BAKKAVÖR GROUP

ANNUAL REPORT 2006

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BAKKAVÖR

ANGLIA CROWN
BAKKAVÖR BIRMINGHAM
BAKKAVÖR OVERSEAS
BAKKAVÖR PIZZA
BARTON BREAD
CALEDONIAN PRODUCE
CINQUIÈME SAISON
CREATIVE FOODS (JV)
CRUDI
ENGLISH VILLAGE SALADS
FRESH CUT PRODUCE
FRESHCOOK
HITCHEN FOODS
INTERNATIONAL PRODUCE
ISLEPORT FOODS
KATSOURIS FRESH FOODS
LAURENS PATISSERIES
LINCS CUISINE
MANOR FRESH (JV)
MARINER FOODS
MELROW SALADS
NEW PRIMEBAKE
PASTA COMPANY
PURE PATISSERIE
SAXON VALLEY FOODS
SOGESOL
SPRING VALLEY FOODS
TILMANSTONE SALADS
VACO
WELLAND FRESH FOODS
WINGLAND FOODS

Bakkavör at a glance

Our markets

Business review

How we run our business

Accounts and information

Bakkavör Group is unique in taking a global view of the high growth fresh prepared foods markets. We buy and integrate strong businesses to enable them to benefit from significant economies of scale and scope.

We aim to improve our business continuously through co-operation and sharing of knowledge and best practices.

Our businesses aim to outperform each of the markets in which they operate.

Bakkavör Group is a leading fresh prepared foods manufacturer with operations in seven countries and 16,000 employees

BAKKAVÖR AT A GLANCE

BAKKAVÖR

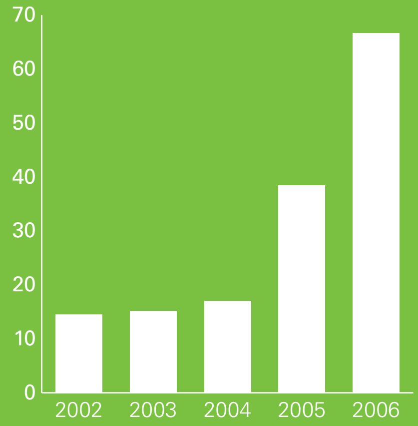
Our vision is to be recognised and respected as the world's leading fresh prepared foods and produce provider.

Our mission is to earn the loyalty of existing and new customers by providing the very best service, quality, value and innovation in the fresh prepared foods and produce market.

Our unwavering commitment to our focused strategy and core business values will ensure our delivery is as good as our promise to both customers and shareholders.

Pre-tax profits*

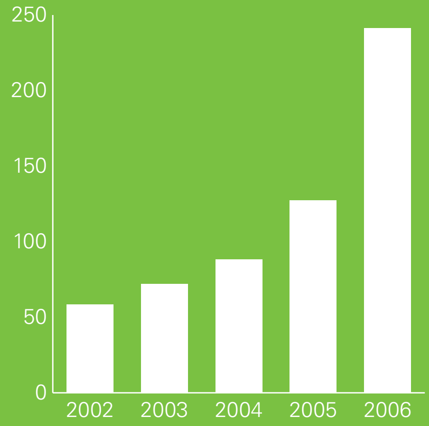
GBP millions



*Continuing business

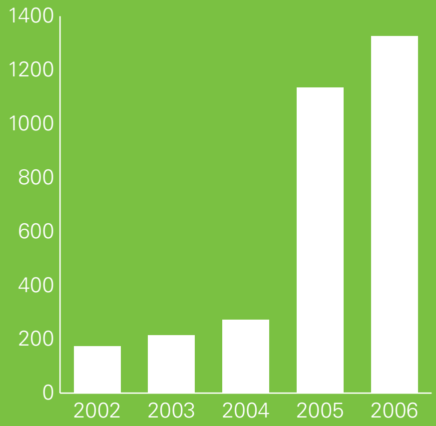
Equity

GBP millions



Assets

GBP millions



WHAT WE DID IN 2006

Strengthened our UK position

We strengthened the Group's position in desserts, speciality breads and ready meals through four acquisitions.

Improved performance in Continental Europe

We improved performance in our existing operations and continued to explore market and acquisition opportunities in Continental Europe.

Expanded internationally

We acquired a stake in Creative Foods in China and continued to explore market and acquisition opportunities in Asia.

Integrated successfully

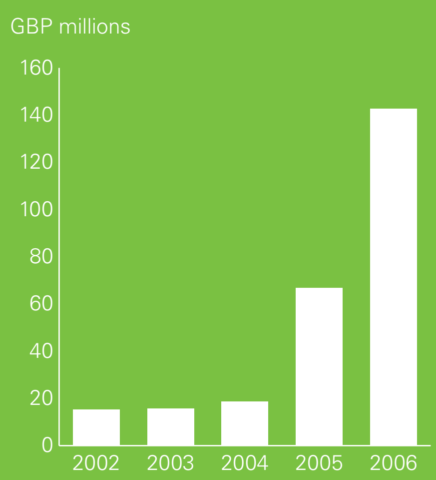
We continued to integrate our acquired businesses.

Rebranded globally

We launched a new logo and rebranded the whole Group during the year. Today, all our businesses operate under one name, Bakkavör.

HOW WE DID IN 2006

Working capital from operations



Record pre-tax profits of £66.6 million – up 73%

Shareholders' earnings £67.6 million – up 111%

Operating profit (EBIT) £113.9 million – up 71%

Sales growth in underlying business 10%

EBITDA £147.8 million – up 72%

Free cash generated by operating activities £93.6 million – up 43%

Total assets £1,326 million

Earnings per share 3.4 pence – up 74%

Return on equity 37% compared with 30% in 2005

+27% sales growth in Continental Europe

+9% sales growth in the UK

A GROWING GROUP WITH GLOBAL ASPIRATIONS

Bakkavör Group – pursuing an ambitious growth strategy, benefiting from significant economies of scale and scope.

784 million potential consumers

16,000 people

4,700 products

46 factories

17 product categories

7 countries

Bakkavör Group's Head Office is in Reykjavík, Iceland, and the Group is listed on the OMX Nordic Exchange in Iceland (formerly Iceland Stock Exchange). For more information on the location of our manufacturing facilities, please refer to our website www.bakkavor.com

The Bakkavör approach

Sharing best practices and knowledge

Aiming to outperform in each of the markets in which we operate.

Experienced people

Innovative culture

Unrivalled industry expertise

Strong customer partnerships

Service
Value
Innovation
Quality

Robust businesses

DIVERSE PRODUCT PORTFOLIO

Our fresh prepared foods can be split roughly into two categories: hot-eating and cold-eating. Hot-eating products are those which need to be cooked or reheated. Cold-eating products are those which are ready to eat or need minimal preparation.

We also market fresh produce such as lettuce, cucumbers, tomatoes, peppers, avocados and a variety of fruit, particularly speciality ranges.

We provide meal solutions that meet people's demands for convenience, health and pleasure.

COLD-EATING

Leafy salads
Convenience salads
Dips
Desserts
Prepared fruit
Salad dressings
Wraps

HOT-EATING

Ready meals
Ready to cook meals
Fresh pizza
Fresh pasta
Soups
Sauces
Stir fries
Ethnic snacks
Prepared vegetables
Speciality bread

PRODUCE

Chinese leaf lettuce
Whole cucumbers
Piccolo tomatoes
Sweet pointed peppers
Blood oranges
Cantaloupe melons
Rocha pears
Gala apples
Organic avocados
and more...

CHAIRMAN AND CEO'S ADDRESS

Perfectly positioned for future growth

Dear Shareholders,

In 2006 we celebrated Bakkavör Group's 20th anniversary. At such an important juncture, we are pleased to report the best performance in the history of the Group. Since its inception we have pursued an ambitious growth strategy and, today, Bakkavör Group is a leading provider of fresh prepared foods and produce with operations in seven countries, 16,000 employees and turnover of £1.2 billion.

Good strategic progress

UK sales represented 92% of the Group's turnover in 2006. Our strategic aim in the UK is to lead the consolidation of the market and, in 2006, we strengthened our position in key product categories with four acquisitions. In Continental Europe, our focus on improving efficiencies across our operations was successful and we are pleased to report that these businesses are now profitable. During the year we also took our first steps in Asia, where the consumer markets are growing quickly, by acquiring a stake in a Chinese salad company.

Throughout the year we improved efficiencies and profitability across our operations as we further integrated our newly acquired businesses, extracting synergies and benefiting from economies of scale. To reflect this successful integration and to celebrate the 20th anniversary of Bakkavör Group, we decided to rebrand the Group and, today, all our businesses operate under the umbrella of one name, Bakkavör. Another strategic change during the year was the decision to swap roles within Bakkavör Group: Ágúst became Chief Executive Officer and Lýdur became Chairman. Lýdur moved his day-to-day focus to Exista hf., a listed financial services company, in which we hold a 47.4% share, together. Exista hf. is the largest shareholder of Bakkavör Group with a 39.6% share today.

Strong performance

The year 2006 was characterised by a strong performance in our key markets, with total turnover amounting to £1.2 billion, growing by 69% year-on-year. Like-for-like sales growth in the underlying business in 2006 was 10%.

In the UK the market growth rate for fresh prepared foods continued to outperform the growth rate for the UK food market in general. Our growth target for UK fresh prepared foods is to achieve sales growth above market growth. In 2006 this objective was achieved with sales growth of 8.6% in a market that grew by 6.6%. We also achieved a strong uplift in fresh produce with sales up by 8.5%, against sector growth of 4.1%.

In Continental Europe our actions to improve performance were successful with pro-forma sales in the Group's Continental European businesses growing by 27% during the year compared with a 5% sales decline in 2005.

Dividends

In view of our strong profit performance and cash flow, the Board of Directors will propose a dividend payment at the Group's Annual General Meeting on 23 March, which corresponds to ISK 0.5 per share or 50% of issued share capital for the year 2006. This decision reflects the confidence of the Board in Bakkavör Group's current performance and future strategic direction.

Market trends supporting strategic growth

We are in a strong position to take advantage of favourable market trends and achieve our goals of ambitious growth worldwide. Consumer behaviour is changing across the globe, affected by greater affluence, complex family structures as well as advances in technology and communication. People are increasingly demanding high quality food but looking to spend less time preparing it. The market trends for convenience, health and pleasure continue to grow stronger and are now prevalent around the world.

The fresh prepared foods sector has been particularly successful in meeting these evolving demands and, as a result, continues to achieve stronger growth than many other food sectors. In the UK, fresh prepared foods sales alone have increased the value of the total food market by £4 billion over the past 10 years. The UK is at the forefront of this development with the largest fresh prepared foods market in the world, and this market continues to grow strongly and outperform growth in the general food market. Elsewhere, the fresh prepared foods sector in Western Europe, for example, is expected to grow by 20% between 2006 and 2010, and the chilled foods sector in China is forecast to grow by 30% between 2007 and 2011. We are well positioned in our target geographical markets to benefit from these trends.

Corporate responsibility

Another key trend is people's heightened awareness of global environmental issues, ethical issues and health concerns. When it comes to food, people are looking for integrity throughout the food chain, demanding more information – not just about the food itself and its contents, but also how and where it has been made and by whom.

At Bakkavör Group we take our responsibilities very seriously. As a food manufacturer, we believe that placing an emphasis on corporate responsibility is pivotal to our performance and an important part of increasing shareholder value, which is our primary goal.

Food safety is always a top priority and we take every precaution to ensure the safety of our products across all our businesses through robust quality controls and risk assessment processes. Unfortunately, in February 2007 we had to take the precautionary step of recalling a range of houmous products after routine testing found the presence of salmonella in a small number of products made for one of our customers. We would like to apologise to any consumers affected by this recall. Our ability to track our products and ingredients throughout the supply chain meant that we were able to isolate the problem rapidly, identify the products for recall and immediately ensure that all the potentially affected products were removed from sale, working closely with our customers. This can only be done if robust traceability and risk management systems are in place, which are monitored throughout the production process. Our responsible handling of the incident and open dialogue with our customers, the Food Standards Agency, the Food Safety Authority of Ireland and our Local Environmental Authorities, enabled us to safely resume production in a matter of days. We continue to work hard on preventing such issues from re-occurring.

We work closely with our customers to develop products which meet other growing corporate responsibility trends – we are sourcing the best quality ingredients, reducing salt content in our products, providing a greater selection of healthy and balanced meals, as well as helping consumers make informed food choices through more detailed product labelling. Furthermore, we are looking to reduce energy use in our processes and our environmental impact.

In addition, we have strict health and safety procedures in place for people working at, or even visiting, our sites. We also work closely with our key suppliers to ensure that their working practices meet our standards for food safety, environmental management and ethical employment. These are demands from our consumers and our customers and are high on our corporate agenda.

Our people

We cannot achieve success without our people, and we would like to take this opportunity to thank our employees for their dedication and hard work. We have ambitious growth plans and, as we expand, we must ensure that our values remain strong. This can only be achieved by investing in the people we have and attracting the right quality of people into the Group to ensure sustainable growth.

The health and safety of all employees is paramount to the Group and we provide extensive safety training for all our employees. As a result we have seen a significant reduction in the level of accidents. Strict health and safety protocols are in place at each site and performance in this area is reported monthly to our Management Board.

We must also ensure that there is good communication throughout the Group. We have strong systems in place which facilitate dialogue through our Site Employee Forum (SEF) and Group European Forum (GEF) structure. Over 40% of our workforce is unionised across 17 manufacturing sites. We support and work closely with union officials at the factories where our employees have chosen to be represented by a union.

In the majority of our manufacturing sites, however, our employees have expressed their wish to deal directly with the Company and are represented through their Site Employee Forum. More information on the SEF and GEF can be found on page 61.

Outlook

Bakkavör Group has performed well despite a tough trading environment in recent years, with aggressive competition and price deflation. We have been able to respond to this by cutting costs through efficiency improvements, investing in new markets, strengthening our customer relationships and ensuring that we remain innovative with new product development, which corresponds to today's consumer needs.

Overall, market conditions remain favourable and we are well positioned to benefit from the strong market trends that we are witnessing globally. We will continue to lead consolidation in the UK market and explore high growth opportunities elsewhere. The Continental European and Asian food markets will play an increasingly important role in the future. We are investing now and will continue to invest aggressively outside the UK to secure the future growth of the company.

With a favourable outlook in our key markets, our continued focus on strengthening the business, a strong financial position and a first class team to execute our plans, we look forward to reporting further progress in the year ahead.

Ágúst Gudmundsson,
Chief Executive Officer

Lýdur Gudmundsson,
Chairman

10 REASONS TO INVEST

European retailer brands will grow by **44%**

Fresh prepared foods now in 45% of UK shopping baskets

The average French meal takes 44 minutes less than in 1978

Fresh prepared foods added **£4 billion** to the UK food market in last 10 years

1

THE FASTEST GROWING FOOD SECTOR

Fresh prepared foods alone have increased the value of the total UK food market by £4 billion over the last 10 years. The sector has consistently outperformed total food growth.

2

RETAILER BRANDS IN EUROPE – A 44% INCREASE BY 2010

By 2010 the IGD forecasts that the European retailer brand market will increase by 44% to €431 billion. Our expertise in this area means we are in a good position to take advantage of this trend.

3

PART OF A MODERN LIFESTYLE

Fresh prepared foods are now bought regularly – in 45% of every UK grocery shopping baskets you will find an item from the fresh prepared foods sector. This is more than any other category, even bread and milk.*

4

DEMAND FOR CONVENIENCE – A GLOBAL TREND

People around the globe are influenced by the convenience trend. In 1978 the average French meal lasted 1 hour and 22 minutes. Today it lasts approximately 38 minutes. Fresh prepared foods are used increasingly in France to reduce meal preparation time.

5

CHINA – 2ND LARGEST FOOD RETAIL MARKET BY 2020

According to IGD, China will become the world's second largest food retail market by 2020. Today the chilled foods market in China is growing annually at 15%. In March 2006 Bakkavör Group acquired a 40% stake in Chinese salads manufacturer Creative Foods and is actively exploring further investment opportunities in this region.

* Source: TNS

6 **UK CONVENIENCE RETAILING – 24% GROWTH BY 2012**

The IGD predicts that convenience retailing in the UK will grow by almost 24% in the next five years, against a wider market growth of 15%. This development is important for Bakkavör Group as fresh prepared foods provide an important product range in these types of stores.

7 **INCREASED AWARENESS OF HEALTH CONCERNS**

Obesity is a global concern. People are more aware than ever of the need to take responsibility of their own well-being with 64% of Europeans taking active steps to improve their health. A key focus of our product development is providing naturally healthy, fresh food solutions that are nutritionally balanced.

8 **WE TRADE WITH 7 OF THE TOP 10 GLOBAL RETAILERS**

In most of the geographical markets in which we operate, the retail market is consolidating, with large retailers increasing their share. Bakkavör Group manufactures products in six different countries and already trades with seven out of the top ten global retailers.

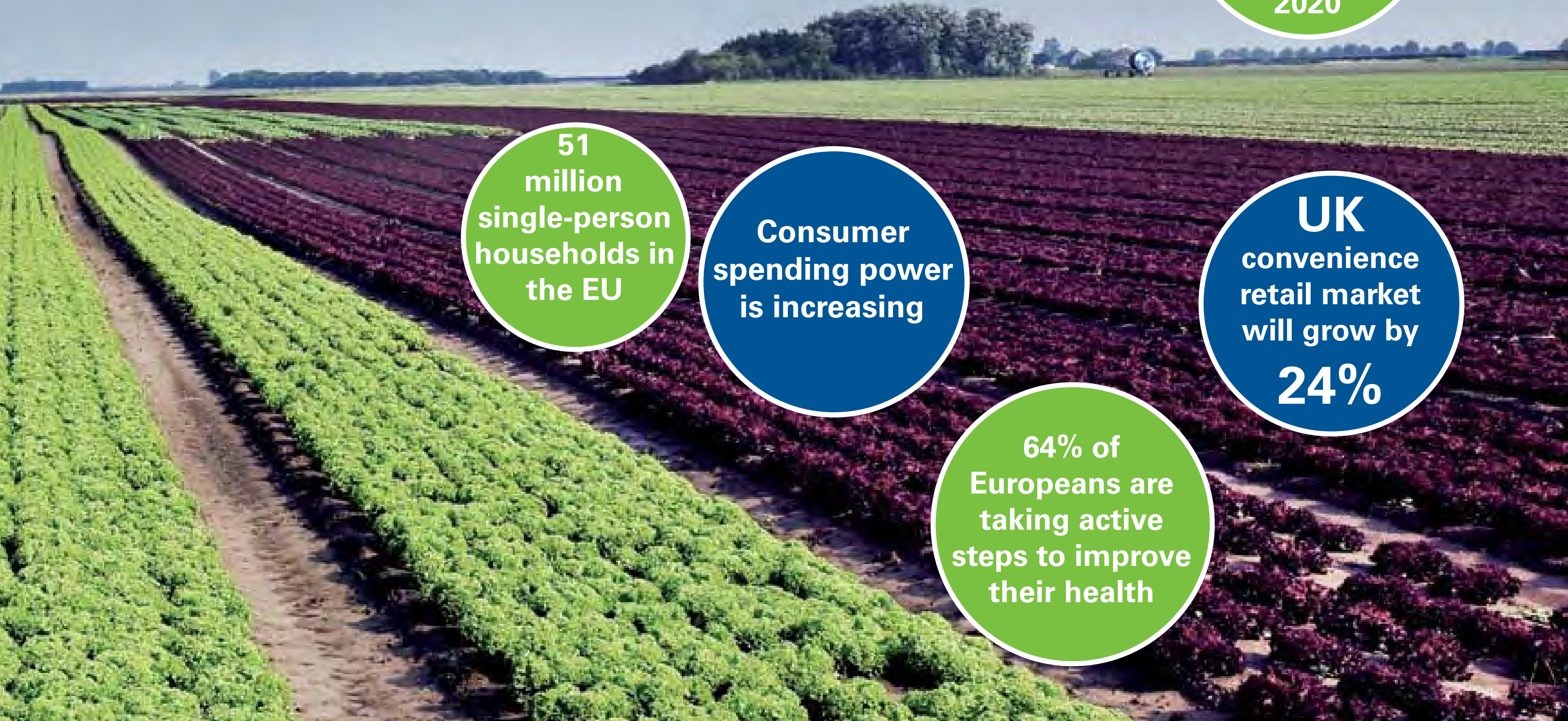
9 **INCREASING DEMAND FOR PREMIUM PRODUCTS**

Datamonitor forecasts that the number of people in Europe who have above average income will increase, rising from 21.3 million in 1995 to 32.0 million in 2009. As people gain more spending power, premium products have become more affordable and on many occasions fresh prepared food are proving to be ideal solutions for people looking for everyday treats.

10 **SINGLE-PERSON HOUSEHOLDS ON THE RISE**

The number of single-person households is increasing significantly and according to Datamonitor is set in the EU to rise from 40.8 million in 1997 to 51 million in 2007. Fresh prepared foods are often a natural choice for people living on their own as there is a wide range of hot and cold-eating products offered in a variety of portion sizes.

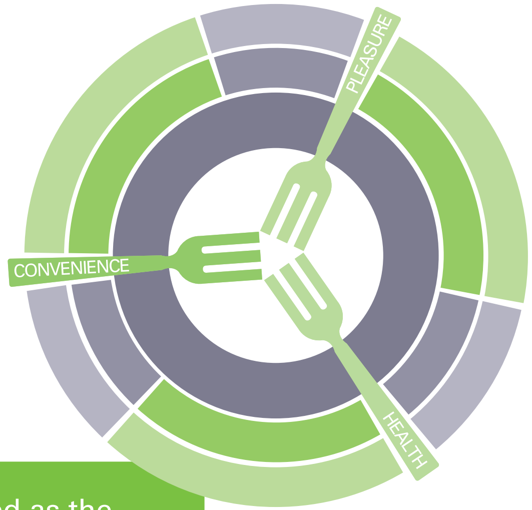
China will become the 2nd largest food retail market by 2020



OUR MARKETS

Sharing our knowledge

In this section we share with you key information on the food markets in the UK, Continental Europe and China. We will explain why we have invested and continue to invest in fresh prepared foods and produce in these markets.



GLOBAL FOOD TRENDS

Convenience, health and pleasure

Bakkavör Group's vision is to be recognised and respected as the world's leading fresh prepared foods and produce provider and, to realise this, we continue to explore new markets – both at a product and geographical level.

In previous reports we have explained how the three mega-trends – convenience, health and pleasure – guide and shape our strategic thinking and product development. This year is no exception as, even though these trends are evolving at different rates in each of our markets, they are prevalent around the world.

In this section, we share with you our knowledge of changing behaviour and how this is influencing people's demand for fresh prepared foods whether they are living in London, Amsterdam or Shanghai. We start with the convenience mega trend.

Convenience

In most of the developed world people are finding it increasingly challenging to achieve an optimal work-life balance and generally feel they have more things to do in less time. Lifestyles are becoming increasingly complex owing to socio-demographic, economic, technological and environmental changes. We explore next how some of these influences are affecting the demand for convenience.

Socio-demographic influences

The changing family structure

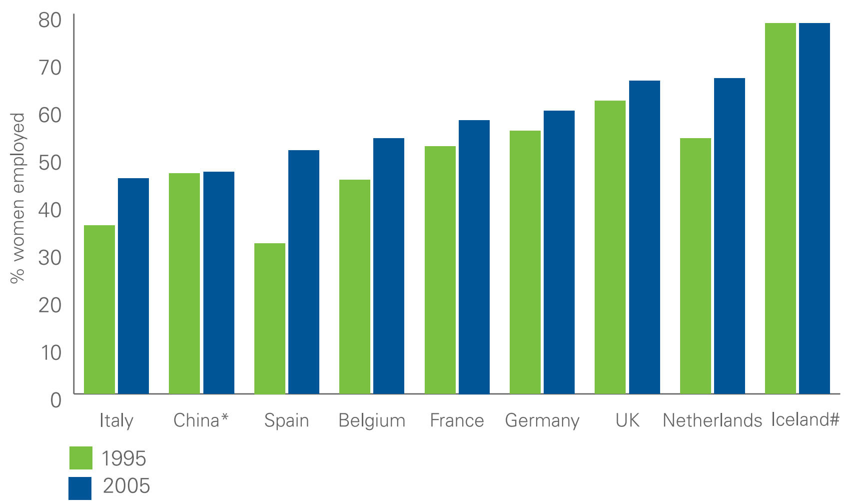
Today, people are staying single longer, having children later (or not at all), getting divorced more quickly, living longer and possibly remarrying once, twice or maybe even more often. Although the traditional 'nuclear family' (of married parents and children) is still the norm in many countries, there are now a number of different family structures, and this is influencing our eating patterns.

For women – whether living alone, with a partner, or in a family with children – it is now likely they will be in part-time or full-time employment. In the last ten years, for example, there has been a marked increase in the number of mothers with young children returning to work. Increasingly, women and men have to juggle a career with a family and social life and this puts pressure on the time they have for shopping and preparing food.

Not leaving the nest

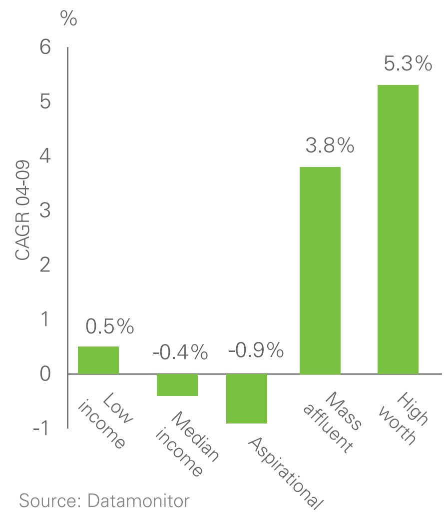
Long gone are the days when all young people left home at the age of 18. Rising housing prices and the cost of living have resulted in this group of people either leaving home only temporarily or staying in the family home for longer to save on living expenses. Across Europe, over half of all 18-24 year olds live with their parents and this rises to in excess of 90% in Spain and Italy. As a consequence, this age group often has more money to spend and is able to influence their parent's decision-making when buying food.

The growth of working women is contributing to economic affluence



Source: Eurostat/ *All-China Women's Federation / #Statistics Iceland
The greatest shift in China has been the rise in female professionals and technicians in state-owned enterprises up from 37.3% in 1995 to 43.6% in 2004 of the total number of professionals.

The change in adult wealth groups in Europe 2004-2009



Source: Datamonitor

Economic influences

Trends indicate that there is a growing divide between the wealthiest and the poorest income groups. However, on the whole, people's personal disposable income has gradually increased due to economic growth, higher levels of employment (particularly for women), and a strong housing market. People are now accustomed to having more spending power and are willing to pay for items that make their lives easier.

Technological influences

It is often stated that we live in a '24-hour society', and with the emergence of technologies such as the Internet, email communication, mobile phones and other handheld devices, it is now possible to access a vast number of goods and services no matter what the time of day. This has had a direct effect on how people work, with an increasing number of people working from home around the clock and adopting more flexible hours to fit the job, rather than a fixed working pattern.

The impact on our eating habits

These changes, whether socio-demographic, economic or technological, affect how we eat and when we eat. It is becoming more common for people to eat around their work and leisure activities rather than to allow their time to be dictated by meals at set hours of the day. The consequence of this more informal approach to eating is the decline of the traditional family evening meal around the table and an increase in the number of snacks and light meals. There is also a strong trend for people to eat alone (even in a family environment) as household members come and go at different times throughout the day.

It is not an easy task to balance the household's food needs around our increasingly complicated lifestyles. Food preparation is more of a challenge and the demand is high for good quality food, which is also easy to prepare.

The change in family structures across Europe 1995-2005

Source: Datamonitor

Health

Across the world, people are taking a more proactive and holistic approach to their food. There is a growing trend for people to concentrate more on eating food that is good for them rather than simply avoiding certain types of food and ingredients perceived to be 'bad'.

Obesity

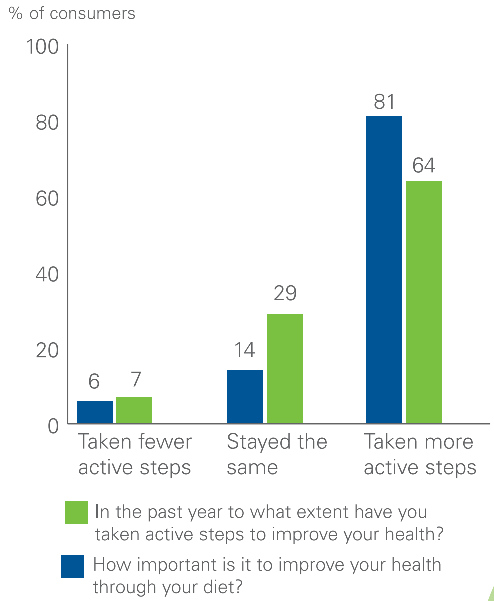
One major factor is the recognition of rising obesity levels. The World Health Organisation (WHO) projects at least 400 million obese adults in 2005. An estimated 1.6 billion people are overweight and the WHO expects this to rise to over 2.3 billion by 2015. Obesity is not just a phenomenon of the developed world. People in the developing world are becoming obese, even in countries where hunger exists. This is a truly global issue and even people in countries renowned for their balanced diet are at risk – in Japan for example, twice as many men are obese today than in 1982[1].

Even more alarming is the rise in childhood obesity. The international Obesity Task Force (IOTF) estimates that worldwide there are about 155 million children who are obese and over 22 million of these are under the age of five. Within the EU countries, 14 million school children are overweight and three million of them are obese.

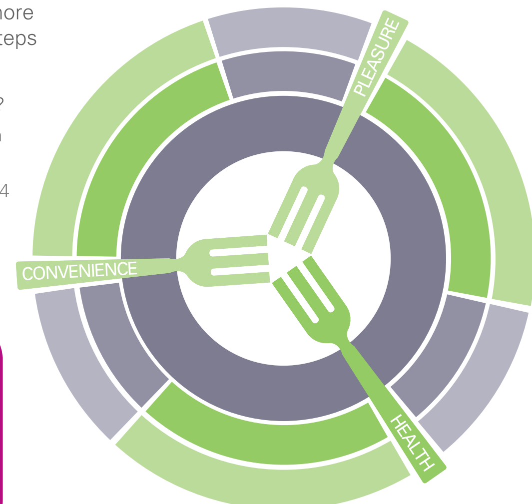
Governments and health organisations have become increasingly worried about the rise in obesity and the increased financial burden it places on their health systems. In the last few years, various campaigns have been carried out in many countries to reinforce the importance of eating fruit and vegetables and participating in physical activity. Alongside this, media attention on this topic has increased considerably, resulting in greater awareness of current and future health issues and the nutritional value of food.

