was the first such machine to be installed in Europe.

While the Reicofil 4 line has a width of 4.2 meters, all other Reicofil lines have widths of 3.2 meters or 1.6 meters. The capacity of the first line is primarily sold for technical and agricultural applications. The capacity from our meltblown line production is used for technical applications requiring a high absorption capacity, such as industrial wipes and absorbents. The Reicofil 4 line, which was installed at the end of 2004, employs a new technology which permits high speed production with improved nonwoven textile formation and uniformity.

In addition to the production lines, PEGAS operates three small finishing lines which enable the cutting, gluing and perforation of processed fabrics according to customer specifications.

The Company places an emphasis on recycling scrap materials which are used in the spunmelt processes (such as edge mater-ials or scrap from batch changeovers). For that purpose, each of the production lines is equipped with co-extruders or similar equipment, which enables the reuse of significant amounts of scrap material.

To optimize recycling further, PEGAS has developed a proprietary technology process that, together with new regranulation equipment, enables waste to be reduced to a minimum, by recycling almost all scrap material. This equipment was installed in the first half of 2006.

6.2.2 Production Process

The process for producing spunmelt nonwoven begins with polymer granules, which are melted and extruded through spinnerets. This produces continuous filaments which are cooled, stretched and laid down onto an air permeable conveyor belt to form a uniform fabric web. Afterwards, the web passes through a system of heated calender rolls and, as a result of the application of pressure and higher temperatures, takes on certain mechanical properties. If necessary, after calendering, the nonwoven can be treated with spinfinishes in order to achieve hydrophilic or other properties. The final steps in the process are winding, cutting and packaging before the material is prepared for delivery to clients.

In the meltblown process, the low viscosity polymer is melted and extruded into a high velocity hot air stream on leaving the spinneret. This air stream scatters the molten filaments, solidifies them and creates a fabric web from the fibres.

Both processes can be combined, in order to attain specific properties such as desired tensile strengths (from spunbond materials) and barrier characteristics (from meltblown materials). In this case, meltblown layers are added to spunbond layers and bonded together with heated calender rolls.

The principal advantage of the Company's production process is that spunmelt nonwovens can be manufactured through a single process using one continuous production line, which processes the raw material from their granulated form into filaments and finally into fabric.

6.3 Plants and Premises

PEGAS operates two production facilities located approximately 100 kilometres from each other in the south east of the Czech Republic. The original site in Bučovice has three production lines installed and further development space is now limited. The newer site in Přímětice was developed on the outskirts of Znojmo and has four production lines. In addition to the production sites, the Company owns an administrative building in Znojmo, close to the Přímětice production plant. All premises have been constructed as greenfield projects. The total production sites cover approximately 134,000 square meters, of which 53,000 square meters are occupied by buildings and other improvements (including the administrative building in Znojmo). PEGAS owns all of its real estate and the improvements constructed on it.

6.4 Customers

Demand for nonwoven output for the hygiene market is neither cyclical nor seasonal. Disposable diapers and feminine hygiene products are basic needs which are gradually influenced by macroeconomic factors, such as birth rates, disposable income and economic development. Central and Eastern Europe and Russia have growing birth rates and increasing levels of disposable income, which results in generally high growth in the personal hygiene market. Western Europe has constant birth rates and already high disposable income. Consequently, sales growth in baby diapers and feminine hygiene products is low. The demand for adult incontinence products is expected to increase in Europe owing to the aging of the population, increasing life expectancy and increasing acceptance of incontinence products. This increase in acceptance is partially due to increasingly lighter and softer nonwovens available for the manufacture of adult diapers.

The present customer concentration of the Company reflects the situation in the hygiene market which is divided among a small number of producers, each of which has a substantial market share. In 2006, PEGAS's top five customers accounted for approximately 84% of total sales, and the largest customer accounted for approximately 55% of the Company's total sales. The proportion of the Company's sales to other customers is expected to increase as a result, in part, of increasing production capacity with the introduction of the new production line.

The Company's portfolio of key customers comprises primarily a number of leading corporations active in disposable hygiene product market in Europe.

The European market leaders in personal hygiene products are Procter & Gamble, SCA (Svenska Cellulosa), Kimberly-Clark, Hartmann, Ontex and Johnson & Johnson. In addition, there are several medium to small size producers which play a significant role in their local markets.

The personal hygiene market is highly consolidated, with the market leader having a share close to 40% and the top five players constituting approximately 75% of total sales in the market.

The present customer concentration reflects the situation in the hygiene market which is divided among a small number of producers, each of which has a substantial market share.

2005 Market share in % in terms of unit volume

Personal hygiene companies	Baby diapers and pants	Feminine hygiene	Adult incontinence
P&G	48%	36%	7%
Kimberly-Clark	13%	8%	3%
SCA Hygiene	16%	10%	39%
Ontex	11%	10%	11%
Johnson& Johnson	–	12%	–
Hartmann	–	–	22%
TZMO	–	4%	2%
Paper Pak	–	–	4%
Others	12%	20%	12%
Total	***100 %***	***100 %***	***100 %***

Source: John R. Starr, Inc.

The risks associated with having a relatively small number of key customers are balanced by the benefits of mutual cooperation focused on the development and manufacture of customer-specific products, in part resulting from joint development programmes.

Agreements with PEGAS's large hygiene industry customers are negotiated and approved each year by senior management. The annual agreements are entered into on a global basis and relate to all of the production facilities of each particular customer which PEGAS supplies with nonwoven textiles. Supplies to these customers are then fixed based on the specific volumes they request in their monthly binding orders. Arrangements with large hygiene customers are customary in the industry and underline the importance of the close cooperation with the Company's key customers.

PEGAS is highly selective in choosing transportation companies, owing to the high importance of timely deliveries of products to customers and the product's sensitivity to contamination.

The Company's success in supplying nonwoven textiles depends on a number of factors, including:

- ***High qualities of our nonwoven textiles*** *– customers need to produce high quality products for their markets and, as a result, PEGAS is required to supply them with nonwoven textiles which meet their high quality standards.*
- ***Consistently reliable qualities at high production volume*** *customers operate high speed, capital-intensive machinery, where the costs of shutdowns are extremely high. PEGAS therefore must provide large quantities of product to consistently high standards, ensured through rigorous testing and inspection of all products.*
- ***Reliable transport*** *– customers require frequent and reliable delivery of products in order to minimize their own working capital and to provide them with certainty that their production lines will not suffer shutdowns because of interrupted supply.*
- ***Geographic proximity*** *– PEGAS sells most products on an INCOTERMS 2000 DDU (delivery and duty unpaid) basis. However, in some cases, customers prefer to arrange the transportation to their premises themselves. Since PEGAS's production facilities are located in the centre of Europe, this represents a significant competitive advantage when supplying manufacturers throughout Europe, including the higher growth areas of Central and Eastern Europe and Russia.*

- ***Modern machinery** – the Company recognizes that customers require nonwoven textiles of ever more demanding technical specifications and lighter weights. These textiles can only be manufactured on the most modern machinery. In order to serve customers in the best possible manner, PEGAS has consistently invested in equipment which is among the most advanced in the industry. While this requires high levels of capital expenditure, it does ensure that PEGAS offers the best possible products to customers.*
- ***Cooperation with and technical support for customers** – in order to help realize new product development and advancement for our customers, it is important that PEGAS (i) maintains strong technical capabilities, and (ii) engages in technical cooperation and assistance with customers in developing these increasingly demanding products.*

6.5 Suppliers

The main raw materials used for spunmelt nonwoven are polymers, most importantly polypropylene, followed by polyethylene, which are petroleum derivatives. In 2006, the consumption of PP and PE accounted for 79% of the Company's total operating costs (excluding depreciation and amortization). Over the past three years, the Company has sourced polymer raw materials from a total of eight suppliers. The polymer raw materials are purchased on both one year and multi-year agreements, the bulk of which are purchased in Euro. The competitiveness among suppliers is maintained by ongoing benchmarking.

As the qualitative characteristics of the input material are critical for the production process, our PP and PE supplies are tested by our suppliers both before and after contracting and are continuously screened according to their internal rules and ISO norms.

Indexation of raw material prices and corresponding effects on revenue

In general, PEGAS purchases PP and PE on the basis of published price indices. Under the terms of sales agreements with main customers, prices for the Company's products are also based on published price indices for the principal raw materials. This practice is common in the hygiene nonwoven industry and to a lesser extent, also in the non-hygiene market. Such indexation partially removes the risk from movements in raw materials prices. Consequently, any time that polymer prices increase or decrease within the contractual time periods, PEGAS records a corresponding increase or decrease in revenue. This results in decreased operating margins whenever polymer prices increase and increased operating margins whenever polymer prices decrease.

6.6 Quality Management and Environment

PEGAS is ISO 9001:2000 and EN ISO 14001:1996 certified. It first received these quality certifications in 1997. In connection with the amendment of the ISO standards of the 9001 series in 2000, the existing system was partially revised and subsequently the Quality Management System and Environmental Management System were integrated in 2002. PEGAS has a certified integrated system of quality according to ISO 9001:2001 by CQS, IQNet and environmental management EN ISO 14001:1997 by CQS. The Company upgraded its certification to ISO 9003 in 2006.

6.6.1 Quality Management System

In addition to the general quality requirements imposed by ISO 9001, the Company is looking continuously to improve and adjust its production process and relevant assets in order to provide superior output quality. In 2002 and 2003, all production premises were provided with overpressure air control to eliminate the risk of insects or particles contaminating the fabrics. Subsequently, an optical quality control system was introduced on all of the hygiene production lines, to monitor both the bonding consistency, uniformity and the presence of external particles. These measures have significantly decreased customers' deficiency claims.

6.6.2 Environmental Management System

PEGAS has implemented and maintained an environmental management system to take care of all environmental aspects as required by ISO 14001:1997. The production process involves the change of PP or PE raw materials into a form of fibers through the application of heat and pressure. This process results in minimal chemical changes to the material and in limited atmospheric emissions. PEGAS has obtained all necessary environmental permits for its operations and is in compliance with Czech environmental laws.

6.7 R&D

6.7.1 Development and Technical Support

Starting in the mid 1990s, the Company has built a team dedicated to product development and technical support. The team provides customers with solutions throughout the production stream by incorporating the input of the technology provider and material suppliers, as well as the final product manufacturer and final customer requirements. New technologies in nonwovens production are tailored to the parameters of the raw material, production lines, customers' specifications and demand for the finished product, with a view to improving the quality and efficiency of the production, especially into the direction of lightweight materials. Resulting benefits are shared with customers. Some of the Company's development projects have also attracted government grants or subsidies, including one that supports a development project for improving waste recycling. These development projects have resulted in the implementation of the regranulation project in 2006 and, additionally, in the reduction of waste. In addition, PEGAS continues to work closely with a number of raw materials suppliers to develop new polymer grades which offer greater efficiency when running on the Reicofil systems.

In the field of totally new materials, the Company successfully commercialised a range of special bicomponent nonwovens in 2006 which have offered clients significantly improved softness and technical properties. In addition, PEGAS is actively working on developing special elastic nonwovens which, if successful, will offer clients signi-ficant enhancements in comfort and other benefits.

06

PEGAS cooperates with several universities and independent research centers in the Czech and Slovak Republics and in Germany.

Research and development costs in 2006 were approximately Euro 1.8 million.

6.7.2 Intellectual Property

PEGAS has registered its trademark and logos in selected European and international markets. The Company has one registered patent for special nonwoven microfilament spunmelt material for hygiene products. The patent is registered internationally for selected European countries.

6.8 Strategy

6.8.1 The Company's Strategy and Outlook

The Company's strategic objective is to participate fully in the growth of the personal hygiene nonwovens market in Europe (especially in Central and Eastern Europe and Russia), the Middle East and North Africa. PEGAS intends to achieve its objective principally through the following strategies:

Remain one of the European nonwoven technology leaders

Investment in Technologically Advanced Machinery: Since commencing operations, PEGAS has consistently focused on acquiring the most technically advanced machinery available in the market. The Company intends to continue this trend by investing in advanced machinery in order to maintain its competitive advantage over other manufacturers of spunmelt nonwovens.

Technical Expertise: PEGAS consistently strives to maintain the highest levels of technical and engineering capabilities through training and constant review of its production facilities. The Company will continue to invest in maintaining this technical advantage.

Cooperation with Customers and Suppliers: PEGAS intends to continue its cooperation with its clients, machinery manufacturers and raw materials suppliers in order to remain at the forefront of technical developments in the industry and in order to supply its customers with the highest quality products.

Remain a leader in "difficult to manufacture" specialty products

Customers require constant improvement in the technical qualities of their nonwoven textiles, especially in terms of weight per square meter, softness and performance. This allows them to maintain competitive advantage in their markets. For this reason, PEGAS will continue to focus on difficult to manufacture, specialty products and will ensure that they account for an increasing proportion of sales.

The Company defines specialty products as super-lightweights and bicomponent nonwovens. PEGAS remains the only manufacturer of bicomponent nonwovens in Europe and will further boost its capacity to make superlightweights with the introduction of its new production line in the fourth quarter of 2007.

The configuration and design of this new production line continues the Company's history of installing and commissioning world-leading technology at regular two to three year intervals. The line will again be the first of its kind in the world and is aimed at allowing PEGAS to produce ultra lightweight materials for both the hygiene and the medical markets. It is therefore a key component of the Company's strategy to increase its production of high margin specialty products. This strategy is designed to keep the Company at the leading edge of nonwovens technology and to maintain its margins at a higher level.

Maintain superior financial performance

PEGAS will further focus on its financial performance and intends to achieve superior results by growing volume through capital investment and close relationships with customers. Margins will be maintained through focusing on costs and through focusing on increasing the proportion of sales which are accounted for by specialty products. The products require more complex production processes but do offer higher margins.

6.9 Human Resources

6.9.1 Employees

PEGAS benefits from highly skilled and motivated workforce, which results in relatively high profitability per employee and productivity growth. By focusing on retaining highly skilled employees, the Company is able to maintain a low staff turnover rate of approximately 5% annually.

