PEGAS NONWOVENS SA
Société Anonyme
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L-2320 Luxembourg
R.C.S. Luxembourg B 112.044
(“PEGAS” or the “Company”)

DIRECTORS’ REPORT
FOR THE ACCOUNTING YEAR ENDED ON DECEMBER 31, 2010

To the Shareholders of PEGAS:

In accordance with our duties as Directors of PEGAS, we hereby submit the annual accounts and the consolidated accounts as of and for the year ended December 31, 2010.

(a) Important events concerning PEGAS and its subsidiaries (collectively the “**PEGAS Group**”) that have occurred since the end of the financial year:

In 2011 PEGAS finalized the analysis of useful lifetime of the property, plant and equipment. Based on this assessment PEGAS decided to prolong the residual estimated useful lifetime of the production technology. This change is effective as from 1 January 2011. The prolongation of the estimated useful lifetime will cause decrease of depreciation and amortization expense in 2011 approximately by EUR 6.7 million, in 2012 by EUR 5.9 million and in 2013 by EUR 1.9 million, while the impact on 2014 and onwards is not material (depreciation and amortization expense in 2010: EUR 16.4 million).

The management of PEGAS is not aware of any other events that have occurred since 31 December 2010 that would have any material impact on PEGAS or the PEGAS Group.

(b) The PEGAS Group’s likely future development:

The PEGAS Group’s strategy for 2011 and into the future is to:

1) develop and take advantage of growth opportunities to strengthen its market position,

2) maintain and extend technological leadership in spunmelt nonwoven textiles for disposable hygiene products in Europe, and

3) provide solid returns to shareholders.

The PEGAS Group intends to achieve its objectives principally through the following strategies:

Continue investing into technologically advanced production capacity: The PEGAS Group will strive to install state-of-the-art production capacities ahead of its European competitors. Its 9th production line in Znojmo is expected to be put into operations in the second half of 2011.

Maintain close relationships with customers and suppliers: The PEGAS Group will continue to work together with its clients, machinery manufacturers and raw material suppliers to research, develop and implement new products ahead of the competition. The PEGAS Group will endeavour to remain at the forefront of technical developments in the industry and supply its customers with the highest quality products and continually develop new materials.

Focus on technologically advanced products: The PEGAS Group is Europe’s largest producer of bi-component spunmelt nonwovens with extensive experience in the design and production of ultra lightweight materials.

Maintain industry leading financial performance: The PEGAS Group's principal objectives are to continue to grow with its core target market, deliver revenues in line with this growth and maintain high operating margins relative to its core competitors. The PEGAS Group has been effective at generating significant levels of cash, which is subsequently used to support expansion, reduce outstanding debt and pay out dividends.

Monitoring investment opportunities: The PEGAS Group will continue to monitor investment opportunities outside the Czech Republic, whether acquisitions or the construction of new capacities abroad.

(c) Activities in the field of research and development:

All research and development activities are conducted by the operating subsidiaries of PEGAS as described below. PEGAS was not involved in any activities in the field of research and development on stand-alone basis.

Research and Technical Support

The development of new applications and products is one of the most important parts of the PEGAS Group' current and future strategic focus. This platform is supported by a team of technicians, who are dedicated to product development, customer and technology support. This team has been built over a period of more than ten years.

Work teams are active in several different areas, which are principally divided into industrial and hygiene applications, with the main focus on the hygiene field as the key driver for the most important projects at the PEGAS Group.

From the technological point of view, the technical department has two main goals, to a) improve quality, performance and production efficiency of standard products and b) develop products with added value using both current and/or new technologies.

Both objectives are achieved in cooperation with raw material suppliers, using standard and special new polymers, and/or with machinery suppliers, allowing the PEGAS Group to produce a competitive edge for its customers.

In the field of technologies, the PEGAS Group is continuing in the commercialisation of ultra light-weight materials produced on the latest production line. This line confirmed the anticipated parameters of the produced material and the overall efficiency of the machinery. The PEGAS Group intends to continue with this trend with the new line which should be launched in the second half of 2011. In addition, this new line should be prepared and ready to bring certain technologically advanced designs to the market, allowing the PEGAS Group again to strengthen its position among technology leaders.

Apart from certain ultra light-weight materials, in terms of new products, the PEGAS Group has successfully developed and started commercialising a new nonwoven material used in medical applications and, thanks to the special treatment of the material, managed to achieve excellent protective properties.

Additionally, the PEGAS Group is actively contributing to the development of soft nonwovens with excellent touch and drapeability properties, elastomeric and extensible nonwovens and spunmelt nonwovens with improved barrier characteristics, which after further development and successful commercialization should bring a number of benefits to clients.