1 www.medicalnewstoday.com

European consumer attitudes and behaviour towards health, 2004

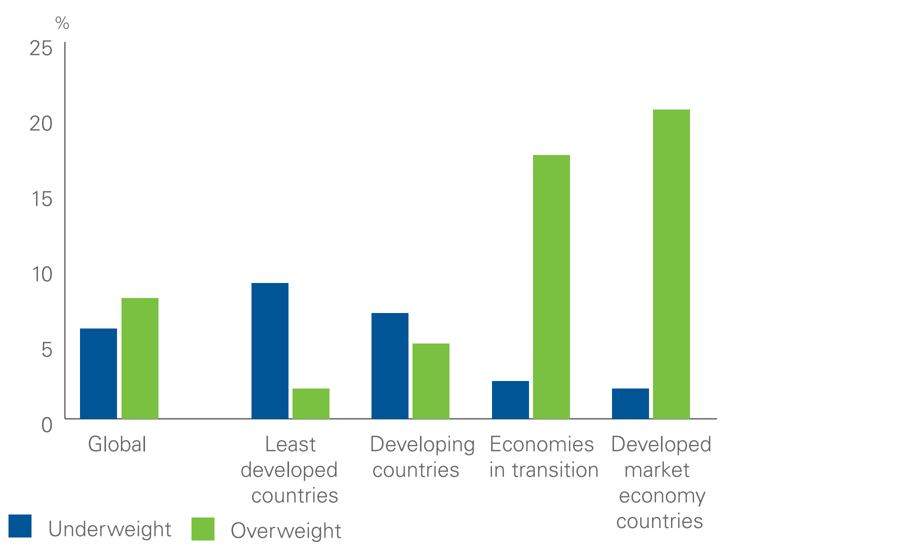


Source: Datamonitor's Global Survey, 2004



By 2015 the World Health Organisation projects there will be 700 million obese adults – almost twice as many as today.

From least to most developed countries: % of people overweight is on the rise



Source: WHO, 2000

Ageing population

Another global trend affecting people's eating habits is the ageing population. The United Nations estimated the global population aged 60 and above to be 688 million in 2006 (one in every nine people) and projected to grow to almost 2 billion by 2050 (one in five people). At that point, the number of older people will be greater than the number of children for the first time in history.

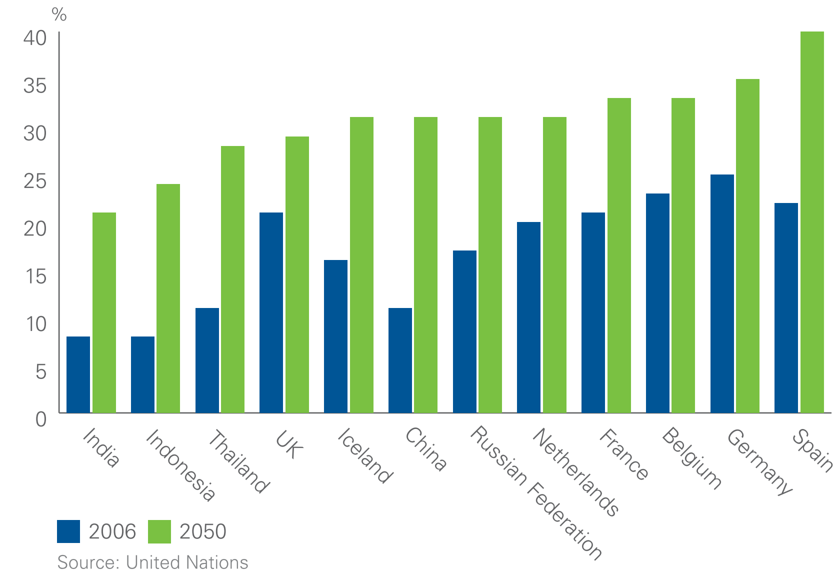
One consequence of this trend is a growing interest in vitamins and minerals and the so-called functional benefits of food. Recently, demand for food which claims to improve both mental and physical health has increased dramatically. These foods contain, for example, ingredients such as omega-3 and pre/pro-biotic elements which help fight age and lifestyle-related illnesses.

Where does it come from?

Increasingly, people are making food choices not only based on health, convenience and pleasure, but also whether or not it has been produced in an ethical way. This includes, for example, a growing interest in the origin of ingredients and how food is produced.

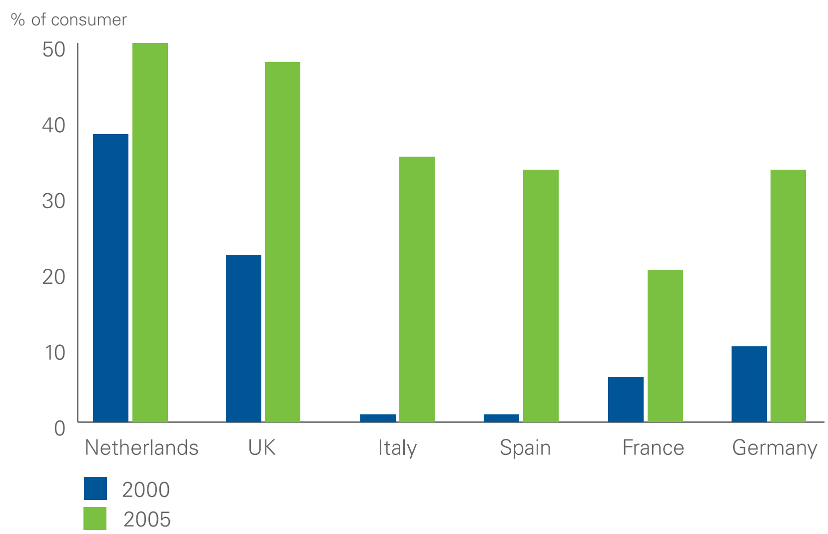
This trend has strengthened owing to the number of worldwide issues in the last twenty years. These have ranged from the threat of global warming and concerns over animal welfare, to the use of chemicals and pesticides, the unfair treatment of food producers in developing countries as well as a number of food scares. The coverage of these events has often been both intense and emotive, making headline news in countries around the world, e.g. the Bovine Spongiform Encephalopathy (BSE) food scare in 1996 and the dioxin scare in Belgium in 1999. As a consequence consumers are becoming more discerning and are demanding more information about what is in their food, where it has been made and how it has been produced.

Ageing population - % of population over 60 years old



Source: United Nations

Ethical consumer behaviour by country, 2000-2005



Source: Datamonitor

% consumers who have participated in 5 or more of the following activities in the last 12 months:

- recycling
- giving money to a good cause
- bought a product with an established link to a good cause
- bought a product labelled as social, ethical, or environmental
- bought organic food
- given voluntary help to a good cause
- bought goods because of a company's social/ethical reputation
- actively campaigned for an environmental cause
- felt guilty about an unethical purchase

Pleasure

Stress is recognised as a condition worldwide and the chief causes are universal – work pressure, time pressure, family pressure and the challenge to achieve a satisfactory work-life balance. Increasingly, people are looking for ways to reduce their stress levels and, in trying to do so, share many similar needs – simplicity, familiarity, indulgence and convenience.

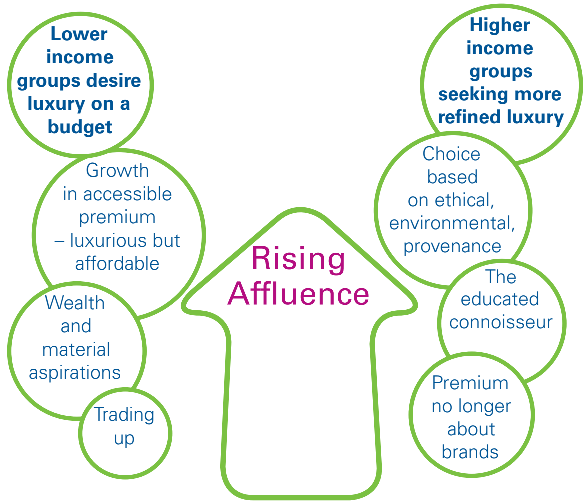
Rewarding behaviour

The combination of the many elements of the pleasure trend have an important influence on the demand for food products across the world – whether for comfort food, indulgent treats, exotic recipes or the familiarity of traditional local dishes.

There is a growing sense of people's need to reward themselves and their families for coping with hard work and the stresses of life. With growing affluence in many countries, such rewards have become everyday treats and whether people are wealthy or aspiring to be wealthier they buy items to help them achieve one goal – a perceived better quality of life.

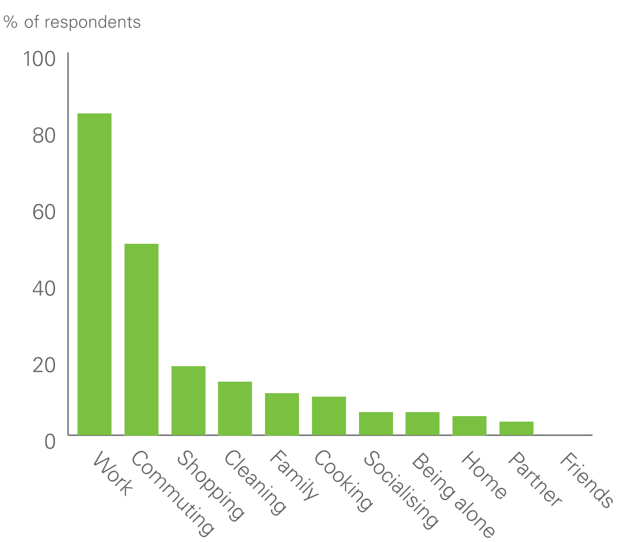
In attempting to reduce stress people also try to find ways to escape and are increasingly taking solace in the simple, familiar pleasures of life (e.g. eating traditional dishes from their childhood). In contrast, people are also becoming more open to experimentation and new experiences. Global travel and a proliferation of ethnic restaurants have exposed people to a myriad of different foods and flavours and the ability to experience new tastes is part of the general pleasure-seeking trend.

All income groups have material aspirations



Source: Adapted from Datamonitor analysis

Stressful activities



Source: Datamonitor 2002

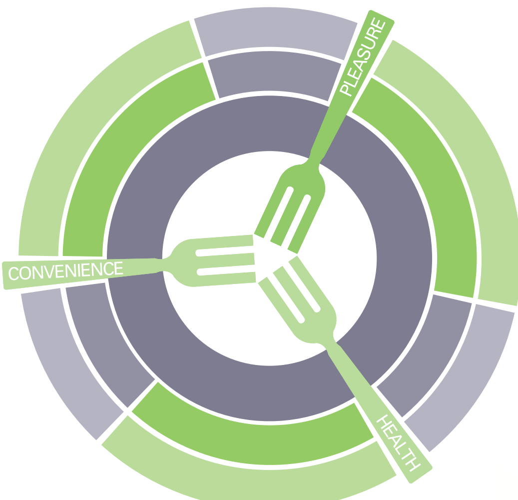
Finding excitement and sensations in life has never been more important to European consumers

The % of respondents who felt that finding ´more excitement and sensations in life´ was either 'important' or 'very important'

France	Germany	Italy	Netherlands	Spain	UK
75%	68%	70%	75%	66%	73%

Source: Datamonitor

What do these global trends mean for Bakkavör Group?



In summary, behaviour is changing across the globe, affected by complex family structures, advances in technology and communication, greater affluence, the increase in the number of working women, and a greater awareness of global environmental issues and health concerns.

These changes influence all aspects of people's lives and, more often than not, their day-to-day shopping and eating habits. People are responding by seeking solutions that offer convenience, health and pleasure. The fresh prepared foods sector has been particularly successful in meeting these evolving needs and, as a result, continues to achieve stronger growth than in many other food sectors.

Bakkavör Group's track record in fresh prepared foods is solid and we believe that as we continue to explore new markets – both at a product and geographical level – we have the understanding, skills and determination to develop successful products that meet people's food needs no matter where in the world.

In the next section of 'Our Markets' we share with you how these global mega-trends influence fresh prepared food developments in the main geographical areas in which Bakkavör Group operates, starting with the UK.

UK FRESH PREPARED FOODS

A relatively mature but growing market

The UK fresh prepared foods sector is relatively mature. Not only is it the largest market for Bakkavör Group but also the largest in the world. The success of fresh prepared foods is due to manufacturers and retailers who have successfully developed products which fulfil the UK's strong lifestyle demand for quality food, which is easy to prepare.

Fresh prepared foods sales alone have increased the value of the total UK food market by £4 billion[1] over the past 10 years. Not only does the fresh prepared foods sector continue to outperform the growth rate of general food, it also continues to grow faster than other food categories. In 1994, for example, the fresh prepared foods sector was around the same size as the frozen prepared foods sector – both valued at around £2 billion. Today the fresh prepared foods sector is more than three times the size of the frozen prepared foods sector and is worth over £7 billion. Strong growth has been achieved through providing solutions that continually meet the evolving consumer demand for convenience, health and pleasure.

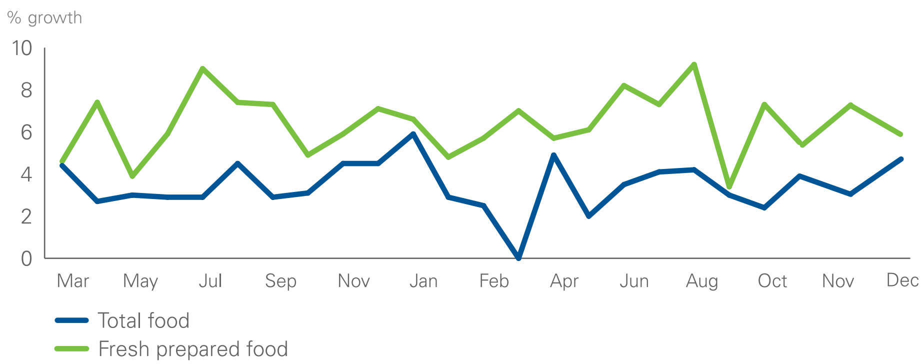
Convenience is a given

Factors such as time pressure, increasingly busy lifestyles, the rising number of working women, a growing number of smaller households, together with a decline in structured meals and culinary skills are now embedded in UK society.

Whilst people have a growing interest in food, the above factors have and will continue to stimulate demand for food which is quick and easy to prepare. In the UK, the offer of convenience is increasingly perceived as a given with additional benefits such as health and/or pleasure required for food to achieve commercial success.

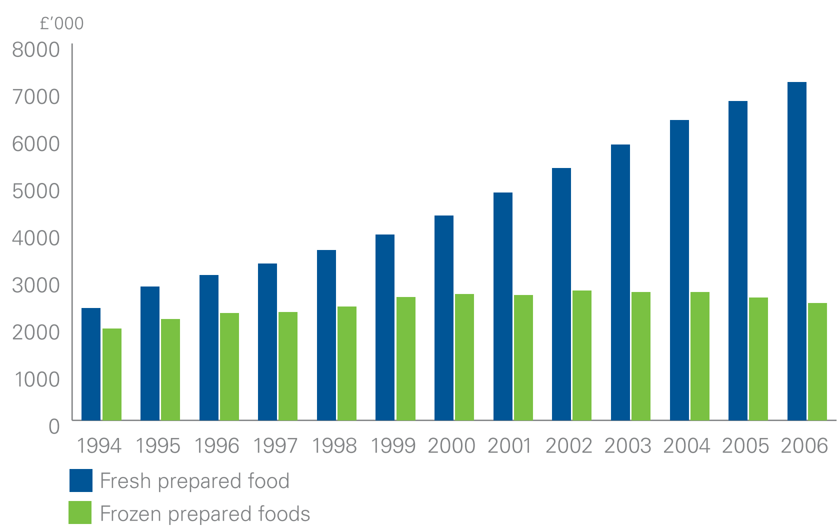
1 TNS

Fresh prepared foods consistently outpaces food growth - Mar 2005 to Dec 2006



Source: TNS RST Summary

Fresh prepared foods versus frozen prepared foods



£'000 - years to October 2006
Source: TNS Worldpanel

Everyday cooking from scratch is not the norm

People in the UK tend to view cooking in two different ways – they either enjoy being involved in the cooking process or they find it too much of a challenge and have little confidence in their ability to make something that will taste good. Whether people like cooking or not there is one common factor – most people do not cook from scratch everyday, as they are unwilling or too busy to devote the time needed.

The extensive range of fresh prepared foods available in the UK provides a variety of flexible options for people depending on the time they want to spend and the level of involvement they wish to have in the cooking process. There are 'ready to eat' foods that, on the whole, can be eaten cold, such as salads, sandwich wraps, prepared fruits and desserts; there are 'ready to heat' foods that can just be warmed up such as ready meals, pizzas and soups and there are 'ready to finish' foods which are, in the main, raw and need to be cooked such as pasta and sauces, and ready to cook meals.

'Ready to finish' foods are becoming increasingly popular in the UK for they allow people to feel more involved in the cooking process without having the disadvantage of spending time shopping for all the specific ingredients and then preparing them. These products, for example, may contain meat or fish which has been dressed, garnished or marinated and vegetables which have been peeled or chopped.

UK cooking/eating statistics

% of in-home meals	1994	2005
Eaten alone	34%	51%
Eaten as a snack	16%	24%
Eaten as a light meal	23%	37%
That are homemade	18%	11%
Time to prepare a main meal	30 mins	19 mins

Source: TNS

Factors affecting the ways consumers eat, drink, cook and shop for food, March 2006

Base: 2026 adults aged 15+	**ALL**
Government-led healthy eating campaigns e.g. Five-a-day fruit and vegetables, salt reduction	32%
Celebrity-led campaigns such as Jamie Oliver's School Dinners	20%
Magazine articles	19%
Food advertising by manufacturers or retailers	17%
Documentary coverage on food issues such as Panorama, Tonight with Trevor McDonalds	17%
Makeover shows such as You Are What You Eat, Food Doctor	17%
Cookery programmes such as Saturday Kitchen, Rick Stein's Local Food Heroes	17%
News headlines on incidents such as bird flu, Sudan 1, badly kept poultry, rising obesity	16%

Source: GfK NOP/Mintel

A healthy body, a healthy mind

The UK has seen a boom in growth in certain food markets. Foods that have functional attributes e.g. spinach (which is high in zinc) and foods which contain functional ingredients (such as omega-3) have become particularly popular. Many fresh prepared foods now feature 'super food' ingredients such as seeds and berries e.g. pumpkin seeds in salads and blueberries in fruit tarts and fruit salads.

Rebuilding trust

The UK food industry is under constant media scrutiny and people increasingly link the perceived healthiness of food with food safety. Today in the UK the notion of 'safety' is interpreted in a variety of ways: no artificial additives or preservatives, no 'bad' fats, the use of natural ingredients and flavourings and complete integrity in respect of the food-making process and the sourcing of ingredients.

The use of natural ingredients has been a major focus of fresh prepared foods development – often as a result of close collaboration between UK retailers and manufacturers. Action has been, and continues to be, taken to remove, for example, hydrogenated fats, artificial additives and preservatives from foods, to use natural ingredients to flavour and preserve and to reduce the amount of salt to meet government targets. In conjunction with these actions, the level of available information has often increased, helping people to make informed choices about the foods they wish to eat whether from a nutritional or a sourcing point of view.

There has also been a growing interest in where and how foods are produced. This has developed as a result of exposure to food scares, the introduction of food standards and a growing awareness of organic, locally produced and ethically produced foods. As a result, people are gradually becoming more discerning about what they buy and eat and an interesting development is taking place whereby people are starting to gain both a moral and emotional pleasure from foods they perceive as being healthy.

Pure pleasure

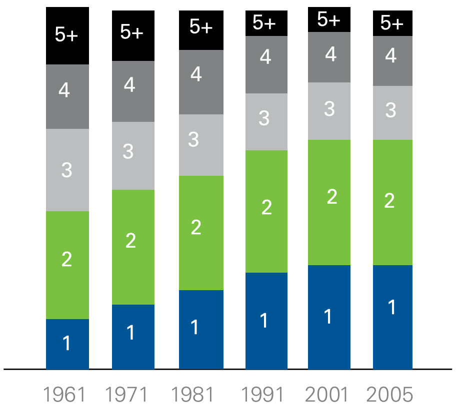
In the UK there is growing interest in food, stimulated by celebrity chefs, food-related TV programmes, more people eating out in restaurants and the influence of global travel.

The rise in disposable income, combined with the challenge of achieving a work-life balance, has resulted in a growing number of people who feel they have earned 'the right' to treat themselves on a regular basis, rewarding themselves with quality foods that make them feel good. The pleasure trend therefore is becoming more closely associated with sensual indulgence.

The trend of individualism remains strong. This has been influenced by the rise in the single-person households in the UK and the importance of the individual even in larger households. Fresh prepared foods are a natural choice as they provide an extensive variety of products available in individual portion sizes.

Pleasure is also about finding comfort and, for many people, this has increasingly involved returning to the familiar and simple pleasures in life, particularly those from childhood. It is becoming more common for people to choose food based on nostalgia and authenticity. As such, old UK favourites have made their way successfully into fresh prepared foods ranges e.g. sausages ('bangers') and mash or beef Wellington.

UK average household size (number of members)



Source: Office for National Statistics

Agreement with selected lifestyle statements, 2001-2005

Base: Adults aged 15+	2001	2003	2005	2001-05 Chg
I appreciate good food	76.4%	79.9%	81.6%	+5.2%
I'm a gourmet	8.8%	8.7%	9.0%	+0.2%

Taken from the TGI Survey of around 25,000 adults
Source: GB TGI, BMRB Spring 2002 & 2004 & QTR 2 2006/Mintel

58% of UK consumers enjoy eating foreign foods.
Source: Datamonitor

The average time it takes to prepare a chilled meal is almost 50% quicker than when preparing a frozen meal, and 37% quicker than a meal made from scratch.
Source: TNS Worldpanel

What do these UK trends mean for Bakkavör Group?

The UK fresh prepared foods market is the largest in the world and a fast-growing sector in the UK food market. Fresh prepared foods continue to be influenced by the three mega-trends – health, convenience, pleasure – which are now embedded in UK society and which we believe will remain strong for the foreseeable future.

Today the UK food market is going through a challenging period, as lifestyles are becoming more complex and people are becoming more interested, discerning and demanding about the foods they eat. However, we continue to believe that fresh prepared foods have the attributes required to fulfil people's lifestyle needs and aspirations more easily than other types of foods.

The responsibility to respond to these changing consumer needs lies with food retailers and manufacturers. At Bakkavör Group we take our responsibilities seriously and will continue to be committed to developing food that is both innovative and trustworthy whilst at the same time addressing the strong demand for convenience.

In the next section we explore how UK grocery retail trends are developing in response to these changing needs.

Some people also gain pleasure from experimenting with bold new tastes and flavours influenced by overseas recipes in restaurants and foreign travel. Similar to those people who seek comfort from foods, people are choosing fresh prepared food dishes with authentic ingredients and are more willing to try more exotic fresh vegetables and fruits. As more people migrate to the UK it is likely that the cuisines and produce on offer will become even more diverse.

Pleasure is also sought from sharing experiences with others. There is a growing trend for people to have meaningful get-togethers with friends or family.

As a result, informal home entertaining has increased, although the time spent preparing for the event has reduced. Fresh prepared foods offer quick 'easy to share' meals which take the pressure off the host, reducing the amount of time spent in the kitchen. Popular dinner party foods include ethnic snacks and dips, speciality breads, leafy and convenience salads and desserts.

UK RETAIL TRENDS

Selling our products through the best channels

The UK grocery market is a concentrated market with relatively few players. Bakkavör Group trades with all the main retailers and we focus on offering the best service, quality, value and innovation in order to earn their loyalty. To achieve this we need to be aware of the key retail trends influencing the market. In this section we share with you the main retail developments of 2006.

The importance of the grocery retailers

In the UK, the total household annual expenditure on goods and services is around £750 billion[1] and, in 2006, £123.5 billion (nearly a fifth) was spent in grocery retailers alone[2].

Over the last ten years grocery retailers have gradually increased their share of the retail market and now hold close to 50%, achieving consistent rates of growth and often outperforming retail sales growth as a whole.

In 2006, this performance was no exception as, despite challenging market conditions, grocery retail sales achieved an increase of 3.1%[3] against a total retail sales growth of 0.9%[4].

The grocery retailing market[5] is dominated by four main players, Tesco, Asda, Sainsbury's and Morrisons (holding a combined share of 71%), coupled with smaller significant players such as Waitrose, Somerfield, Co-op, Aldi and Lidl.

The potential impact of market regulation

The continuing consolidation of the UK grocery retail market, however, has caused some concern regarding the impact of the larger grocery retailers on small shops in the UK. In March 2006, following a report published by the All-Party Small Shops Group on the impact of supermarkets, the Office of Fair Trading (OFT) announced it would be referring the UK food retailing industry to the Competition Commission for a full investigation. The enquiry is expected to last a minimum of 18 months and will focus on the main grocery product categories (food and drink, along with pet food, cleaning and household goods), and the impact of property planning systems, supermarket land holding policies and buying power.

It is difficult to predict the outcome of the enquiry at this stage; however we believe it is likely that grocery retailers will continue to concentrate on developing their hypermarket and their convenience store formats which represent their main sales growth opportunities.

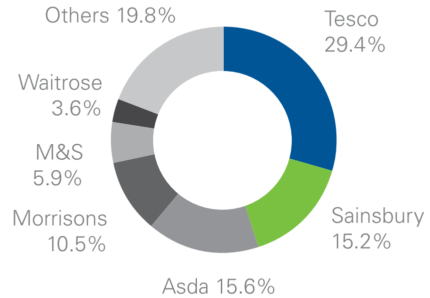
Retail developments

The last few years have marked an intense period of strategic development in grocery retailing. The retailers have been highly competitive not only on price, store expansion and format development, but also in terms of range differentiation through retailer sub-brands and social responsibility initiatives.

Price awareness

UK shoppers have become considerably more price conscious owing to aggressive price competition among the grocery retailers and access to a growing range of Internet price comparison websites. This has resulted in what the Institute of Grocery (IGD) terms 'smart shopping' behaviour where people spend as little as possible on commodity items in order to spend more on premium products such as fresh prepared foods.

UK grocery share by retailer



Source: TNS Till Roll 52 we 28 Jan 2007

Inventive new convenience store formats

The successful grocery retailers have gained competitive advantage through acquisitions and the development of store formats based around people's lifestyle needs. For example, there has been an increase in the number of grocery convenience stores as well as store formats in petrol forecourts, motorway service stations, train stations and airports. The IGD predicts that convenience retailing will grow by almost 24% in the next five years, against the wider market growth of 15%. These developments are important for Bakkavör Group as many shoppers are looking for fresh, easy to prepare food in stores which are conveniently located near their place of work or on the way home.

1 ONS 2005 data
2 IGD Grocery Retailing 2006
3 TNS
4 ONS
5 Including M&S which generally is classified as a general retailer

Retailer brands continue to evolve

In the UK retailer brands have a 40%[6] share of the grocery retail market and have become recognised brands in their own right. They have enabled retailers to build customer loyalty and gain competitive advantage by differentiating their product.

Retailer brands have developed around three distinctive offers – value (or 'economy'), standard and premium. This clear branding enables retailers to attract customers no matter what their income, helps customers find the products they are looking for and provides an opportunity for customers to trade up to products as and when they aspire to do so.

However, as food and lifestyle trends have evolved, retailer sub-brands have become increasingly sophisticated. This development is particularly prevalent in the fresh prepared foods sector where you can find sub-brands relating to health, organic foods, children, specific cuisines, restaurant and dinner party cooking and many more.

Retailer brands now account for 72%[7] of the total fresh prepared foods sector and 93%[8] of the markets in which Bakkavör Group operates. This reflects the importance of this sector to the retailers and how crucial the close co-operation between food manufacturers and retailers is, in order to develop relevant products for the retailers' various sub-brands.

The development of retailer brands is set to continue and by 2010, the IGD estimates that retailer brands in the UK will account for 45% of the grocery retail market.

Social responsibility in the spotlight

In 2006, retailer corporate responsibility policies came under scrutiny from the media and the public more than ever before. As previously mentioned (pages 21 and 25) there has been an increasing amount of interest and media coverage on issues such as food safety, ethical trading and the environment. In addition, the UK government has also launched new environmental reporting guidelines and the 'Food Industry Sustainability Strategy'. These factors have resulted in retailers promoting their 'responsible retailing' credentials more openly than in the past and for some retailers this has afforded another way to differentiate themselves from the competition. At Bakkavör Group we have worked closely with our retail customers to develop products, which match their corporate public image.

Online shopping continues to grow

Almost 60%[9] of the UK population can now access the Internet at home, with Broadband accounting for over 70% of connections.

In 2006 online retail sales were estimated to increase by 40% to £30 billion[10]. By 2010, it is predicted that 6%[11] of all UK spending on goods and services will be made online, with the number of online shoppers rising from 10 million to 25 million. More importantly, food and grocery items are estimated to make up 30% of online shopping by 2010, up 235% on 2005.

Grocery retailers are committed to growing their online operations and this offers a good opportunity for fresh prepared foods, which are now permanent features on retailer websites.

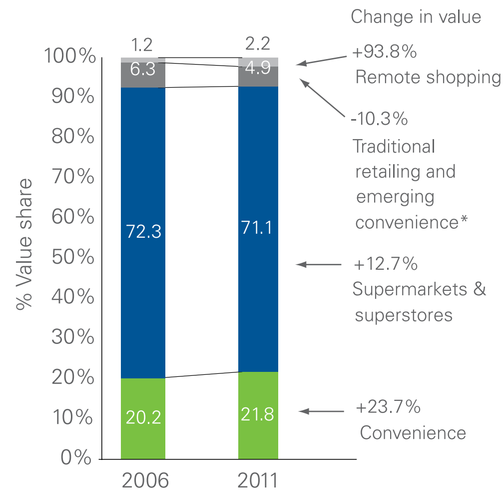
6 IGD European Private Label Growth 2006
7 TNS
8 TNS

9 ONS
10 IMRG
11 PayPal study – BBC News Article 12/05/2006

What do these retail trends mean for Bakkavör Group?

The UK food retail market remains demanding with pressures from price competition, new government initiatives, along with shoppers who are increasingly wanting more reassurance in terms of food safety, quality and corporate responsibility. We are convinced that in the UK the grocery retail market still represents the best route for sales of fresh prepared foods whether it be through traditional stores or online Internet sites and that we are in a strong position to benefit from these positive retail growth trends.

Convenience stores forecast to rise



Forecast for grocery segment sales values 2006-2011
* CTNs, Off licences, Bakers, Butchers, Greengrocers, Other Specialists
Source: IGD Research

UK ECONOMIC TRENDS

Favourable market conditions

Overall, the UK economy picked up in 2006, with a recovery in GDP. However, inflationary pressures and rising interest rates resulted in people becoming more cautious, and we believe this is likely to continue into 2007. In this section we look at the key economic statistics of 2006, which affected consumer attitudes and behaviour in the UK.