The table below indicates the number and functional breakdown of employees and data on total sales and EBITDA per employee:

As at December 31st			
	2004	**2005**	**2006**
Senior Management	9	6	6
Management	12	12	11
Specialists	38	48	46
Laboratory Staff	32	31	32
Qualified Workers	57	48	52
Manual Workers	187	167	180
Total	**335**	**312**	**327**
Average no. of employees	**311**	**333**	**324**

Euro thousands	**2004**	**2005**	**2006**
Total sales/average number of employees	234.1	328.8	373.3
EBITDA[8]/average number of employees	94.3	122.2	129.8

8 Adjusted EBITDA for 2006

The Company's workforce has a high level of education and approximately 12% of employees have university educations. PEGAS provides continuous training, some of which is compulsory, in areas such as work security, computer skills and foreign languages.

The average monthly wages of Company employees grew by a CAGR of 5.6% (calculated on the basis of wages in Czech korunas) between 2002 and 2006, from Euro 582 per employee in 2002 to Euro 899 per employee in 2006. The monthly wage of the Company's employees (including management) of approximately Euro 899 in 2006 is still significantly below the average in Western Europe, but substantially more than the average in the South Moravian region of the Czech Republic. The remuneration structure is highly motivational, with the fixed salary part of the basic salary ranging from approximately 80% for manual workers to approximately 60% for management. The salary of workers varies in relation to the volume produced on a specific line, including the quality of the product, and is capped. There are no trade unions in PEGAS.

6.10 Comments on Financial Results[9]

Revenues, Costs and EBITDA

Consolidated revenues (revenues from sales of products) reached Euro 120.9 million in 2006, up by 10.5 % yoy. The key drivers of this growth were higher polymer prices (which were fully passed through to customers) and higher sales mainly of specialty products.

Total consolidated operating costs before depreciation and amortization and after exclusion of realized and unrealized FX changes including hedging increased by 14.6% yoy to Euro 78.9 million. The main reason was the increase in polypropylene prices, higher consumed volumes and also higher electricity prices.

Adjusted EBITDA amounted to Euro 42.1 million, up by 3.4 % yoy, which confirmed that Company's strong operating performance has continued from previous periods. Adjusted EBITDA margin in 2006 was 34.8%, down by 2.4% in comparison with 2005. This decline in percentage margins was a direct result of higher polymer prices and the ability of the Company to pass through polymer price rises to customers.

Operating costs

Total raw materials and consumables (including Research and Develepment) used in 2006 amounted to Euro 73.7 million, a 16.5% increase on 2005.

Total staff costs amounted Euro 5.1 million in 2006, a 9.5% yoy increase. However, total staff costs, denominated in Czech korunas, went up by only 4.2% yoy. Total number of employees at December 31st, 2006 was 327, up by 4.8 % yoy.

Other net operating income / (expense) amounted to Euro 11.2 million in 2006 and mainly represented both realized and unrealized FX changes related to balance sheet revaluations and a mark-to-market revaluation of the interest rate swap at December 31st, 2006. This is an income which depends on Euro/CZK exchange rate development and mainly on the level of the Company's indebtedness.

9 Audited Income Statement under IFRS of Pegas a.s. for 2005 and of PEGAS NONWOVENS SA for 2006.
Audited Balance Sheet under IFRS of PEGAS NONWOVENS SA for both 2005 and 2006.

Depreciation and amortization

Consolidated depreciation and amortization reached Euro12.2 million in 2006. This cannot be compared with PEGAS a.s. in 2005 as fixed assets (long-term tangible and intangible assets) were revalued as part of the acquisition of PEGAS a.s. in December 2005.

Profit from Operations

Adjusted profit from operations (EBIT) amounted to Euro 29.9 million and cannot be compared with PEGAS a.s. in 2005 owing to changes in the basis of Depreciation and Amortization discussed above.

Finance Costs

Finance costs amounted Euro 18.8 million in 2006. This related mainly to interest charges on the senior term loans, mezzanine and shareholder loans which were taken on in December, 2005 to finance the acquisition of PEGAS a.s. from its previous owners.

Income tax

In 2006, income tax amounted to Euro 1.6 million, a reduction of 60% yoy from the Euro 4.0 million charge in 2005 for PEGAS a.s. The reduction is a result of the tax shield on interest costs resulting from the acquisition loans taken on in December, 2005.

Net Profit

Net profit in 2006 amounted to Euro 20.7 million, down by 22.3% yoy, due to higher finance costs.

CAPEX and Investments

In 2006, total consolidated capital expenditure amounted to Euro 5.3 million, a 52.3% reduction on 2005. Capital expenditure was focused on the construction of the new eighth production line and on improving the efficiency of the existing production lines. The largest one of these improvements was the scrap recycling project. The CAPEX to Revenues ratio was 4.4% in 2006.

Cash and Indebtedness

The total amount of the consolidated financial debt (both short-term and long-term) at December 31st, 2006 was Euro 136.2 million, a 35.2% reduction compared with December 31st, 2005. Cash and cash equivalents reached Euro 22.0 million at December 31st, 2006. Net debt at December 31st, 2006 was therefore Euro 114.2 million. This was equivalent to a Net Debt / adjusted EBITDA ratio of 2.7 times.

The Company hedges its interest rate risk related to its financial debt with interest rate swaps. The currency risk is not hedged since the Company has a natural hedge having most of its revenues and costs in Euro.

06

2006 Performance Overview

PEGAS's principal focus is on growing revenues from specialty products where margins are higher. Specialty products accounted for 23.6% of total revenues in 2006 compared with 16.3% in 2005. This percentage could be capable of being increased once the new production line is introduced in the fourth quarter of 2007.

Although the Company did not install any new production equipment in 2006, the Group was able to increase total output by 5.7% from 51.3 thousand tonnes in 2005 to 54.2 thousand tonnes in 2006 owing to improved production efficiencies.

Revenues from sales of nonwoven textiles for the hygiene industry were 88.8% of total revenues in 2006. This was similar to the proportion of hygiene revenues in 2005 which was 88.6%.

Revenues from sales of standard textiles for hygiene products reached Euro 78.9 million, a reduction of 0.3% in comparison with 2005. Revenues from sales of non-hygiene products (for construction, agriculture and medicine) amounted to Euro 13.5 million in 2006, an increase of 8.0% over 2005.

PEGAS sold its products to both international and domestic Czech customers. Exports accounted for 87.8% of total revenue for 2006, reflecting the fact that the majority of manufacturers in the hygiene industry are located outside the Czech Republic.

Outlook for 2007

In 2007, the main priorities for PEGAS NONWOVENS SA will be:

- *Successfully to bring on its new production line on time and on budget and therefore increase its capacity by more than 27% (based on current production basis weights);*
- *To develop new specialty products which will prove attractive to its customers;*
- *To improve further its production efficiency;*
- *To maintain its position as a leader in the market for spunmelt nonwoven textiles for the disposable hygiene products market;*
- *To maintain its low production costs.*

The new production line is currently under construction and due to enter service in the fourth quarter of 2007. It will be the Company's eighth line and will enable a rapid increase in production capacity from the current 54.2 thousand tonnes per annum to 69 thousand tonnes per annum in 2008 (based on current production basis weights).

This line is therefore a key component of the Company's strategy of increasing its production of high margin specialty products. This strategy is designed to keep the Company at the leading edge of nonwoven technology and to maintain its margins at a higher level. The line will allow the Company to increase the proportion of its sales which are specialty products.

The new production line will lead to an increase of the number of its employees from 327 at the end of 2006 to approximately 380 during 2007.

With respect to the expansion of production outside the Czech Republic, the Company will continue to monitor the development goals and programs of its customers, which may lead to a shift or opening of new production capacity in other territories.

The Company will continue to focus on the development of new materials which may potentially become specialty products and will therefore increase the proportion of sales in this area.

6.11 Czech Investment Incentives

Investment incentives granted to PEGAS

PEGAS has applied three times for various investment incentives programmes organised by the Czech authorities. In connection with these schemes, PEGAS incorporated its subsidiaries PEGAS - DS a.s., PEGAS-NT a.s. and PEGAS - NW a.s. as special purpose companies to accommodate each investment and to obtain the incentives.

PEGAS – DS a.s.

When PEGAS a.s. applied for investment incentives for PEGAS - DS a.s., the scheme for the manufacturing sector was operated under a different legal regime that existed before the current Investment Incentives Act came into force. Incentives were granted on the basis of individual arrangements entered into between the state and the recipient and were referred to as "memoranda of understanding". PEGAS - DS a.s. was granted a package of incentives based on the Memorandum of Understanding signed on June 29th, 1999. The investment incentives for PEGAS - DS a.s. consist of:

- *full corporate income tax payment relief for the first five years and a subsequent grant for the next five years which cannot exceed the amount of the grant for the first five-year period. This grant was subsequently changed and now covers the full ten-year grant for full corporate income tax relief;*
- *interest-free loans for establishing new jobs and re-training of employees in an amount of CZK 4.5 million; these loans were subsequently reclassified as grants after fulfillment of the conditions stated in the Memorandum of Understanding;*
- *exemption of imported fixed assets from import duties.*

The total amount of the incentives granted to PEGAS - DS a.s. cannot exceed 50% of the expended amount, i.e. currently, approximately CZK 807.9 million. PEGAS - DS a.s. started making use of the incentives in fiscal year 2001 and, as a result, its corporate tax relief incentive will expire in 2010.

PEGAS–NT a.s. The Czech government granted PEGAS-NT a.s. the following investment incentives in its decision of July 2002:

- *full corporate income tax relief for up to a 10 year period*
- *a job creation grant in the amount of CZK 5.4 million.*

The total amount of the incentives cannot exceed 45% of the investment, which is currently equal to CZK 375.0 million; and in any case cannot exceed CZK 509.9 million. PEGAS-NT a.s. started making use of the incentives in fiscal year 2005.

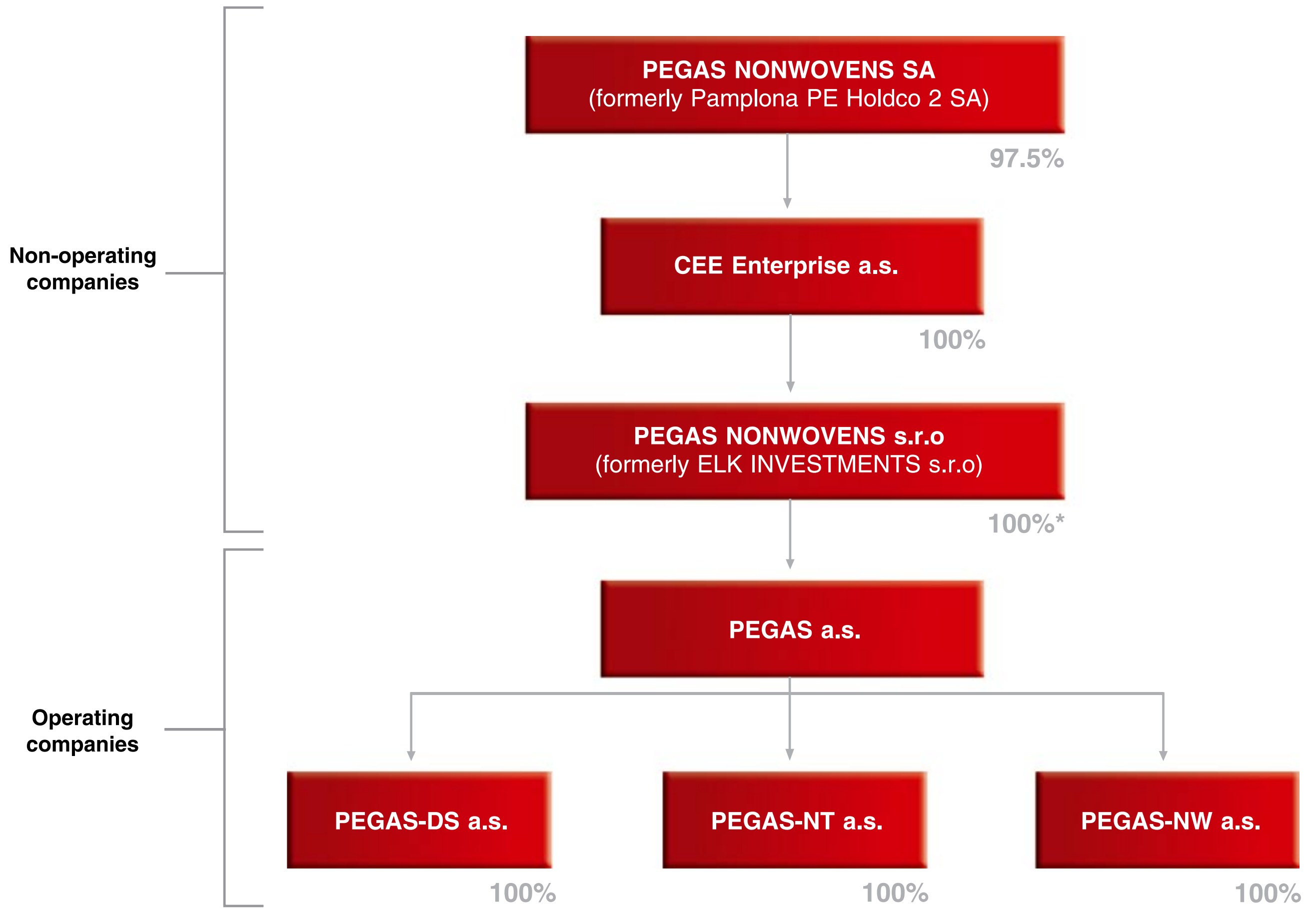
PEGAS - NW a.s.

PEGAS - NW a.s. obtained its investment incentives based on the decision of the Czech government on June 10th, 2005. The incentives consist of corporate income tax relief for up to 10 years. The tax relief may not exceed 48% of the invested amount (equal to CZK 1.075 bln), and in any case cannot exceed CZK 573.6 million. PEGAS - NW a.s. is planning to start making use of this incentive in 2008.