The PEGAS Group cooperates with many different institutes, which positively support the PEGAS Group's research, especially in the areas of plasma textile treatment, modelling of nonwoven structure with the purpose to achieve bulky and soft touch and feeling, highly efficient barrier function and/or special polymers. There are several universities and R&D centres, mainly in the Czech Republic and Slovakia, and also in Western Europe, offering the PEGAS Group special support in various specialised fields and/or highly sophisticated lab resources.

In order to better utilise its production lines and accelerate the development of its projects, the PEGAS Group takes advantage of several pilot lines, which are made available under certain agreements at the suppliers' sites. All projects are related either to new technologies themselves or to the utilisation of newly developed raw materials in technologies or projects, which are designed directly for specific customers. There are several projects where all three parties cooperate, thereby, complete the supplier chain.

Research costs in 2010 were EUR 2.1 million.

(d) Information in respect of the acquisitions of own shares:

No acquisition of own shares was conducted in 2010.

(e) The existence of branches of PEGAS and the PEGAS Group entities

To translate the registered capital of Czech subsidiaries, the exchange rate of the Czech National Bank of CZK/EUR 25.060 effective on 31 December 2010 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*
PEGAS NONWOVENS s. r.o. *	5 December 2005	100 %	3 633	145	100% participation of TCZK 3 633
PEGAS - DS a.s.	14 December 2005	100 %	800 000	31 923	64 shares at TCZK 10 000 per share and 64 shares at TCZK 2 500 per share
PEGAS-NT a.s.	14 December 2005	100 %	550 000	21 947	54 shares at TCZK 10 000 per share and 10 shares at TCZK 1 000 per share
PEGAS - NW a.s.	14 December 2005	100 %	650 000	25 938	64 shares at TCZK 10 000 per share and 10 shares at TCZK 1 000 per share
PEGAS - NS a.s.**	3 December 2007	100 %	105 000	4 190	5 shares at TCZK 1 000 per share and 10 shares at TCZK 10 000
PEGAS NONWOVENS International s.r.o. ***	5 November 2010	100 %	200	8	100% participation of TCZK 200

* 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.; the merger was entered in the Commercial Register and PEGAS a.s. was deleted from the Commercial Register on 12 May 2006. CEE Enterprise a.s. merged with PEGAS NONWOVENS s.r.o.; the merger was entered in the Commercial Register and CEE Enterprise a.s. was deleted from the Commercial Register on 20 August 2007.

** PEGAS - NS a.s. was established by PEGAS in December 2007 for the purpose of a new production line project. On 26 November 2010, PEGAS – NS a.s. increased its registered capital from TCZK 5 000 to TCZK 105 000.

*** PEGAS NONWOVENS International s.r.o. serves as a special purpose vehicle established for the purpose of making potential future investments. The establishment of this company is not related to the execution of any specific investment.

(f) Proposals of resolutions of the 2011 annual general meeting of the shareholders of PEGAS (the "**AGM**" or the "**Meeting**"):

Resolution No. 1

1.1 The AGM elects Mr. Neil J. Everitt as chairman of the AGM.

1.2 The AGM elects Mr. Frédéric Franckx as scrutineer of the AGM.

Resolution No. 2

The Meeting resolves to acknowledge the reports of the auditor and of the Board of Directors regarding the statutory accounts and the consolidated accounts as of and for the financial year ended 31 December 2010.

Resolution No. 3

The Meeting resolves to approve (i) the statutory accounts for the financial year ended 31 December 2010 and (ii) the consolidated accounts for the financial year ended 31 December 2010.

Resolution No. 4

The Meeting resolves to allocate (i) 5% of the profits, i.e. the amount of EUR 335,826.28, to the legal reserve, (ii) the amount of EUR 899,554.69, to cover the losses of previous years, and (iii) the remaining amount, i.e. the amount of EUR 5,481,144.57, to profit carried forward.

Resolution No. 5

5.1 The Meeting resolves to grant discharge to the members of the Board of Directors for the performance of their duties during, and in connection with, the financial year ended 31 December 2010 (i.e. from 1 January 2010 until 31 December 2010).

5.2 The Meeting further resolves to give discharge to Deloitte S.A., the independent auditor ("*réviseur d'entreprises")* of PEGAS for the performance of its duties during, and in connection with, the financial year ended 31 December 2010 (i.e. from 1 January 2010 until 31 December 2010).