Gross Domestic Product (GDP)

In 2005, GDP growth in the UK was lower than expected at 1.9%. However in 2006 the growth rate recovered rising by 2.8%[1] over the year. Growth was aided by an increase in household expenditure (for example, around the time of the World Cup) and prolonged warm weather over the summer, which increased commodity prices (e.g. wheat), resulting in a knock-on effect on the price of staple household shopping items.

Housing market

In 2006, housing prices in the UK remained buoyant, with a shortage of sellers and an insufficient number of houses being built – a combination which led to an increase in prices, particularly in London and the South East of England. According to Nationwide (a leading UK building society), prices rose by 10.5% during 2006 – an increase which was three and a half times higher than in 2005.

This has widened further the affluence gap with existing owners on one side, whose property value is appreciating, and potential first-time buyers on the other side, who are finding it increasingly difficult to get their feet on the property ladder. The average house now costs six times the average wage (nine times the average in London) and potential first-time buyers are more than ever having to rely on parental support.

It is not easy to predict whether house prices will rise or fall going forward. Influencing factors will include the rise in the number of households, (particularly single-person households), an ageing society, as well as the influx of people from other countries coming to live in the UK. Nationwide analysts believe that in 2007 house prices will continue to rise but not to the same extent as in 2006.

Inflation

The UK inflation target is based on the Consumer Price Index (CPI) which has a set target of 2%. The Retail Price Index (RPI) annual rate tends to exceed the CPI as it includes housing costs (such as council tax), which have been rising over the last few years.

The rate of inflation increased gradually over the course of 2006, reaching a 15-year high in December of 4.4%. This has largely been influenced by higher fuel costs. Further contributions came from higher prices for digital equipment and music, utility and housing costs and, in the second half of the year, food.

Interest rates

People's buying behaviour is influenced heavily by interest rates, which determine the cost of mortgage and credit repayments. Interest rates rose gradually throughout the year and in December 2006 the base rate set was 5% (the highest rate recorded for five years) in a move by the Bank of England to dampen down rising inflationary pressures. This is good news for savers, but it is likely to dent consumer confidence in general.

Credit card borrowing

People started to tighten their belts in 2006, becoming more cautious as a result of uncertainties over interest rate rises and a growing awareness of the

1 Eurostat

What does this mean for Bakkavör Group?

The UK economy remains relatively robust with good GDP growth and medium unemployment rates compared with other European countries. However, rising inflation and increasing interest rates left people feeling more cautious towards the end of the year. This was compounded further by another rise in interest rates at the beginning of 2007. However, people still have to eat and at the time of writing, grocery sales remain strong despite these external economic pressures.

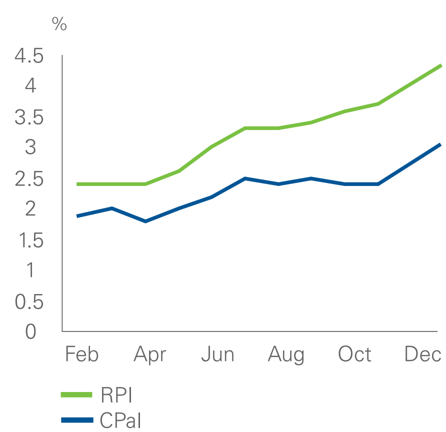
Fresh prepared foods have become an integral part of people's lives in the UK and as long as the economy remains relatively robust and these foods continue to meet people's lifestyle demands, we expect the market to remain strong. Bakkavör Group is the market leader in the UK and it is our job to remain innovative as well as use our economies of scale to ensure the right products are developed at the right price.

implications of buying on credit. Bank of England figures showed that in August, for example, credit card users repaid more money than they borrowed for the first time since May 1994. This trend of debt repayment rather than spending is likely to continue if interest rates remain high or rise again.

Unemployment rate

The rise in the UK population has led to an increase in the absolute number of people in work. However the rate of unemployment also increased gradually in 2006 and reached 5.6% in the third quarter. The manufacturing sector was most affected, impacted by the sharp rise in production costs due to higher energy bills. Latest data indicates that this upward trend is starting to ease.

UK Inflation Rate in 2006



Source: ONS

CONTINENTAL EUROPE FRESH PREPARED FOODS

Well placed to expand our development

In the following section we share with you our knowledge of fresh prepared foods in Continental Europe, the retail trends that are developing and the economic indicators of these geographical markets. We have found that these factors differ by country but there are also some strong commonalities due to the influence of the global mega-trends – convenience, health and pleasure. We start with our view of the Continental European fresh prepared foods markets.

Fresh prepared foods

We estimate the key fresh prepared foods markets in Continental Europe[1] are worth £4 billion (€ 5.9 billion). The relative sizes of the selected fresh prepared foods markets can be seen in the table opposite.

There are a number of factors behind the different levels of market development for fresh prepared foods across Continental Europe. For example, in countries which are more densely populated, where transport networks are more sophisticated and where social and family structures are less traditional, the fresh prepared foods market is often at a more advanced stage than in other countries.

Investment made by retailers in-store and in their logistics infrastructure also dictates the level of success of fresh prepared foods and some of these developments are covered in the Continental Europe retail trends section on page 36.

However, the fresh prepared foods markets are growing even though certain product areas, by country, are more popular than others – often a reflection of local tastes and traditions. The overriding trend is that fresh prepared foods are seen, increasingly, as quality products which help meet the demand for convenience, health and pleasure and there is still plenty of potential for growth. In this section we cover a summary of the main factors influencing the growth of fresh prepared foods in the countries where Bakkavör Group sells its products.

Value growth of selected fresh prepared foods in Western Europe, 2006-2010

	Value growth
Ready meals	22%
Pizza	12%
Pasta	14%
Soups	38%
Sauces	20%
Prepared salads	23%

Source: Leatherhead FRA

1 Continental Europe key markets = France, Germany, Italy, Spain, Belgium, Netherlands

Selected fresh prepared foods by geographical market

€ million	Ready meals	Pizza	Pasta	Soups	Sauces	Leafy salads	Convenience salads	Total
UK	2,591	464	135	115	79	457	276	4,117
France	511	278	286	44	108	450	280	1,957
Germany	40	12	194	25	na	110	747	1,128
Italy	190	36	547	na	83	560	63	1,479
Spain	92	298	53	57	13	160	44	717
Belgium	88	86	10	5	na	112*	na	301
Netherlands	235	24	8	18	na	na	na	285
	1,156	734	1,098	149	204	1,392	1,134	5,867

*Belgium/Netherlands consolidated for leafy salads
Source: UK = TNS, Continental Europe = Leatherhead International, TNS Europanel, Bakkavör estimates

France

The French are renowned for their passion for food, enjoyment of cooking and loyalty to local ingredients and recipes. However, the French are spending less and less time preparing and eating food. For example, in 1978 the average French meal lasted 1 hour and 22 minutes; today it lasts approximately 38 minutes[2].

Cooking meals in the evening or at the weekend from fresh ingredients is still popular. However people are increasingly starting to move towards quick and easy-to-prepare foods – particularly products that provide partial rather than complete meal solutions such as fresh prepared vegetables, fresh sauces and leafy salads. Bakkavör Group provides leafy salads nationally in France and, today, over half of the households in France buy leafy salads in any one year.

Two other fresh prepared food categories have proved popular in France. The ready meals sector continues to grow, with sales rising by over 50%[3] in the last four years, particularly those of ethnic origin or fish/poultry based. In addition, chilled pizza sales are now greater than frozen pizza sales. In recent years, French retailers have invested in their chilled infrastructure and in-store space allowing them to sell fresher products which are increasingly appealing to the French shopper.

Household penetration of fresh prepared foods in France is almost 97%.
Source: Leatherhead

2 www.enjoyfrance.com

3 Leatherhead International

Spain

The Spanish are also passionate about their food. However in a survey carried out by TGI Europa, one fifth of Spanish adults stated that they did not have time to spend on preparing and cooking food, considering themselves the most time-pressed of Europeans.

Although the fresh prepared foods market in Spain is relatively small — certain categories such as chilled pizzas, ready meals, prepared fruits and salads are developing quickly. The Spanish also have a penchant for ready-to-eat desserts, which are gaining in popularity.

Spanish retail has undergone considerable change in recent years owing to the investment in stores by French retailers in particular and, as such, has relatively modern stores and distribution centres. However smaller retailers and food halls in department stores often offer the most developed range of fresh prepared foods as they are located in towns and city centres where there is a strong demand for people to easily pick up fresh convenient meal solutions.

Chilled pizza accounts for almost 50% of the value sales of the Spanish fresh prepared foods market.
Source: Leatherhead International

Bakkavör Group supplies salads to Spanish retailers and European foodservice providers from its facilities in Spain.

Germany

With the largest population in mainland Europe of 83 million and one of the highest numbers of single-person households, the potential for fresh prepared foods in Germany appears highly attractive. In addition, the growing number of working women has increasingly contributed to Germany's high average net household income, leading to a strong growth in convenient food options.

4 in 10 Germans are prepared to pay more for products that make life easier.
Source: Datamonitor

However, given the prevalence of discounter stores (and hence a very price-orientated focus) historically there has been little investment in chilled infrastructure and in chilled space in-store. As such, the high demand for convenience, health and pleasure has been met by frozen foods and eating out. Fresh prepared foods hold a relatively small share (under 9%) of the German retail food market.

Nonetheless, Germans are increasingly becoming more willing to pay a premium for products that make their lives easier and they generally perceive fresh prepared foods to be of a higher quality than frozen foods. In recent years, some retailers have broken out of the mould and have invested considerably in expanding the space in-store dedicated to fresh prepared food and produce and have been rewarded with strong uplifts in sales.

Within the fresh prepared foods sector, convenience salads, such as potato salads, hold a relatively large share of the market and people are trading up to more premium products. The Germans are also very open to influences from other countries and Italian dishes in particular have been very popular. Chinese and Greek food is widely available and Indian, Thai and other Asian cuisines are also rapidly gaining a presence. These influences can be seen in the emerging chilled ready meals market.

The Netherlands

For its size, the Dutch fresh prepared foods market is relatively well-established. This is aided by a high density of single-person households in its cities, a small well-connected landmass which allows efficient distribution of fresh, perishable products, and strategic vision from Dutch retailers to invest in the fresh prepared foods sector and convenience store formats.

The impact of the food mega-trends is highly visible. The Dutch are turning to healthier cooking methods such as grilling, roasting and steaming, and naturally healthy products, such as meal salads and prepared fruits, are becoming increasingly popular. Dutch consumers are also looking for products that are 'rewarding' – offering them indulgence and/or fulfilling an emotive need. As such, the focus on fresh prepared premium and healthy ranges has been high among retailers developing specific sub-brands to address these consumer needs.

Today, almost 55% of Dutch households eat fresh prepared meals in a year. Chilled ready meals is the largest fresh prepared foods category with a range of traditional Dutch recipes (e.g. Stamppotten) and meals based on Asian recipes. Similar to the UK, the Dutch look for convenient options that also offer a level of 'involvement' and consumers can now 'pick and choose' meal components such as a meat or fish, fresh sauce and prepared vegetables to make up their favourite dish.

The Dutch chilled ready meals market grew by 11% in 2005.
Source: Leatherhead International

What do these Continental European fresh prepared food trends mean for Bakkavör Group?

The fresh prepared foods markets in Continental Europe have developed uniquely in each country owing to a combination of many factors, including the food customs in each country, socio-economic influences and the varying degrees of investment in fresh prepared foods markets by national retailers.

However, the trends of convenience, health and pleasure unite the different nationalities and, although these are met in different ways in different countries, fresh prepared foods are seen increasingly as a viable quality solution.

Bakkavör Group approaches each market individually, investing in local expertise and good local facilities. Working closely with retailers and foodservice providers and making use of expert local knowledge of food and retail trends, the Group is well placed to expand its development in Continental Europe.

CONTINENTAL EUROPE RETAIL TRENDS

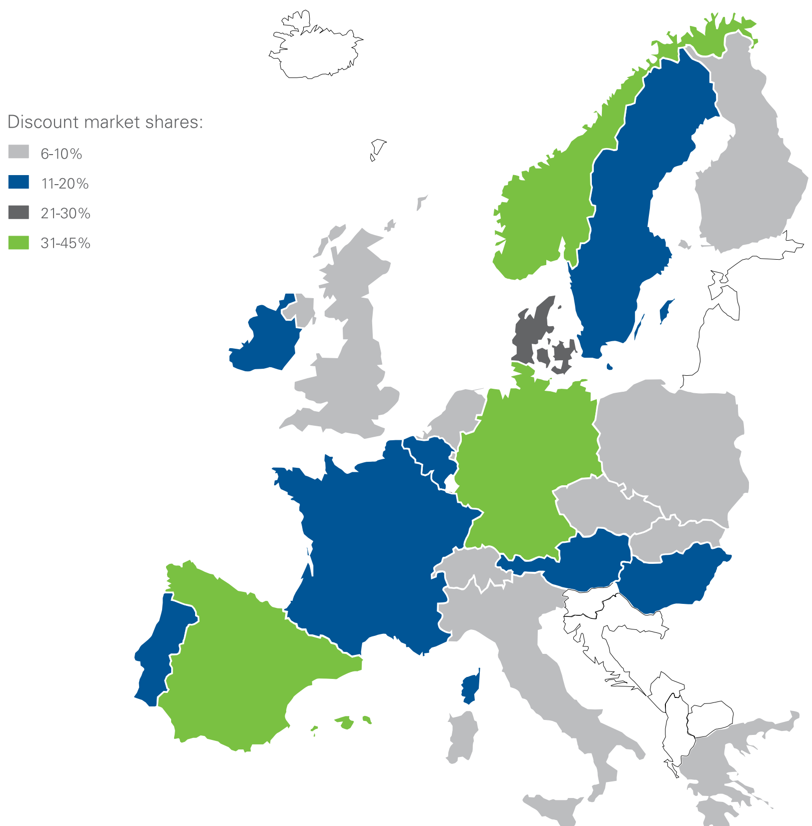
Fresh prepared foods – moving up the retail agenda

Bakkavör Group has manufacturing operations in Belgium, France and Spain and, from these sites, serves customers in France, Germany, the Netherlands and Spain. Each country has very different retail characteristics and developments. However there are some key trends which characterise the market as a whole and provide a useful indication of general retail trends. We outline these trends in the following section.

When it comes to retailing, France, Germany, the Netherlands and Spain account for 43% of the total value of the Continental European grocery market (excluding the UK). Despite their proximity to each other and their relatively relaxed boundaries, each country has unique retail characteristics and has experienced different developments. These vary owing, amongst many other things, to the size of the country, the relative development of an efficient logistics infrastructure, the importance of independent stores and local markets, and, of course, the different preferences and influences of shoppers in each market.

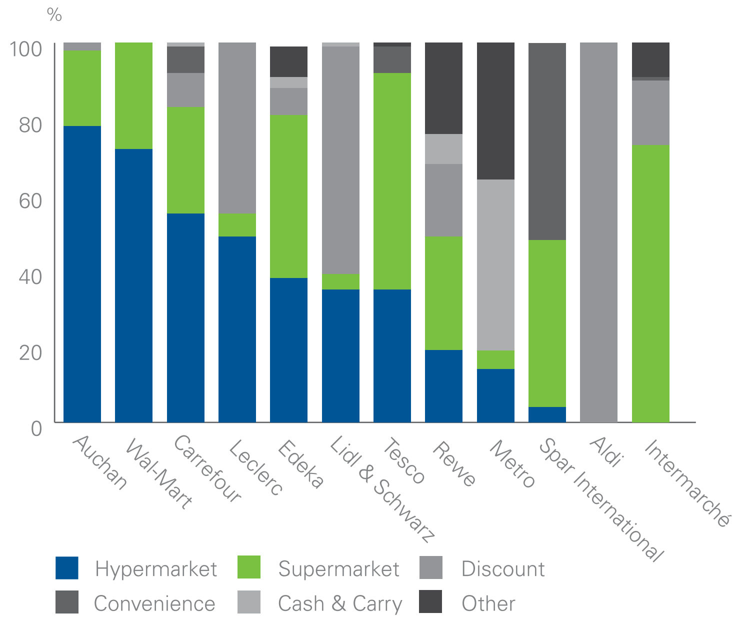
Nonetheless, there are some documented key trends which characterise the Continental European grocery market and, even though these vary in importance by country, they act as a useful indication of general retail trends that influence the developement of fresh prepared foods. The key developments are covered on the following pages.

Discounters have an 18% value share of the European grocery market and this is expected to grow



Source: AC Nielsen, GfK 2003

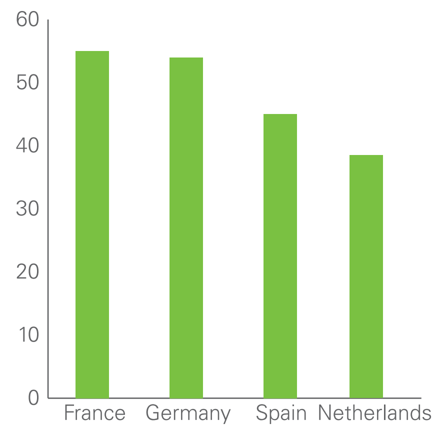
European retailers' portfolio split



Source: IGD research

Consolidation of markets

% market share of top five retailers in each market



Source: IGD research

Discounter success and price pressure

The Germans pioneered discount retailing and since the 1990s the German discounters have established themselves in other European countries at a fast rate. Their unique outlet format, aggressive pricing and advertising strategies have proved popular to shoppers. This format can be split into two categories: 'hard' discounters (offering in the main a limited number of dry/ambient foods often presented in bulk, stacked on pallets) and 'soft' discounters (holding a larger range which includes more fresh, chilled and frozen foods with retailer brands playing a key role in highlighting their price differential).

In 2004, the discounter share of the total European grocery market stood at around 18% and this market share is estimated to have doubled in around 13 years. However, in certain countries, the market share of the discounters accounts for over a third of the total national grocery market.

The influence of the hard discounters in particular cannot be underestimated as their presence has resulted in ongoing price competition which, in turn, has influenced the mainstream grocery retailers to compete on price by developing their own discount store fascia and product ranges.

The discounters will continue to be strong competition as they have ambitious expansion programmes, aided by European planning regimes which favour smaller store formats. To this extent, it is predicted that they will continue to exert price pressure on the retail market in general.

Multiple retail formats continue to gain share

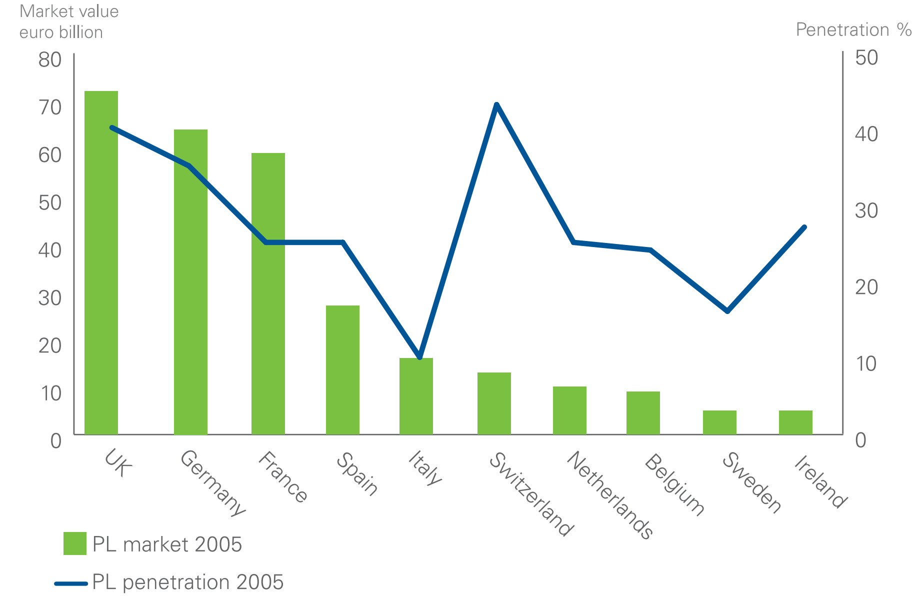
In recent years the Continental European grocery retail market has shifted from being dominated by small food specialists and independent grocers to grocery retailers with larger supermarket and hypermarket store formats, alongside the discounters. In many cases, the grocery retailers have developed a variety of store formats and names to ensure they compete across all levels of the market.

Continental Europe grocery retail markets

	Food retail market € billion
Germany	201.9
France	196.3
Spain	74.2
Netherlands	42.4

Source: IGD European Grocery Retailing, 2005

Top 10 European private label markets 2005



Source: IGD

By 2010, the IGD forecasts that the European retailer brand market will have increased by 44%.

Going forward, competition is likely to intensify with multiple retailers continuing to take share from independent shops. This might be particularly noticeable in France, where at the end of 2006, the European Commission gave French supermarkets the freedom to advertise on French television for the first time since a ban was placed in 1968. This will allow the main multiple grocery players to raise their profiles further in a bid to gain grocery share. In the countries in which Bakkavör Group operates, the top five retailers hold between around 40% and 60% of each national market and these levels of consolidation are set to intensify.

Retailer brands – now brands in their own right

Consolidation in the grocery retail market has resulted in larger sales volumes by retailer and the ability to invest in retailer brands. These brands, once perceived as cheap, lower quality alternatives to manufacturer brands, are now being used by grocery retailers as an important vehicle to differentiate their retail offer. This is an attractive development for retailers as it helps to set them apart from their competition and build shopper loyalty. Again, the level of importance of retailer brands varies hugely by country with just under 60% of the value of German retail accounted by retailer brand sales compared to around 40% in the Netherlands. This level also varies by different retailer groups, but the importance of retailer brands is growing across Continental Europe. By 2010 the IGD expects the value of the European retailer brand market to reach €430.8 billion versus €298.1 billon in 2005 with France, Germany and the UK dominating total share and substantial increases in Central and Eastern Europe.

What does this mean for fresh prepared foods and Bakkavör Group?

In general, the markets for fresh prepared foods across Continental Europe have developed more slowly than in the UK. The reasons behind this include: the difference in population size and density, the retailers' ability to distribute fresh, perishable goods efficiently and safely, as well as the social, economic and cultural differences.

However, with few exceptions, most Continental European grocery retailers are investing in their fresh prepared foods range and also in their infrastructure to handle such products, albeit to varying degrees. For example, as a reaction to changing demand, the hard discounters are starting to broaden their range and now stock fresh items, such as meat, produce and a limited range of prepared foods.

The leading mainstream Continental European grocery retailers have moved from having just a token interest in fresh prepared foods to actively participating in the market with increased shelf space in-store and a greater investment in chilled logistics. As in the UK, retailers in Continental Europe are attracted to the fresh prepared food market as it offers higher margins, faster stock turn-around and helps portray a fresher image.

It is likely that grocery retailing in Continental Europe will continue to be characterised by price pressures and further consolidation. Retailer brands are forecast to grow and we believe retailers will develop their brands further to offer their customers a range of products based on their income and aspirations.

Fresh prepared foods will also continue to grow and will play a fundamental part in allowing the retailers to differentiate their offer from their competition and meet the changing needs of the Continental European shopper.

We intend to maximise our position in these geographical markets by strengthening our existing retailer and foodservice partnerships as well as actively seeking further opportunities in the growing fresh prepared foods markets.

CONTINENTAL EUROPE ECONOMIC TRENDS

Attractive growth markets

Continental European economic trends have historically been marked by relatively high unemployment and slow growth. However there are indications that these trends are changing and, although the Euro zone economy is forecast to slow in 2007, it is expected to withstand a lower US economic performance. Furthermore, consumer demand is forecast to remain robust. In this section we review the economic situation of each of the countries in which we trade.

France

In 2006, GDP in France increased by 2.0%. However, the French economy experienced mixed fortunes during the year. GDP growth in the first half of the year was helped by a strong increase in business investment and consumer spending. However, the third quarter marked an unexpected slowdown in business activity and by the end of the year there was speculation about whether France's level of export activity could be sustained. Questions have also been raised about the level of investment required for economic sustainability in France's industrial sector.

In 2006, one of the top priorities for the French government was tackling the unemployment rate which decreased from 9.6% in 2005 to 9.0% in 2006.

The French CPI rose by 1.9% over the year and was in line with economic forecasts. Underlying core inflation, which excludes products with either regulated or highly volatile prices, rose by 1.4% over the year and retail price increases recorded by the major French retailers was 1.3%.

Germany

The German economy appears to be making a recovery after a prolonged period of high unemployment and increased taxes. German GDP rose by 2.7% in 2006 (its best rate since 2000) and there is optimism that growth will stay robust in 2007 with lower unemployment rates. This will result in more solid consumer spending.

Unemployment in Germany posted its sharpest monthly fall since 1950 in December 2006, pushing the unemployment rate below 10% for the first time in over four years and this was the ninth consecutive annual decline.

German inflation in 2006 rose by 1.8%, owing mainly to higher energy prices. Excluding energy prices, average 2006 inflation would have been 0.9%.

What does this mean for Bakkavör Group?

Bakkavör Group sells to relatively mature and stable economies across Continental Europe. Despite varying economic indicators, employment levels still remain relatively high and we believe people will continue to shop and eat around work and leisure activities. As detailed on pages 32-35, the convenience, health and pleasure trends are expected to strengthen further, continuing to make Continental Europe an attractive growth market for future investment.

European economic comparatives 2006

	GDP growth %	Inflation %	Unemployment %
UK	2.8	2.3	5.5*
France	2.0	1.9	9.0
Germany	2.7	1.8	8.4
Spain	3.9	3.6	8.6
The Netherlands	2.9	1.7	3.9

Sources: Eurostat Economic Overview
*ONS Dec 2006
Inflation rate: Annual average rate of change in Harmoized Indices of Consumer Prices (HICPs)

Spain

In 2006, economic activity remained buoyant with GDP growth of 3.9%. The Spanish government remains confident and has increased its 2007 GDP growth forecast from 3.4% to 3.5% and expects the annual rate of around 4% to be achievable until 2010.

Spanish CPI rose by 3.6% in 2006. The Spanish rate is one of the highest rates in Europe and has consistently been above the Euro zone average.

Household consumption was robust and there was a high level of activity in the construction and services sectors. Unemployment rate fell from 9.2% in 2005 to 8.6% in 2006.

The Netherlands

The Dutch economy is performing well, with GDP growth of 2.9% in 2006.

Economic growth is the result of a number of factors, such as growth in consumer expenditure, employment, exports and investment. Employment growth in 2006 was estimated to be 1.3% and the unemployment rate fell from 4.7% in 2005 to 3.9% in 2006.

The Dutch inflation rate remained low at 1.7%. The rise in energy prices contributed significantly to this inflation rate but was lower, overall, than in 2005. After several years of deflation, food prices increased by 1.4%, soft drink by 4.8% and clothing and shoes by 0.5%.

Continental Europe summary

Although the Euro zone economy is forecast to slow in 2007, it is expected to be strong enough to withstand a lower US economic performance and a projected reduction in exports, according to a European Commission projection in December 2006. Consumer demand is forecast to remain robust and, overall, corporate spending is expecting to improve.

CHINA

Recognising opportunities in high growth markets

The market for fresh prepared foods in China is relatively small but the trends are positive and the market is growing rapidly due to tremendous social and economic changes over the last ten years. In the following section we explore this geographical market and highlight why we are actively seeking opportunities for further development.

The significant social and economic changes that China has experienced in the last decade has brought unprecedented prosperity to its main urban areas. China's manufacturing capability is recognised globally as is its potential as an important consumer market in its own right – and the food market is no exception. With the largest population in the world and a rapidly changing infrastructure, the development opportunities in foodservice and food retail are considerable, attracting overseas investment from manufacturers and retailers alike.

Changing society

China is the most populated country in the world with 1.3 billion people and this figure is expected to increase to 1.6 billion by 2020[1]. As in the UK and Continental Europe, China's population is ageing – over 7% of the total population is over 65 years old and by 2015, this figure is expected to rise to around 12%[2]. Despite this, every year, about 20 million[3] Chinese (a population the size of Australia) turn 18 years old and this age group is becoming an important group of shoppers.

In 2005, women made up 46%[4] of the working population and over the last 10 years there has been a great rise in the number of female professionals and technicians. Similar to trends in Western Europe, women in China are marrying and having children later. China's 'one-child policy' which came into operation in 1979 is still promoted and enforced for those living in urban areas.

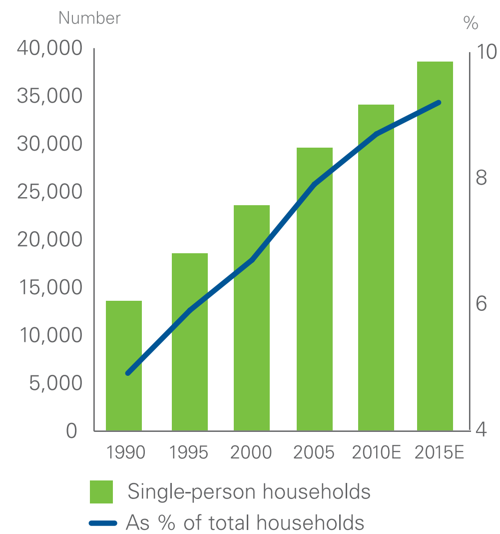
This has had an impact on the average size of Chinese households. Single-person households now account for almost 8% of all households – a small percentage by Western standards, but this is growing.

Economic boom

China is the fastest-growing economy in the world. Following investment in its manufacturing sector in the 1990s, China is now recognised as the world's leading producer of consumer goods, making 60% of all toys, 50% of all cameras and 30% of all televisions[5]. The importance of the manufacturing industry has had a profound influence on the Chinese people. Over the last decade 120 million[6] people abandoned jobs in the traditional agriculture sector in search of the economic opportunity afforded by China's manufacturing boom.

Although main industries are still held in the hands of the State (e.g. utilities), the private sector is expanding and its share rose from 6.1% in 2000 to 16.5% in 2004[7]. However, China's central government remains influential and has encouraged fast economic development, accelerating the pace of growth in urban areas.

China's growing single-person households



E = Euromonitor International Estimates
Source: Euromonitor, Morgan Stanley Research

Urbanisation and rising affluence

Enormous growth is expected in major Chinese towns and cities as China's urban population, now representing approximately 43% of the total population, is projected to rise to 70% by 2050.

In 2004 about 26 million urban Chinese households had a disposable income of at least RMB 25,000 (about $3,000 dollars a year)[8]. By local standards, this level of disposable income categorises this section of the population as

1 Glitnir
2 Glitnir
3 The McKinsey Quarterly 2006 special edition
4 All-China Women's Federation

5 Glitnir
6 Access Asia
7 Glitnir

8 The McKinsey Quarterly 2006 special edition

middle class and the number of these households is expected to triple to 105 million by 2009[9]. Given the link between urbanisation and rising affluence, the majority of consumers who have buying power in excess of USD 10,000 live in cities such as Beijing, Shanghai and Guangzhou. Other research forecasts a rise in the number of upper-middle class people to 520 million people by 2025[10] and it is this projected rise in affluence which is attracting investors from around the world, expecting China not only to remain an important producer of consumer goods but also an important market for consumer goods in its own right.