7 Corporate Governance

7.1 Organizational Structure and its Development

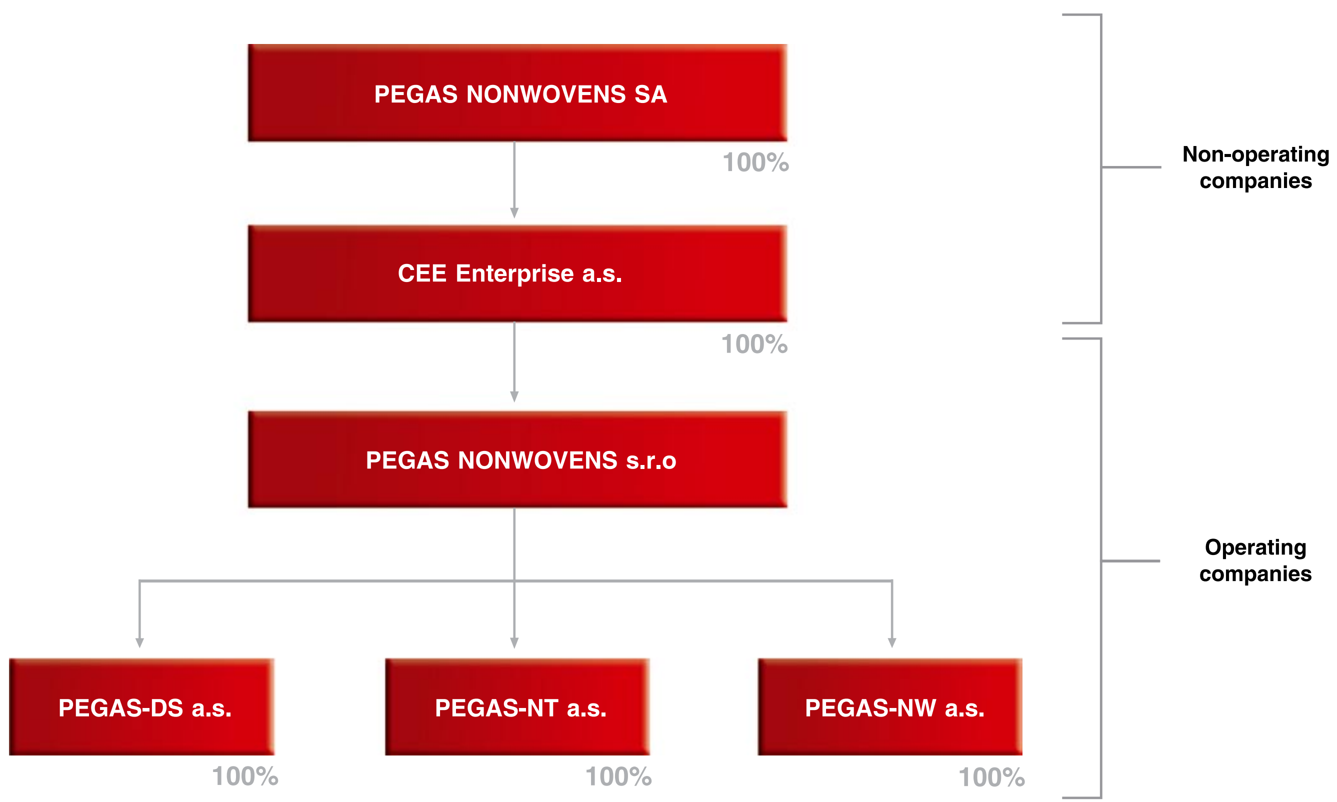
The diagram below represents the structure of the Group immediately prior to the merger between PEGAS NONWOVENS s.r.o. and PEGAS a.s.:



*except for one share in PEGAS a.s. held by the Company

07

The diagram below represents the current structure of PEGAS Group as of December 31st, 2006:



All of the operating assets (except for a software operating licence) are owned by PEGAS NONWOVENS s.r.o. and its three subsidiaries: PEGAS - DS a.s., PEGAS-NT a.s. and PEGAS - NW a.s., which are companies incorporated in the Czech Republic. The software licence is held by CEE Enterprise a.s. The Company's relations with suppliers and customers are carried out by PEGAS NONWOVENS s.r.o., and consequently PEGAS presents itself to the market as a single entity.

The allocation of our production assets among the four operating subsidiaries facilitates the utilisation of the Czech tax incentives. The operating subsidiaries PEGAS - DS a.s. and PEGAS-NT a.s. began benefiting from these incentives in fiscal years 2001 and 2005, respectively. In February 2005, the Company established the subsidiary PEGAS - NW a.s. to take advantage of Czech tax incentives which are anticipated following the installation of the eighth production line.

The table below indicates the country of incorporation and direct and indirect shareholdings in PEGAS's subsidiaries:

Company name	Country of Incorporation	% ownership interest
CEE Enterprise a.s.	Czech Republic	100.00
PEGAS NONWOVENS s.r.o.	Czech Republic	100.00
PEGAS – DS a.s.	Czech Republic	100.00
PEGAS–NT a.s	Czech Republic	100.00
PEGAS – NW a.s.	Czech Republic	100.00

PEGAS NONWOVENS SA was previously named Pamplona PE Holdco 2 SA. It was incorporated on November 18th, 2005 and consequently has only a limited operating history. In addition, both the Company and its directly held subsidiary, CEE Enterprise a.s., serve only as holding companies, with the exception of an SAP computer software license held by CEE Enterprise a.s., which is that subsidiary's sole operating asset. Apart from that license, operating assets are held entirely by PEGAS NONWOVENS s.r.o. and its three wholly-owned subsidiaries, PEGAS - DS a.s., PEGAS-NT a.s. and PEGAS - NW a.s.

December 2005

In December 2005, PEGAS NONWOVENS SA completed the acquisition of 100% of the share capital and voting rights of PEGAS a.s. In order to facilitate the acquisition, PEGAS NONWOVENS SA acquired CEE Enterprise a.s., a joint stock company incorporated in the Czech Republic, which in turn acquired ELK INVESTMENTS s.r.o., a private limited liability company incorporated in the Czech Republic, which served as the vehicle for the acquisition of PEGAS a.s.

Since December 2005, PEGAS NONWOVENS SA has owned all of the share capital of CEE Enterprise a.s. and ELK INVESTMENTS s.r.o. except for a minority interest in CEE Enterprise a.s. held by some members of PEGAS' management, which was converted in November 2006 into a shareholding in the Company.

January 2006

In January 2006, management of PEGAS NONWOVENS SA acquired an aggregate 2.5% participation in the share capital of CEE Enterprise a.s., which was subsequently sold to PEGAS NONWOVENS SA, while at the same time management subscribed for a 2.5% participation in PEGAS NONWOVENS SA.

April 2006

In April 2006, ELK INVESTMENTS s.r.o. changed its name to PEGAS NONWOVENS s.r.o. and in May 2006 PEGAS a.s. was merged into it, with PEGAS NONWOVENS s.r.o. being the surviving entity.

Before the merger, one share in PEGAS a.s. was transferred from ELK INVESTMENTS s.r.o. to the Company. Therefore, after the merger, PEGAS NONWOVENS s.r.o. had two owners, CEE Enterprise a.s. and PEGAS NONWOVENS SA.

PEGAS NONWOVENS s.r.o. had no trading or operational assets or liabilities and had never conducted any business other than that of a holding company prior to the merger with PEGAS a.s. As a result of the merger, PEGAS NONWOVENS s.r.o. acquired all of the former assets, liabilities and business activities of PEGAS a.s.

November 2006

In November 2006, CEE Enterprise a.s. acquired the full participation in PEGAS NONWOVENS s.r.o. from PEGAS NONWOVENS SA.

December 2006

On November 27th, 2006, PEGAS launched its IPO of 5,042,750 shares in total, including 1,810,000 shares newly issued in the Company's share capital and 3,232,750 shares offered by the selling shareholder private equity fund Pamplona Capital Partners I, LP. Following the IPO, and exercise of the Over-allotment option, Pamplona retained a share stake of 43.4% and the management of the Group retained a share stake of 2.0%. The balance of the shares, 54.6%, remains as a free float.

07

7.2 Board of Directors

The Company is administered and managed by a board of directors (the "Board of Directors").

The director(s) of the Company are appointed by a General Meeting of Shareholders for a term which may not exceed six years. The director(s) may be dismissed at any time and at the sole discretion of the General Meeting of Shareholders, and may be reappointed without restrictions.

Members of the Board of Directors

The following table sets out information with respect to each of the members of the Company's Board of Directors, their respective ages, and their positions, within the Company:

Name	Age	Position/Function	Business Address
Miloš Bogdan	43	Executive director	Přímětická 86, 669 04, Znojmo, Czech Republic
Aleš Gerža	33	Executive director	Přímětická 86, 669 04, Znojmo, Czech Republic
František Klaška	50	Executive director	Přímětická 86, 669 04, Znojmo, Czech Republic
František Řezáč	33	Executive director	Přímětická 86, 669 04, Znojmo, Czech Republic
Henry Gregson	48	Non-Executive director	25 Park Lane, London W1K 1RA, United Kingdom
John Halsted	42	Non-Executive director	25 Park Lane, London W1K 1RA, United Kingdom
Bernhard Lipinski	60	Non-Executive director	Steinertsweg 44b, 64753, Brombachtal, Germany
David Ring	44	Non-Executive director	Western Avenue, Western Docks, Southampton SO15 0HH, United Kingdom

Board of Directors

Miloš Bogdan

CEO

Mr. Bogdan is the Chief Executive Officer and a director of PEGAS Group. Mr. Bogdan has been with PEGAS for 11 years, starting as a plant director in 1995. Before joining PEGAS, he worked as the Production Director in UNEX, a specialized engineering company. He was named Chief Executive Officer in 2000. Mr. Bogdan is a graduate of the Czech Technical University.

Aleš Gerža

CFO

Mr. Gerža is the Chief Financial Officer of PEGAS Group. Mr. Gerža joined PEGAS in 1999, after having worked for 5 years in Danzas, a freight forwarding company. He was promoted to his current position in 2000. Mr. Gerža is a graduate of the Prague School of Economics.

Henry Gregson

Non-Executive Director

Mr. Gregson was appointed a director of PEGAS Group in December 2005. Mr. Gregson is currently a partner of Pamplona Capital Management, LLP which advises the General Partner of the Pamplona Capital Partners I, LP. Prior to helping found Pamplona Capital Management, LLP, Mr. Gregson was a director at Royal Bank Equity Finance and before that a partner at Phildrew Ventures. Mr. Gregson holds a Bachelor of Science in Civil Engineering from the University of Bristol and an MBA from Harvard Business School.

John Halsted

Non-Executive Director

Mr. Halsted is the Managing Partner of Pamplona Capital Partners, LLP which he co-founded in September 2004. Prior to joining Pamplona, he served as a Senior Vice President of Beacon Capital Partners, a real estate investment firm with operations in the United States and Europe. Previously he was a Vice President of the Harvard Private Equity Group, the private equity investment arm of the Harvard University endowment. Mr. Halsted holds a Bachelor of Science in Economics from the University of California at Berkeley and an MBA from Harvard Business School.




František Klaška

Technical and Development Director

Mr. Klaška has been with the Company since 1991, having previously worked for 5 years in Zbrojovka Brno, a diversified engineering company. He was promoted to his current position of Technical and Development Director of PEGAS Group in 2001. Mr. Klaška is a graduate of the Czech Technical University.

Bernhard W. Lipinski

Non-Executive Director

Bernhard W. Lipinski joined PEGAS Group as an advisor in January 2006. He spent 33 years with BP Chemicals in Düsseldorf, Geneva, Antwerp and London. He managed BP Amoco's Film & Nonwovens business focusing on hygiene and relevant industrial markets until its divesture to RKW in 2002. Mr. Lipinski served as non-executive director to RKW, Germany, and Verdugt, the Netherlands.

František Řezáč

Commercial Director

Mr. Řezáč joined the Company in 1996. He was promoted to his current position of Commercial Director of PEGAS Group in 2004, after having worked as the HR Director and Legal Counsel. Mr. Řezáč is a graduate of the Law Faculty of Masaryk University Brno.

David Ring

Non-Executive Director

Mr. Ring is currently Chief Executive of the A&P Group, the UK's leading shiprepair and conversion company. Prior to joining A&P in 1999, Mr. Ring held senior positions in the aerospace and automotive industry. Mr. Ring holds a BA in Economics from the University of Lancaster.




07

Key Management

Biographical details of the remaining key members of our senior management are provided below:

Rostislav Vrbácký
Aged 43, Production Director of PEGAS NONWOVENS s.r.o. Mr. Vrbácký has been with the Company since 1991, having previously worked for five years in Zbrojovka Brno, a diversified engineering company. He was promoted to his current position in 2001. Mr. Vrbácký is a graduate of the Czech Technical University.

Lukáš Trávníček
Aged 33, HR Director and Legal Counsel of PEGAS NONWOVENS s.r.o. Mr. Trávníček joined the Company in his current position in 2004, having previously worked for 4 years in Pricewaterhouse-Coopers and Landwell. Mr. Trávníček is a graduate of the Law faculty at Západočeská University.

There are a further 12 members of the management team not listed above.

7.3 Remuneration of directors and management

The objective of the Company's remuneration policy is to provide a compensation programme that allows us to attract, retain and motivate members of the Board of Directors who have the character traits, skills and background successfully to lead and manage the Company.

Share option plan

In 2006, the Company did not create any share option plan or management bonus scheme linked to the shares of the Company with the exception of for a minority interest in CEE Enterprise a.s. held by some members of the Group's management, which was converted in November 2006 into a shareholding in the Company. A management bonus scheme is currently being prepared and will be subject to the approval in the Annual General Meeting of the Company in June 2007. The proposal of the share option plan presented in the Offering Circular of the IPO has not been implemented.

The Company and the operating companies are currently not intending to create and have not created a share option plan for the benefit of their employees.