Resolution No. 6

The Meeting resolves to appoint Deloitte S.A. as the independent auditor (*"réviseur d'entreprises")* of PEGAS for a term ending at the annual general meeting of the shareholders to be held in 2012, to review the statutory accounts and the consolidated accounts as at 31 December 2011.

Resolution No. 7

In respect of the financial year ending on 31 December 2011, the Meeting resolves that Mr. Marek Modecki and Mr. Neil J. Everitt (the Non-Executive Directors) should receive an aggregate amount of EUR 135,000 as directors' fee, payable in cash. The Meeting resolves to authorise and empower the Board of Directors to split this remuneration among the Non-Executive Directors.

Resolution No. 8

In respect of the financial year ending on 31 December 2011, the Meeting resolves that Mr. František Řezáč, Mr. František Klaška and Mr. Marian Rašík (the Executive Directors) should receive an aggregate amount of CZK 5,213,604 as directors' fee, payable in cash. The Meeting resolves to authorize and empower the Board of Directors to delegate the splitting of this remuneration among the Executive Directors to the Board's Remuneration Committee.

Resolution No. 9

The Meeting resolves to authorize the Board of Directors to decide on the acquisition of own shares by PEGAS, within the limits set forth by the Luxembourg law of 10 August 1915 on commercial companies (the "**Law**") pursuant to the following modalities:

(i) a maximum of ten per cent (10%) of the total number of PEGAS' shares, *i.e.* nine hundred twenty-two thousand nine hundred forty (922,940) shares, may be acquired by PEGAS;

(ii) the consideration paid by PEGAS for such acquisition shall, in any case, range between CZK 100 and CZK 1,000 (or the equivalent amounts in other currencies), included, per share; and

(iii) this authorization shall be valid for a period of five (5) years starting from the date of the present Meeting.

The Meeting further grants full power to the Board of Directors to (a) perform such acquisition (in one or several tranches) of own shares by PEGAS, at any time when, and in any manner as, deemed appropriate by the Board of Directors, provided that the conditions laid down in the present resolution and the Law are respected when an authorized acquisition of PEGAS' own shares takes place, (b) fix the amount or the price range of the consideration within the limits determined by the Meeting in the present resolution in accordance with PEGAS' corporate interest, and (c) undertake all such acts and matters deemed appropriate, by the Board of Directors, in order to proceed with the authorized acquisition of PEGAS' own shares by PEGAS.

(g) PEGAS's shares and share capital:

Shareholders as of 31 December 2010:

Free Float	100%
Of which Management	0.9%

Changes in the Shareholders' Structure in 2010:

The total stake held by the management of PEGAS as of 31 December 2010 was 0.9% and declined from the 1.2% stake as of 31 December 2009.

On 14 June 2010 PEGAS received a notification that Genesis Smaller Companies SICAV held as of 12 June 2010 472,700 shares of PEGAS (managed by custodian Brown Brothers Harriman /Luxembourg/), constituting 5.12% of the share capital and of the total voting rights attached to the shares issued by PEGAS.

On 8 December 2010 PEGAS received a notification that as of 3 December 2010 PKO Towarzystwo Funduszy Inwestycyjnych SA held 466,421 shares in PEGAS, constituting 5.05% of the share capital and of the total voting rights attached to the shares issued by PEGAS.

(h) Other corporate information on PEGAS:

As of the date of the 2011 Annual General Meeting, the issued capital of PEGAS will amount to EUR 11,444,456, being divided into 9,229,400 shares with a par value of EUR 1.24 each; and the authorised capital of the Company will amount to EUR 999,999.24 being divided into 806,451 shares with a par value of EUR 1.24 each.

The rules of appointment and dismissal of the members of the Board of Directors are described in Article 8 of the Articles of Association of PEGAS, which reads as follows:

For so long as the Company only has one shareholder, the Company may be managed by one (1) director only. In case of plurality of shareholders, the Company shall be managed by a Board of Directors of at least three (3) members. The director(s) of the Company, either shareholders or not, are appointed for a term which may not exceed six (6) years by a General Meeting. The director(s) may be dismissed at any time and at the sole discretion of a General Meeting.

When a legal entity is appointed as a director of the Company (the Legal Entity), the Legal Entity must designate a permanent representative in order to accomplish this task in its name and on its behalf (the Representative). The Representative is subject to the same conditions and obligations, and incurs the same liability as if he was performing this task on his own behalf, without prejudice to the joint liability of the Legal Entity. The Legal Entity cannot revoke the Representative unless it simultaneously appoints a new permanent representative.

Retiring members of the Board of Directors are eligible for re-election.