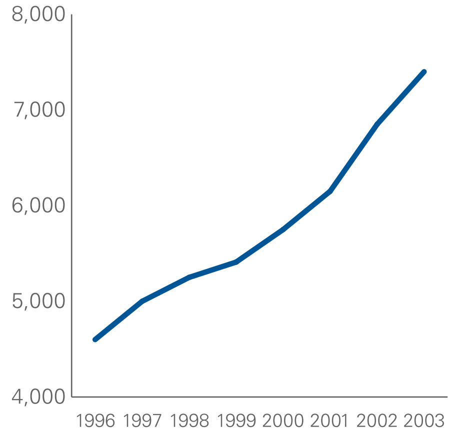
The Chinese food market

Traditional food wholesalers and foodservice operators accounted for 87% of the Chinese food market by value in 2004[11]. Growth has been witnessed in all three areas – food retail and foodservice (reflecting the demand for convenience) and wholesalers who are serving the sudden rise in large national food retail chains.

The potential for growth in food retail, however, is considerable and, according to IGD, China will become the world's second largest food retail market by 2020 behind the US. In 2003 the Chinese food market was 35% of the size of the US market; this figure is expected to rise to 82% by 2020.

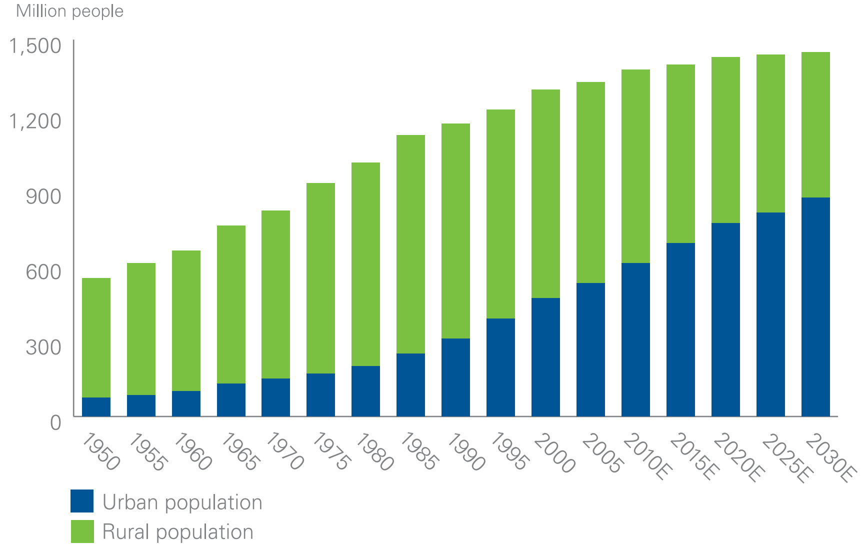
9 The McKinsey Quarterly 2006 special edition
10 The McKinsey Quarterly 2006 special edition
11 Glitnir

Rising disposable income in China



Source: CEIC, Morgan Stanley Research

China's growing urban population



E= United Nations Population Division Estimates Source: UN, Morgan Stanley Research

Top 10 food retail markets

		Food retail market $bn	Cumulative share of total %
1	United States	759.2	22%
2	Japan	450.9	35%
3	China	277.0	43%
4	India	194.3	48%
5	UK	155.7	53%
6	France	152.3	57%
7	Germany	136	61%
8	Italy	133.2	65%
9	Russia	128.8	68%
10	Spain	63.5	70%
	Rest of world	1,044.8	100%
	Global total	3,495.7	-

Source: IGD Research

Retail expansion

China's economic prosperity has facilitated the establishment of modern distribution channels such as chain stores and hypermarkets/supermarkets which have been able to offer competitive prices for bulk purchases, and have helped drive the gradual change from loose to pre-packaged products. In December 2004, the Chinese government lifted restrictions on international retailers as part of its commitment to the World Trade Organisation. This means that international retailers no longer need to operate with a local partner, store numbers are no longer limited and retailers can source from suppliers that have previously only been allowed to export.

Supermarkets are the largest and most widespread retail format in China and in Shanghai, for example, most homes are within walking distance of a supermarket. This sector is dominated almost exclusively by domestic chains. Operators include Lianhua and Hualian (who are by far the largest) as well as Nonggongshang, Suguo and Wumart. China's supermarkets tend to focus more on dried and frozen foods with less than a third of its food space given to fresh foods. The supermarket sector is under increasing pressure from hypermarkets and convenience stores. Overseas competitors, such as Carrefour, Metro, Tesco and Wal-Mart are the strongest hypermarket operators and the main domestic supermarket operators are focusing on building their own hypermarkets. Despite rapid development, the Chinese retail market remains highly fragmented and it is predicted that there will be considerable change to come.

Foodservice chains

Eating out is not new in China - noodle and jiaozi (dumpling) stalls and restaurants are a traditional part of Chinese culture. However, it is now big business for western restaurants, fast food chains, such as Yum! Brands and local entrepreneurs who are benefiting from the increase in the urban population and higher levels of disposable income.

In 2005, foodservice sales increased by 13% to CNY 874 billion. The market is highly fragmented with the top ten foodservice companies only accounting for 5% of the market; however these companies have been very successful, growing more than 200%[12] since 2000.

The continued increase in the number of people dining out is influenced by rising standards of living, a rising number of expatriates living in the cities and visiting tourists. This bodes well for the foodservice market which is expected to be boosted further by the Beijing Olympic Games in 2008 and the World Exposition two years later in Shanghai.

12 Planet Retail

Food trends

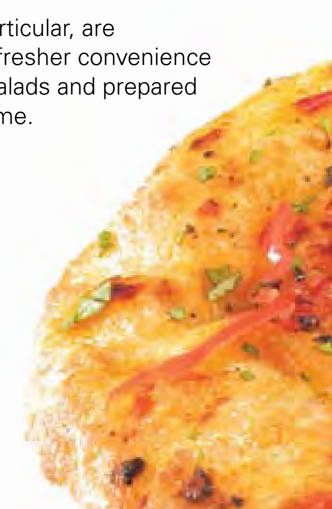
Despite the strong influences of rising prosperity and urbanisation, the main household food expenditure in China is still on fresh foods as they are cheaper than canned and processed food and are also perceived to have greater health and nutritional benefits. This is of particular significance in the rural areas. Fresh vegetables are a particularly important part of the Chinese diet, as many Chinese recipes use vegetables to enhance the flavour of the dish. Nonetheless, the global food trends of convenience, health and pleasure are changing consumption patterns.

Convenience

The pace of life in urban areas is increasing and there is evidence that wealthier people are spending more money on prepacked food and in restaurants rather than preparing food from scratch. Packaged food growth in China remains promising. Sales through retail outlets grew 51% between 2000 and 2005 and are forecast to grow by nearly 7% (CAGR) between 2005 and 2010[13]. As a percentage of total expenditure, the percentage spent on food by people in urban areas is lower than the percentage spent on food in rural areas. However, the absolute food expenditure in urban areas (for people on high incomes) is almost three times greater than the average spend in rural regions.

Urban dwellers, in particular, are beginning to choose fresher convenience foods such as leafy salads and prepared vegetables to save time.

13 Access Asia



What does this mean for Bakkavör Group?

Health

The Chinese people place great importance on the safety of food and healthy food due, in part, to the impact of scares such as the SARS outbreak and Sudan 1. In addition, despite the rising affluence in the cities, malnutrition is prevalent in certain areas of China and this has attracted heightened government focus. Manufacturers have responded by developing organic and functional/fortified food encouraged by new legislation and government focus. In 2005, new food labelling standards were introduced which require information on named ingredients and weight. Prepacked foods have benefited from these changes, as they are perceived to have consistent quality.

Pleasure

Rising affluence has resulted in people eating out more in China particularly in the cities. Given the rapid expansion of western-style foodservice outlets, the Chinese are becoming exposed increasingly to new concepts and tastes and are more open to try foods outside their traditional Chinese diet. The Chinese continue to embrace traditional food values, but they are becoming more eager for a combination of modern products with distinctly Chinese tastes.

The market for fresh prepared foods in China is still relatively very small at RMB 6.07 billion (US$ 766.4 million) but the trends are positive and the fresh prepared foods market is growing rapidly owing to high levels of refrigerator ownership in Chinese households, the increased number of food retail chains with refrigerated display cabinets, the rise in popularity of fresh prepared foods and the ability for foodservice chains to handle chilled foods safely.

Bakkavör Group has recognised the potential opportunities and entered the Chinese market in partnership with Glitnir through the acquisition of a 40% shareholding in Creative Foods. Creative Foods supplies leafy salads and vegetables (an important part of the Chinese diet) to foodservice outlets and, more recently, to the food retail market. We believe Creative Foods is well placed to take advantage of the business opportunities in this dynamic market place and we will continue to look for further development in this geographical region.

Total retail market value for chilled food in China

Year	RMB billion, Current Prices	% annual growth
2000	2.6	14.4
2001	3.0	16.8
2002	3.4	12.4
2003	3.9	16.2
2004	4.7	18.6
2005	5.3	13.0
2006	6.1	15.4

Source: Chilled Foods in China

Household ownership of refrigerators by urban/rural divide, 1999-2005

Ownership per 100 households, year end	1999	2000	2001	2002	2003	2004	2005
Urban refrigerators	79.9	83.3	86.6	90.1	93.5	97.0	100.4
Rural refrigerators	10.9	12.4	13.8	15.3	16.7	18.1	19.5

Source: NBS

BUSINESS REVIEW

KEY EVENTS IN 2006

Bringing the best together

Strengthening our leading position in the UK

During the year, Bakkavör Group continued its targeted consolidation of the UK market with four acquisitions and strengthened its position in key product categories: desserts (Laurens Patisseries Ltd. and Rye Valley Patisseries), speciality breads (New Primebake) and ready meals (Fresh Cook).

During the year, a strong focus remained on the integration of these businesses into the Group in order to take advantage of economies of scale, improved efficiencies and sharing of knowledge and best practice.

Desserts

In April 2006, Bakkavör Group acquired Laurens Patisseries Limited ('Laurens'), a well-established, family-run manufacturer of chilled desserts in the UK, for £130 million. Laurens' leading niche position in the chilled desserts and cake market and its complementary UK customer base further strengthened Bakkavör Group's presence in this market sector. The business operates one site in Newark and employs approximately 1,200 people.

The acquisition was financed by shares in Bakkavör Group (£30 million) and a £150 million loan provided by Barclays PLC. Part of the loan was used to re-finance Hitchen Foods which was originally financed by a bridge loan from Kaupthing Bank. Following the acquisition, Laurens' previous owners became key shareholders, holding 3.7% of Bakkavör Group's shares at the end of the year.

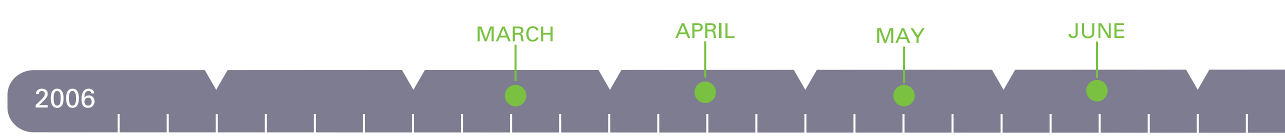
In November 2006, Bakkavör Group further strengthened its position in the desserts market through its acquisition of Rye Valley Patisseries, part of Kerry Foods Limited, a division of Kerry Group PLC. The consideration price, which remained confidential, was financed through the Group's own cash resources. Rye Valley Patisseries (now known as Pure Patisserie) is based in Birmingham and employs 250 people.

Speciality bread

In April 2006, Bakkavör Group acquired New Primebake Limited ('New Primebake'), a leading manufacturer of chilled bread in the UK. The acquisition was financed through the Group's own cash resources and was completed in July, making Bakkavör Group the largest supplier of chilled bread products in the UK. New Primebake operates one site in Nantwich and employs around 340 people.

Ready meals

In November 2006, Bakkavör Group acquired the remaining 50% of the issued share capital of Fresh Cook Ltd., a manufacturer of ready meals, which Bakkavör Group and Rannoch Foods operated as a 50:50 joint venture business since October 2004. Fresh Cook is based in Lincolnshire in the UK and employs 360 people.



Expanding in high growth markets overseas

China

In March 2006, Bakkavör Group acquired a 40% stake in the Chinese salad manufacturer, Creative Foods, in co-operation with Glitnir Bank. To facilitate this transaction, Bakkavör Asia, a subsidiary of Bakkavör Group, and Glitnir Bank established a new company, Bakkavör China. Bakkavör Group holds a 60% stake in Bakkavör China and Glitnir holds 40%. The company's purpose is to focus on investment opportunities in China and this was its first project.

Prioritising our resource from the top down

At Bakkavör Group's Annual General Meeting on March 24 2006, it was announced that Lýdur Gudmundsson, CEO of Bakkavör Group, would move his day-to-day focus to Exista hf. as its Executive Chairman. Exista hf., which is a financial services company, listed on the OMX Nordic Exchange in Iceland, is a major shareholder of Bakkavör Group, holding a 38.3% stake in the company. Ágúst Gudmundsson and Lýdur Gudmundsson are the largest shareholders of Exista with a 47.4% share.

In May 2006, Ágúst Gudmundsson was appointed CEO of Bakkavör Group and Lýdur Gudmundsson became non-executive Chairman of the Group. Ágúst now leads the consolidated Group as CEO and Gareth Voyle, who was CEO of Geest Limited, left the Group at the end of May. Lýdur continues to play an active role in the strategic development of the Group as Chairman.

Realigning our brand to reflect successful integration

A new logo was launched in October 2006, on the 20th anniversary of Bakkavör Group, to reflect the successful integration of the Group's businesses. Today, all businesses in the Group operate under one name, Bakkavör.

UK:
Rye Valley Patisseries
Desserts

UK:
Fresh Cook Ltd
Ready meals

AUGUST | OCTOBER | NOVEMBER | DECEMBER | 2007

OUR STRATEGY

Ambitious growth in our chosen markets

Our strategy

- To focus on the fresh prepared foods and produce markets, fast-growing sectors of the food industry.
- To target growth sectors where a strong market share can be achieved by building strong relationships with major customers, understanding their needs and the needs of the consumer.
- To create an empowered group of independent management teams, whilst maximising synergy across the Group in areas which help develop competitive advantage.
- To ensure a highly valuable, quality service is provided to our customers through the recruitment and retention of excellent people, investment in first-class facilities and strong support for innovation.

Strategic development

In the year 2006, Bakkavör Group continued working towards its long-term strategic goal – to be recognised and respected as the world's largest fresh prepared foods and produce provider. In the UK, Bakkavör Group acquired four businesses during the year which strengthened its position in key product categories – desserts, ready meals and speciality bread. The Group made good operational progress in its exisiting Continental European businesses and continued exploring various opportunities for growth across the Continent. Bakkavör Group also successfully entered the Chinese food market by acquiring a 40% stake in the salad manufacturer, Creative Foods, in co-operation with Glitnir Bank. During the year, the Group continued to explore a number of opportunities in the fast-growing food markets across Asia.

Our long-term growth goals

Bakkavör Group defines its long-term goals for sales growth by its geographical markets:

- In the UK, the Group aims to achieve growth which is above the overall growth of the fresh prepared foods market at any given time. Growth will be mainly organic with bolt-on acquisitions where consolidation opportunities arise.
- In Continental Europe, the Group aims to strengthen its position and grow mainly through acquisitions.
- Following the acquisition of a stake in Creative Foods, Bakkavör Group is now in a strong position to take advantage of further opportunities in China. The Group aims to achieve significant market share in the Chinese food market and gain strong foothold in the various other high-growing markets across Asia.

UK: Growth through further consolidation

44% of the UK fresh prepared food market still in the hands of small players.

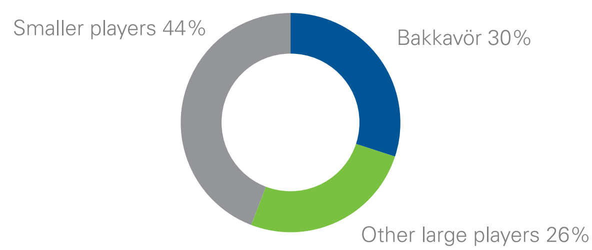
Continental Europe: Growth through acquisitions

The fresh prepared foods market in Western Europe expected to grow by 20% between 2006 and 2010.
Source: Leatherhead International

Asia: Growth through acquisitions

Chilled foods in China forecast to grow by 30% between 2007 and 2011.
Source: Access Asia

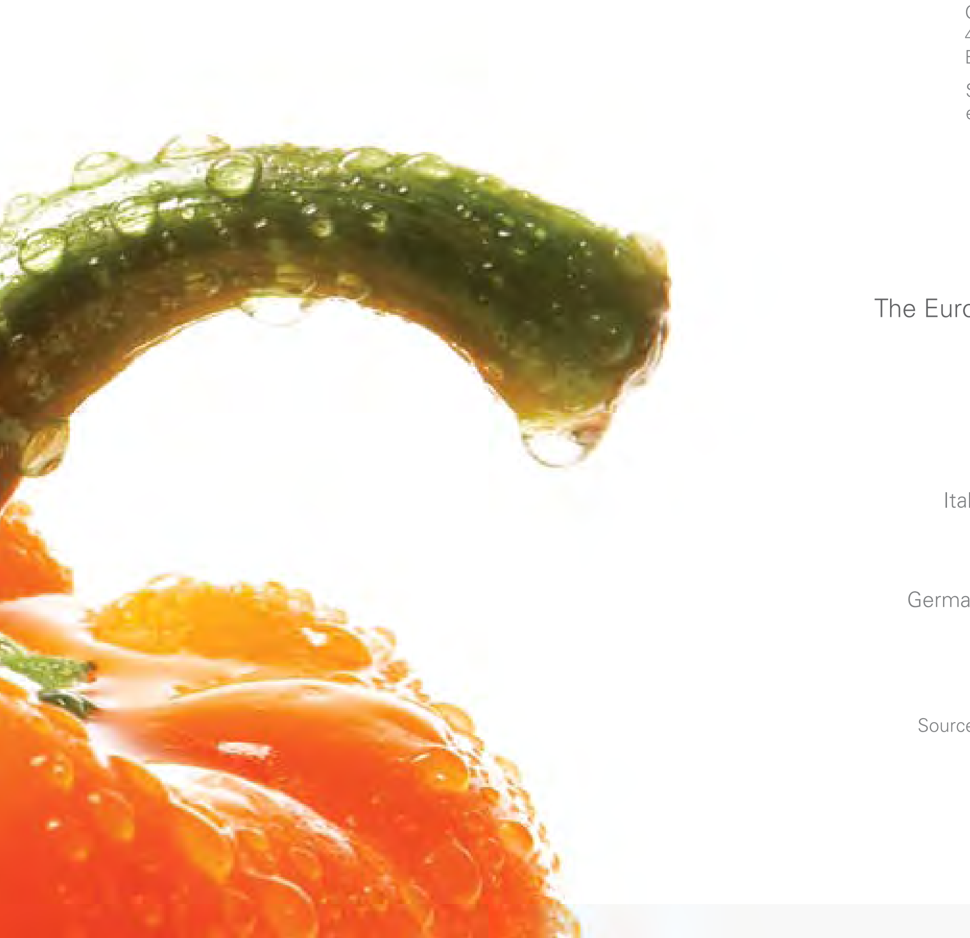
Bakkavör Group UK market share*



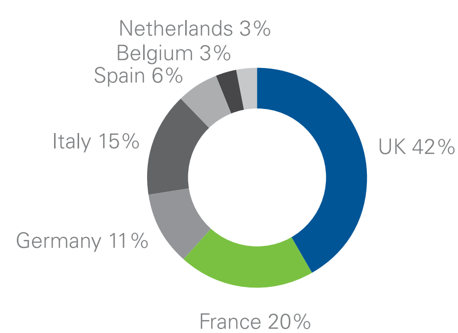
*Bakkavör Group's market share in the market sectors in which the Group operates

Other large players are defined as those with over 4% market share in the market sectors in which Bakkavör Group operates

Source: Bakkavör Group market data estimates year end 2006



The European fresh prepared foods market split by country share



Source: Leatherhead International, TNS, Bakkavör estimates

SALES AND MARKET REVIEW 2006

Performing well in all our markets

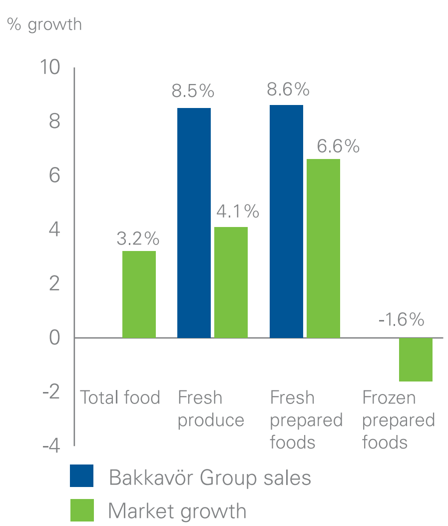
United Kingdom

Overview

Bakkavör Group's growth target for UK fresh prepared foods is to achieve sales growth that is above market growth. In 2006, this objective was achieved with sales growth of 8.6% in a market that grew by 6.6%. In addition, the business also achieved a strong uplift in fresh produce with sales increasing by 8.5%, against a sector growth of 4.1%. During the year, the market growth rate for fresh prepared foods was particularly strong versus other areas of the food market.

Overall, the UK economy grew by 2.7% in 2006, which is the strongest growth in more than a decade. However, inflationary pressures, owing to higher oil prices and rising interest rates, are influencing economic confidence both at a business and an individual level.

Market growth 2006



Source: TNS period ending 31 Dec 2006, Bakkavör Group UK retail sales

Ongoing price competition among the grocery retailers in 2006 and the subsequent proliferation of Internet price comparison websites has inevitably generated increased price awareness, with a trend for people to spend as little as possible on commodity items. However, this does not seem to have affected the rising demand for premium products, with many UK retailers confirming that sales of premium products were strong in the fourth quarter. Many fresh prepared food products are perceived to be premium products, offering people high-quality ingredients and a wide choice of time-saving meal solutions. The fresh prepared foods sector also benefited from the prolonged warm weather during the summer, as well as the World Cup. Sales in fresh salads, pizzas and dips were particularly strong owing to these two factors.

People are becoming increasingly concerned about social, environmental and ethical issues and this trend has influenced our customers' corporate responsibility programmes – particularly for food, where there is demand for increased information (e.g. for ethically-sourced ingredients). Food safety and product integrity are at the top of Bakkavör Group's agenda and management is working closely with its customers to ensure clear communication of responsible practices.

Product groups

Sales in the UK include fresh prepared foods (e.g. ready meals, leafy salads, convenience salads and pizzas) and also fresh produce (e.g. whole head lettuce, tomatoes and cucumbers). Bakkavör Group divides its UK fresh prepared products into two main product groups – hot-eating and cold-eating. The Group's sales ratio of hot-eating versus cold-eating products for the year was 52:48.

Hot-eating product overview

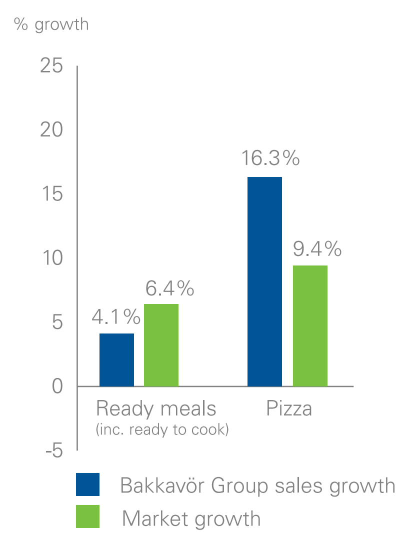
The ready meals market is the largest fresh prepared foods category in which the Group operates and this market (including ready to cook meals) was estimated to be worth almost £1.7 billion[1] at retail sales value for the year, with 6.4% market growth by value. This market growth is influenced mainly by traditional British and premium ready meals as well as ready to cook meals. This has stemmed from a revival of interest in 'contemporary British' dishes brought to life by the popularity of 'gastropubs' coupled with the assured provenance and high quality ingredients associated with premium meals.

Bakkavör Group's overall sales growth was affected negatively by business rationalisation at the beginning of 2006. However the Group's performance improved as the year progressed owing to its strong position in the key growth segments and successful product launches. Going forward into 2007, the Group continues to focus on developing products that meet consumer needs and anticipates that further growth should be achieved.

The chilled prepacked pizza market experienced strong growth with sales by value increasing by 9.4% for the year. Bakkavör Group is market leader in chilled prepacked pizza with core business in the Italian, premium and deep-based segments.

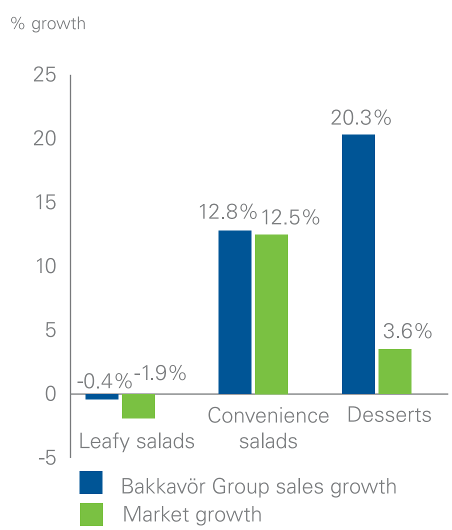
1 TNS

Hot-eating products 2006



Source: TNS period ending 31 Dec 2006, Bakkavor Group UK retail sales

Cold-eating products 2006



Source: TNS period ending 31 Dec 2006, Bakkavor Group UK retail sales

The pizza market is estimated to be worth £317 million[2]. The popularity of both Italian and American-style restaurants as well as the growing trend of people wanting to know the provenance of ingredients have led to an increased demand for authenticity. As a result, traditional Italian pizzas, positioned under the retailers' own ranges or a premium brand, such as PizzaExpress, as well as American-style deep pizzas are experiencing strong sales growth. Bakkavör Group's sales were ahead of the market, 16% growth in 2006, benefiting from these consumer trends and successful growth in the key pizza segments in which the Group operates.

During 2006 the Group also performed well in other markets in the hot-eating sector, including prepared vegetables (13% growth year-on-year), stir fry (13% growth year-on-year) and sauces (12% year-on-year). The Group's fresh pasta sales continued to be restricted as a result of the fire in April 2005, which destroyed two manufacturing facilities (bread and pasta). However the Group's sales growth in speciality bread is improving following the acquisition of New Primebake, with pro-forma sales growth of 3% in 2006.

Cold-eating product overview

Within the leafy salads market there are three key segments based on flavour – sweet, mild and strong – and the Group operates within all three segments. The market was estimated to be worth £312 million[3] at retail sales value for the year with sales declining by 2% despite strong sales during the warm summer months. Bakkavör Group faired better than the market in this sector.

We believe that people's buying behaviour has been influenced by constant negative media attention coupled with poor sales of the sweet varieties due to consumer preference for the stronger varieties. The Group has and will continue to focus on product integrity in this market and has, for example, implemented new leaf washing methods and provided additional information on labels such as when and where the crop was picked and these initiatives are proving to be successful. The Group's organic leafy salads are also performing well, albeit from a small base, with sales up by over 40% year-on-year.

The convenience salads market grew by 12.5% in 2006 with both segments of the market – accompaniment salads and meal salads – experiencing strong growth, up in value terms by 11% and 16%, respectively. Bakkavör Group sales growth was in line with the market, up 12.8% for the year. This market is benefiting from consumer preference for premium and non-traditional salads (such as cous-cous and rice-based salads).

The chilled desserts market was estimated to be worth £415 million[4] and grew by 3.5% by value for the year. Bakkavör Group pro-forma sales grew at almost six times the market growth rate, up 20.3% due to strong sales in the key growth segments of whole cheese cakes and family dairy desserts.

During 2006 the Group also performed well in other markets in the cold-eating

2 TNS

3 TNS

4 TNS

sector, including dips (Group sales up 17% year-on-year) and prepared fruit (Group sales up 37% year-on-year).

UK fresh produce

The fresh produce market grew by 4.1% in 2006. Bakkavör Group sales grew at over twice the rate of the market, with sales up 8.5% for the year. The prolonged warm weather over the summer had an inflationery impact on the market as crop yields of certain fruit and vegetable fell, leading to higher prices. Our growth was strengthened by our ability to supply premium ranges of products to the market, which sold well.

Continental Europe

Pro-forma sales in the Group's Continental European businesses grew by 27%, amounting to £98.0 million for the year. These businesses provide fresh prepared foods and produce to retail and foodservice customers in France, Spain, Netherlands and the UK. On the whole, the fresh prepared food market in Continental Europe is underdeveloped compared to the UK. However, the health, convenience and pleasure mega-trends are strengthening in these geographical markets owing to socio-demographic and economic developments, such as changing family structures, increased disposable income and rising health concerns. As in other markets, these developments offer Bakkavör Group further opportunities for growth.

Bakkavör Asia

Creative Foods' core business is to grow and prepare salads, vegetables and fruits to supply supermarket and foodservice chains in China as well as export markets. The company has performed well since the acquisition, with pro-forma sales growth of 23% year-on-year.

Rapid urbanisation and increasingly busy lifestyles are just two factors driving the growing acceptance of refrigerated foods. In addition, the arrival of western-style fast-food chains and supermarkets, greater awareness of chilled foods and the emergence of a generation both willing and able to try new products are all combining to increase sales of chilled foods in China.

Socio-economic and consumer lifestyle developments in China and the rest of Asia offer Bakkavör Group extensive opportunities and we will continue to actively explore various markets to ensure we maximise our position in this high-growth market.

New product development

Consumer behaviour is changing across the globe, affected by more complex family structures, increase in the number of working women, advances in technology and communication, increased prosperity and disposable income, and a greater awareness of global environmental issues and health concerns. These dramatic lifestyle

Bakkavör Group market sector positions in the UK

Hot-eating markets	
Ready meals	1
Pizza	1
Prepared vegetables	1
Stir fry	1
Speciality bread	1
Ready to cook meals	2
Pasta	2
Soups	2
Sauces	2
Cold-eating markets	
Desserts	1
Leafy salads	1
Convenience salads	1
Dips	1
Dressings	1
Wraps	2
Prepared fruit	2

Source: Bakkavör Group market data estimates 2006

changes have influenced people's eating habits and the development of the food market.

The fresh prepared foods sector has been particularly successful in meeting these evolving needs for health, convenience and pleasure and, as a result, continues to achieve stronger growth than many other food sectors. The UK is at the forefront of this development, but these trends are prevalent around the world and are evolving rapidly across Continental Europe and Asia, for example.

The Group's development teams remain focused on understanding how these three key trends are developing globally and influencing people's food choices. As a result, the Group has already strengthened its position in a number of key product categories by developing and launching over 1,500 new products during 2006 to meet today's modern lifestyle needs.