Remuneration in Euro, 2006

		PEGAS NONWOVENS SA	Other Group Companies		
		Pecuniary Income	Pecuniary Income	Received in kind	Total
Members of the Board of Directors	Remuneration	212 224	1 764	0	213 988
	Salaries and other similar income	0	202 598	13 781	216 379
	Other Income	150 000	29 913	0	179 913
	TOTAL	**362 224**	**234 275**	**13 781**	**610 280**
Management of the Group Companies*	Salaries and other similar income	0	529 413	30 130	559 543
	Other Income	0	1 941	0	1 941
	TOTAL	**0**	**531 354**	**30 130**	**561 484**
GRAND TOTAL		**362 224 ****	**765 629**	**43 911**	**1 171 764**
Shares in CEE Enterprise a.s.		168 897	0	0	168 897
Shares in CEE Enterprise a.s.		84 323	0	0	84 323

* Number of managers included (14)

** Payments in respect of 2006 will be subject to approval at the Annual General Meeting of the Company in june 2007

7.4 Corporate Governance

Pursuant to the Warsaw Stock Exchange By-laws, and in connection with the listing of the Company's shares on the Warsaw Stock Exchange, the Company is required to declare which of the Polish principles of corporate governance contained in the WSE Corporate Governance Rules it intends to comply with, as well as to enumerate the principles which it does not intend to comply with and stating the reasons for the non-compliance.

The Company has decided to observe the majority of the WSE Corporate Governance Rules as stated in detail below.

STATEMENT ON WARSAW STOCK EXCHANGE CORPORATE GOVERNANCE RULES

No.	RULE	YES/NO	COMMENT OF PEGAS NONWOVENS SA
	GENERAL RULES		
I	Objective of the Company The main objective of a Company's authorities is to further the Company's interests, i.e. to increase the value of the assets entrusted to them by the shareholders, taking into consideration the rights and interests of entities other than the shareholders that are involved in the functioning of the Company, especially the Company's creditors and employees.	YES	
II	Majority Rule and Protection of the Minority A joint-stock Company is a capital venture, therefore it must respect the principle of capital majority rule and the primacy of majority over minority. A shareholder who contributes more capital also bears a greater economic risk. It is, therefore, justified that his interests be considered in proportion to the capital he contributes. The minority must have a guarantee that their rights will be properly protected within the limits set by the law and commercial integrity. When exercising his rights, a majority shareholder should take into account the interests of the minority.	YES	The Company is a public limited liability Company (société anonyme), incorporated under the laws of Luxembourg.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	GENERAL RULES		
III	Honest Intentions and No-Abuse of Rights The exercising of rights and reliance on legal institutions should be based on honest intentions (good faith) and cannot go beyond the purpose and economic reasons for which these institutions are established. No actions should be taken which, by exceeding the limits set, constitute an abuse of the law. The minority should be protected against any abuse of ownership rights by the majority and the interests of the majority should be protected against any abuse by the minority of its rights, thus ensuring the best possible protection of the equitable interests of the shareholders and other market participants.	YES	
IV	Court Control The Company's authorities and persons chairing the general meeting cannot decide on issues which should be resolved by a court judgment. This does not apply to activities which the Company's authorities and persons chairing general meetings are authorised or obliged to undertake by force of law.	YES	
V	Independent Opinions Ordered by the Company When choosing an entity to provide expert services, particularly an auditor, financial and tax advisors or legal advisors, the Company should examine whether there are any circumstances that would limit the entity's independence when performing the tasks entrusted.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF GENERAL MEETINGS		
1	A general meeting should take place in a location and at a time that allows the participation of as many shareholders as possible.	YES	
2	A request made by parties entitled to do so for a general meeting to be convened and for certain issues to be put on its agenda should be justified. Draft resolutions proposed for adoption by the general meeting and other key documents should be presented to the shareholders together with justification and a supervisory board opinion before the general meeting to allow them time to review and evaluate the same.	YES	
3	A general meeting convened on the shareholders' request should be held on the date given in the request and, if this date cannot be kept, on the nearest date that would allow the general meeting to settle the issues on its agenda.	YES	
4	A general meeting whose agenda includes certain issues at the request of authorized entities or which has been convened on such a request can only be cancelled with the consent of the requesting parties. In all other instances, a general meeting can be cancelled if its holding is hindered (force majeure) or is obviously groundless. A meeting is called off in the same way as it is convened, limiting negative consequences for the Company and its shareholders as far as possible and no later than three weeks before the original meeting date. A change in the date of a general meeting is made in the same way as a cancellation, even if the proposed agenda does not change.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF GENERAL MEETINGS		
5	Before a shareholder's representative can participate in a general meeting, his right to act on the shareholder's behalf should be duly documented. It should be presumed that a written document confirming the right to represent a shareholder at a general meeting conforms with the law and does not require any additional confirmations or acknowledgement unless the Company's management board or the chairman of the general meeting has doubts about its authenticity or validity prima facie (when drawing up the list of attendance).	YES	
6	The general meeting should have regular by-laws setting out in detail the principles on which meetings are conducted and resolutions adopted. The by-laws should, in particular, contain provisions on elections, including elections to the supervisory board by voting in separate groups. The by-laws should not be subject to frequent change; it is advisable for any changes to enter into force as of the following general meeting.	YES	
7	The person opening the general meeting should immediately organise the election of the meeting chairman and should refrain from making any substantial or formal decisions.	YES	
8	The chairman of the general meeting ensures that the meeting is run efficiently and that the rights and interests of all the shareholders are observed. The chairman should, in particular, counteract any abuse of rights by meeting participants and should guarantee that the rights of minority shareholders are respected. The chairman should not, without good reason, resign from his function or delay signing the meeting minutes.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF GENERAL MEETINGS		
9	A general meeting should be attended by the members of both the supervisory board and the management board. The auditor should also be present at an annual general meeting and an extraordinary general meeting if the Company's financial matters are to be discussed. The absence of a supervisory or management board member from the general meeting requires an explanation, which should be given at the meeting.	NO	We are partially unable to comply with this rule as there is a single board structure in the Company – there is no Supervisory Board.
10	Supervisory and management board members and the Company's auditor should, within their powers and to the extent needed to settle issues discussed at the general meeting, provide meeting participants with explanations and information about the Company.	NO	We are partially unable to comply with this rule as there is a single board structure in the Company –there is no Supervisory Board.
11	All answers provided by the management board to questions posed by the general meeting should take into account the fact that a public Company carries out its reporting obligations in the way stipulated in the Law on the Public Trading in Securities; certain information cannot be provided in any other way.	YES	
12	Short breaks in the session which do not constitute an adjournment and are ordered by the chairman in justified cases cannot be aimed at hindering the exercising by the shareholders of their rights.	YES	Under Article 5.4 of the Regulations of the General Meeting of the Shareholders, No breaks in the Meeting may be ordered or motions of participants approved if they would impair in any way the rights of shareholders.

07

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF GENERAL MEETINGS		
13	Voting on administrative issues may only concern issues related to the running of the meeting. Resolutions which may have an impact on the exercising by the shareholders of their rights cannot be voted on in this way.	YES	Under Article 6.4 of the Regulations of the General Meeting the only procedural matters which may be voted upon are those relating to the conduct of the General Meeting. For the avoidance of doubt, no resolutions which could impact the exercise of shareholders' rights shall be treated as relating to procedural matters.
14	A resolution not to consider an issue on the agenda may be adopted only if it is supported by sound reasons. Any motion in this respect should be accompanied by a detailed justification. A decision to remove an item from the agenda or not to consider an issue put on the agenda at a shareholder's request requires a general meeting resolution, once all the shareholders present who put the issue on the agenda have given their consent, supported by 75% of the votes present at the meeting.	NO	Under Article 6.4 of the Regulations of the General Meeting a resolution which seeks to prevent or delay discussion or vote on a matter which is contained in the agenda may be adopted only if it is supported by sound reasons.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF GENERAL MEETINGS		
15	Any party objecting to a resolution must be given the opportunity to put forward concise reasons for its objections.	YES	Under Article 6.4 of the Regulations of the General Meeting any party who raises objection to a resolution shall be given the opportunity to justify concisely the reason for the opposition.
16	As the Code of Commercial Companies does not provide for court control in the event of a resolution not being adopted by the general meeting, the management board or the meeting chairman should form resolutions in such a way that anyone who does not agree with the merits of a decision being the subject of the resolution has the possibility of challenging the same, provided that he is entitled to do so.	YES	Under Article 6.7 Regulations of the General Meeting in order to give to all shareholders equal opportunity to challenge the substance of the decisions of the General Meetings regardless of whether the vote vas rejected or approved, the resolutions shall be formulated in a manner allowing for a challenge by a shareholder.
17	Written statements made by a participant at a general meeting are recorded in the minutes at the participant's request.	YES	Under Article 6.8 of the Regulations of the General Meeting at the request of a participant of the General Meeting, any written declaration by the participant shall be recorded in the minutes of the Meeting.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF SUPERVISORY BOARDS		
18	The supervisory board submits a concise evaluation of the Company's standing to the general meeting every year. The evaluation should be made available to all shareholders early enough to allow them to become acquainted with the contents before the annual general meeting.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
19	A member of the supervisory board should have the relevant education, the appropriate professional and practical experience, be of high moral standing and be able to devote the time required to perform his supervisory board function properly. Supervisory board candidature should be announced and supported by reasons sufficiently detailed to enable an informed choice to be made.	YES	This rule applies to the Bard of Directors.
20	a) At least half the members of the supervisory board should be independent members, subject to point (d) below. Independent members of the supervisory board should not have relations with the Company and its shareholders or employees which could significantly affect the independent member's ability to make impartial decisions. b) Detailed independence criteria should be laid down in the Company's statutes. c) Without the consent of the majority of independent supervisory board members, no resolutions should be adopted on the following issues: - performances of any kind by the Company and any entities associated with the Company in favour of management board members;	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF SUPERVISORY BOARDS		
20	- consent to the execution by the Company or a subsidiary of a key agreement with an entity associated with the Company, a member of the supervisory board or management board, or with their associated entities; and appointment of an auditor to audit the Company's financial statements. d) In companies where one shareholder holds a block of shares carrying over 50% of all voting rights, the supervisory board should consist of at least two independent members, including an independent chairman of the audit committee, should such a committee be set up.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
21	A supervisory board member should, above all, keep the Company's interests in mind.	YES	This rule applies to the Board of Directors.
22	Supervisory board members should take the relevant action to receive from the management board regular and complete information on any and all significant issues concerning the Company's operations and on any risks related to the business and ways of managing such risks.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
23	A supervisory board member should inform the other members of the board of any conflict of interest that arises, and should refrain from participating in discussions and from voting on any resolution on the issue in respect of which the conflict of interest has arisen.	YES	This rule applies to the Board of Directors.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF SUPERVISORY BOARDS		
24	Information on a supervisory board member's personal, actual and organizational connections with a given shareholder, particularly with the majority shareholder, should be made publicly available. The Company should have a procedure in place for obtaining such information from supervisory board members and for making it publicly available.	YES	Under Article 9.16 of the Articles of Association, a director having a personal interest contrary to that of the Company in a matter submitted to the approval of the Board of Directors shall be obliged to inform the Board of Directors thereof and to have his declaration recorded in the minutes of the meeting. He may not take part in the relevant proceeding of the Board of Directors. At the next General Meeting, before votes are taken in any other matter, the shareholder shall be informed of those cases in which a director had a personal interest contrary to that of the Company.
25	Supervisory board meetings should be accessible and open to management board members, save for issues which directly concern the management board or its members, especially the removal, liability and remuneration (of management board members).	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF SUPERVISORY BOARDS		
26	A supervisory board member should make it possible for the management board to present publicly and in an appropriate manner information on the transfer or acquisition of shares in the Company or in its dominant Company or subsidiary and of transactions with such companies, provided that such information is relevant to his financial standing.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
27	Supervisory board members' remuneration should be set on the basis of a set of transparent procedures and rules. The remuneration should be fair but should not constitute a significant cost item in the Company's business or have a material impact on its financial results. It should also be in reasonable relation to the remuneration of members of the management board. The total amount of all supervisory board members' remuneration, as well as the remuneration of individual members, with a breakdown of its various elements should be disclosed in the annual report together with information on the procedures and rules applied to determine it.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
28	The supervisory board should operate in accordance with its by-laws, which should be publicly available. The by-laws should stipulate that at least two committees should be set up: audit, and remuneration. The audit committee should consist of at least two independent members and at least one person possessing the relevant qualifications and experience in accounting and finance. The committee's tasks should be specified in the board by-laws. The committees should present reports on their activities to the supervisory board every year. The Company should then make these reports available to its shareholders.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.