In the event of a vacancy on the Board of Directors because of death, retirement or otherwise, the remaining directors may meet and may elect by majority vote a director to fill such vacancy until the next General Meeting.

Any reference to the Board of Directors in the Articles shall be a reference to the sole director (if at all the Company only has one) as long as the Company shall have one (1) Shareholder.

The Board of Directors is vested with the broadest powers to perform all acts of administration and disposition in PEGAS' interest. All powers not expressly reserved by Luxembourg law or PEGAS' Articles of Association to PEGAS' general meeting of shareholders fall within the powers of the Board of Directors.

The power of the Board of Directors to issue shares is governed by the fourth, fifth and sixth paragraphs of Article 5 of the Articles of Association of PEGAS, which read as follows:

As a consequence, the Board of Directors is authorised and empowered to:

- implement a capital increase by issuing from time to time new shares to be paid up in cash or by way of contribution of assets in kind, by incorporating reserves or profits carried forward or in any other manner, including the exercise of warrants and the conversion of convertible bonds;

- fix the place and the date of the issue or the successive issues of shares, the issue price, with or without a premium, the date from which the shares shall bear dividend and the terms and conditions of subscription and payment of the new shares;

- abolish or limit the preferential subscription right of the shareholders when proceeding to the issue of new shares to be paid up in cash.

The above mentioned authorisation will be valid for a period of five years from 1 March 2006 and it may be renewed by a resolution of the extraordinary general meeting of shareholders as to the shares of the authorised capital which will not have been issued by the Board of Directors before then.

Each time the Board of Directors acts to render effective the increase of capital as authorised above, the present article of the Articles shall be amended so as to reflect the increase of the subscribed capital, and the Board of Directors or any person authorised by the Board of Directors shall state such amendment in the form prescribed by law.

However, as the Board of Directors' authorization to issue shares under the Articles of Association of PEGAS expired on 1 March 2011 and has not been renewed, the Board of Directors is thus no longer authorised to issue shares of the Company in accordance with article 5 of the Articles of Association.

PEGAS is not a party to any significant agreement which takes effect, alters or terminates upon a change of control of PEGAS following a takeover bid, and the effects thereof.

PEGAS' Articles of Association may be amended by a resolution of PEGAS' general meeting of shareholders duly convened and held in the presence of a Luxembourg notary. The resolution amending PEGAS' Articles of Association must be taken with a quorum of one half of the share capital being present or represented at the meeting. If such quorum is not reached at the meeting, a second meeting can be convened in accordance with article 67-1 paragraph 2 of the Luxembourg law of 10 August 1915 on commercial companies and such second meeting will validly deliberate regardless of the proportion of share capital present or represented at the meeting. At both meeting, the resolution to amend PEGAS' Articles of Association must be taken, to be adopted, with a majority of two thirds of the vote cast. The agenda of the meeting must indicate the proposed amendments to the Articles of Association and, where applicable, the text of those which concern the objects of the form of PEGAS.

All shares issued by PEGAS have one vote and carry equal voting dividend rights, there are no shares with special control rights.

There are no agreements between shareholders known to PEGAS which may result in restrictions on the transfer of securities and/on voting rights.

PEGAS and the operating companies have not created and do not currently intend to create a share option plan for the benefit of their employees other than those described in the Annual Report 2010 chapter 6.3 Remuneration of Directors and Management.

PEGAS is a party to three service agreements with its executive directors, Mr. František Řezáč, Mr. František Klaška and Mr. Marian Rašík which provide for compensation if the executive director is made redundant for other reasons than for breach of his obligations. Each executive director is entitled to receive from PEGAS his monthly remuneration (but not bonus) which he would be entitled to receive from all companies of the PEGAS Group under all service agreements in the year preceding the year when all such service agreements were terminated, until the earlier of (i) the expiry of the period of three years following the date of such termination and (ii) the date of the executive director entering into any form of employment, directorship, or other form of service relationship with a third party. The service agreements with Mr. František Řezáč and Mr. František Klaška were entered into in May 2007, the service agreement with Mr Rašík was entered into in March 2010. All service agreements are governed by Luxembourg law.

PEGAS is not a party to any other agreements with its board members or employees providing for compensation if they resign or are made redundant without valid reason or if their employment ceases because of a takeover bid.

The Board of Directors has decided to waive the application of 10 December 2010 on the introduction of international accounting rules for companies in accordance with article 4 of said law.

Luxembourg, 16 May 2011

Marek Modecki
Chairman of the Board of Directors
of PEGAS NONWOVENS SA

František Řezáč
Member of the Board of Directors
of PEGAS NONWOVENS SA