Convenience

During the year, the Group's development teams have been focused on developing products that reflect people's busy lifestyles and the level of involvement they wish to commit to the preparation and cooking process. As a consequence we have launched a variety of meal solutions that are either 'ready to eat' or 'ready to heat'. Furthermore, a growing interest in food has resulted in increased popularity of 'ready to finish' foods as they allow people to feel more involved in the cooking process without having to take the time to shop for and prepare all the specific ingredients. Bakkavör Group has taken a leading position in this area.

Health

The health trend played a major role in the Group's product development in 2006. One of our key objectives has been to develop products free from hydrogenated fats, artificial additives and preservatives, using only natural ingredients to flavour and preserve our products. We have, for example, launched a number of natural, nutritionally balanced meals that are becoming a particularly popular choice for those consumers looking to maintain a balanced, healthy diet.

Bakkavör Group's new product development reflects the fact that we take our responsibility to develop safe products, produced in an ethical way, seriously. Some of our initiatives in 2006 included a focus on using local ingredients wherever possible, as well as adapting our manufacturing processes, such as, for example, the way in which we wash our leafy salads. Furthermore, we are looking at new environmental initiatives for our food packaging.

Pleasure

To meet the pleasure trend, we have focused on using high quality premium ingredients that exceed people's expectations whether it be for exciting new tastes and flavours or old favourites. We are proud to have won food industry awards for two of our premium products this year based on their high level of quality.

INNOVATION

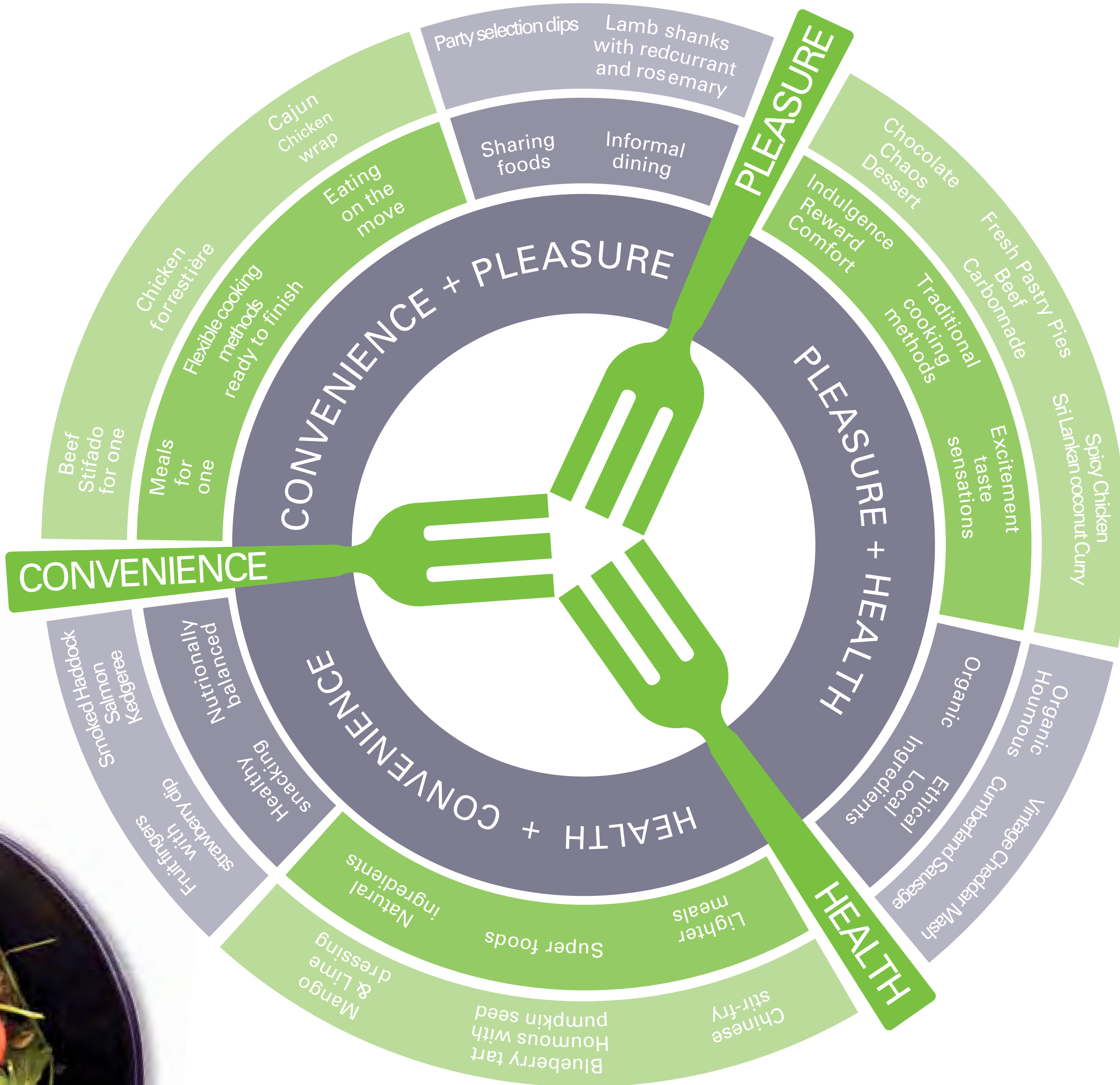
Strengthening our competitive advantage

Innovation is going to become more and more important. We all work hard towards doing the things we do well even better, but our greatest opportunity is to generate totally new ideas which will forge a gap between ourselves and the competition. This will only happen if we give people the space to think differently and see things from a new perspective. I am determined to continue to nurture this culture at Bakkavör Group.

Ágúst Gudmundsson at the Bakkavör Group Leadership Conference, 2006

As ever, we have had a busy twelve months of product development across Bakkavör Group and, as a result, we have strengthened our leadership position in fresh prepared foods. Innovation and the ability to create an innovative environment in which our people are allowed to invest time and money in new ideas is one of our Company values and we believe there is a direct correlation between innovation and being a successful business.

Our knowledge and understanding of key food trends and our ability to translate these into successful products is something that we must never lose sight of. The diagram on this spread illustrates some examples of how we have interpreted the food mega-trends influencing our markets and how we have translated these into new product ideas. For more information on the mega-trends – convenience, health and pleasure – please turn to page 18.



The fresh prepared food sector is more enjoyable to work in than other food areas because it provides fresher foods – foods you want to eat and as good as you would find in a restaurant or at home. As a chef this is very much in line with my food values and beliefs.
Peter Dow, Development Director

There is such a passion in our development teams because everyone loves food and wants to be the best.
Deborah Rainert, Development Director

I get inspiration from anywhere and anyone – from my travels, from cookery books, cookery schools, farmers' markets, restaurants, and my past culinary experiences. My favourite recipes are anything ethnic from Indian to Pan-Asian. I love the vast array of aromatic spices and fresh, vibrant, punchy flavours.
Paul Lees – Development Chef, Lincs Cuisine

OUR CUSTOMERS

Serving our customers to the highest level

Four key areas

Almost 90% of Bakkavör Group's products are sold to large multiple retailers. Our remaining sales are to smaller retailers, foodservice providers, hospitals, care homes and schools. Given the overall importance of retail customers to our business and the increasing consolidation of retailers across the countries we serve (see pages 28 and 37), we have a relatively small number of customers.

Our main focus is to develop products under the retailers' or foodservice providers' own brands and, as such, we are entrusted with a part of their brand equity. For these reasons, a great emphasis has always been placed on maintaining close working relationships with our customers and a high level of service.

Our sales profile varies by product and by country and we need to be flexible in how we approach each market. However, one thing unites the Group – namely its deep-rooted commitment to its customers, based around four key areas: quality, service, innovation and value.

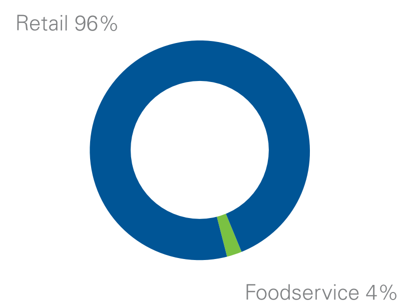
Quality

We are committed to supplying our customers with safe and innovative products that meet consumer demands, to agreed specification, quantities and times. We engage with our customers at all levels of their organisations to understand their needs and requirements and we treat all customer information with integrity.

Service

The planning and scheduling required to deliver our products each day is complicated in our 'just-in-time' environment. We aim to exceed customers' expectations at every point of contact. To achieve that we must work closely with them in terms of information exchange and forecasting to ensure optimal manufacturing, scheduling and the planning of raw materials further along the supply chain (e.g. working on crop programmes).

Customer Split



Source: Bakkavör Group, pro-forma

Our experts in our planning, purchasing and logistics teams help ensure timely delivery day-in day-out. A high service culture is embedded across all parts of Bakkavör Group, especially where people have direct contact with the customer, whether at Director level, the accounts invoicing department, product development, or our sales teams.

Innovation

Innovation is necessary to stimulate market growth. It is our job to be at the forefront of food trends and arm our customers with suitable development ideas which fit the needs of their own customers – in whichever country they may live.

Value

It is our job not just to develop the right products but to do so at a commercial cost which reflects the strategic position of our customers. We pool our resources across the Group to leverage economies of scale neither compromising the needs of our individual customers nor our flexibility and ability to service local customers.

How we work

We need to understand our customers' corporate needs as well as the needs of the people who shop in their stores, eat in their restaurants or hospitals across all the different markets and countries where we operate. At Bakkavör Group, our structure reflects the way in which we do business to achieve these goals.

In 2006 we despatched 33.5 million cases from our Spalding Warehouse and on our peak day just before Christmas we despatched over 1 million cases.

Our decentralised structure plays a very important role in the way we manage our relationships with our customers. We have teams on the ground – often specific to a market sector – who are responsible for running the day-to-day business and looking at the longer-term strategic development for their customers. People from both parties work together across different layers of the organisations and we are in contact with each other daily. It is a partnership approach, creating unique products for each of our customers.

OUR EMPLOYEES

Investing in our people

We recognise that our employees are fundamental to the Group's future development and ambitious growth plans. Committed people are vital to our success, especially as we continue to grow rapidly. Our aim is to become an employer of choice, and the continued positive trend in employee retention confirms that our employees want to be part of our business going forward.

Health and safety

It is our responsibility to create a safe and productive working environment for our employees and people who visit us. The health and safety of all employees is paramount and we provide extensive safety training to all our employees. We are pleased to report a continued downward trend in the number of accidents across our UK sites. We continue to work extremely hard on reducing accidents by focusing on new safety initiatives across our business units and ongoing employee training.

Training and development

Our culture and decentralised business structure attract people who are 'self-starters' but we are aware of the need to train people in order to help them attain their career aspirations. Much work has been completed to ensure that we offer strong functional and professional training and good development and succession planning, which allow our people to be recognised, rewarded and progressed across the Group. We have a fast-track programme (Accelerated Management Programme) open to current employees and new graduates which helps people specialise in one of five areas of strategic importance to the Group: Manufacturing, Product Development, Technical (food safety), Produce (procurement) and Finance.

Our values

Our five core values – customer care, can-do attitude, teamwork, innovation and efficiency – underpin the way we do business. We also recruit, reward and appraise our people against these values to ensure that their spirit is lived within the Group.

Communicating with our employees

At each Bakkavör business unit we elect employees to champion the views of the workforce on all matters of employee relations and health and safety.

The Site Employee Forum (SEF) provides an excellent platform for employee communication and for the discussion of all matters within the business. The SEFs also play a significant role in community initiatives and arrange social functions for their colleagues.

In addition to the individual SEFs we communicate across the Group via our Group Employee Forum (GEF). This is composed of nominated SEF representatives from each of our businesses. The GEF's purpose is to provide a forum for two-way communication and discussion on topics affecting the whole Group. At the annual meeting of the GEF, awards are given to the best SEF and Employee Representative as recognition of their exceptional efforts during that year.

Bernard Sparkes, Development Manager for Melrow Salads, won the grand award for lifetime achievement at this year's Grower of the Year Awards.

Want to know more?

For more detailed information on our values, training, succession planning, Accelerated Management Scheme, SEFs and GEFs, among others, please refer to the 'Our people' section of our corporate website:

http://www.bakkavor.com/our-people/

Diversity

We are proud of our multi-cultural workforce at Bakkavör Group and work pro-actively to help integrate our people into our businesses.

EU-wide labour markets are an important source of labour for our business and we offer a range of facilities across our business units to ensure that we are able to communicate effectively with our employees.

We continue to provide food hygiene and health and safety training in a range of languages including Tamil, Polish and Portuguese. We also offer ESOL (English for Speakers of Other Languages) training to employees, which helps them carry out their roles and also provides them with additional skills for their everyday lives.

We have also initiated 'diversity training' at a number of sites where employees learn to understand and respect cultural differences.

Sharon Read, Finance Administrator at Bakkavör Spalding's Logistics Centre, was named Certificate Student of the Year 2006 by The Chartered Institute of Logistics and Transport (UK).

Across the Group we operate in both union and non-unionised environments. Around 40% of our workforce is unionised across 17 manufacturing sites. We support and work closely with union officials at the factories where our employees have chosen to be represented by a union. In the majority of our manufacturing sites, however, our employees have expressed their wish to deal directly with the Company and are represented through their Site Employee Forum.

OUR SUPPLIERS

Growing strong relationships

We make on average 4,500 different fresh prepared food products and pride ourselves on the quality and freshness of each and every product. Our diverse product portfolio means that having a skilled purchasing team is a fundamental part of our food manufacturing process.

Unique network

At Bakkavör Group, our purchasing team has over 275 years of experience and its members are passionate about sourcing the best materials for the Group which can include anything from overalls to olives. Our Category Purchasing Managers are trained to use a number of sophisticated purchasing tools, including the use of e-auctions and specialist software, which provide data on the price movements of commodity materials.

Our purchasing team operates as part of a unique interdependent 'intelligence network' which works at both an individual site level and at Group level. For example, each team member is responsible for the sourcing of products for the business site where he or she works, but also has Group responsibility for a specific product category (e.g., meat or cheese) and the development of the relationship with specific suppliers. The whole purchasing team, therefore, depends on and works with each other to achieve their requirements at a Group and business site level.

This 'network' system has proved successful – it has brought the Group efficiencies of scale without compromising the need for business independence. It has allowed our purchasing experts to work as a tight, cohesive team, both 'thinking locally' and 'acting globally' and to develop strong relationships with our main suppliers – working with them to understand and implement our core values of quality, service, innovation and value.

Long-term partners

Our suppliers are an important part of our business and our aim is to build long-lasting and mutually trustworthy relationships with them. Over the years, we have demonstrated that we are a responsible business through our commitment to good relationships.

The Group supports the United Nations' Universal Declaration of Human Rights and the core conventions of the International Labour Organisation. As a minimum standard we require our suppliers to comply with all local and national laws, particularly in the areas of working hours and conditions, health and safety, rates of pay, terms of employment and minimum age of employment.

As relationships develop, we work with our suppliers towards achieving standards promoted by the Ethical Trading Initiative (ETI). Many of our retail customers are also ETI members. For more information on ETI policies, please view: www.ethicaltrade.org

Bakkavör Group is also one of the founding members of the Suppliers Ethical Data Exchange (SEDEX), www.sedex.org.uk – a not for profit organisation which aims to be recognised throughout global supply chains as the first choice for the collection, management, analysis and reporting of ethical data.

The use of this web-based tool helps businesses identify labour standards operating within their supply chain and to promote the improvement of labour standards. SEDEX has introduced the latest technology to enable companies to maintain and share data online on labour standards throughout the supply chain and, at Bakkavör Group, we ask our suppliers to become members. Around 200 of Bakkavör suppliers have already joined, with more joining every month.

From October 2006, temporary labour providers in the UK are obliged to obtain a Gangmasters Licence in order to operate legally in the agriculture and food processing and packaging sectors. Bakkavör Group has carefully selected a small group of temporary labour providers with whom we work to ensure they hold the necessary licence. In addition, in order to promote good relationships we offer transparency through the adoption of a trading policy. This ensures all our temporary workers are treated according to the UK legislative framework.

We are proud that a number of our suppliers have been with the Group for more than a quarter of a century! As our business needs have evolved to meet changing consumer needs, these suppliers have also been willing to adapt and evolve to meet our needs and we have worked with them to help them achieve this.

Going forward we are committed to using the best suppliers, to source the best products and to ensure we meet and exceed our core values. We will achieve this through developing our supply relationships using our 'intelligent network', maximising the synergies throughout the Group, whilst supporting the independence of the businesses within it.

FACTS

- Our purchasing team has over 275 years of experience
- We purchase enough flour to give a bag to everyone in New York, Sydney, London and Paris!
- We have organised over 160 successful e-auctions to date
- We purchase 400 million potatoes a year – enough to give every household in the UK 2 bags of potatoes
- If we were to put the carrots we purchase end to end they would be 8,000 miles long – nearly seven times the distance between London and Reykjavík

OUR RESPONSIBILITY

Going the extra mile

We recognise that we have a responsibility to the many parties that are affected, directly and indirectly, by our business activities. In this section we talk about our key areas of responsibility which we have grouped into three areas of focus:

- the place to work
- the partner of choice
- caring for our community

What links all three areas is our belief that sound good business ethics and integrity make good business sense.

The place to work

We recognise that our employees are fundamental to the Group's future development and ambitious growth plans. Committed people are vital to our success, especially as we continue to grow rapidly. Our aim is to become an employer of choice, and the continued positive trend in employee retention confirms that our employees want to be part of our business going forward. We are committed to ensure the welfare of our people, providing a safe and productive environment. For more information, please turn to the 'Our Employees' on page 60 in this chapter.

The partner of choice

We aim to be the partner of choice for our customers, suppliers and shareholders.

Our customers

Strong relationships with our customers are a cornerstone of our business model. We are committed to a high level of customer service, supplying safe and innovative products to agreed specifications and quantities which fulfil our customers' strategic requirements. We engage with our customers at all levels of our businesses and we treat customer information with integrity. For more information on our customers, please refer to the 'Our customer' section on page 58 in this chapter.

Food safety

Through our retail and foodservice customers we supply food every day to, literally, millions of people. We are committed to producing safe, legal, quality food products which are manufactured under stringent conditions of hygiene and control. All our factories operate documented quality management systems (QMS) based on Hazard Analysis Critical Control Point (HACCP) principles and customer Codes of Practice. Each step in the manufacture of our products is assessed for risk and the necessary controls are put in place to maintain food safety standards.

Employee training is paramount to the management of food safety and we are committed to providing this at all levels within our operations.

Food integrity

As the UK's leading supplier of fresh prepared foods, we are aware of our responsibilities to provide foods that taste good, look appealing, are ethically and environmentally sound and help contribute to a balanced diet and lifestyle. Media attention on this topic remains high and corporate responsibility has risen up on our customers' agenda. As a supplier to large supermarket and foodservice brands, we work in conjunction with our major customers to constantly develop and improve our products. Our initiatives in 2006 included:

- ongoing work to reduce the salt content of our products
- provision of better quality foods for 'Meals on Wheels' (food delivered to the elderly at home) and to hospitals through our public sector foodservice business, Anglia Crown
- continued work to incorporate only 'store cupboard'[1] ingredients in our foods
- investing in the development and manufacturing capacity of new ranges with fresher ingredients such as the 'ready to cook' range
- encouragement at site level of community programmes on healthy living (see examples below)

1 Ingredients that are typically used at home

In 2006 we reduced our electricity usage across our businesses by 3% whilst our sales growth was 10%.

Our suppliers

Critical to our ability to deliver products daily to our customers is our ability to secure a supply of high quality ingredients and services, many daily. We work closely with our suppliers and more information on our approach is provided in the 'Our suppliers' section on page 62 in this chapter.

Our shareholders

Our primary goal is to increase shareholder value and we are committed to communicating openly with our shareholders. For more information, please refer to the 'Shareholders' section on page 68 in this chapter.

Caring for our community

Our environment

We recognise that our operations have direct and indirect impact on the environment. We are committed to identifying and complying with all relevant environmental legislation. We aim to manage environmental responsibilities in a manner that minimises the effects of our operations on the quality of life in each of the local communities where we operate.

Through our manufacturing excellence programmes we continuously focus on promoting good practice throughout our operations. Good practice encourages, among other things, efficient waste management and effective use of scarce and expensive resources such as energy and water. We recycle water, where appropriate and safe, at high water-use sites (see our Tilmanstone case study) and are proactively investigating alternative 'green' sources of energy to power our businesses. To do this effectively we have set up an Environmental Conscious Group which is, for example, working with the Carbon Trust on a number of initiatives to reduce our carbon emissions, and help us develop low carbon technologies which we can implement across our businesses.

Reduction in water use at Tilmanstone Salads

Tilmanstone Salads is one of Bakkavör Group's leafy salads businesses and has a relatively high water usage. In 2006, the business teamed up with Environwise, which offers UK businesses independent advice and support on practical ways to minimise waste and reduce environmental impact. As part of the 'Big Splash' Initiative, Environwise helped the team at Tilmanstone to identify areas where water usage could be reduced. An initial site water audit identified a number of major water-saving initiatives, including:

- greater use of recirculated chilled water
- improved maintenance of drainage holes to minimise overflow
- use of self-closing nozzles when cleaning down equipment
- installation of solenoid valves to help switch off water supply

In total, the teams identified the potential to save over 7,000 m^3 of water. The success of the initiatives has helped raise the profile of water-saving and prompted the investigation of further, long-term water-saving investments.

At one of our salad businesses, Wingland Foods, we have launched a range of produce and prepared produce which carries the LEAF (Linking Environment And Farming) Marque standard.

The LEAF Marque is awarded to certified farms who choose to grow food according to Integrated Farm Management (IFM) principles, integrating beneficial natural processes into modern farming practices using advanced technology. This demonstrates that affordable food can be produced in harmony with the environment.

Our neighbourhood

Our businesses are encouraged to support initiatives in the communities in which they operate and the annual Bakkavör Good Neighbours Award is a way of encouraging our businesses to become involved positively. It is also a good way to reward sites for their oustanding effort as they are sometimes too modest to shout about their achievements! The annual prize money is re-invested into local community projects. It is shared across sites judged to have made the greatest positive impact in their local communities and to have integrated neighbourhood issues successfully into their business. In addition, Bakkavör Group has an ongoing commitment to encourage support of the Spring Valley community project in a township near our operating site in South Africa.

The results of this year's winners of the Bakkavör Good Neighbours Award will be announced at the Group Employee Forum this year, and will be posted on our corporate website shortly thereafter. Below are just a few examples of community achievements from around the globe.

In addition to local events, Bakkavör Group supported the London's Science Museum during 2006 and also sponsored Pure Iceland, an exhibition exploring how Iceland is using its natural resources to power itself and protect the environment. In Iceland, where our head office is based, we continued to sponsor the National Museum of Iceland as part of a three-year sponsorship programme. We also continued our sponsorship of the University of Iceland where we have sponsored entrepreneurial studies for the past three years. In addition, we supported various charities, sports clubs and educational projects throughout the year.

Cooking days for kids –Katsouris Fresh Foods

Dan Lucas, Development Chef at Katsouris Fresh Foods, visited Gunnersbury Catholic School for boys, taking along a selection of vegetables to be used to make soups which the children prepared and then sold for charity at their Parents' evening. The session started with a discussion about organic farming and a chance for the boys to identify vegetables and express their preferences.

Between them the children chose to make Carrot, Pumpkin, Coriander and Mediterranean Vegetable, Sweet Potato and Herb soups. Dan demonstrated how to make the soups from scratch and let the children taste them before adding salt and pepper to show them the differences in flavours and the importance of correct seasoning. The soups were then decanted into pots and labelled, ready for sale. In conjunction with Dan's visit, the school held an Art and Design competition for the labelling and logo for the soup.

Bakkavör Group sponsored the Science into Practice Award at this year's Grower of the Year Award.

Stockbridge Technology Centre was the worthy winner for its research into the causes of root malformation disorder in red beet.

Spring Valley Community Centre Project, South Africa

The community centre project started in 2004, prompted by the lack of social and welfare services from the local municipality in an area populated by many of our employees from Spring Valley Foods. The aim of the centre is to act as a local haven where people with social and welfare problems can find basic shelter, food and comfort. In 2005, donations from Spring Valley and other sites across Bakkavör Group were channelled into improving the kitchen facilities and painting and equipping the crèche. The outside children's play area was upgraded, grass was planted and a jungle gym was installed. The fundraising for 2006 continued under the banner of 'The Spring Valley Roof Appeal'. At the end of 2006, the roof was finally completed, heralding the long-awaited end of the building's hard core renovation work. During this renovation period, the kitchen continued to provide daily nutritious meals to the needy and the elderly, with food donated on a daily basis from many of the farms in the area. The aim for 2007 is to develop the services at the centre further, promoting it as a safe refuge for abandoned HIV babies and abused women and children.

Crudi's involvement with GEIQ

Since 2004, one of Bakkavör Group's French businesses, Crudi, has supported Groupes d'Employeurs pour l'Insertion et la Qualification (GEIQ) – an organisation whose aim is to promote the employment of disadvantaged and/or unqualified people who have been unemployed for long periods of time. Crudi works alongside the 10 largest employers in the Perpignan region and is also Treasurer of the group. Crudi has employed 10 people from this scheme to date and plans to recruit another six people in 2007, making it the second most successful member of the group. The new recruits have been integrated successfully into the Crudi workforce and the scheme has been received enthusiastically by the existing employees.

SHAREHOLDERS AND INVESTOR RELATIONS

Focusing on increasing shareholder value

Bakkavör Group's primary goal is to increase shareholder value. The Group has been listed on the OMX Nordic Exchange in Iceland (formerly Iceland Stock Exchange) since 2000 with the ticker BAKK. Bakkavör Group is part of the ICEX-15 Index, which consists of the 15 largest companies on the OMX Nordic Exchange in Iceland by market value, and the VINX Benchmark Index, which consists of the largest and most traded stocks on the OMX Nordic Exchanges and the Exchange in Oslo.

Shareholder report

Our primary goal is to increase shareholder value and we are commited to communicating openly with our shareholders.

The OMX Nordic Exchange in Iceland

In October 2006, the Iceland Stock Exchange was acquired by the OMX Group and its operations became a part of the OMX Group at year end 2006. The integration with the OMX Exchanges in Denmark, Sweden and Finland is currently underway and from April onwards, Icelandic companies will be listed on a common Nordic List and included in OMX indices. The OMX Nordic List Segment indices, which are based on the Nordic List, are divided into Large Cap, Mid Cap and Small Cap. Bakkavör Group will become part of the Large Cap index. Also from April onwards, Icelandic market data will be integrated into the OMX Nordic market data offerings. These changes will transform the securities trading in Iceland as they will increase the visibility of Icelandic companies and provide better services to investors.

Share performance

In 2006, Bakkavör Group's share price rose 23%, from ISK 50.9 per share to ISK 62.5 per share. At the same time, the value of the ICEX-15 increased by 16%. Bakkavör Group's market capitalisation at year end 2006 amounted to ISK 135 billion (£956 million), making Bakkavör Group the 8th largest company on the OMX Nordic Exchange in Iceland by market capitalisation.

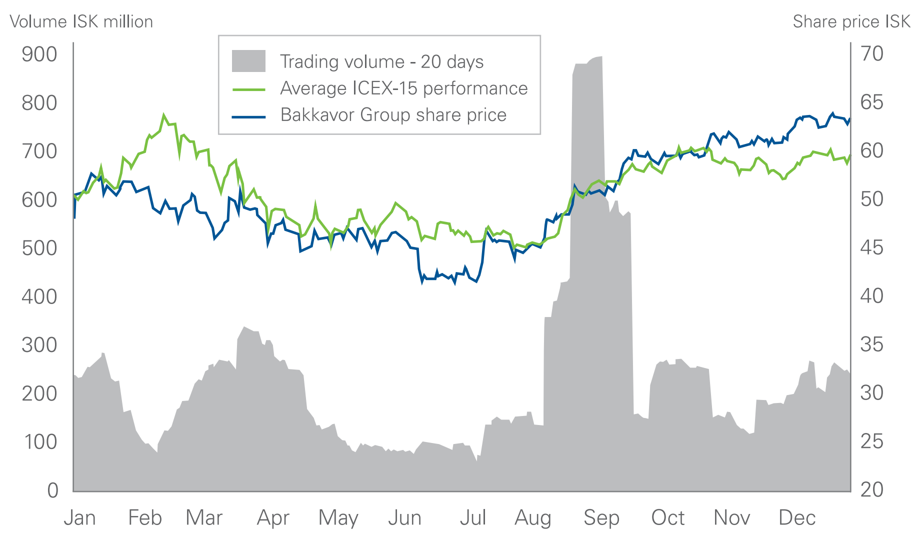
Share capital

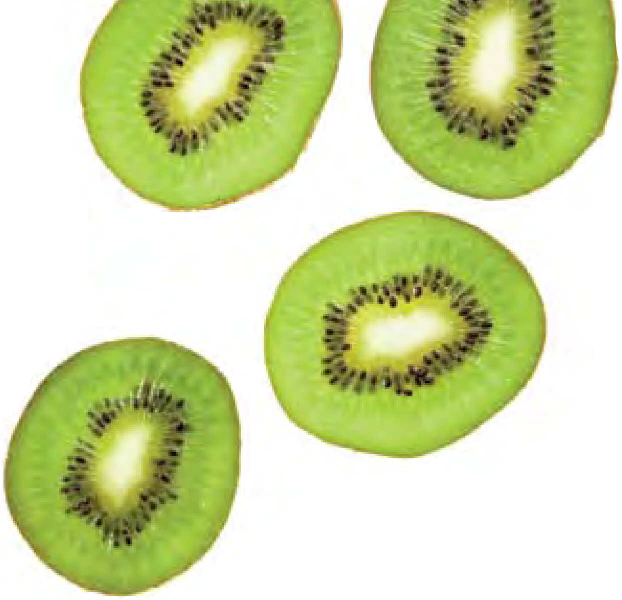
The registered share capital of Bakkavör Group is ISK 2,157,888,219 at nominal value. All issued share capital in the Group is listed on the OMX Nordic Exchange in Iceland. Each share represents one vote.

Liquidity of shares

In 2006, liquidity of Bakkavör Group's shares was high. Shares in the Group were traded 4,805 times for a total market value of ISK 74 billion (£525 million), which corresponds to a turnover of 71.1%. The average spread of the Group's shares during the year was 0.74%.

Bakkavör Group share price performance in 2006





Shareholders

At year end 2006, 3,804 shareholders in Bakkavör Group were recorded on the shareholder register, compared with 3,828 shareholders at year end 2005. Exista B.V. is the largest shareholder of Bakkavör Group with 38.3% of the total share capital at year end 2006. Together, Lýdur Gudmundsson (Chairman of Bakkavör Group) and Ágúst Gudmundsson (Chief Executive Officer of Bakkavör Group) own 47.4% in Exista B.V.