07

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF SUPERVISORY BOARDS		
29	The agenda of a supervisory board meeting should not be amended or supplemented during the meeting to which it relates. This requirement does not apply if all the supervisory board members are present and agree to the amendment or supplementation, and if certain actions have to be taken by the supervisory board to protect the Company against damage and in the case of a resolution assessing whether there is a conflict of interests between a supervisory board member and the Company.	YES	
30	A supervisory board member delegated by a group of shareholders to permanently exercise supervision should submit detailed reports on the performance of his task to the supervisory board.	NO	As there is no Supervisory Board in the Company, we are unable to comply with this rule.
31	A supervisory board member should not resign from his function during his term of office if this would make it impossible for the board to function, particularly if it could hinder the timely adoption of an important resolution.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF MANAGEMENT BOARDS		
32	With the Company's interests in mind, the management board sets out the strategy and the main objects of the Company's operations and submits them to the supervisory board. The management board is responsible for implementation and performance. The management board sees that the Company's management system is transparent and effective and that its business is conducted in accordance with legal regulations and best practice.	YES	
33	When making decisions on corporate issues, management board members should act within the limits of justified business risk, i.e. after considering all information, analyses and opinions, which, in the reasonable opinion of the management board, should be taken into account in a given case in view of the Company's interest. When determining the Company's interests, the long-term interests of the Company's shareholders, creditors and employees should be kept in mind, as well as those of other entities and persons cooperating with the Company, also the interests of the local community.	YES	
34	In transactions with shareholders and other persons whose interests affect those of the Company, the management board should act with the utmost care to ensure that the transactions are carried out at arm's length.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF MANAGEMENT BOARDS		
35	A management board member should always be loyal to the Company and avoid actions which could lead to the advancement of his own material interests only. If a management board member receives information about the opportunity to make an investment or another advantageous transaction relating to the Company's objects, he should put this information immediately before the management board to be reviewed in terms of the Company taking advantage of it. Such information may only be used by a management board member or passed on to a third party with the consent of the management board and only if it does not infringe on the Company's interests.	YES	
36	A management board member should treat his shares in the Company and its dominant companies and subsidiaries as a long-term investment.	YES	
37	Management board members should inform the supervisory board whenever a conflict of interests arises, or if there is a risk of a conflict of interests arising in connection with the function performed.	YES	
38	The remuneration of management board members should be set on the basis of transparent procedures and principles, taking into account its incentive nature and ensuring effective and smooth management of the Company. The remuneration should correspond to the size of the Company's business enterprise, should be in reasonable relation to business results, and be related to the scope of liability in a given function, taking into account the level of remuneration of members of management boards in similar companies on a similar market.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES OF MANAGEMENT BOARDS		
39	The total amount of all management board members' remuneration, as well as the remuneration of individual members, with a breakdown of its various elements should be disclosed in the annual report together with information on the procedures and rules applied to determine it. If the amount of the remuneration of individual members of the management board significantly differs, it is recommended that a relevant explanation be published.	NO	Under Art. 3.1 of the Regulations of the Board of Directors, the principles and the level of remuneration of Directors shall be set by the General Meeting.
40	The management board should lay down in the by-laws principles and procedures for operating and allocating powers. These principles should be clear and generally available.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES IN RELATIONS WITH THIRD PARTIES AND THIRD PARTY INSTITUTIONS		
41	When selecting an auditor, the Company should ensure that he will perform the tasks entrusted to him impartially.	YES	
42	In order to ensure an impartial opinion, the Company should change its auditor once every five years at the least. The change of auditor should also be understood as a change in the individual carrying out the audit. Additionally, over a long period of time the Company should not use the services of the same auditing entity.	YES	
43	The auditor should be selected by the supervisory board on the recommendation of the audit committee, or by the general meeting on the recommendation of the supervisory board containing the audit committee recommendation. If an auditor other than the one recommended by the audit committee is chosen by either the board or the general meeting, detailed reasons should be given. Information on the selection of an auditing entity together with the relevant justification should be disclosed in the annual report.	NO	According to Article 14 of the Articles of Association the audit of the Company's annual accounts shall be entrusted to one or several external auditors (réviseurs d'entreprises), appointed by the General Meeting which shall fix their number, remuneration, and their term of office.
44	The current auditor or the auditor auditing the annual accounts of the Company or its subsidiaries in the period under examination cannot act as a special purpose auditor for the same Company.	YES	

No.	RULE	YES / NO	COMMENT OF PEGAS NONWOVENS SA
	BEST PRACTICES IN RELATIONS WITH THIRD PARTIES AND THIRD PARTY INSTITUTIONS		
45	A Company should acquire its own shares in such a way that no group of shareholders is privileged.	YES	
46	The Company's statutes, its basic internal regulations, information and documents related to general meetings, and its financial statements should be made available in the Company's registered office and on its website.	YES	
47	A Company should have appropriate media relations procedures and regulations and an information policy ensuring coherent and reliable information about the Company. The Company should, in compliance with legal regulations and to safeguard its interests, make information on its current operations and business standing available to media representatives and allow them to attend general meetings.	YES	
48	In its annual report, a Company should include a statement to the effect that corporate governance standards are applied. Any departure from these standards should also be publicly explained.	YES	

7.5 Risk Factors

The Company's business, results of operations and financial condition may be adversely affected by the following risks:

Marketing and Sales

PEGAS operates in a highly competitive market and the emergence of new competitors could adversely affect sales.

A high concentration of customers account for a significant percentage of the total sales, and the loss of one or more of them could significantly affect the Company's revenues and profitability.

Production

Any disruption to the production facilities would have a material adverse effect on the Company's business. PEGAS is dependent on one manufacturer for production line equipment and technical support. There is a risk that PEGAS may not be able to reconfigure production lines on a timely basis in order to respond to changing demand for particular kinds of spunmelt nonwovens.

The Company's competitors may have access to more and cheaper sources of capital allowing them to modernize and expand their operations more quickly and giving them a substantial competitive advantage over PEGAS.

The steady supply and transportation of products from the Company's plants to the customers are subject to various uncertainties and risks.

PEGAS depends on external suppliers for key raw materials. Therefore increases in the cost of raw materials and electricity could have a material adverse impact on the Company's financial condition and results of operations, although polymer price increases are normally transferred to customers through increased prices.

Potential Expansion

PEGAS may face risks associated with potential acquisitions, investments, strategic partnerships or other ventures, including opportunities identification, risk of the completion of the transaction and the integration of the other parties into PEGAS's business.

Legal and Intellectual Property

PEGAS's operations are exposed to financial and operating uncertainty and being subject to government laws and regulations that may adversely affect results of operations and financial conditions.

PEGAS may be in breach of intellectual property rights of others.

Adverse outcomes in litigation to which PEGAS is a party could harm the business and its prospects.

Finance

The indebtedness of PEGAS could adversely affect financial condition and results of operations. There is a risk that the fluctuations in the value of the Czech koruna against the Euro could adversely affect the Company's profitability. PEGAS's operating subsidiaries avail themselves of tax benefits offered by the Czech government. Hence, the Company's profitability could decrease owing to any adverse change in general tax policies or if the tax benefits were reduced or withdrawn.

Insurance coverage may not adequately protect PEGAS against possible risk of loss.

Security, Environment and Safety

Compliance with, and changes in, safety, health and environmental laws and regulations may adversely affect the Company's results of operations and financial conditions.

Key Personnel and Technical Expertise

The loss of the services of key management personnel could adversely affect the Company's business.

PEGAS may not be able to hire and retain sufficient numbers of qualified professional personnel because these personnel are limited in number and are in high demand.

Major Shareholder

The major shareholder will continue to exercise significant control over the Company, and its interests may differ from the Company interest and those of other shareholders.

08

Consolidated Financial Statements and Notes to the Financial Statements, Independent Auditor's report

8.1 Independent Auditor's Report

KPMG

KPMG Audit
31, Allée Scheffer
L-2520 Luxembourg

Téléphone +352 22 51 51 1
Fax +352 22 51 71
audit@kpmg.lu
www.kpmg.lu

To the Shareholders of:
PEGAS NONWOVENS S.A.
68-70, boulevard de la Pétrusse
L-2320 Luxembourg

REPORT OF THE REVISEUR D'ENTREPRISES

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of PEGAS NONWOVENS S.A., which comprise the consolidated balance sheet as at December 31, 2006 and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Board of directors' responsibility for the consolidated financial statements

The board of directors is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Responsibility of the Réviseur d'Entreprises

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing as adopted by the Institut des Réviseurs d'Entreprises. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the judgement of the réviseur d'entreprises, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the réviseur d'entreprises considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the board of directors, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

KPMG

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of PEGAS NONWOVENS S.A. as of December 31, 2006, and of its financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Report on other legal and regulatory requirements

The consolidated management report, which is the responsibility of the board of directors, is in accordance with the consolidated financial statements.

Luxembourg, April 28, 2007

KPMG Audit S.à r.l.
Réviseurs d'Entreprises

Thierry Ravasio

2

8.2 Consolidated Statement of Income for the Year end December 31st

PEGAS NONWOVENS S.A.
Consolidated Income Statement
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Note	2006	from 18 November to 31 December 2005
Revenue	8.6.5 a), b)	120 941	4 787
Raw materials and consumables used	8.6.5 c)	(71 936)	(3 981)
Staff cost	8.6.5 f), g)	(5 111)	(209)
Depreciation and amortisation expense	8.6.5 h)	(12 152)	(535)
Research and development expense	8.6.5 e)	(1 803)	–
Other operating income (expense) – net	8.6.5 d)	11 172	(460)
Profit (loss) from operations		**41 111**	**(398)**
Finance costs	8.6.5 i)	(18 805)	(714)
Profit (loss) before income tax		**22 306**	**(1 112)**
Income tax expense	8.6.5 j)	(1 601)	(255)
Profit (loss) for the year / period		**20 705**	**(1 367)**
Attributable to:			
Equity holders of the Company		20 274	(1 367)
Minority interest		431	–
Net profit (loss) for the year / period		**20 705**	**(1 367)**
Earnings (loss) per share	8.6.5 k)		
Basic earnings (loss) per share (Euro)		24.66	(13.56)
Diluted earnings (loss) per share (Euro)		2.92	(0.15)

The Notes are an integral part of these consolidated financial statements.

8.3 Consolidated Balance Sheet as at December 31st

1/2

PEGAS NONWOVENS S.A.
Consolidated Balance Sheet
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Note	2006	2005 As restated*
Assets			
Non-current assets			
Property, plant and equipment	8.6.5 m)	110 522	111 113
Intangible assets	8.6.5 n)	102	24
Goodwill	8.6.5 n)	84 384	79 991
Total non-current assets		**195 008**	**191 128**
Current assets			
Inventories	8.6.5 o)	8 363	8 622
Trade and other receivables	8.6.5 p)	23 640	23 785
Cash and cash equivalents	8.6.5 q)	22 014	27 034
Total current assets		**54 017**	**59 441**
Total assets		**249 025**	**250 569**
Equity and Liabilities			
Share Capital and reserves	8.6.5 r),s)		
Share capital		11 444	125
Share premium		41 011	–
Other reserves		–	4 432
Translation reserves		725	(4)
Retained Earnings		23 770	(1 367)
Total share capital and reserves		**76 950**	**3 186**

The Notes are an integral part of these consolidated financial statements.

8.3 Consolidated Balance Sheet as at December 31st

2/2

PEGAS NONWOVENS S.A.
Consolidated Balance Sheet
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Note	2006	2005 As restated*
Non-current liabilities			
Bank loans	8.6.5 t)	122 851	157 268
Other payables	8.6.5 u)	275	37 224
Deferred tax liabilities	8.6.5 v)	15 225	14 952
Total non-current liabilities		**138 351**	**209 444**
Current liabilities			
Trade and other payables	8.6.5 w)	20 212	21 670
Tax liabilities	8.6.5 x)	192	19
Bank current liabilities	8.6.5 t)	13 320	16 250
Total current liabilities		**33 724**	**37 939**
Total liabilities		**172 075**	**247 383**
Total equity and liabilities		**249 025**	**250 569**

* See Note 8.6.5 (n)
The Notes are an integral part of these consolidated financial statements.

8.4 Consolidated Cash Flow Statement for the Year end December 31st

1/2

PEGAS NONWOVENS S.A.
Consolidated Cash Flow Statement
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Note	2006	from 18 November to 31 December 2005
Profit (loss) for the year / period before tax		**22 306**	**(1 112)**
Adjustment for:			
Amortization and depreciation		12 152	535
Foreign exchange gains		(6 894)	(4)
Interest expense		18 805	714
Fair value changes of interest rate swap		(1 869)	
Cash flows from operating activities			
Decrease (increase) in inventories		259	(593)
Decrease (increase) in receivables		2 013	2 703
Increase (decrease) in payables		(1 484)	1 397
Income tax paid		(1 601)	–
Net cash from operating activities		**43 687**	**3 640**
Cash flows from investment activities			
Purchases of property, plant and equipment		(5 265)	(77)
Acquisition of subsidiary		–	(191 405)
Net cash used in investing activities		**(5 265)**	**(191 482)**

8.4 Consolidated Cash Flow Statement for the Year end December 31st

2/2

PEGAS NONWOVENS S.A.
Consolidated Cash Flow Statement
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Note	2006	from 18 November to 31 December 2005
Cash flows from financing activities			
Increase (decrease) in bank loans		(34 381)	173 518
Increase (decrease) in long term debt		(28 104)	37 224
Issuance of share capital		40 513	125
Issuance (repayment) of convertible debt		(1 460)	4 432
Interest paid		(18 801)	(423)
Net cash from (used in) financing activities		**(42 233)**	**214 876**
Net increase (decrease) in cash and cash equivalents		**(3 811)**	**27 034**
Cash and cash equivalents at the beginning of the period		27 034	–
Effect of exchange rate fluctuations on cash held		(1 209)	–
Cash and cash equivalents at 31 December	**8.6.5 q)**	**22 014**	**27 034**

The Notes are an integral part of these consolidated financial statements.

8.5 Consolidated Statement of Changes in Equity for the Year end December 31st, 2006

PEGAS NONWOVENS S.A.
Consolidated Statement of Changes in Equity
prepared under International Financial Reporting Standards (IFRS)

(in thousands of Euro)

	Share capital	*Share premium*	*Other reserves*	*Translation reserves*	*Retained earnings*	Total equity attributable to equity holders of the Company	*Minority interest*	*Total equity*
at 18 November 2005	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Capital increase	125	–	–	–	–	**125**	–	**125**
Exchange differences	–	–	–	(4)	–	**(4)**	–	**(4)**
Net loss for the period	–	–	–	–	(1 367)	**(1 367)**	–	**(1 367)**
Equity element of convertible debt	–	–	2 972	–	–	**2 972**	–	**2 972**
Equity element of mezzanine loan	–	–	1 460	–	–	**1 460**	–	**1 460**
at 31 December 2005	**125**	**–**	**4 432**	**(4)**	**(1 367)**	**3 186**	**–**	**3 186**
Share issue	11 319	46 626	–	–	–	**57 945**	–	**57 945**
Equity issue expenses recognized directly in equity net of tax	–	(5 615)	–	–	–	**(5 615)**	–	**(5 615)**
Conversion of convertible debt	–	–	(2 972)	–	2 972	**–**	–	**–**
Repayment of mezzanine loan			(1 460)	–	1 460	**–**	–	**–**
Exchange differences	–	–	–	729	–	**729**	–	**729**
Net profit for the year	–	–	–	–	20 274	**20 274**	431	**20 705**
Acquisition of minority interest	–	–	–	–	431	**431**	(431)	**–**
at 31 December 2006	**11 444**	**41 011**	**–**	**725**	**23 770**	**76 950**	**–**	**76 950**

The Notes are an integral part of these consolidated financial statements.

8.6 Notes to Consolidated the Financial Statements

8.6.1 General Information and Definition of the Consolidated Entity

Description and principal activities

PEGAS NONWOVENS S.A. ("the Company"), originally incorporated under the name Pamplona PE Holdco 2 S.A., is a commercial company incorporated in Luxembourg on 18 November 2005, under the legal form of a "Société anonyme". The registered office is at 68-70, boulevard de la Pétrusse, L-2320 Luxembourg and the Company is registered with the Commercial Register of Luxembourg under number B 112.044. The Company acts only as a holding company.

On 14 December 2005, the Company acquired full control over the activities of PEGAS a.s. (now PEGAS NONWOVENS s.r.o.)

PEGAS NONWOVENS s.r.o. is incorporated in the Czech Republic. Its registered office is located in Znojmo, Přímětická 86, 669 04. PEGAS NONWOVENS s.r.o. and its subsidiaries are engaged in the production of non-woven textiles.

The consolidated financial statements of the Company as at and for the year ended 31 December 2006 comprise the Company and its subsidiaries (together referred to as the "Group"). The financial statements for the period ended 31 December 2005 were prepared for the period from 18 November 2005 to 31 December 2005. As a result, the information about revenues, expenses, results of operations, cash flows and changes in equity is not fully comparable.

8.6.2 Basis of Preparation

a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and its interpretations adopted by the International Accounting Standards Board (IASB) for use in the European Union.
These consolidated financial statements were approved by the Board of Directors and authorized for issue on 19 April 2007.

b) Functional Currency

The financial statements are presented in thousands of Euro ("TEUR"). In accordance with IAS 21, the underlying functional currency of PEGAS NONWOVENS s.r.o. and its subsidiaries is Czech Koruna ("CZK"). Their financial statements were translated from the functional currency to the presentation currency. The underlying functional currency of PEGAS NONWOVENS S.A. is Euro.

c) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for derivative financial instruments which are measured at fair value.

d) Use of estimates and judgements

The preparation of financial statements in compliance with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making the judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. The actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both the current and future periods.

8.6.3 Summary of Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements and have been applied consistently by Group entities.

a) Consolidation methods

The consolidated financial statements incorporate the financial statements of PEGAS NONWOVENS S.A. and entities controlled by the Company (its subsidiaries). Control exists where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Assets, liabilities and contingent liabilities, which fulfill the criteria for accounting recognition pursuant to IFRS 3, are measured to fair value at the date of acquisition.

Any excess of the cost of acquisition over the fair value of the net identifiable assets acquired is accounted for as goodwill. Any excess of the fair value of the net identifiable assets acquired over the cost of acquisition is accounted for in the income statement in the accounting period in which the acquisition takes place.

Minority interests and ownership interests of minority investors of the consolidated subsidiaries are valued at the minority shareholder's proportionate interest in the net fair value of assets and liabilities recognized in the accounting.

As and when necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with those used by other members of the Group.

All intra-group transactions, balances, income, expenses and dividends are eliminated on consolidation.

b) Foreign currencies

All Czech based companies in the Group operate in the Czech Republic which is their primary economic area. Consequently, the Czech Koruna (CZK) is the functional currency of these entities. Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. Foreign currency differences arising on retranslation are recognized in profit or loss.

For the purpose of presenting consolidated financial statements, the assets and liabilities are expressed in Euro using exchange rates ruling at the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used.

Exchange rates used CZK/EUR (source: official rates of Czech National Bank):

	1 January 2006 - 31 December 2006
Period average (P&L)	28.343
	31 December 2006
Balance sheet date	27.495

Exchange differences arising from the above stated exchange rates, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognized in profit or loss in the period in which the foreign operation is disposed of.

c) Revenue recognition

Revenues are recognized at fair value of the consideration received or the consideration to be received and represent receivables for goods and services delivered in the normal course of business, net of discounts, VAT and other sales-related taxes.

Revenues from the sale of products are recognized when products are delivered and either the title to the products has been passed to the customer or the risks to the products have been passed to the carrier. Revenues from the sale of services are recognized when the service is rendered.

d) Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing related products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

e) Research and development

Expenditure on research activities, undertaken with the prospect of acquiring new scientific or technical knowledge and understanding, is recognized in the income statement as an expense as incurred.

Expenditure on development activities is capitalized if the product or process is technically and economically feasible. The expenditure capitalized includes the cost of materials, direct labour and an appropriate proportion of overheads. Other development expenditure is recognized in the income statement as an expense as incurred. Capitalized development expenditure is stated at cost less accumulated amortization and impairment losses.

f) Costs associated with the initial public offering

Costs incurred to increase equity are deducted from the amount of equity, but only to the extent related to the issue of new shares. Transaction costs attributable to the issue of new shares are directly debited to equity less all related tax implications. These costs primarily include external costs incurred for legal, accounting and other advisory services, direct communication with investors and remuneration paid to financial institutions mediating the subscription of shares in the public market. All costs that have been incurred continuously but do not directly relate to the increase in equity are charged to expenses.

g) Borrowing costs

Borrowing costs are recognized in the income statement in the period to which they relate.

h) Taxation

The tax expense in the income statement includes current and deferred tax expenses.

Current tax

Current income tax is based on taxable profit and the tax base. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other periods and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted under local legislation by the balance sheet date.

Deferred tax

Deferred tax liabilities and assets arising on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases of these assets and liabilities used in the computation of taxable profit are accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences and deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realized. Deferred tax is charged or credited to the profit or loss account.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

i) Government grants

Grants and subsidies relating to employees

The Government of the Czech Republic has provided grants to train employees and subsidies to establish new jobs. These grants and subsidies were accounted for in the year in which related expenses were incurred.

Grants relating to income tax

Grants relating to income tax represent investment incentives. The Group does not account for a total tax liability but records its tax liability less the expected amount of investment incentives.

j) Property, plant and equipment

Property, plant and equipment is stated at cost (including costs of acquisition) less accumulated depreciation and any recognized impairment loss.

The cost of assets (other than land and assets under construction) is depreciated over their estimated useful lives, using the straight-line method, on the following basis:

Major groups of assets	Number of years
Production lines	12 – 20
Factory and office buildings	30 – 60
Cars and other vehicles	5 – 6

The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

k) Intangible assets

Purchased intangible assets are stated at cost less accumulated amortization. They are amortized on a straight-line basis over their estimated useful lives.

The carrying amounts of intangible assets are reassessed to identify impairment losses where events or changes of facts indicate that the carrying amount of each individual asset exceeds its recoverable amount.

Intangible assets primarily include software, which is amortised on a straight-line basis over its estimated useful life, which is eight years.

l) Goodwill

Goodwill represents a positive difference between the cost of acquisition and the fair value of the acquired interest in net identifiable assets and liabilities of a subsidiary as at the date of acquisition. Goodwill arising on an acquisition of subsidiaries is included in intangible assets. After the initial recognition, goodwill is stated at cost less impairment losses.

At the acquisition date, goodwill is allocated to each of the Group's cash generating units expected to benefit from the synergies of the combination.

m) Impairment of assets

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). If the asset is not a separate cash-generating unit, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

For the purposes of impairment testing, goodwill is allocated to each of the Group's cash generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognized for goodwill is not reversed in a subsequent period.

The management has determined that for goodwill testing purposes all acquired subsidiaries are considered as one cash generating unit.

n) Inventories

Inventories are stated at the lower of cost and net realisable value. The cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. The cost is calculated using the weighted average method. The net realisable value is the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

The cost of finished products comprises direct materials and direct labour costs and a proportion of production overheads based on normal operating capacity, excluding finance costs.

o) Financial instruments

Financial assets and financial liabilities are recognized in the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

p) Derivative financial instruments

The Group's operating activities are primarily exposed to the financial risks such as changes in foreign exchange rates and interest rates. Where necessary, the Group uses derivative financial instruments to hedge these risks.

Derivative financial instruments are initially measured at fair value on the contract date, and are remeasured to fair value at subsequent reporting dates.

A derivative is a financial instrument or other contract which fulfils the following conditions:

- *its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract*
- *it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and*
- *it is settled at a future date.*

Derivative financial instrument which do not fulfill the criteria for hedging instruments are classified as held-for-trading and carried at fair value, with changes in fair value included in net profit or loss of the period in which it arises.

The Group uses interest rate swaps to hedge the risk of changes in interest rates. As the group does not perform hedge accounting, these swaps are regarded as held-for-trading and changes in their fair values are recognized directly in the income statement.

q) Trade receivables

Short-term trade receivables do not carry any interest and are stated at their nominal value reduced by appropriate allowances for estimated irrecoverable amounts.

Long-term trade receivables are discounted to their present value.

r) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, bank accounts and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

s) Financial liabilities and equity

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

For convertible debts, the part which corresponds to a potential interest in equity of the Company is reported as part of equity.

t) Borrowings

Interest-bearing bank loans

Interest-bearing bank loans and overdrafts are initially measured at fair value, and are subsequently measured at amortized cost, using the effective interest rate method.

Any difference between the proceeds (net of transaction costs) and the settlement or redemption of borrowings is recognized over the term of the borrowings using the effective interest rate method.

Convertible loan notes

Convertible loan notes are regarded as compound instruments, consisting of a liability component and an equity component. At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for similar non-convertible debt. The difference between the proceeds of issue of the convertible loan notes and the fair value assigned to the liability component, representing the embedded option for the holder to convert the loan note into equity of the Group, is included in equity (capital reserves).

u) Provisions

Provisions are recognized when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the management's best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to the present value where the effect is material.

v) Trade payables

Short-term trade payables are stated at their nominal value. Long-term trade payables are discounted to their present value.

w) New standards and interpretations not yet adopted

Certain new standards, amendments and interpretations to existing standards have been published. There application is mandatory for accounting periods beginning on or after 31 December 2006. The Company has not opted for their early adoption. These include:

- *Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures (effective for annual periods beginning on or after 1 January 2007). The Standard will require increased disclosure in respect of the Group's capital. Amendments arise from the issue of IFRS 7. The management will apply this amendment from the annual period beginning on 1 January 2007.*

- *IFRS 7 Financial Instruments: Disclosures (effective for annual periods beginning on or after 1 January 2007). The Standard requires the entities to provide disclosures in the financial statements that enable users to evaluate the significance of financial instruments for the entity's financial position and performance, and the nature and extent of risks arising from financial instruments and how the entity manages the risks. Management does not expect any significant effects on adoption of this Standard.*
- *IFRS 8 Operating Segments: Management does not expect any significant effects on adoption of this Standard.*
- *IFRIC 7 Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies (effective for annual periods beginning on or after 1 March 2006). The Interpretation contains guidance on how an entity would restate its financial statements pursuant to IAS 29 in the first year it identifies the existence of hyperinflation in the economy of its functional currency. IFRIC 7 is not relevant to the Group as its functional currency is not a currency of a hyperinflationary economy.*
- *IFRIC 8 Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006). The Interpretation clarifies that the accounting standard IFRS 2 Share-based Payment applies to arrangements where an entity makes share based payments for apparently nil or inadequate consideration. IFRIC 8 is not relevant to the Group.*
- *IFRIC 9 Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006). The Interpretation requires that a reassessment of whether an embedded derivative should be separated from the underlying host contract should be made only when there are changes in the terms of the contract that significantly modify the cash flows that otherwise would be required under the contract. The Group has not yet completed its analysis of the impact of the new Interpretation.*
- *IFRIC 10 Interim Financial Reporting and Impairment: The Group has not yet completed its analysis of the impact of the new Interpretation.*
- *IFRIC 11 Group and Treasury Share Transactions: The Group has not yet completed its analysis of the impact of the new Interpretation.*
- *IFRIC 12 Service Concession Arrangements: The Group has not yet completed its analysis of the impact of the new Interpretation.*

8.6.4 Financial Risks

In connection with its activities the Group is exposed to financial risks, in particular currency and interest rate risks. When managing its financial risks, the Group concentrates on unpredictability of financial markets and endeavours to minimise potential negative effects on the results of operations.

Currency risk

Even though the Group carries out its activities only in the Czech Republic, it makes business on an international level, which results in the exposure to currency risks in respect of both its operating and financial activities. The functional currency of PEGAS NONWOVENS s.r.o. and its subsidiaries is Czech Koruna (CZK) but the majority of purchases are carried out in Euros. The majority of financial activities (such as repayment of loans and interest) are also carried out in Euros. Sales of products are carried out in CZK, EUR and USD.

The sales of own production in EUR and CZK cover the purchases of raw material and debt servicing, which results in natural hedging of the Group's activities by cash flows in these currencies. (Consequently, the Group did not use any foreign exchange derivatives to reduce currency risk as at 31 December 2006).

Credit risk

The vast majority of sales are on credit to customers. Risks arising from the provision of credit are fully covered by insurance policies in respect of individual customers' receivables or by receiving advanced payments from customers.

Interest rate risk

The interest rate risk arises from bank loans bearing variable interest rates. Interest rate swaps are used to hedge the interest rate exposure.

8.6.5 Notes to the Consolidated Financial Statements

a) Revenue

Product groups:

	2006		2005	
	% of total		% of total	
Hygiene Sales				
Hygiene-specialty	28 498	23.6	353	7.4
Hygiene-other	78 870	65.2	3 841	80.2
Total hygiene	**107 368**	**88.8**	**4 194**	**87.6**
Non-hygiene	**13 573**	**11.2**	**593**	**12.4**
Total sales	*120 941*	*100.0*	*4 787*	*100.00*

Markets

	2006	2005
Domestic sales	14 729	559
Export	106 212	4 228
Total	*120 941*	*4 787*

b) Segment reporting

The Group solely produces non-woven textiles and the management has not identified any reportable segments.

Geographical segments are defined as follows:

Region	2006
Western Europe	52 006
Central and Eastern Europe	31 853
Russia	4 099
Others	32 983
Total	*120 941*

In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of the customer.