With 13.2%, the founders and former owners of Katsouris Fresh Foods controlled the second largest portion of shares and, following the acquisition of Laurens Patisseries Limited, its previous owners controlled 3.7% of shares at the end of the year. Bakkavör Group employees and other Board members held another 0.6% of the shares in total at year end. Institutional investors held 23.4% of shares and private investors 18.0% of shares at the end of the year.

Dividends and dividend policy

At the Group's AGM on 24 March 2006 it was approved that a dividend of 25% of nominal share value be paid out, which corresponded to ISK 0.25 per share or 11% of net earnings for the year 2005. Given the continued strong cash flow and solid profit generation, the Board of Directors will propose at the Group's AGM on 23 March 2007 that ISK 1,079 million be paid in dividends, which corresponds to ISK 0.5 per share or 50% of Bakkavör Group's issued share capital.

Responsibilities to our shareholders

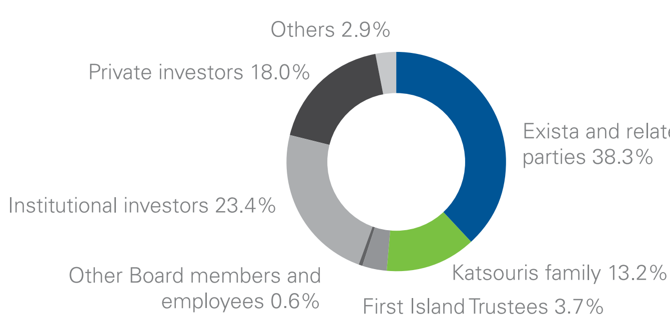
The Board of Directors fully appreciates that our shareholders are the owners of the Group and that its duty is to act in their best interest. The Board seeks to protect shareholder investments by ensuring that effective risk management policies are in place across the Group. These policies are reviewed and approved formally each year by the Board. More information on the Group's risk management approach can be found on page 92.

In addition, procedures are in place to help ensure that Company information is disseminated promptly and without prejudice. More information on shareholder structure and Bakkavör Group's approach to investor relations can be found on pages 70 and 71.

Employee shareholdings

The Board of Directors and employees held 52.1% of shares in Bakkavör Group at year end 2006. No share option programmes are currently in place for employees at Bakkavör Group. Trading of shares by the Board of Directors and employees is strictly monitored by the Group's Compliance Officer who is guided by the Financial Supervisory Authority's *Rules on Treatment of Insider Information and Insider Trading.* Information on shares held by the Board of Directors can be found on page 91. A list of primary insiders can be found on the Group's website, www.bakkavor.com, and the Financial Supervisory Authority's website, www.fme.is.

Groups of shareholders 31 December 2006



Bakkavör Group's approach to investor relations

Bakkavör Group aims to ensure that current and potential investors' perception of the Group's performance and future prospects is in line with management's understanding of the Group's situation at any given time. This approach is fundamental in achieving a fair market price for the Group's shares.

Information policy

The cornerstone of the Group's information policy is to provide current and potential investors with equal access to consistent, transparent and as detailed information as is commercially sensible.

Regulatory announcements are published first on the website of the OMX Nordic Exchange in Iceland, www.icex.is, and then on Bakkavör Group's website, www.bakkavor.com. Financial results are issued quarterly in accordance with the requirements of the OMX Nordic Exchange in Iceland. All price sensitive information is published in a timely manner. Results are webcast and available to view in real time on Bakkavör Group's website.

Major announcements such as acquisitions or disposals are presented at extraordinary investor meetings and also published on the Group's website.

Investor meetings

Bakkavör Group places great emphasis on developing its relations with existing and potential investors. This is achieved by several means, most notably through regular investor meetings, roadshows and participation in capital markets days.

Investors and potential investors are also invited to the Group's Head Offices in Reykjavík or in London where management has the opportunity to present an overview of the Group's operations. These meetings focus primarily on recently announced financial results or corporate activity and the long-term goals of the Group. No new information is disclosed at these meetings which might affect investment decisions.

Distribution of shares

No. of shares	Shareholders	Ratio	Shares	Ratio
1 - 9,999	1,628	42.80%	7,349,710	0.34%
10,000 - 49,999	1,463	38.46%	33,253,728	1.54%
50,000 - 99,999	319	8.39%	21,410,886	0.99%
100,000 - 999,999	314	8.25%	72,434,347	3.36%
1,000,000 - 9,999,999	58	1.52%	174,580,635	8.09%
10,000,000 - 99,999,999	19	0.50%	767,164,722	35.55%
100,000,000 -	3	0.08%	1,081,694,191	50.13%
	3,804	100.00%	2,157,888,219	100.00%

The 20 largest shareholders

as of 31 December 2006 are listed below:

Name	Shares	%
Exista B.V. and related parties	826,209,416	38.3%
Lífeyrissjódur verslunarmanna	136,545,130	6.3%
Gildi - lífeyrissjódur	118,939,645	5.5%
Arion safnreikningur	90,033,192	4.2%
Lífeyrissjódir Bankastraeti 7	85,810,105	4.0%
First Island Trustees Limited	80,269,613	3.7%
Antonios Prodromou Yerolemou	74,534,353	3.5%
Norvest ehf.	60,983,333	2.8%
Panikos Joannou Katsouris	52,336,471	2.4%
Eleni Pishiris	52,336,471	2.4%
Stella Andreou	52,336,470	2.4%
Demos Habeshis	52,336,470	2.4%
Samvinnulífeyrissjódurinn	31,887,179	1.5%
Kaupthing banki hf.	23,230,537	1.1%
Fjárfestingasjódur Ís-15	21,118,671	1.0%
Sameinadi lífeyrissjódurinn	20,475,510	0.9%
Tryggingamidstödin hf.	18,147,059	0.8%
Eignarhaldsfélagid Stofn ehf.	16,942,062	0.8%
Sund ehf	14,616,897	0.7%
Lífeyrissjódurinn Lífidn	11,983,169	0.6%
Total	1,841,071,753	85.3%
Others	316,816,466	14.7%
Total	2,157,888,219	
Total number of shareholders	3,804	

Group website – www.bakkavor.com

In addition to Bakkavör Group's regulatory announcements, the website contains detailed information about the Group, its history, operations and activities. Past and current press releases, presentations and annual reports are archived on the website and available to download. Bakkavör Group's current and historic share price and traded volume are available to view against key indices. In 2006, as part of Bakkavör Group's rebranding, the corporate website was redesigned and is now the focal point for the whole Group.

Annual report

The Group's Annual Report is an important communication tool and the Group strives to provide a balanced picture of all key aspects of the business, including financial and non-financial information. A hard copy of the Annual Report is sent to all shareholders and is also available on request at: investor.relations@bakkavor.com. Downloadable versions of current and past annual reports are available on the Group's website. From 2005 onwards an interactive version of reports is available from the website which facilitates page by page downloads and printing. The current report is also accessible on the website of the OMX Nordic Exchange in Iceland: www.icex.com.

Financial statements

The latest financial statements can be viewed at the Group's Head Office.

Annual General Meeting

Bakkavör Group will hold its Annual General Meeting on Friday 23 March 2007 at the Reykjavík Art Museum - Hafnarhus at 5:15 pm.

Financial calendar 2007

Quarter one results	26 Apr 2007
Quarter two results	26 Jul 2007
Quarter three results	25 Oct 2007
Annual results 2007	31 Jan 2008

(All future dates may be subject to change. Please contact us or refer to the website for latest information).

Dividend dates

Announcement date	23 Mar 2007
Ex dividend date	26 Mar 2007
Record date	26 Mar 2007
Payment of dividend	24 Apr 2007

Email alerts

If you wish to receive alerts by email or mobile phone, please subscribe to our email alert service at: www.bakkavor.com/investor-relations/subscribe/

Contact us

We are happy to answer queries from current and potential shareholders. Similarly, please let us know if you wish to be put on electronic or postal mailing lists. Please contact us by phone, email, fax, mail or via the website.

Contact details

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Investor Relations
Bakkavör Group
Ármúla 3, 108 Reykjavík, Iceland
Tel: +354 550 9715
Fax: +354 550 9701
Email: investor.relations@bakkavor.com

FINANCIAL REVIEW

Five-year summary

	2006	2005	2004	2003	2002
Operating revenues	1,219,189	722,065	149,584	137,867	133,684
Operating expenses	(1,071,109)	(636,061)	(124,803)	(115,444)	(110,876)
Share of profit (loss) in associates	(318)	75	3,176		
EBITDA	147,762	86,079	27,957	22,423	22,808
Depreciation and amortisation	(33,829)	(19,429)	(3,799)	(4,108)	(3,414)
EBIT	113,933	66,650	24,158	18,315	19,394
Net finance costs	(47,360)	(28,269)	(7,092)	(4,043)	(3,957)
Net income from operating activities	66,573	38,381	17,066	14,272	15,437
Income tax	(15,237)	(6,048)	(3,962)	(3,882)	(4,062)
Profit from continuing operations	51,336	32,333	13,104	10,390	11,375
Discontinuing operation, net of tax	16,910			3,123	(434)
Profit for the year	68,246	32,333	13,104	13,513	10,941
Shareholders' earnings	67,617	31,986	13,104	13,513	10,941
Minority interest	629	347			
Working capital from operations	142,764	66,939	18,582	15,825	15,274
Capital expenditure	37,902	16,413	3,529	5,691	15,879
Balance sheet					
Non-current assets	1,028,878	840,400	217,285	129,805	137,081
Current assets	296,929	294,207	55,108	84,965	36,324
Total assets	1,325,807	1,134,607	272,393	214,770	173,405
Equity	241,447	127,352	88,214	72,056	58,611
Subordinated convertible loan	0	12,868	12,868	15,923	15,923
Non-current liabilities	715,677	691,355	151,950	96,068	63,256
Current liabilities	368,683	303,032	19,361	30,723	35,615
Liabilities	1,084,360	1,007,255	184,179	142,714	114,794
Total equity and liabilities	1,325,807	1,134,607	272,393	214,770	173,405
Key ratios					
Quick ratio	0.7	0.9	2.6	2.6	0.7
Current ratio	0.8	1.0	2.8	2.8	1.0
Equity ratio	18.2%	12.4%	37.1%	41.0%	43.0%
EBITDA ratio	12.1%	11.9%	18.7%	16.3%	17.1%
EBITDA ratio, net of agency sales change	12.6%	11.9%	18.7%	16.3%	17.1%
EBIT ratio	9.3%	9.2%	16.1%	13.3%	14.5%
EBIT ratio, net of agency sales change	9.7%	9.2%	16.1%	13.3%	14.5%
Return on equity	37.0%	30.0%	16.4%	20.7%	20.7%
Earnings per share (GBP pence)	3.4	2.0	0.8	0.9	0.7

Amounts in thousands of GBP

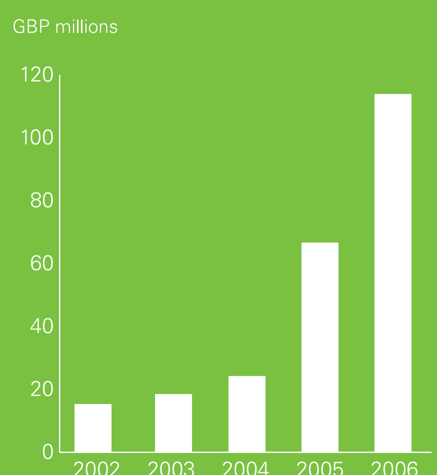
Financial highlights 2006

- Growth in like-for-like sales in underlying business 10%
- Shareholders' earnings £67.6 million – up 111%
- Operating profit (EBIT) £113.9 million – up 71%
- Operations in Continental Europe turned into profitable position
- EBITDA £147.8 million – up 72%
- Pro-forma EBITDA – up 20%
- Cash generated from operations £165.1 million – up 59%
- Free cash generated by operating activities £93.6 million – up 43%
- Equity £241.4 million – up 90%
- Equity ratio 18.2%, up from 12.4% at year-end 2005
- Return on equity 37% compared with 30% in 2005
- Earnings per share 3.4 pence – up 74%

EBITDA/EBITDA ratio*

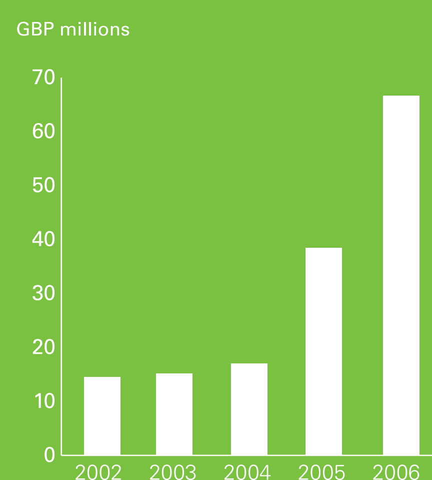
*Continuing business

EBIT*



*Continuing business

Pre-tax profit*



*Continuing business

Executive summary

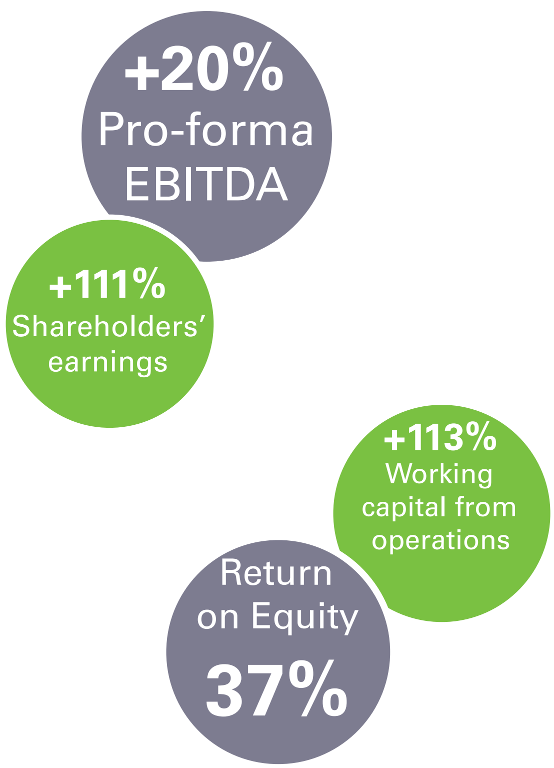
The year 2006 was characterised by a strong performance in the UK and Continental Europe.

Group sales in 2006 were £1.2 billion, which is a 69% increase compared with 2005 sales. Like-for-like sales growth in the underlying business in 2006 was 10%.

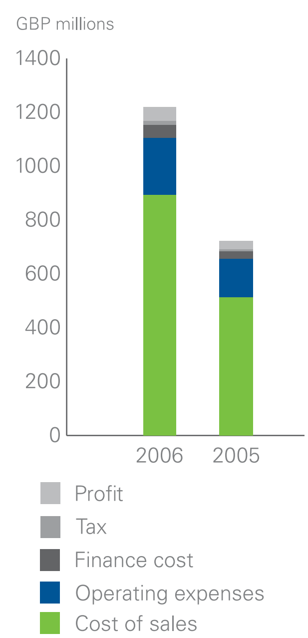
Operating profit amounted to £113.9 million, increasing by 71% and earnings before interest, tax, depreciation and amortisation (EBITDA) increased by 72%, amounting to £147.8 million. Pro-forma EBITDA increased by 20% in 2006. Profit before tax increased by 73%, amounting to £66.6 million.

Shareholders' earnings totalled £67.6 million in 2006, increasing by 111%. Cash generated from operations amounted to £165.1 million, increasing by 59% and free cash generated by operating activities was £93.6 million, up 43%.

Earnings per share were 3.4 pence, a 74% increase, and return on equity was 37% compared with 30% in 2005.

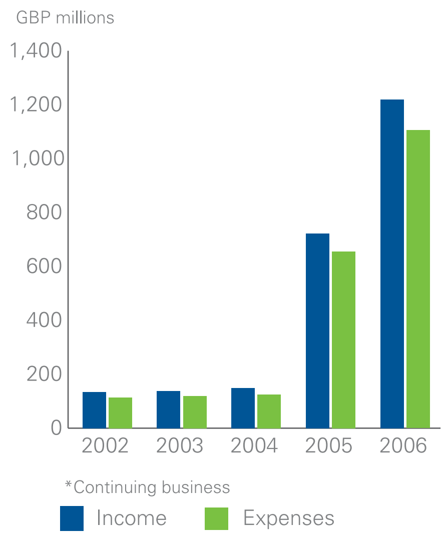


Income statement*

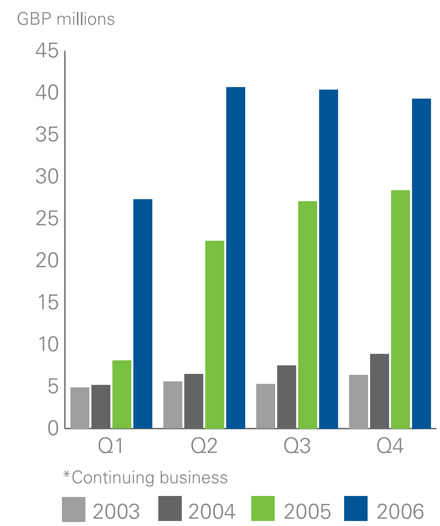


*Continuing operations

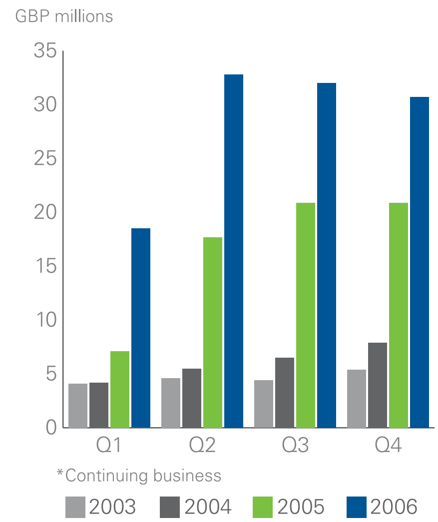
Income and expenses*



EBITDA*



EBIT*



2007 outlook

In 2007, Bakkavör Group will continue to pursue an ambitious growth strategy, focusing on organic and acquisitive growth. The Group will continue to lead the consolidation of the UK food market and improve efficiencies across existing operations. An emphasis will be placed on growth in new markets in 2007, mainly across Continental Europe and Asia.

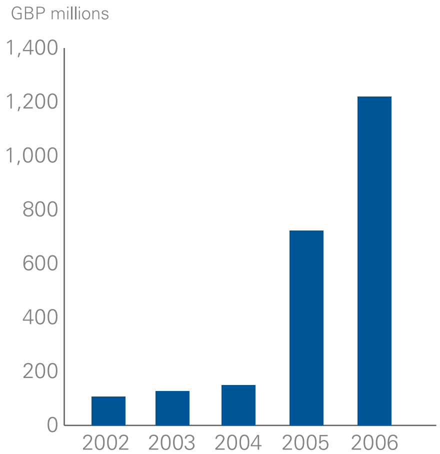
The three global mega-trends – health, convenience and pleasure – continue to influence people's eating behaviour and thereby strengthen the demand for fresh prepared foods. Demand for our products in the UK market remains strong and the fresh prepared foods sector continues to develop rapidly in Continental Europe. Furthermore, China, along with other Asian markets, presents a wealth of future growth opportunities for the Group.

Bakkavör Group is in a strong position to take advantage of these favourable global trends with a balanced product portfolio, excellent businesses in its chosen geographic markets and commitment to making high quality fresh prepared foods, meeting consumer demand wherever it operates.

Accounting policies

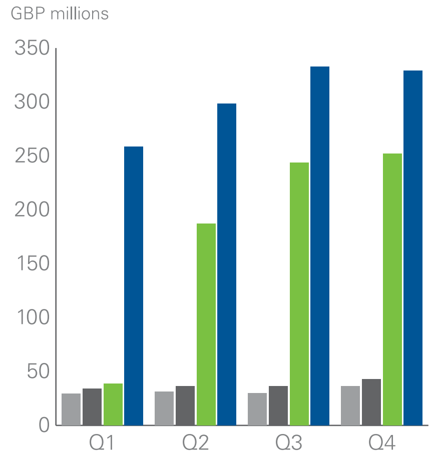
The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. Laurens Patisseries Limited was included in the Group's financial statements as of 1 May 2006, New Primebake Limited as of 1 July 2006, Rye Valley Patisseries (now Pure Patisserie) as of 10 November 2006 and Fresh Cook Ltd. as of 22 November 2006.

Net sales*



*Continuing business

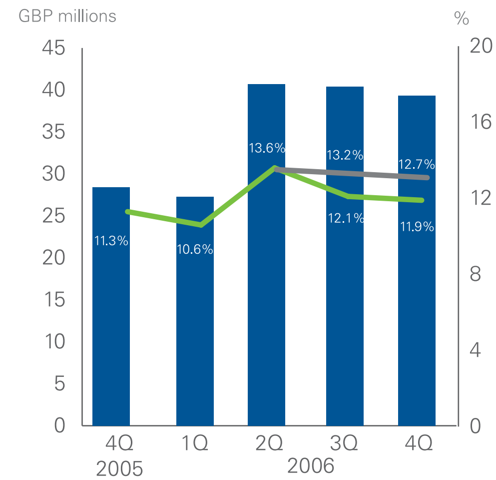
Net sales by quarter*



*Continuing business

2003 2004 2005 2006

EBITDA/EBITDA ratio



Robust sales growth

Group sales in 2006 amounted to £1.2 billion, which is a 69% increase compared with 2005 sales. Like-for-like sales growth in the underlying business in 2006 was 10%. UK sales represented 92% of Bakkavör Group's turnover, with sales amounting to £1.1 billion. Pro-forma sales in Continental Europe grew by 27%, amounting to £98 million in 2006.

Solid performance

Operating profit (EBIT) increased by 71%, from £66.7 million in 2005 to £113.9 million in 2006. Performance in Continental Europe improved during the year with operating profit amounting to £1.4 million compared with an operating loss of £2.6 million in 2005.

EBITDA increased by 72% in 2006, amounting to £147.8 million compared with £86.1 million in 2005. EBITDA ratio in 2006 was 12.1% compared with 11.9% in 2005. Pro-forma EBITDA increased by 20% in 2006.

Changes were made to a supply strategy agreement with one of the Group's customers in July 2006. As a result, part of the Group's produce sales from Q3 onwards is now reported on a full sales basis instead of an agency sales basis as before. Although the Group's sales growth and margins are affected, there is no impact on operating results. Had this change not occurred, sales for the full year 2006 would have amounted to £1,172.2 million instead of the reported £1,219.2 million and the EBITDA ratio would have been 12.6% instead of 12.1% in 2006.

Share of associates

The Group's share of loss in associates in 2006 was £0.3 million compared to £0.1 million share of profit in 2005.

Interest

Net finance costs amounted to £47.4 million in 2006 compared with £28.3 million in 2005, reflecting the full-year effect of increased leverage undertaken since the acquisition of Geest in May 2005. Conversely, net finance costs in the last quarter of 2006 increased by only 3% compared with 2005, despite debt finance of the Laurens Patisseries Limited acquisition, which demonstrates the Group's strong cash generation. Interest cover remains, as in previous years, well within our banking covenants.

Income tax

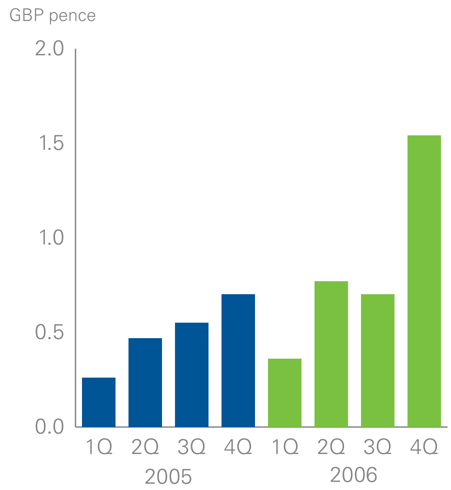
Income tax totalled £19.6 million compared with £6.0 million in 2005. The effective tax rate was 22.3% for the year, compared with 15.8% in 2005. The tax rate on underlying profit before tax was 26.3% compared with 24% in 2005. The tax rate in 2006 was impacted, among other things, by the internal financing structure of the Company, utilisation of previously unrecognised tax losses and other tax incentives recognised.

Trading between the Group's subsidiaries is monitored carefully to ensure that all transactions are based on arm's length principles. Careful management of income tax will continue to be an important contribution to the overall result of the Group.

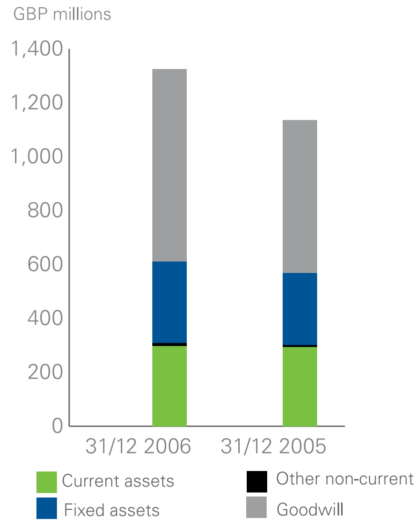
Profit from discontinued operations

Profit from discontinued operations, net of tax, amounted to £16.9 million (pre-tax profit amounted to £21.3 million), and comprises insurance reimbursement in excess of book value of the assets destroyed and impairment of other related assets following the fire at the Barton site on 3 April 2005. A decision

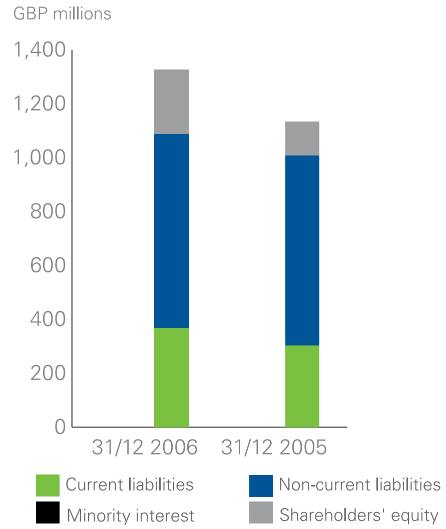
Earnings per share by quarter



Assets



Equity and liabilities



was made not to replace the assets and discontinue operations in this facility.

Minority interests

Profit attributable to minority interests in 2006 was £0.6 million, compared with £0.3 million in 2005.

Dividends

The Group continues to pursue an ambitious expansion strategy and, in accordance with this, was successful in making significant investments last year. Despite funds required to support these plans, the strength of the Group's cash flow and profit generation is such, that the Board of Directors will recommend at the Group's Annual General Meeting on 23 March 2007 that ISK 1,079 million be paid in dividends to shareholders. This corresponds to ISK 0.5 per share or 50%of Bakkavör Group's issued share capital.

Earnings per share

Basic earnings per share rose by 74% to 3.4 pence from 2.0 pence in 2005. This reflects clearly the Group's strong performance despite the new share capital issued in relation to the acquisition of Laurens Patisseries Limited and the conversion of bonds into shares in 2006.

Prudent capital structure

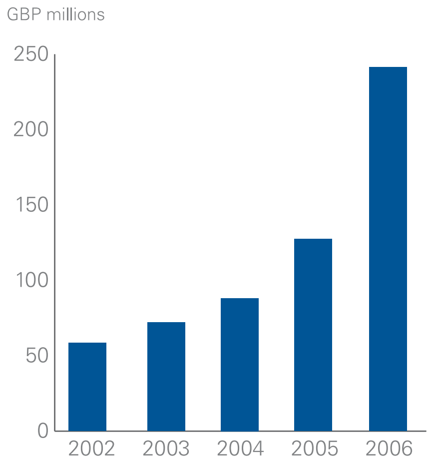
Equity increased from £127.4 million at year end 2005 to £241.4 million at the end of 2006, clearly reflecting the Group's strong performance as well as new share capital issued during the year. Part of the acquisition price of Laurens Patisseries Limited was satisfied by the issue of new shares. In addition, share capital was further increased to fulfil Bakkavör Group's obligations pursuant to convertible bonds owned by Kaupthing Bank. All obligations regarding convertible bonds have now been fulfilled. Following these share capital increases, the total number of shares in Bakkavör Group is 2,157,888,219.

The equity ratio at year end was 18.2%, increasing from 12.4% at year end 2005. Dividends of ISK 404 million, corresponding to ISK 0.25 per share, were paid in April 2006. Return on equity for the year 2006 was 37% compared with 30% in 2005.

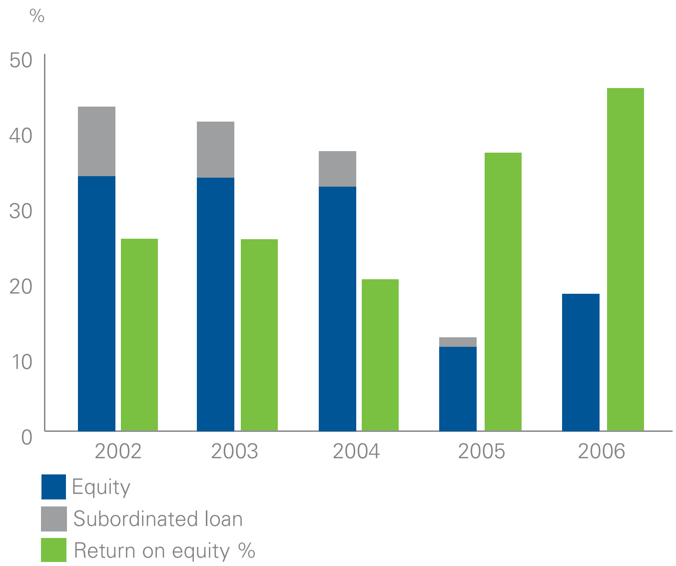
During 2006 the Group's market capitalisation increased by approximately £200 million to £956 million, due to new share capital issued during the year and a 23% increase in the share price during the year to ISK 62.5 per share at 29 December 2006. Net borrowings increased during the year from £695.0 million at the end of 2005 to £715.5 million at the end of 2006, representing 75% of total market capitalisation.

The Group intends to manage its capital structure pro-actively to maximise shareholder value whilst maintaining flexibility to take advantage of arising opportunities to grow its business. One element of the Group's strategy is to make targeted acquisitions. It is intended that these will, where possible, be funded from cash flow and increased borrowing.

Equity



Equity ratio / return on equity



Borrowings

At the end of 2006, the total of non-current and current borrowings increased by just 3% to £715.5 million from £695.0 million at year end 2005. At year end 2006, 95% of the gross debt was due after one year and 84% of debt due within one year at year end 2006 was supported by undrawn committed facilities maturing after more than one year.

Barclays provided a £155 million loan to Bakkavör Group to finance part of the acquisition price of Laurens Patisseries Limited, of which £43 million was used to refinance Hitchen Foods, acquired by Bakkavör Group in October 2005.