All the assets are located in, and all expenditure on assets is in, the Czech Republic.

c) Raw materials, consumables and services used

	2006	2005
Raw materials consumed	64 207	2 977
Consumed spare parts and repairs	2 623	24
Energy consumed	3 553	125
Other consumables	467	348
Other services	1 086	507
Total raw materials and consumables used	***71 936***	***3 981***

Raw materials consumed amount to 89% of the total amount of raw materials and services consumed.

d) Other operating income / (expense) (net)

	2006	2005
Realized and unrealized foreign exchange gains (losses)	9 334	(1)
Fair value changes of interest rate swap	1 869	--
Gain/(loss) on the sale of equipment	25	12
Interest income	613	22
Insurance proceeds	101	--
Insurance cost	(504)	--
Other taxes	(25)	(6)
Other expenses	(241)	(487)
Other operating income/ (expense) net total	***11 172***	***(460)***

e) Research and development

In 2006, the Group invested TEUR 1 803 in research and development. The most significant part represents expenditure on raw materials for products testing in the amount of TEUR 1 423.

f) Average number of employees and executive managers of the Group and expenses

	Average number of employees	Total	Wages and salaries	Social securityand health insurance expenses	Social expenses
Employees	306	3 916	2 827	994	95
Executives	18	1 195	935	254	6
Total	*324*	*5 111*	*3 762*	*1 248*	*101*

Apart from using the company vehicles for both business and private purposes, executive managers do not receive any other benefits in addition to their salaries.

g) *Remuneration, advances, loans, guarantees and other kind of performance, both monetary and in kind, provided to current and former board members*

In 2006, remuneration to members of the board of directors and supervisory board amounted to TEUR 217.

Board members did not receive any loans, share options, advances or any other benefit in kind in both 2006 and 2005.

h) *Depreciation and amortization expense*

	2006	2005
Depreciation of tangible assets	12 056	535
Amortization of intangible assets	96	--
Total	***12 152***	***535***

i) *Finance costs/(income) (net)*

	2006	2005
Interest and debt settlement expenses on loans and borrowings	18 238	622
Interest on employee deposits	77	92
Other	490	--
Total	***18 805***	***714***

j) *Income tax expense*

	2006	2005
Current income tax	1 703	345
Deferred income tax	(102)	(90)
Total	***1 601***	***255***

Effective tax rate

	2006		2005	
Profit/(loss) before tax	***22 306***		***(1 112)***	
Income tax calculated using the effective tax rate	5 353	24.0 %	(289)	26.0 %
Effect of tax non-deductible expenses	70	0.3 %	--	--
Effect of non-taxable revenues	(28)	(0.1 %)	--	--
Effect of consolidation and IFRS adjustments that do not have impact on deferred tax	1 140	5.1 %	--	--
Effect of tax incentives	(4 951)	(22.2 %)	(149)	13.4 %
Tax relating to prior periods	(112)	(0.5 %)	--	--
Effect of items deductible from the tax base	(60)	(0.3 %)	--	--
Effect of unrecognized deferred tax asset in the Czech Republic	(2)	(0.0 %)	--	--
Effect of the difference between the tax rate in the Czech Republic and Luxembourg and effect of unrecognized deferred tax asset relating to PEGAS NONWOVENS S.A. in Luxembourg	190	0.9 %		
Tax discounts	(7)	(0.0 %)		
Lump sum tax PEGAS NONWOVENS S.A.	8	0.0 %	693	(62.3 %)
Total income tax / effective tax rate	***1 601***	***7.2 %***	***255***	***(22.9 %)***

Three companies of the Group received investment incentives in the Czech Republic.

Investment incentives are tax savings granted by the government provided certain conditions have been fulfilled (such as level of incremental investments) by the Group. When considering the principle of prudence and the fact that the amount of a subsidy depends on the actual economic performance, the companies do not account for any intangible asset that arise from investment incentives and correspond to income tax subsidies. The estimate of the unrecognized asset would not be reliable.

Since nearly all taxable income were generated from the operating activity in the Czech Republic, the tax rate of 24 % (2005 - 26 %) in the Czech Republic was used to calculate the total income tax.

k) Earnings (loss) per share

The calculation of basic earnings per share as at 31 December 2006 was based on the net profit attributable to equity holders of TEUR 20 274 and a weighted average number of ordinary shares in 2006. Diluted earnings per share are calculated based on a weighted average number of shares in circulation (determined similarly as in the case of basic earnings per share) adjusted by the effect of the expected issue of all potential diluted securities, i.e. the effect of convertible loan notes in the case of the Group. Convertible bonds are the bonds with a right to convert to ordinary shares.

As at 31 December 2006, there were no minority interests in subsidiary companies. Minority interest was attributable to the 6 manager's participation in CEE Enterprise a.s. The participation commenced in January 2006 and was terminated in November 2006 when the 6 managers became shareholders of the Company.

Weighted average number of ordinary shares

2005

	Number of outstanding shares in 2005	Weighted average
November - December	100 806	100 806

2006

	Number of outstanding shares in 2005	Weighted average
January - November	100 806	91 692
December	9 229 400	730 302
Total		***821 994***

Basic earnings (loss) per share

		2006	2005
Net profit attributable to equity holders	TEUR	20 274	(1 367)
Weighted average number of ordinary shares	Number	821 994	100 806
Basic earnings (loss) per share	***EUR***	***24.66***	***(13.56)***

Earnings Per Share (EPS) is calculated as net profit for the year attributable to equity holders of the Company divided by weighted average of number of shares existing each day in the year 2006.

The Basic EPS attributable to equity holders of the Company based on the number of shares existing as at 31 December 2006 is 2.20 EUR.

Weighted average number of ordinary shares for calculation of diluted earnings per share

2005

	Number of outstanding shares in 2005	Weighted average
Shares:		
November - December	100 806	100 806
Convertible bonds and warrants (recalculated to potential ordinary shares): November - December	8 588 659	8 588 659
Total		***8 689 465***

2006

	Number of outstanding shares in 2005	Weighted average
Shares:		
January - November	100 806	91 692
December	9 229 400	730 302
Convertible bonds and warrants (recalculated to potential ordinary shares): January - November	8 592 541	7 872 123
For the whole year		***8 694 117***

Diluted earnings (loss) per share

		2006	2005
Net profit (loss) for the year / period attributable to equity holders	TEUR	20 274	(1 367)
Finance costs related to convertible bonds	TEUR	5 375	59
Tax effect of the finance costs	TEUR	(240)	–
Net profit attributable to equity holders adjusted by finance costs related to convertible bonds including income tax effect	TEUR	25 409	(1 308)
Weighted average number of ordinary and potential ordinary shares	Number	8 694 117	8 689 465
Diluted earnings (loss) per share	***EUR***	***2.92***	***(0.15)***

l) Acquisition of subsidiary

On December 14, 2005, the Group acquired full control over the activities of PEGAS a.s. (now PEGAS NONWOVENS s.r.o.) and its subsidiaries. The net assets acquired in the transaction and the goodwill arising were as follows:

	Pre-acquisition carrying amounts	*Fair value adjustments EUR '000*	*Recognised values on acquisition*
Property, plant and equipment	93 439	17 420	110 859
Intangible assets	192		192
Inventories	8 508	603	9 111
Trade and other receivables	24 968		24 968
Cash and cash equivalents	25 366		25 366
Bank loans and overdrafts	2 000		2 000
Deferred tax liabilities	9 681	4 215	13 896
Trade and other payables	16 760		16 760
Tax payables	18		18
Net identifiable assets and liabilities	***124 014***	***13 808***	***137 822***
Goodwill on acquisition			78 949
Cost of combination			***216 771***

The goodwill arising on the acquisition is attributable primarily to customer relationships, management skills, the skills and technical talent of the acquired workforce, the reputation for quality and the anticipated future profitability of the combined group. The management was not able to measure reliably the fair value of customer related intangibles due to the fact that demand from individual customers cannot be reliably predicted.

m) Property, plant and equipment

	Land and buildings	*Production machinery*	*Other equipment*	*Under Construction*	*Pre-payments*	*Total*
Acquisition cost						
Balance at 18/11/2005	--	--	--	--	--	--
Effect of acquisition of subsidiaries at 14/12/2005	28 271	77 015	5 005	220	348	110 859
Additions	--	643	47	7	--	697
Exchange differences	(22)	(83)	(6)	--	(1)	(112)
Balance at 31/12/2005	28 249	77 575	5 046	227	347	111 444
Additions	--	1 166	523	1 119	2 893	5 701
Disposals	(49)	--	(187)	(2)	--	(238)
Transfers	17	356	--	(17)	(356)	--
Exchange differences	1 756	6 653	484	46	98	9 037
Balance at 31/12/2006	29 973	85 750	5 866	1 373	2 982	125 944
Accumulated depreciation						
Balance at 18/11/2005	--	--	--	--	--	--
Depreciation expense	32	441	62	--	--	535
Exchange differences	(3)	(198)	(3)	--	--	(204)
Balance at 31/12/2005	29	243	59	--	--	331
Depreciation expense	1 189	10 464	403	--	--	12 056
Disposals	--	--	(100)	--	--	(100)
Exchange differences	245	2 681	209	--	--	3 135
Balance at 31/12/2006	1 463	13 388	571	--	--	15 422
Net book value						
18/11/2005	--	--	--	--	--	--
31/12/2005	28 220	77 332	5 807	227	347	111 113
31/12/2006	28 570	72 362	5 295	1 373	2 982	110 522

n) Intangible fixed assets

	Software	Goodwill	Total
Acquisition cost			
Balance at 18/11/2005	–	–	–
Effect of acquisition of subsidiaries at 14/12/2005	192	78 949	79 141
Disposals	(168)	–	(168)
Balance at 31/12/2005	24	78 949	78 973
Restatement	–	1 042	1 042
Balance at 31/12/2005 as restated	24	79 991	80 015
Additions	63	–	63
Exchange differences	46	4 393	4 439
Balance at 31/12/2006	133	84 384	84 517
Accumulated amortisation			
Balance at 18/11/2005	–	–	–
Balance at 31/12/2005	–	–	–
Amortisation expense	96	–	96
Exchange differences	(65)	–	(65)
Balance at 31/12/2005	31	–	31
Net book value			
18/11/2005	--	--	--
31/12/2005	24	78 949	78 973
31/12/2005 as restated*	24	79 991	80 015
31/12/2006	102	84 384	84 486

The Group reassessed the amount of a deferred tax liability as at the date of acquisition in respect of subsidiaries drawing investment incentives in the form of tax relief. As at the date of acquisition, the deferred tax liability was increased by TEUR 1 042 together with an increase in goodwill.

Item of the financial statements	Balance at 31. 12. 2005	Restatement	Balance at 31. 12. 2005 as restated
Goodwill	78 949	1 042	79 991
Deferred tax liability	13 910	1 042	14 952

o) Inventories

	2006	2005
Materials	3 724	5 043
Products	2 593	1 903
Semi-finished products	395	333
Spare parts	1 482	1 256
Other	169	87
Total	***8 363***	***8 622***

“Spare parts” include items with useful life shorter than one year or of immaterial individual value.

p) Short-term receivables

	2006	2005
Receivables from sales of products	19 632	21 410
Advance payments	41	--
Fair value of interest rate swaps	1 869	--
Value added tax receivables	1 842	1 368
Prepaid expenses	126	87
Accrued income	40	833
Other	90	87
Total	***23 640***	***23 785***

In 2006, the Group concluded interest rate swaps at a fixed interest rate of 3.236 % p.a. These swaps hedged 69.9 % of the Group's debts as at 31 December 2006.

q) Cash and cash equivalents

	2006	2005
Cash in hand	24	32
Current accounts	5 739	2 319
Overnight-deposits	16 251	24 683
Total	***22 014***	***27 034***

r) Share capital

Until November 2006, the Company's share capital consisted of 12 500 shares at EUR 10 per share. In November 2006, this number was split into 100 806 shares at EUR 1.24 per share. Subsequently, on 28 November 2006, the Company increased the share capital by EUR 9 075 056.56 by incorporation of debt into capital and by issuing 7 318 594 shares at EUR 1.24 per share. Pamplona Capital Partners I, LP acquired 7 133 109 shares and some of the Group's management 185 485 shares. Within the issue of shares in the public market, in December 2006 the Group issued 1 810 000 new ordinary shares. These newly issued shares were subscribed by investors at EUR 27 per share. The difference between the subscribed value of newly issued shares (EUR 27) and the nominal value (EUR 1.24) was recorded in equity as share premium in the total amount of TEUR 46 626. The total number of shares as at 31 December 2006 is 9 229 400 shares at EUR 1.24 per share.

s) Retained earnings

There were no dividends paid in the year ended 31 December 2006. The statement of equity line item 'Exchange differences' represents the effect of the translation of the financial statements from the functional to the presentation currency.

Consolidated Financial Statements and Notes to the Financial Statements, Independent auditor's report

t) Bank overdrafts and loans

2006	Bank loan liability	Arrange-ment fees	Due amount	Short-term	Long-term	Interest rate	Interest rate at 31/12/2006
Bank loans:							
Revolving loan	--	(126)	(126)	--	(126)	--	--
Credit tranche A	75 485	(1 504)	73 981	13 320	60 661	1,3,6M EURIBOR +2.25% (+2.00)*	5.674 %
Credit tranche B	26 781	(464)	26 317	--	26 317	1,3,6M EURIBOR +2.75%	6.424 %
Credit tranche C	36 648	(649)	35 999	--	35 999	1,3,6M EURIBOR +3.25%	6.924 %
Bank loans total	**138 914**	**(2 743)**	**136 171**	**13 320**	**122 851**		

* 2.25% margin was applied till 13 December 2006. From 14 December 2006 2.00% margin is applied.

2005	Bank loan liability	Convertible part	Arrange-ment fees	Due amount	Short-term	Long-term	Interest rate
Bank loans:							
Revolving loan	2 000	–	–	2 000	2 000	–	1M EURIBOR +2%
Mezzanine loan	15 000	(1 444)	(150)	13 406	–	13 406	3M EURIBOR +10%
Credit tranche A	95 000	–	(1 805)	93 195	14 250	78 945	1,3,6M EURIBOR +2.25%
Credit tranche B	28 500	–	(542)	27 958	–	27 958	1,3,6M EURIBOR +2.75%
Credit tranche C	37 700	–	(741)	36 959	–	36 959	1,3,6M EURIBOR+3.25%
Bank loans total	**178 200**	**(1 444)**	**(3 238)**	**173 518**	**16 250**	**157 268**	

Rate of 1M EURIBOR was 2.401 % at December 31, 2005.
The carrying amount of the bank loans approximates their fair value.