Cash and cash equivalents decreased 52% to £39.7 million at year end 2006 from £82.3 million at the end of 2005. The Group's borrowings, net of cash, amounted to £675.8 million at year end 2006, compared to £612.7 million at year end 2005. The net debt cover remains comfortably above our target level and well within our banking covenants.

Estimated future interest rate payments on debt are based on the applicable floating rates of interest at the end of the year for all floating rate debt or interest rate swap liabilities. Details of borrowings, currency and interest rate profile of the Group's borrowings are disclosed in Notes 20 and 21 to the Consolidated Financial Statements on pages 119-120.

The Company has guaranteed borrowings and other liabilities of certain subsidiary undertakings. The amounts outstanding at 31 December 2006 were £25.3 million.

Committed payments at year end 2006 amounted to £113.1 million. These payments have not been provided for in the accounts and relate to lease payments under non-cancellable operating leases, contracted capital expenditure and purchase commitments.

Assets

The Group's total assets at 31 December 2006 amounted to £1,325.8 million compared with £1,134.6 million at 31 December 2005. This increase is mainly due to the acquisitions during the year.

Non-current assets totalled £1,028.9 million compared with £840.4 million at year end 2005. Goodwill and other intangible assets amounted to £713.9 million compared with £565.7 million at year end 2005, an increase of £148.2 million that relates mainly to the acquisition of Laurens Patisseries Limited. The assessment of fair value of Geest was completed in April 2006 and that of Hitchen Foods in September 2006. No material changes were necessary to the previously reported fair value of net assets. The assessment of fair value of the net assets of Laurens Patisseries Limited and New Primebake Limited (acquired in April 2006 and July 2006, respectively) and Rye Valley Patisseries (now Pure Patisserie) and Fresh Cook Limited (both acquired in November 2006) is provisional and will be completed within 12 months of the acquisition date. Under IFRS the value of goodwill will be tested annually for impairment. At year end 2006 an impairment test was performed on the goodwill of Bakkavör Group and, as a result of the test, goodwill impairment was not required.

Current assets totalled £296.9 million at 31 December 2006 compared with £294.2 million at year end 2005. Current liabilities increased from £303.0 million at year end 2005 to £368.7 million in 2006. At year end 2006, the current ratio was 0.8 and the quick ratio was 0.7, compared with 1.0 and 0.9 at year end 2005. These ratios are affected by a £109.9 million payment of long-term debt during the year.

Net cash provided by operating activities (GBP '000)	2006	2005
Profit for the year	68,246	32,333
Items not affecting cash	74,518	34,606
Working capital provided by operating activities	142,764	66,939
Changes in current assets and liabilities	(11,264)	15,120
Cash flow from operating activities	131,500	82,059
Property, plant and equipment	(37,902)	(16,413)
Free cash generated by operating activities	93,598	65,646

Strong cash flow generation

As in previous years, Bakkavör Group's cash flow generation remained strong during the year and was £165.1 million in 2006 compared with £103.6 million in 2005, an increase of 59%. Cash flow after deducting payments of interest and tax amounted to £131.5 million compared with £82.1 million in 2005, an increase of 60%.

The Group defines free cash flow as the amount of cash generated by the business, after meeting all its obligations for interest, tax and after investments in tangible assets. The Group generated free cash flow of £93.6 million in 2006, compared with £65.6 million in 2005, which is a 43% increase.

The increase arose from operating profit and profit from discontinued operations, partially offset by increases in net cash outflows from the servicing of finance, higher tax payments and increased capital expenditure.

The Group remains strongly cash generative, reflecting healthy margin and the cash generative nature of the Group's business. At year end the Group held cash and cash equivalents amounting to £39.7 million and had unused committed credit lines amounting to £27.9 million.

Cash outflows on acquisitions

During the year, Bakkavör Group continued its targeted consolidation in the UK market with four acquisitions. The cash outflow in 2006 on acquisitions was £127.1 million. In May 2006 Bakkavör Group acquired a leading manufacturer of chilled desserts in the UK, Laurens Patisseries Limited Ltd, for a total consideration of £130.8 million. In July 2006 Bakkavör Group acquired a leading manufacturer of chilled bread products in the UK, New Primebake Limited, for a total consideration of £20.2 million. In November 2006 Bakkavör Group further strengthened its position in the UK chilled desserts market through the acquisition of Rye Valley Patisseries (now Pure Patisserie) and acquired the remaining 50% of the issued share capital of Fresh Cook Limited, a manufacturer of 'ready to cook' meals. Fresh Cook Limited was operated as a 50:50 joint venture since October 2004 by Bakkavör Group and Rannoch Foods.

There were no disposals during 2006.

For further information on the impact of acquisitions refer also to the cash flow section of the Consolidated Financial Statements on page 101 and to Note 24 on page 121.

Capital expenditure and investments

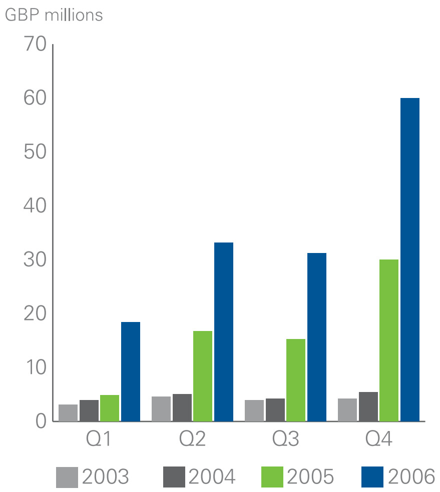
Capital expenditure for the year was £37.9 million, an increase of 131% from the level of expenditure in 2005, with key areas of expenditure being additional production facilities and capacity improvements at four of our sites and general improvement and maintenance at other production facilities. Capital expenditure during the year was kept at the level of depreciation. All these projects were funded from internal resources.

At 31 December 2006 the Group had capital commitments of £7.8 million not provided for in the accounts. It is anticipated that these commitments will be financed from the Group's operational free cash flow.

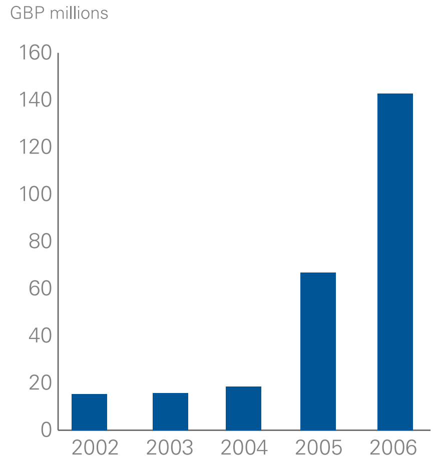
Investments total £2.4 million which comprise the Group's share in the 40% stake in Creative Foods Group, acquired in co-operation with Glitnir Bank in April 2006.

All costs related to new product development are expensed in the Profit and Loss Account, as in previous years.

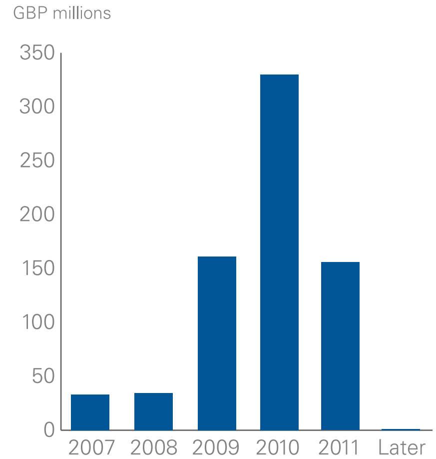
Working capital from operations by quarters



Working capital from operations



Maturities of debt



Financial risk

Bakkavör Group is exposed to a variety of risks. Set out below is a description of factors that may affect our business, results and share price from time to time. The responsibility of the Treasury department is to identify and manage these risks in accordance with guidelines set out by the Board. The Treasury is run as a non-profit centre, reports regularly to the Board and is subject to internal audits. The Group's Hedging Committee sets the risk policy and approves all major derivative transactions after a careful review, which is supported by statistical analysis. No speculative transactions are permitted.

Interest rates

The fair value of the Group's financing, investments and related hedging instruments is affected by movements in interest rates. This risk is both macro (market fluctuations and liquidity) and micro (Group's margin).

Backed by strong operational cash flow, the Group is a net borrower in order to maintain liquidity and optimise its weighted average cost of capital (WACC) and fund operations.

In accordance with the Hedging Committee's policy, the Group operates a risk neutral policy which maintains the ratio between floating and fixed interest rates at 40:60. Therefore, adverse movements in rates can have a negative impact on the Group's results. In order to reduce these fluctuations, the Group uses derivative instruments such as swaptions, swaps and collars. In addition, the Group also varies the duration of its interest periods and spreads the fixing dates.

In 2003 and 2005 the Group issued index-linked fixed rate bullet bonds in Icelandic króna with a 5-year and a 5½-year maturity respectively. The interest rate on those bonds was swapped to floating rate GBP LIBOR at the time of issue, thus eliminating the exposure to the Icelandic consumer price index.

External capital market conditions, beyond the Group's control, can affect the margin offered to the Group for debt either for refinancing or for financing value added investments. To reduce the level of risk the Group varies the maturity of its loans.

The level of hedging may vary from time to time within the Hedging Committee's policy. At the end of 2006 around 44% of interest-bearing debt was hedged against interest risk to some degree.

Among the actions taken to monitor the interest rate risk are stress tests to establish sensitivity to possible movements in rates and how they might affect the Group's results. These tests are presented to the Board.

Liquidity

Seasonal working capital fluctuations are mitigated by the Group's diverse portfolio of products. Nonetheless it must ensure necessary short-term funding, as well as adequate medium- and long-term funding.

Short-term available funding is set up in the most cost-efficient way to fund forecasted peaks and to provide reasonable operating headroom. Surplus funds are either in cash or marketable securities. To monitor these objectives, forecasts are made using maturities of a week, month and up to a year. These forecasts, along with current cash position and variations, are sent each week to the Group's management. At the end of 2006 the Group had £39.7 million in available funds and £27.9 million undrawn in committed facilities and overdraft.

In the medium and long-term, the Group's objective is to have in any one year the

ability to repay or refinance maturing debt. To enforce this objective the Group varies the maturity of its loans. At the end of 2006 more than 95% of the Group's interest-bearing debt had a maturity of over one year.

Currency

The Group's functional currency is pounds sterling. The value of other currencies in regard to trading activities and the translation of its financial statements is therefore subject to currency fluctuations.

Exposure to trading activities arises from the sale and purchases in currencies other then the functional currency. These currencies are mainly the euro, Icelandic króna, US dollar and South African rand. Derivatives may be used to hedge net currency exposure.

The Group has three major operating sites in Continental Europe. Translation exposure to these euro investments is hedged in accordance with hedge accounting for hedges of a net investment.

The bonds issued in 2003 and 2005 were denominated in Icelandic króna. These bonds were swapped into pounds sterling at the time of issue, thus eliminating currency risk.

Commodity

The Group has some exposure to price changes in commodity markets. In order to reduce the risk, the Group enters into forward contracts on vegetable oil, utilities and imported raw materials.

Retirement benefits

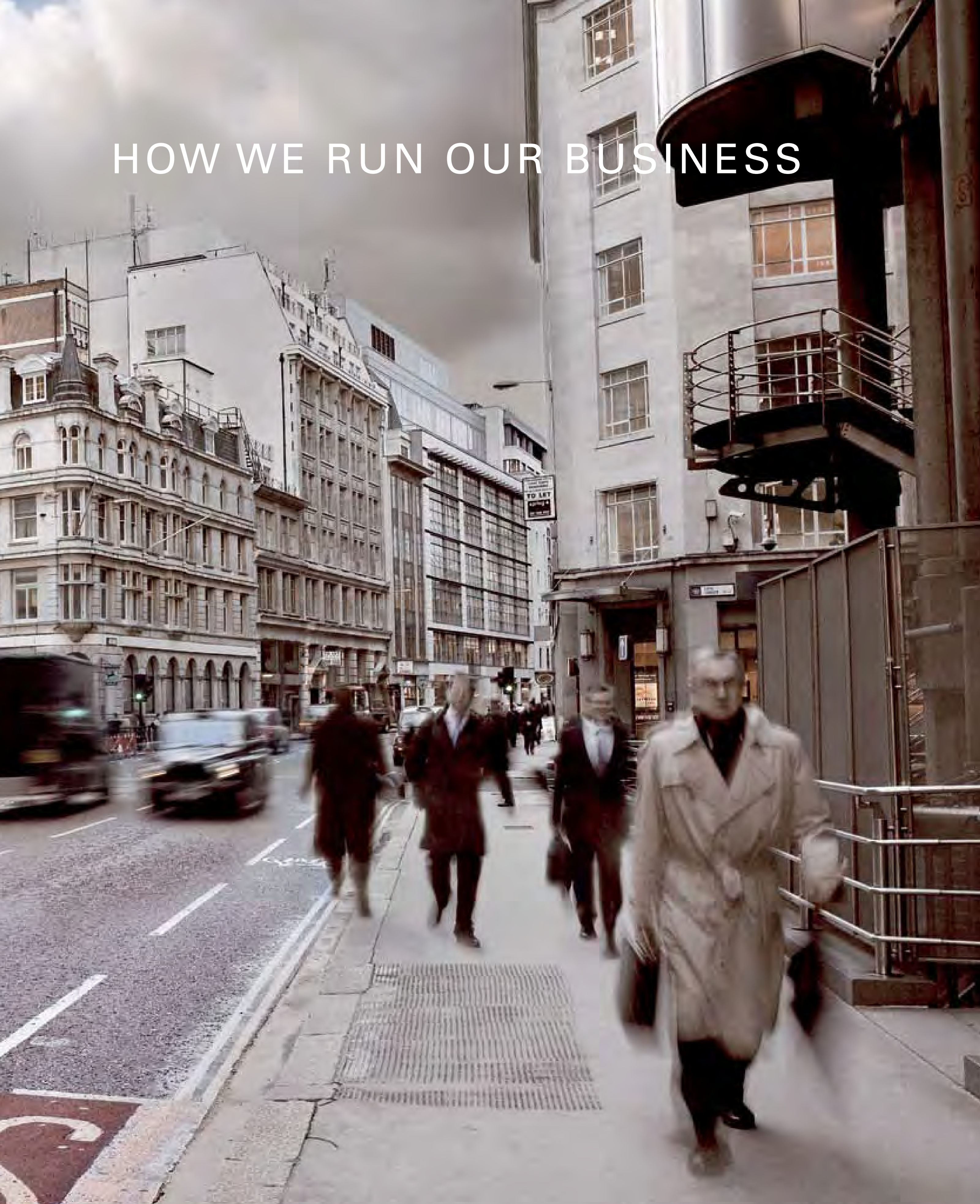
The Group operates a pension scheme for its employees both in the UK and overseas. It is funded with investments in equities, bonds and other financial assets. The value of these assets is dependent on capital markets, which are inherently volatile. Short-term market risk is balanced by a long-term spread over time and the portfolio effect. These assets are held separately from the assets of the Group, in an administered fund. An actuarial valuation at the end of 2006 showed that the scheme was in surplus.

Credit

The Group is exposed to potential concentrations of credit-related losses, in the event of non-performance, that consist principally of financial instruments and trade receivables. As its main customers are major retailers and financial institutions with high credit ratings, the risk at the end of December 2006 is not considered to be material.

Additional information on risk and its effects on the Group's results can be found in the Notes to the Consolidated Financial Statements on page 105.

HOW WE RUN OUR BUSINESS



BOARD OF DIRECTORS

Managing the future of our business

Ágúst Gudmundsson
Chief Executive Officer

Born: 1964
Nationality: Icelandic
Principal Occupation: Chief Executive Officer of Bakkavör Group
Professional Background: Founder of Bakkavör Group in 1986, Executive Chairman 1986 - May 2006 and Chief Executive Officer from May 2006
First elected to the Board: 1986
Education: College of Armuli
Other activities and functions: Board member of Exista hf., Fram Foods hf. and Icelandic Mountain Guides
Favourite dish: Oysters and sushi

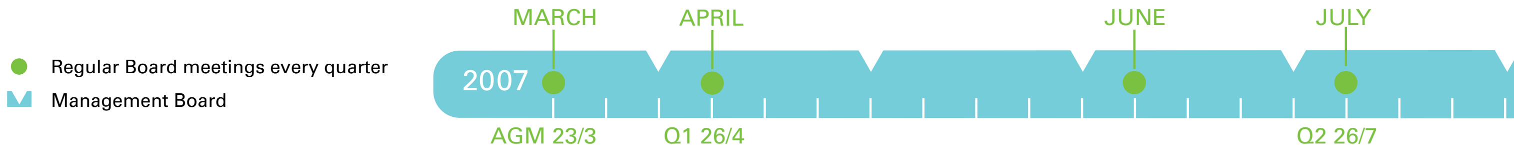
Lýdur Gudmundsson
Non-executive Chairman

Born: 1967
Nationality: Icelandic
Principal Occupation: Executive Chairman of Exista hf.
Professional Background: Founder of Bakkavör Group in 1986, Chief Executive Officer 1986 - May 2006. Executive Chairman of Exista hf. from May 2006
First elected to the Board: 1986
Education: The Commercial College of Iceland
Other activities and functions: Chairman of Iceland Telecom and Board member of Fram Foods hf. and Iceland Chamber of Commerce
Favourite dish: Houmous

Ásgeir Thoroddsen
Non-executive Director

Chairman of Audit Committee and member of Compensation Committee
Born: 1942
Nationality: Icelandic
Principal Occupation: Attorney to the Supreme Court of Iceland
Professional Background: Lawyer and Partner in a Reykjavik law firm since 1977
First elected to the Board: 2000
Education: Cand. juris from University of Iceland and a degree in Public Administration from New York University
Other activities and functions: Chairman of Intrum Iceland hf. Board member of Kaupthing Bank hf., Vátryggingafélag Íslands, Líftryggingafélag Íslands and Lýsing hf.
Favourite dish: Wienerschnitzel

The year at Bakkavör



Antoniou P. Yerolemou
Non-executive Director

Panikos J. Katsouris
Non-executive Director

Hreinn Jakobsson
Non-executive Director

Erlendur Hjaltason
Non-executive Director

Antoniou P. Yerolemou

Vice Chairman of the Board of Directors
Member of Compensation Committee
Born: 1942
Nationality: British
Principal Occupation: Non-executive Director of a number of companies
Professional Background: Chief Executive Officer of Katsouris Fresh Foods 1982-2002
First elected to the Board: 2001
Education: Primarily educated in Cyprus. Studied Business Administration in London.
Favourite dish:'Plokkfiskur'(hashed fish – Icelandic specialty)

Panikos J. Katsouris

Member of Audit Committee
Born: 1950
Nationality: British
Principal Occupation: Chief Executive Officer of Katsouris Brothers Ltd.
Professional Background: Finance Director of Katsouris Fresh Foods 1982-2002
First elected to the Board: 2001
Education: BSc Economics
Other activities and functions: Board member of Iceland Telecom
Favourite dish: Any seafood

Hreinn Jakobsson

Chairman of Compensation Committee and member of Audit Committee
Born: 1960
Nationality: Icelandic
Principal Occupation: Chief Executive Officer of ANZA hf.
Professional background: The Industrial Bank of Iceland 1985-1989, Thróunarfélag Íslands hf. 1989-1997 – Managing Director 1993-1997. CEO of Skýrr hf. 1997-2006, CEO of ANZA from 2006.
First elected to the Board: 2000
Education: Cand.Oecon. in Business Administration. Management from EVCA
Other activities and functions: Chairman of Sirius IT Holding A/S and related companies in Denmark, Norway and Sweden
Favourite dish: Seafood – any which way

Erlendur Hjaltason

Born: 1957
Nationality: Icelandic
Principal Occupation: Chief Executive Officer of Exista hf.
Professional background: Director of Eimskip 1990-2002, CEO of Eimskip 2002-2004, CEO of Exista hf. from 2004
First elected to the Board: 2006
Education: BSc Business Administration and MBA from Copenhagen Business School
Other activities and functions: Chairman of Iceland Chamber of Commerce and Board member of Iceland Telecom and Reykjavik Savings Bank (SPRON)
Favourite dish: Icelandic lamb with fresh salad

KEY MANAGEMENT

Bringing expertise to our business

Our management team has a wide variety of relevant experience. Between them they have over 50 years of financial expertise and over 200 years of experience in the food industry.

Hildur Árnadóttir
Chief Financial Officer of Bakkavör Group

Length of service within Group: 2.5 years
Nationality: Icelandic
Professional background: Chartered Accountant at KPMG from 1990 and Partner from 1997. CFO of Bakkavör Group since October 2004
Education: BSc Business Administration from University of Iceland. Chartered Accountant
Favourite dish: Lobster with garlic and Isleport cheese cakes

Costas Constantinou
Group Strategic Development Director

Length of service within Group: 23 years
Nationality: Greek Cypriot
Professional background: Various roles at Katsouris since 1984
Education: Graduate in BSc Electronic Engineering
Favourite dish: I enjoy all foods

Stephen Collyer
Group HR & Business Improvement Director

Length of service within Group: 4 years
Nationality: British
Professional background: Various senior Finance and Operational/General Management roles within the Food/Drink Manufacturing sector including Unigate, Cadbury Schweppes and Coca Cola Enterprises. Formerly Finance Director for Katsouris.
Education: Graduate, qualified Accountant
Favourite dish: Crab and lobster

Stephen Draisey
Managing Director, Bakkavör Prepared Foods

Length of service within Group: 17 years
Nationality: British
Professional background: Various roles in the food industry throughout career, in companies such as Unigate, J.Marr Seafoods, Northern Foods and Geest.
Education: Graduate in Languages
Favourite dish: Fish – any which way

Einar Gústafsson
Managing Director, Bakkavör Asia

Length of service within Group: 2 years
Nationality: Icelandic
Professional background: Completed two turnaround efforts in the seafood industry after spending initial career at Deloitte Consulting
Education: Graduate in BSc Business Administration and MBA
Favourite dish: New York strip Sirloin with French fries and béarnaise sauce, and my wife's molten chocolate cake

Richard Howes
Group Finance Director

Length of service within Group: 8 years
Nationality: British
Professional background: Qualified as a Chartered Accountant before moving into Corporate Finance with Dresdner Kleinwort Benson. Joined Geest in 1999 as Corporate Finance Manager and has worked in various finance roles within the Group before taking up latest role in May 2006.
Education: BSc (Hons) in Geography, qualified Accountant.
Favourite dish: Fresh grilled fish

Gordon Pates
Managing Director, Bakkavör Select Produce

Length of service within Group: 38 years
Nationality: British
Education and professional background: Joined Geest in 1969 in the Horticulture division. Spent 10 years in produce businesses before moving into prepared produce and prepared food businesses in the late 1990s.
Favourite dish: Italian cuisine

Chris Thomas
Managing Director, Bakkavör Fresh Foods

Length of service within Group: 4 years
Nationality: British
Professional background: Various roles in food manufacturing over 30 years with Mars, Pepsi, St. Ivel and Geest from 2003.
Education: Chartered Electrical Engineer and MBA degree.
Favourite dish: Lemon Sole

Brian Walton
Managing Director, Bakkavör Fresh Produce

Length of service within Group: 32 years
Nationality: British
Professional background. Joined Geest as a Technologist in 1975 and has worked in various roles within the produce division.
Education: BSc(Hons) in Horticulture
Favourite dish: Pie and chips

Ann Savage
Group Technical Director

Length of service within Group: 7 years
Nationality: British
Professional background: A variety of roles, spanning 30 years, in technical and research and development departments (with a brief spell in manufacturing), for Cooperative Wholesale Society (CWS) Northern Foods and Geest.
Education: Studied at the Open University. Post Graduate Diploma in Management Studies
Favourite dish: Christmas dinner

CORPORATE GOVERNANCE

Running our business with integrity

Bakkavör Group defines Corporate Governance as the code of conduct by which the Group is directed and controlled. This involves its relations with shareholders, employees, customers, suppliers and other key stakeholders.

Policy and context

The duties of the various bodies within Bakkavör Group are determined by Icelandic law and by the Group's corporate governance policy, which is based on the Guidelines on Corporate Governance ('the Guidelines'). These were first issued in 2004 by the Iceland Chamber of Commerce, the OMX Nordic Exchange in Iceland and the Confederation of Icelandic Employers, and were re-issued in December 2005.

Structure and bodies

Bakkavör Group's organisational structure is decentralised, which enables the business to respond quickly to the demands of the fast-moving fresh prepared foods and produce markets in which it operates. Bakkavör Group's governance structure reflects the organisational structure of the Group.

Following is a description of each of the key governance bodies: shareholder meetings, the Board of Directors, the Board Committees, the Chief Executive Officer and the Bakkavör Group Management Board.

Shareholder meetings

Shareholder meetings are the supreme authority in Bakkavör Group's affairs (within the restrictions made by the Group's Articles of Association and Icelandic law). The Annual General Meeting (AGM) is scheduled once a year and other shareholder meetings are convened when necessary.

All shareholders, as well as their representatives, have the right to attend shareholder meetings. The members of the Board of Directors and the Chief Executive Officer also have the right to speak and submit motions at shareholder meetings, even if they are not shareholders. Shareholder meetings are also open to the media and representatives of the OMX Nordic Exchange in Iceland. Each share equals one vote, and motions are passed by majority vote unless otherwise stated in the Group's Articles of Association or Icelandic law.

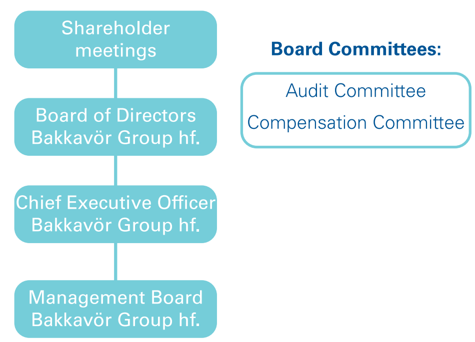
The Group's AGM is held before the end of June each year and, for 2007, is scheduled to take place on 23 March. The AGM is advertised publicly with at least one week's notice and details of the meeting are set out on the Group's website: www.bakkavor.com, and on the OMX Nordic Exchange in Iceland website: www.icex.is.

The Board of Directors

The Board of Directors has supreme authority in the Group's affairs in the period between shareholder meetings.

The Board of Directors is elected annually by shareholders at the AGM. The Board currently comprises seven members: the Chairman, five non-executive Directors (including the Vice Chairman of the Board) and one executive Director. At the Group's AGM on 24 March 2006, the members of the Board of Directors were re-elected for the term of one year, and Erlendur Hjaltason, CEO of Exista hf., was elected to the Board.

Governance structure and bodies



Comply or explain

According to the Guidelines, it is preferable that the majority of the Directors are independent. Since February 2005, the majority of Bakkavör Group's Board Directors has not been independent. In 2006, the Board consisted of three independent members and four non-independent members. However, one Board member, Antonios P. Yerolemou, will qualify as an independent Director within one year. [1]The Board of Directors complied with the Guidelines in all other respects during the year.

Together, the Board members bring a valuable and balanced range of experience as they have all held, or hold, senior positions in professional and public life. Profiles of the Board members are set out on pages 84 and 85.

1 Antonios P. Yerolemou is a non-executive Director but not yet considered independent as he was the Executive Chairman of the Group's subsidiary, Katsouris Fresh Foods. According to the Guidelines, Board members may not be defined as independent if they become Board members within three years of being an employee of the company.

The Board elects a Chairman and Vice Chairman of the Board of Directors and appoints the Chief Executive Officer (CEO).

The responsibilities of the Board

The Board is responsible for the overall management and performance of the Group and has adopted written working rules specifying its responsibilities.

The Chairman of the Board is responsible for leading the Board, facilitating its work and ensuring that the Board is capable of operating in the interests of the Group's shareholders. The Chairman also serves as the Board's spokesperson.

The Board's responsibilities to shareholders encompass:

- setting the Group's strategy
- providing leadership within a framework of controls for managing risk
- maintaining the policy and decision-making framework in which the Group's strategy is implemented
- ensuring that necessary financial and human resources are in place to meet strategic goals
- monitoring performance against key financial and non-financial indicators
- overseeing the system of risk management
- setting values and standards in governance matters

The Board has a formal agenda of matters reserved to it for decision-making, which include: strategy formulation, approval of annual and interim statements, approval of annual budget and business plan, approval of acquisitions and disposals, approval of major capital investments, monitoring of internal controls and important policy matters.

Summary of Board governance in 2006

Name	Independent	Audit Committee	Compensation Committee
Antonios P. Yerolemou	No*	No	Yes
Ágúst Gudmundsson	No	No	No
Ásgeir Thoroddsen	Yes	Chairman	Yes
Erlendur Hjaltason	No**	No	No
Hreinn Jakobsson	Yes	Yes	Chairman
Lýdur Gudmundsson	No	No	No
Panikos J. Katsouris	Yes	Yes	No

*Antoniou P. Yerolemou is a non-executive Director but is not yet considered independent as he was the Executive Chairman of the Group's subsidiary, Katsouris Fresh Foods. According to the Guidelines, Board members may not be defined as independent if they become Board members within three years of being an employee of the company.

**Erlendur Hjaltason is a non-executive Director but is not considered independent as he is the CEO of Exista hf., the largest shareholder in Bakkavör Group, and both Ágúst Gudmundsson and Lýdur Gudmundsson are on the Board of Directors of Exista hf.

Board meeting attendance

Board member	Board meeting attendance	Compensation Committee meeting attendance	Audit Committee meeting attendance
Antonios P. Yerolemou	12/14	3/3	N/A
Ágúst Gudmundsson	14/14	N/A	N/A
Ásgeir Thoroddsen	13/14	3/3	2/2
Erlendur Hjaltason*	10/11	N/A	N/A
Hreinn Jakobsson	12/14	3/3	2/2
Lýdur Gudmundsson	13/14	N/A	N/A
Panikos J. Katsouris	12/14	N/A	2/2
Total	91%	100%	100%

*Erlendur Hjaltason was elected a member of the Board of Directors at the Annual General Meeting on 24 March 2006.

The Board reviews and determines the compensation of the CEO. The Compensation Committee discharges the Board's responsibility in reviewing and determining the CEO's remuneration. The Board also approves the organisational structure of the Company.

The Board plans to assess its activities and work procedures regularly with the assistance of outside parties, as applicable. All Directors are required to deal at arm's length with the Group and its subsidiaries and to disclose circumstances that might be perceived as a conflict of interest.

Board meetings

The Board of Directors convened 14 times in 2006. The average attendance at the Board meetings was 91%.

The Board is provided with a report in advance of each Board meeting and, in addition, a comprehensive monthly report of the Group's financial performance, operations and market conditions. Board members are informed about all significant matters immediately.

Board Committees

The Board's work is supported by its Committees – the Audit and Compensation Committees. Each Committee's Chairman and members are appointed by the Board annually.