These bank loans are secured by:

- *the ownership interest in PEGAS NONWOVENS s.r.o.*
- *security over the enterprise of PEGAS NONWOVENS s.r.o.*
- *security over the plant and machinery of PEGAS NONWOVENS s.r.o.*
- *bank accounts of PEGAS NONWOVENS s.r.o. and shares of subsidiaries PEGAS - DS a.s., PEGAS-NT a.s. and PEGAS - NW a.s.*

u) Other payables due after one year

	2006	*2005*
Convertible preferred equity certificates	--	10 645
Less: Equity element	--	(2 929)
Non convertible preferred equity certificates	--	29 000
Preferred equity certificates	--	36 716
Other	275	508
Total	***275***	***37 224***

In 2006, all payables to Pamplona Capital Partners I LP of TEUR 36 716 and the interest accrued in 2006 were settled by cash and shares.

The balance of other payables of TEUR 275 comprises:

- *TEUR 204 representing the funds received from Pamplona Equity Advisors I Ltd. to cover operating expenses before IPO;*
- *TEUR 71 representing an interest-free loan provided by the state to fund research and development projects.*

v) Deferred tax

	Assets		Liabilities		Net	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**
Property, plant and equipment	--	--	(15 642)	(14 969)	(15 642)	(14 969)
Inventories	65	27	--	--	65	27
Other	352	--	--	(10)	352	(10)
Deferred tax asset / (liabilities)	**417**	**27**	**(15 642)**	**(14 979)**	**(15 225)**	**(14 952)**
Offset of deferred tax assets and liabilities	(417)	(27)	417	27	--	--
Deferred tax asset / (liabilities)	**--**	**--**	**(15 225)**	**(14 952)**	**(15 225)**	**(14 952)**

w) Short-term trade and other payables

	2006	*2005*
Trade payables	15 980	13 243
Advances received	67	--
Liabilities to employees	1 797	1 500
Deferred income	1 735	5 700
Other	633	1 227
Total	***20 212***	***21 670***

x) Tax liabilities and other tax liabilities

Tax liabilities of TEUR 192 comprise employment tax (TEUR 66) and corporate income tax liability reduced by income tax prepayments (TEUR 126).

The Group reassessed the amount of a deferred tax liability presented as at 31 December 2005. For detail refer to Note 8.6.5 n.

The increase in deferred tax of TEUR 273 consists of deferred tax income of TEUR (102) and effect of foreign exchange loss of TEUR 375.

y) Group Entities

To translate the registered capital of Czech subsidiaries, the CZK/EUR 27.495 rate of exchange effective on 31 December 2006 was used.

Subsidiaries included in the consolidated entity

Company	Acquisition date	Share in the subsidiary	Registered capital TCZK	Registered capital TEUR	Number and nominal value of shares
CEE Enterprise a.s.	5.12.2005	100 %	3 600	131	100 shares at TCZK 20 per share and 1 600 thousand shares at CZK 1 per share
PEGAS NONWOVENS s.r.o.*	5.12.2005	100 %	3 633	132	100% interest of TCZK 3 633
PEGAS - DS a.s.	14.12.2005	100 %	800 000	29 096	64 shares at TCZK 10 000 per share and 64 shares at TCZK 2 500 per share
PEGAS–NT a.s.	14.12.2005	100 %	550 000	20 004	54 shares at TCZK 10 000 per share and 10 shares at TCZK 1 000 per share
PEGAS - NW a.s.	14.12.2005	100 %	5 000	182	5 shares at TCZK 1 000 per share

* PEGAS NONWOVENS s.r.o. was registered on 14 November 2003 as ELK INVESTMENTS s.r.o and changed its name to PEGAS NONWOVENS s.r.o. in 2006. PEGAS a.s., the subsidiary of PEGAS NONWOVENS s.r.o., was established in 1990. It merged with PEGAS NONWOVENS s.r.o. with effect from 1 January 2006 and was deleted from the Commercial Register on 12 May 2006.

8.6.6 Related Parties Transactions

- *In 2006, there were no transactions with Pamplona Capital Partners I LP other than described under Note 8.6.5 r and 8.6.5 u;*
- *As at 31 December 2006, the Group had a liability to Pamplona Equity Advisors I Ltd. in the amount of TEUR 204 as described in Note 8.6.5 u;*
- *The Group was paying an advisory fee to Pamplona Capital Management, LLP of EUR 62 500 per quarter. However, this fee ceased being paid following the IPO;*
- *In connection with termination of the Shareholder Agreement due to IPO, the Group agreed to pay to Pamplona Capital Management, LLP a fee amounting to TEUR 1 250 for corporate development and know-how. The fee also represented a settlement for the cancellation of the annual advisory fee referred under c);*
- *One of the current board members rendered his advisory services to the Group for a total amount of TEUR 30;*
- *The Group accrued TEUR 150 representing an expected emolument for one of the members of the Board of Directors in connection with his advice on the IPO;*
- *Some of the managers of the Group sold their shares in CEE Enterprise a.s. to the Company in November 2006 for a total consideration of TEUR 253 and subsequently subscribed for newly issued shares in the Company for a total consideration of TEUR 230;*
- *Except for the information provided under Note 8.6.5 f and 8.6.5 g there were no other transactions between the Group and the management.*

8.6.7 Contingencies and Commitments

The Group has no material contingencies or commitments which would not be reported in the balance sheet except for potential liabilities arising from bank loan security as described in Note 8.6.5 t.

8.6.8 Material Subsequent Events

The management of the Group are not aware of any events that have occurred since the balance sheet date that would have any material impact on the consolidated financial statements as at 31th December 2006.

Date: April 28th, 2007
Signature of the authorised representative:

Miloš Bogdan
CEO of PEGAS NONWOVENS s.r.o
and membert of the Board of PEGAS NONWOVENS SA

Henry Gregson
Non-Executive Director of PEGAS NONWOVENS s.r.o.
and member of the Board of PEGAS NONWOVENS SA

9 Other information

9.1 Basic Information on the Company

Name

PEGAS NONWOVENS SA

Address:

68–70, boulevard de la Pétrusse, L-2320 Luxembourg, Luxembourg

Registry and registration number:

Registered with the Luxembourg trade and companies register under number B 112.044

Incorporated:

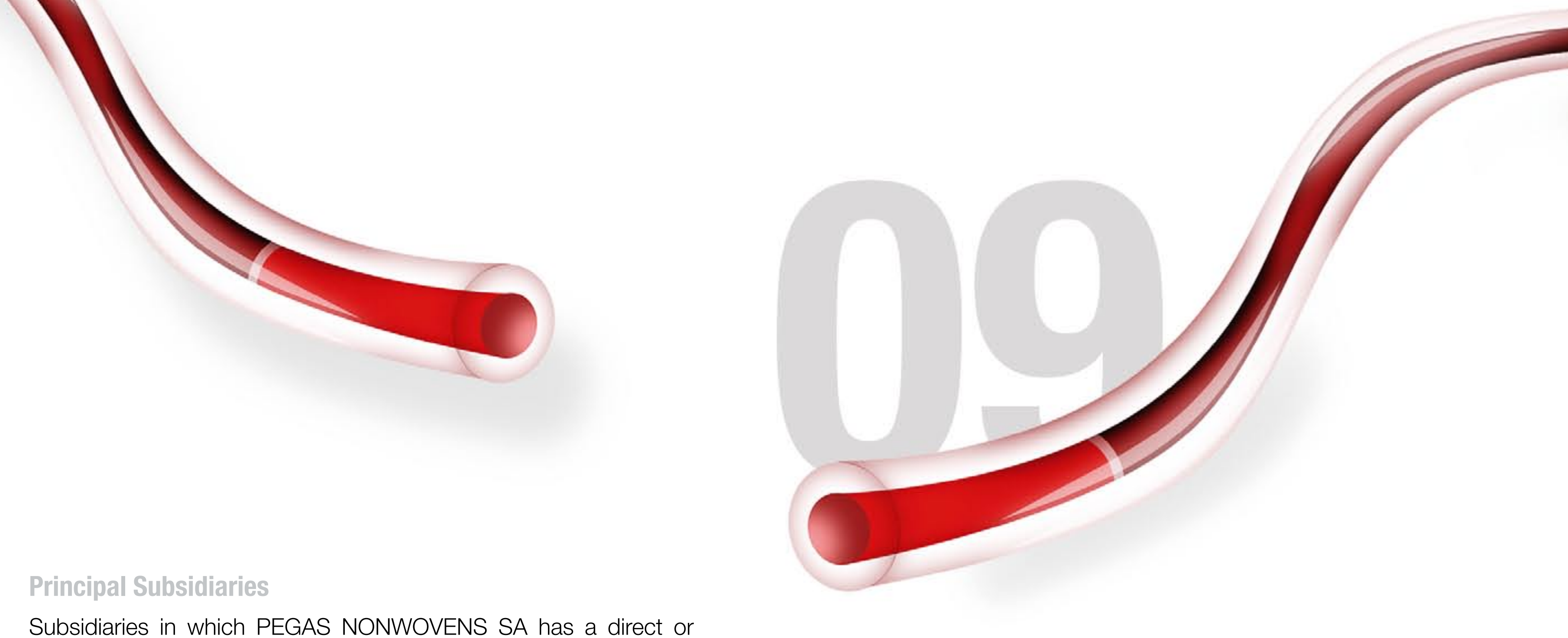
November 18th, 2005 under the name Pamplona PE Holdco 2 S.A.

The holding company of The PEGAS Group, PEGAS NONWOVENS SA, was incorporated in Luxembourg as a public limited liability company (société anonyme) for an unlimited duration on November 18th, 2005 under the name Pamplona PE Holdco 2 S.A. and is registered with the Luxembourg trade and companies register under number B 112.044. The articles of incorporation of the Company have been published in the Mémorial, Recueil des Sociétés et Associations number C 440 of March 1, 2006. The Company's registered office is at 68–70, boulevard de la Pétrusse, L-2320 Luxembourg, Luxembourg. The registered office and principal place of business of the main operating and trading company, PEGAS NONWOVENS s.r.o., is at Přímětická 86, 669-04 Znojmo, Czech Republic.

Scope of business (according to Article 3 of the Articles of Association):

The object of the Company is:

- *to take participations and interests, in any form whatsoever, in any commercial, industrial, financial or other, Luxembourg or foreign entities;*
- *to acquire any securities and rights through participation, contribution, underwriting firm purchase or option, negotiation or in any other way and namely to acquire patents and licences, and other property, rights and interest in property as the Company shall deem fit, and generally to hold, manage, develop, sell or dispose of the same, in whole or in part, for such consideration as the Company may think fit, and in particular for shares or securities of any Company purchasing the same;*
- *to enter into, assist or participate in financial, commercial and other transactions, and to grant to any holding Company, subsidiary, or fellow subsidiary, or any other Company associated in any way with the Company, or the said holding Company, subsidiary of follow Company, in which the Company has a direct or indirect financial interest, any assistance as e.g. pledges, loans, advances or guarantees;*
- *to borrow and raise money in any manner and to secure the repayment of any money borrowed;*
- *to borrow funds and issue bonds and other securities; and*
- *to perform any operation which is directly or indirectly related to this purpose.*



Principal Subsidiaries

Subsidiaries in which PEGAS NONWOVENS SA has a direct or an indirect interest amounting to at least 10% of the consolidated equity or 10% of the consolidated net profit:

Name	Registered Office	Identification number	Activity
CEE Enterprise a.s.	Znojmo, Přímětická 3623/86, PSČ 66904	27218724	Lease of properties and premises and general activities related to lease of properties. Activities of business, financial, organizational and economic advisors.
PEGAS NONWOVENS s.r.o.	Znojmo, Přímětická 3623/86, PSČ 66904	25478478	Production of textiles, production of plastic and rubber products.
PEGAS – DS a.s.	Znojmo, Přímětická 3623/86, PSČ 66904	25554247	Production of nonwoven textiles. R&D of technology, textiles and manufacturing
PEGAS–NT a.s	Znojmo, Přímětická 3623/86, PSČ 66904	26287153	Production of textiles
PEGAS – NW a.s.	Znojmo, Přímětická 3623/86, PSČ 66904	26961377	Production of textiles

Expenses of PEGAS Group related to external auditors services in year 2006

Euro thousands	*Audit*	*Other*	*Total*
PEGAS NONWOVENS SA	181.5	8.1	189.6
Other companies within PEGAS Group	346.6	3.9	350.5
TOTAL	***528.1***	***12.0***	***540.1***

Affirmation

Miloš Bogdan, CEO of PEGAS NONWOVENS s.r.o. and member of the Board of PEGAS NONWOVENS SA,

Henry Gregson, Non-Executive Director of PEGAS NONWOVENS s.r.o. and member of the Board of PEGAS NONWOVENS SA,

hereby declare that the information contained in this Annual Report is accurate and that no significant facts could influence the accurate and correct evaluation of PEGAS NONWOVENS SA or its shares have been omitted or distorted.

Miloš Bogdan
CEO of PEGAS NONWOVENS s.r.o
and member of the Board of PEGAS NONWOVENS SA

Henry Gregson
Non-Executive Director of PEGAS NONWOVENS s.r.o.
and member of the Board of PEGAS NONWOVENS SA

Note

Note

PEGAS NONWOVENS SA

Address:

68–70, boulevard de la Pétrusse
L-2320 Luxembourg
Luxembourg

Registry and registration number:

Registered with the Luxembourg trade and companies register under number B 112.044

Incorporated:

CEE Enterprise a.s.

Znojmo, Přímětická 3623/86, PSČ 66904

IČ: 27218724

PEGAS NONWOVENS s.r.o.

Znojmo, Přímětická 3623/86, PSČ 66904

IČ: 25478478

PEGAS – DS a.s.

Znojmo, Přímětická 3623/86, PSČ 66904

IČ: 25554247

PEGAS–NT a.s

Znojmo, Přímětická 3623/86, PSČ 66904

IČ: 26287153

PEGAS – NW a.s.

Znojmo, Přímětická 3623/86, PSČ 66904