Audit Committee

The powers and duties of the Audit Committee are determined in the Audit Committee Charter, which is approved by the Board. The Audit Committee is responsible for monitoring the Group's internal control system and financial reporting process. To this effect, the Audit Committee is in regular contact with the external auditor to ensure that observations made by the auditor are adhered to. The Audit Committee receives written confirmation from the external auditor as to any relationships which may reasonably be thought to influence its independence. The external auditor also confirms whether it considers itself independent within the meaning of the professional requirements. The Committee reviews with the external auditor and the Chief Financial Officer (CFO) the effectiveness of the internal control system and financial reporting process. The Committee keeps under review the scope and results of the audit. The Audit Committee, acting with the Board of Directors, is responsible for the selection, evaluation and nomination, when applicable, of an external auditor for shareholder approval.

Members of the Audit Committee are: Ásgeir Thoroddsen (Chairman), Hreinn Jakobsson and Panikos J. Katsouris. The Audit Committee met twice in 2006.

According to the Guidelines, employees are not allowed to be members of the Audit Committee, and the majority should be independent.

All committee members must have thorough knowledge of accounting and preparation of financial statements.

Auditors

An external auditing firm is elected by the shareholders at the Annual General Meeting for a term of one year. The auditors shall not be members of the Board of Directors or employees of the Group and are not allowed to own shares in the Company. The auditors shall have access to all books and documents of Bakkavör Group at all times and shall ensure that the Group's annual accounts are in accordance with generally accepted accounting standards.

Deloitte hf. was elected the Group's auditor at the AGM on 24 March 2006. Auditors on Deloitte's behalf are Hilmar A. Alfredsson, State Authorised Public Accountant and Gudlaugur Gudmundsson, State Authorised Public Accountant. Deloitte hf. has been the Group's auditor since the Company's foundation in 1986. Mr. Gudmundsson has acted on its behalf since 1986 and Mr. Alfredsson since 1992.

Auditing fees

Clear guidelines exist which outline other professional services which are appropriate for Deloitte hf. to provide in their capacity as Group auditor. These services include: due diligence on mergers, acquisitions and disposals, and tax and business risk assurance. These guidelines ensure the independence of the Group's auditors. Details of auditing fees and other fees paid to Deloitte hf. are set out in note 7 on page 115.

Compensation Committee

The powers and duties of the Compensation Committee are determined in the Compensation Committee Charter, which is approved by the Board. The Compensation Committee discharges the Board's responsibility in matters relating to executive compensation. This work includes administration of the Group's incentive compensation and equity-based plans. Executive performance and compensation is evaluated annually. The Committee prepares an annual report on executive compensation for inclusion in the Company's Annual Report, in accordance with applicable rules and regulations. The principal responsibility in compensating executives is to co-ordinate the incentives of the executives with actions that will enhance long-term shareholder value.

Members of the Compensation Committee are: Hreinn Jakobsson (Chairman), Antonios P. Yerolemou and Ásgeir Thoroddsen. The Compensation Committee met three times in 2006.

According to the Guidelines, employees are not allowed to be members of the Compensation Committee, and the majority should be independent.

Chief Executive Officer

The Board of Directors appoints a Chief Executive Officer (CEO) and decides the terms of his employment. The CEO is responsible for the daily management of the Group as well as the implementation of the Group's strategy as set out by the Board. Furthermore, the CEO shall ensure that the accounts and finances of the Group conform to law and accepted accounting standards and that the disposal of the Group's assets are securely handled.

Bakkavör Group Management Board

Below Board level, the management of the operations is delegated to the Group's Management Board. The Management Board is headed by Bakkavör Group's Chief Executive Officer, Ágúst Gudmundsson. Other members of the Management Board are: four Managing Directors, the Business Improvement and Human Resource Director, the Group Technical Director, the Group Finance Director and the Strategic Development Director. Profiles of the members of the Management Board are set out on page 86. The Management Board meets monthly.

The Management Board sets policies in important risk areas such as food safety, employee matters, health and safety as well as the environment. Led by a General Manager, each of the Group's businesses must comply with these policies as well as be responsible for running their businesses, meeting the demands of their customers, and the strategic and financial targets that have been set by their Managing Director.

Compliance

In accordance with statutory law, Bakkavör Group complies with the Rules on Treatment of Insider Information and Insider Trading ('the Rules') issued by the Financial Supervisory Authority. In accordance with the Rules, an independent Compliance Officer, appointed by the Board of Directors, is responsible for monitoring and supervising the handling of insider information. In addition, the Group has in place Rules on the handling of inside information and insider trading. These additional rules of the Group state, among other things, that it is preferable that primary insiders do not trade in the securities of the Group except during a six-week period from the publication of the Group's financial reports, regardless of whether they possess inside information or not. The Compliance Officer is responsible for keeping employees informed about these rules.

Compensation

Board compensation

Compensation to the Board of Directors is decided at the Annual General Meeting. For 2006, the agreed annual fee was £25,000 for each Board member (including the Chairman). During 2006 the Board was compensated as stated in the table below.

No severance payment was made to any person giving up their function on the Board during 2006. No options, warrants or other rights were granted during 2006, and no member of the Board or other Directors holds such rights. There are no outstanding guarantees, loans, advances or credits to members of the Board or other Directors. No shares were allotted to members of the Board or other Directors in 2006 and there are no programmes for share allotment in place.

Besides the compensation table below, some Board members have been involved in commercial trading with Bakkavör Group: Katsouris Brothers Ltd. (chaired by Panikos J. Katsouris) has supplied Katsouris Fresh Foods with raw materials. Panikos J. Katsouris is also in control of buildings rented by the Group. The Group rents office space from Tjarnargata 35 ehf., which is owned by Ágúst Gudmundsson, CEO, and Lýdur Gudmundsson, Chairman of the Board of Bakkavör Group hf. All such transactions are based on arm's length principles and are not considered to be part of the Board's compensation. Details of related-party transactions can be found in note 27 on page 124 of the accounts section.

Compensation overview (GBP '000)

Board member	Salary	Benefits	Bonus	Pension fund payments	Total	Shares at year-end*
Lýdur Gudmundsson, Chairman	341	68		1	410	826,209,416**
Ágúst Gudmundsson, CEO	584	153	300	1	1,038	826,209,416**
Antonios P. Yerolemou	25			1	26	74,534,353
Ásgeir Thoroddsen	25			1	26	1,418,164
Erlendur Hjaltason	19#			1	20	1,192.400
Hreinn Jakobsson	25			1	26	1,500,000
Panikos J. Katsouris	25			1	26	52,336,471
Management team member						
Gareth Voyle, former CEO of Bakkavör Invest Ltd.	2,051	129	708	32	2,920	

* In Icelandic Krona (ISK) and includes holdings of their spouses, dependent children and companies owned by them, if any.
**Ágúst Gudmundsson and Lýdur Gudmundsson in total held control of 826,209,416 shares in Bakkavör Group through Exista B.V. and related parties at year end.
#Erlendur Hjaltason was elected a member of the Board of Directors at the Annual General Meeting on 24 March 2006.

RISK MANAGEMENT

Highlighting our Board agenda

Board's approach to risk management

Bakkavör Group is faced with a number of risks in its business environment, both operational and financial. The purpose of risk management is to determine which factors are critical and material to the Group's success. It is the Board's responsibility to ensure that management sets out procedures to control the identified risks and deals with changes in the business environment, where possible, to minimise the effect of these risks on the Group's operations.

Board agenda

The Bakkavör Group Board has identified five key areas of risk which, if managed incorrectly, could be detrimental to the long-term sustainability and profitability of the Group. Consequently, performance in these areas is kept high on the Board agenda. The five key areas are as follows:

Growth

Bakkavör Group has been characterised by substantial growth in recent years. The Group has set itself ambitious growth targets and aims to continue to grow both organically and through strategic acquisitions. (Please turn to page 50 in 'Our strategy'.)

It is important to ensure that our business remains sustainable and profitable while it grows. Major acquisitions entail numerous risk factors for Bakkavör Group. These risk factors are primarily related to the Group's ability to execute the integration and realise the benefits underlying the rationale of the acquisition. Underestimating the importance of cultural integration is also a risk in merging companies. Any factors leading to failed integration would have adverse effect on Bakkavör Group's operations.

Food safety

Food safety is paramount to the continued success of our business as millions of people buy our products every day. All our factories operate documented quality management systems (QMS) based on Hazard Analysis Critical Control Point (HACCP) principles and customer Codes of Practice to manufacture products that are safe, legal and of the quality required by the individual customer. Each step in the manufacturing of our products is assessed for risk, and the necessary controls are put in place to maintain food safety standards.

Traceability is a critical component in our management of food safety, allowing us to trace ingredients quickly from the source through to the finished product and vice versa. We work closely with our suppliers to source safe, legal, quality ingredients to a consistent standard. This includes regular visits to their factories to assure ourselves of the integrity of their quality systems and factory operations. Employee training is paramount to the management of food safety and we are committed to providing this at all levels within our operations.

Customers

As with most suppliers in the fresh prepared foods sector, our customers are few, but of critical importance to us, and it is our intention to continue to build strong relationships with them. Our products carry our customers' brand names and we develop products in close partnership with our customers. At various levels of our organisation, our employees talk to their customer peers (often daily). At a senior level, we appoint 'Customer Champions' who are responsible for managing overall customer relations with their specific contacts. This communication facilitates the day-to-day business as well as longer-term strategic planning.

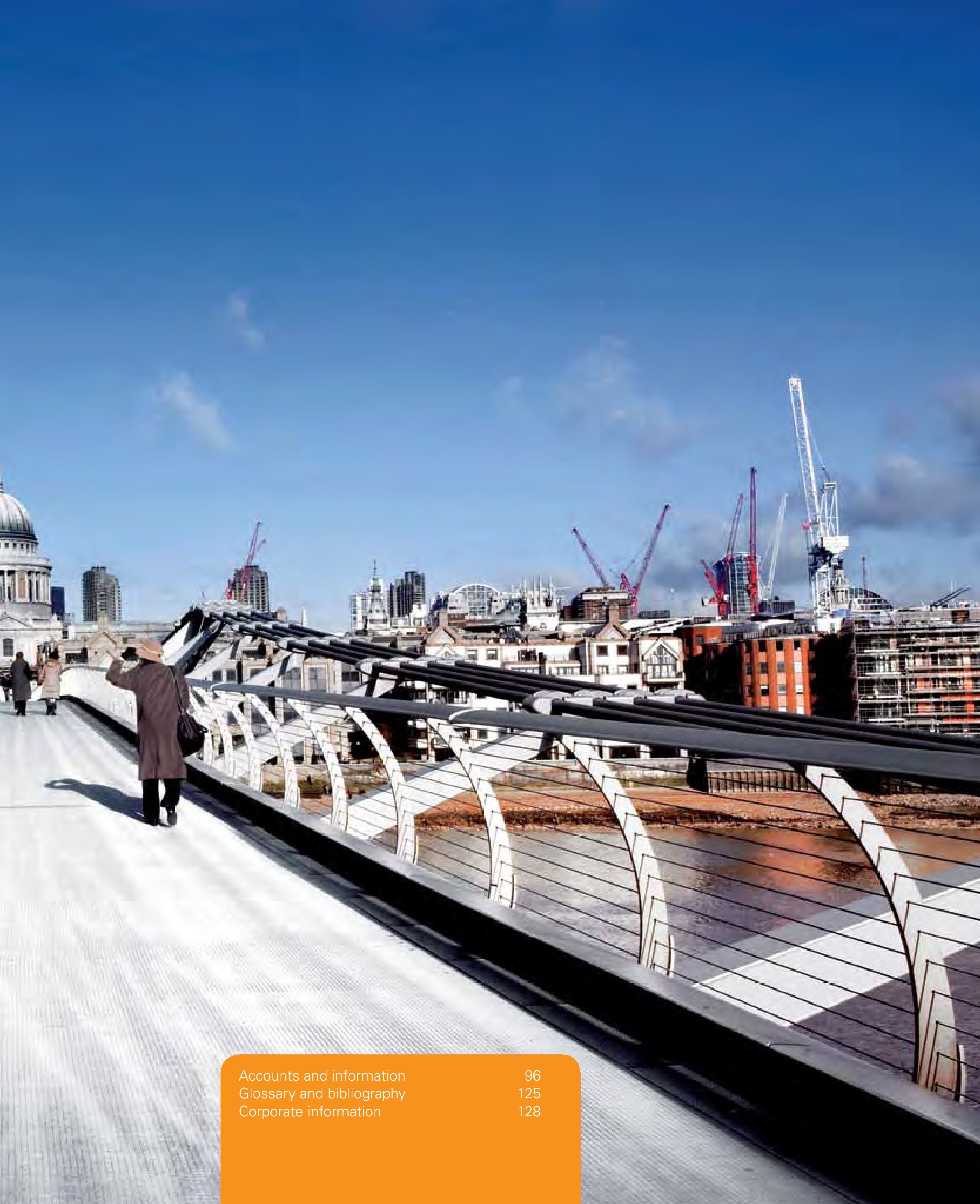
Consumers

At the heart of our success are the people who buy and eat our finished products – our consumers. It is important for us to listen to their demands in order to provide them with innovative meal solutions which are of high quality and quick and easy to prepare. Development and innovation skills remain a high priority in the business. For examples of how we keep abreast of evolving trends, please turn to page 18.

Shareholder value

We value the trust that our shareholders place in us, and the principal goal of Bakkavör Group is to provide good, long-term returns for its shareholders. The key to achieving this goal is the development and communication of a clear strategic vision and the recruitment and retention of talented management to fulfil this strategic vision. (Please turn to page 68 to see our performance in creating value for our shareholders.)

ACCOUNTS AND INFORMATION



Endorsement by the Board of Directors and CEO

The Consolidated Financial Statements for the year ended 31 December 2006, have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. The Consolidated Financial Statements include the Financial Statements of Bakkavör Group hf. and its subsidiaries together referred to as the Company.

Ágúst Gudmundsson became CEO of Bakkavör Group from 26 May whilst Lýdur Gudmundsson, the former CEO of the Group, became Non-Executive Chairman.

In May 2006 Bakkavör Group hf. acquired the leading manufacturer of chilled desserts in the UK, Laurens Patisseries Ltd. In July 2006 Bakkavör Group hf. acquired a leading manufacturer of chilled bread products in the UK, New Primebake Ltd. In November 2006 Bakkavör Group hf. acquired Rye Valley Patisserie (now Pure Patisseries), which specialises in the manufacturing of chilled desserts, and acquired remaining shares of Fresh Cook Ltd., a manufacturer of 'ready to cook' meals.

The Board of Directors and the CEO of Bakkavör Group hf. are of the opinion that the Consolidated Financial Statements for the year 2006 contain all the information necessary to form a clear picture of the Company's standing at year end, the year's operating results and the year's financial development.

Profit for the year, according to the Income Statement, amounted to GBP 68.2 million. Total equity amounted to GBP 241.4 million at the end of the year. The Board of Directors recommends a payment of dividend ISK 0.5 per share, which equals 50% of share capital, but otherwise refers to the Consolidated Financial Statements regarding changes in the Company's equity and disposal of profits.

At year end the number of shareholders were 3,804. At the beginning of the year there were 3,828 shareholders. At year end one shareholder holds more than 10% of the shares, Exista B.V. and related parties with 38.3% of the shares.

The Board of Directors and the CEO of Bakkavör Group hf. hereby confirm the Consolidated Financial Statements for the year 2006 with their signature.

Reykjavík, 31 January 2007

Board of Directors and CEO

Lýdur Gudmundsson Chairman	Ágúst Gudmundsson CEO
Antonios P. Yerolemou	Ásgeir Thoroddsen
Erlendur Hjaltason	Hreinn Jakobsson
Panikos J. Katsouris	

Independent Auditor's Report

To the Board of Directors and shareholders of Bakkavör Group hf.

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

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

Reykjavík, 31 January 2007

Deloitte hf.

Hilmar A. Alfredsson State Authorized Public Accountant	Gudlaugur Gudmundsson State Authorized Public Accountant

Consolidated Income Statement for the year 2006

	Notes	2006 Q4	2005 Q4	2006	2005
Net sales	5	329,161	252,170	1,219,189	722,065
Cost of sales		(239,047)	(180,599)	(892,912)	(513,521)
Gross profit		90,114	71,571	326,277	208,544
Other operating income		10	12	24	164
Operating expenses		(59,943)	(50,447)	(212,050)	(142,133)
Share of profit (loss) in associates		470	(278)	(318)	75
		(59,463)	(50,713)	(212,344)	(141,894)
Operating profit		30,651	20,858	113,933	66,650
Net finance costs	8	(10,098)	(9,764)	(47,360)	(28,269)
Profit before tax		20,553	11,094	66,573	38,381
Income tax	9	(4,714)	193	(15,237)	(6,048)
Profit from continuing operations		15,839	11,287	51,336	32,333
Discontinuing operation, net of tax	10	16,910	0	16,910	0
Profit for the year		32,749	11,287	68,246	32,333
Attributable to:					
Shareholders of Bakkavör Group hf.		32,753	11,271	67,617	31,986
Minority interest		(4)	16	629	347
		32,749	11,287	68,246	32,333
Earnings per share (GBP pence)	11	1.5	0.7	3.4	2.0

Amounts in thousands of GBP

Consolidated Balance Sheet at 31 December 2006

	Notes	2006	2005
Non-current assets			
Goodwill and other intangible assets	12	713,928	565,723
Property, plant and equipment	13	303,758	267,898
Investments in joint ventures and associates	14	7,395	4,699
Deferred income tax asset	18	3,797	2,080
		1,028,878	840,400
Current assets			
Inventories	15	35,767	31,839
Trade and other receivables	16	221,467	180,051
Cash and cash equivalents	16	39,695	82,317
		296,929	294,207
Total assets		1,325,807	1,134,607
Equity			
Share capital	17	14,924	10,813
Capital reserve		77,154	38,416
Translation reserves		(1,437)	(484)
Retained earnings		149,307	78,471
Shareholders' equity		239,948	127,216
Minority interest		1,499	136
Total equity		241,447	127,352
Non-current liabilities			
Deferred income tax liability	18	33,237	24,957
Subordinated convertible loan		0	12,868
Borrowings	20	682,440	666,398
		715,677	704,223
Current liabilities			
Current maturities of non-current liabilities	20	33,094	28,589
Other current liabilities		335,589	274,443
		368,683	303,032
Total equity and liabilities		1,325,807	1,134,607
Off Balance Sheet Items			
Mortgages and commitments	22		

Amounts in thousands of GBP

Consolidated Statement of Changes in Equity for the year 2006

	Shareholders' equity						
	Share capital	Capital reserve	Translation reserves	Retained earnings	Total	Minority interest	Total equity
Equity 1 January 2005	10,813	38,416	0	38,985	88,214	0	88,214
Translation reserves			(484)		(484)		(484)
Actuarial gain recognised on pension plan				7,500	7,500		7,500
Profit for the year				31,986	31,986	347	32,333
Change in minority interest						(211)	(211)
Equity 1 January 2006	10,813	38,416	(484)	78,471	127,216	136	127,352
Translation reserves			(953)		(953)		(953)
Actuarial gain recognised on pension plan				6,500	6,500		6,500
Dividends				(3,281)	(3,281)		(3,281)
Increase of share capital	4,111	38,738			42,849		42,849
Profit for the year				67,617	67,617	629	68,246
Change in minority interest						734	734
Equity 31 December 2006	14,924	77,154	(1,437)	149,307	239,948	1,499	241,447

Amounts in thousands of GBP

Consolidated Cash Flow Statement for the year 2006

	Notes	2006	2005
Cash flow from operating activities			
Operating profit		113,933	66,650
Discontinued operation	10	21,299	0
Depreciation and amortisation	12, 13	33,829	19,429
Other items		(9,175)	(751)
Changes in current assets and liabilities		5,180	18,225
Cash generated from operations		165,066	103,553
Payments of interest income and interest expense		(24,530)	(18,635)
Payments of tax		(9,036)	(2,859)
Cash flow from operating activities		131,500	82,059
Investing activities			
Property, plant and equipment	13	(37,902)	(16,413)
Acquisitions, net of cash acquired	24	(127,108)	(427,344)
Shareholdings		(2,404)	(2,343)
Investing activities		(167,414)	(446,100)
Financing activities			
Dividends		(3,281)	0
Bank loans		1,079	1,696
New borrowings		153,126	423,352
Payments of non-current liabilities		(157,299)	(3,114)
Financing activities		(6,375)	421,934
Net (decrease) increase in cash		(42,289)	57,893
Effects of foreign exchange adjustments		(333)	(84)
Cash and cash equivalents at beginning of year		82,317	24,508
Cash and cash equivalents at year end		39,695	82,317
Other information:			
Net cash provided by operating activities			
Profit for the year		68,246	32,333
Items not affecting cash		74,518	34,606
Working capital provided by operating activities		142,764	66,939
Changes in current assets and liabilities		(11,264)	15,120
Cash flow from operating activities		131,500	82,059
Property, plant and equipment		(37,902)	(16,413)
Free cash generated by operating activities		93,598	65,646
Non-cash transaction, part of acquisition price and subordinated loans paid with treasury stock		42,849	0

Amounts in thousands of GBP

Notes to the Consolidated Financial Statements

1. General information

Bakkavör Group hf. is a company incorporated and domiciled in Iceland. The Consolidated Financial Statements for the year 2006 comprise Bakkavör Group hf. (the parent) and its subsidiaries (together referred as the Company).

The Company prepares its Consolidated Financial Statements in GBP, which is the company's functional currency.

2. Significant accounting policies

Statement of compliance

The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. The Consolidated Financial Statements have been prepared under the historical cost basis, except for revaluation of certain properties and financial instruments.

New and revised Standards

At the date of authorisation of these financial statements, the following Standards were in issue but not effective:

	Effective date:
• IFRS 7, Financial Instruments: Disclosures	1 January 2007
• IFRS 8, Operating Segments	1 January 2009

At the date of authorisation of these financial statements, the following Interpretations were in issue but not effective:

	Effective Date: annual periods beginning:
• IFRIC 7, Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies	On or after 1 March 2006
• IFRIC 8, Scope of IFRS 2	On or after 1 May 2006
• IFRIC 9, Reassessment of Embedded Derivatives	On or after 1 June 2006
• IFRIC 10, Interim Financial Reporting and Impairment	On or after 1 November 2006
• IFRIC 11, IFRS 2: Group and Treasury Share Transactions	On or after 1 March 2007
• IFRIC 12, Service Concession Arrangements	On or after 1 January 2008

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material financial impact on the financial statements of the Company.

Basis of preparation

The preparation of the Consolidated Financial Statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The principal accounting policies adopted are set out below.

Amounts in thousands of GBP

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bakkavör Group hf. and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The Consolidated Financial Statements have been prepared using the purchase method of consolidation accounting. When ownership in subsidiaries is less than 100%, the minority interest in the subsidiaries' income and loss and equity is accounted for in the calculation of the consolidated income or loss and the consolidated equity.

On acquisition, the assets and liabilities and contingent liabilities of a subsidiary are measured at their fair value at the date of acquisition. Any excess of the cost of the acquisition over the fair value of the identifiable net assets acquired is recognised as goodwill.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Company.

All intra-company transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets of consolidated subsidiaries are identified separately from the Company's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Company except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations

The Consolidated Financial Statements have been prepared using the purchase method of consolidation accounting. When ownership in subsidiaries is less than 100%, the minority interest in the subsidiaries' income or loss and stockholders equity is accounted for in the calculation of the consolidated income or loss and the consolidated stockholders equity.

The cost of the acquisition is measured at the aggregate of the fair value, at the date of exchange, of assets given, liabilities incurred or assumed and equity instruments issued by the Company in exchange for control of the acquiree, plus any costs directly attributable to the business combination.

Goodwill arising on acquisition is recognised as an assets and initially measured at cost, being the excess of the cost of the business combination over the Company's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Company's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair value of the assets, liabilities and contingent liabilities recognised.

The results of subsidiaries acquired or disposed of during the period are included in the income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Investments in associates

An associate is an entity over which the Company has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results of associates are incorporated in the Consolidated Financial Statements using the equity method of accounting.

Any excess of the cost of acquisition over the Company's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of the associate recognised at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment and is assessed for impairment as part of the investment. Any excess of the Company's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in the income statement.

Where a company entity transacts with an associate of the Company, profits and losses are eliminated to the extent of the Company's interest in the relevant associate.

Interests in joint ventures

A joint venture is a contractual arrangement whereby the Company and other parties undertake an economic activity that is subject to joint control, that is when the strategic financial and operating policy decision relating to the activities requires the unanimous consent of the parties sharing control.

Where a group company undertakes its activities under joint venture arrangements directly, the Company's share of jointly controlled assets and any liabilities incurred jointly with other ventures are recognised in the financial statements of the relevant company and classified according to their nature. Liabilities and expenses incurred directly in respect of interest in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Company's share of the output of jointly controlled assets, and its share in joint venture expenses, are recognised when it is probable that the economic benefits associated with the transactions will flow to/from the Company and their amount can be measured reliably.

Joint venture arrangements which involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities. The Company reports its interest in jointly controlled entities using the alternative equity method.

Where the Company transacts with its jointly controlled entities, unrealised profits and losses are eliminated to the extent of the Company's interest in the joint venture, except to the extent that unrealised loss provide evidence of an impairment of the assets transferred.

Non-current assets held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Goodwill

Goodwill arising on consolidation or a jointly controlled entity represents the excess of the cost of acquisition over the Company's interest in the fair value of the identifiable assets and liabilities and contingent liabilities of a subsidiary or jointly controlled entity at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses and reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to each of the Company'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. Any impairment is recognised immediately in profit or loss and is not subsequently reversed.

On disposal of a subsidiary or a jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit and loss on disposal.

The Company's policy for goodwill arising on the acquisition of an associate is described under "Investments in associates" above.

Financial risk management

i) Financial risk factors

Financial risk management is an integrated part of the way the Company is managed. The Company's activities expose it to a variety of financial risks: market risks (including foreign exchange risk), credit risk, liquidity risk, cash flow risk and fair value interest-rate risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Company's financial performance. The Company uses derivative financial instruments to manage certain risk exposures. Risk management is carried out within the Company under policies approved by the Board of Directors.

ii) Market risk

The Company operates internationally and is exposed to foreign exchange risk arising from various currency exposures primarily with respect to EUR and USD. The Company uses forward contracts to manage its foreign exchange risk arising from future commercial transactions, recognised assets and liabilities. Foreign exchange risk arises when future commercial transactions, recognised assets and liabilities are denominated in a currency that is not the entity's functional currency.

iii) Credit risk

The Company has no significant concentrations of credit risk. The Company has policies in place to ensure that sales made to customers with an appropriate credit history and that products are not delivered until payments are secured. The Company has policies that limit the amount of credit exposure to any of the subsidiaries.

iv) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash, the availability of funding through an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, the Company aims to maintain flexibility in funding by keeping committed credit lines available.

v) Cash flow and fair value interest rate risk

The Company's income and operating cash are substantially independent of changes in market interest rates. The Company's cash flow interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the Company to cash flow interest rate risk. Borrowings issued at fixed rate expose the Company to fair value interest rate risk.

Foreign currencies

Transactions in currencies other than GBP are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are retranslated at the rates prevailing on the balance sheet date. Profits and losses arising on exchange are included in net profit or loss for the period.

On consolidation, the assets and liabilities of the Company's overseas operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period. Exchange differences arising, if any, are classified as equity and transferred to the Company's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

Financial assets

Investments are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as at fair value through the income statement, which are initially measured at fair value.

Financial assets are classified into the following specified categories: financial assets as 'at fair value through profit and loss' (FVTPL), 'held-to-maturity investments', 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

i) Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments other than those financial assets designated as at FVTPL.

ii) Financial assets measured at fair value through profit and loss

Financial assets are classified as at FVTPL where the financial asset is either held for trading or it is designated as at FVTPL. A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset. Fair value is determined in the manner described below.

iii) Held-to-maturity investments

Bills of exchange and debentures with fixed or determinable payments and fixed maturity dates that the Company has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortised cost using the effective interest method less impairment, with revenue recognised on an effective yield basis.

iv) Available for sale (AFS) financial assets

Listed shares and listed redeemable notes held by the Group that are traded in an active market are classified as being AFS and are stated at fair value. Fair value is determined in the manner described below. Gains and losses arising from changes in fair value are recognised directly in equity in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest rate method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the investments revaluation reserve is included in profit or loss for the period.

Dividends on AFS equity instruments are recognised in profit or loss when the Company's right to receive payments is established.

The fair value of AFS monetary assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the balance sheet date. The change in fair value attributable to translation differences that result from a change in amortised cost of the asset is recognised in profit or loss, and other changes are recognised in equity.

v) Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method less any impairment. Interest income is recognised by applying the effective interest rate, except for short term receivables where the recognition of interest would be immaterial.

vi) Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised directly in equity.

Financial liabilities and equity instruments issued by the Company

i) Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

ii) Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of direct issue costs.

iii) Compound instruments

The component parts of compound instruments are classified separately as financial liabilities and equity in accordance with the substance of the contractual arrangement. At the date of issue, the fair value of the liability component is estimated using the prevailing market interest rate for a similar nonconvertible instrument. This amount is recorded as a liability on an amortised cost basis until extinguished upon conversion or at the instrument's maturity date. The equity component is determined by deducting the amount of the liability component from the fair value of the compound instrument as a whole. This is recognised and included in equity, net of income tax effects, and is not subsequently remeasured.

iv) Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies set out above.

v) Financial liabilities

Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

vi) Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company’s documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability. Fair value is determined in the manner described below.

vii) Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derivative financial instruments

The Company uses derivative financial instruments (primarily foreign currency forward contracts) to hedge its risks associated with foreign currency fluctuations relating to certain firm commitments and forecasted transactions. The significant interest rate risk arises from bank loans. The Company’s policy is to convert a proportion of its floating rate debt to fixed rates. The Company designates these as cash flow hedged of interest rate risk.

The use of financial derivatives is governed by Company’s policies approved by the board of directors, which provides written principles on the use of financial derivatives consistent with the Company’s risk management strategy. The Company does not use derivative financial instruments for speculative purposes.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit or loss depends on the nature of the hedge relationship. The Company designates certain derivatives as either hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedges), hedges of highly probable forecast transactions or hedges of foreign currency risk of firm commitments (cash flow hedges), or hedges of net investments in foreign operations.

The fair value of hedging derivatives is classified as a non-current asset or a non-current liability if the remaining maturity of the hedge relationship is more than 12 months and as a current asset or a current liability if the remaining maturity of the hedge relationship is less than 12 months. Derivatives not designated into an effective hedge relationship are classified as a current asset or a current liability.

i) Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value with changes in fair value recognised in profit or loss.

ii) Hedge accounting

The Company designates certain hedging instruments, which include derivatives, embedded derivatives and non-derivatives in respect of foreign currency risk, as either fair value hedges, cash flow hedges, or hedges of net investments in foreign operations. Hedges of foreign exchange risk on firm commitments are accounted for as cash flow hedges.

At the inception of the hedge relationship the entity documents the relationship between the hedging instrument and hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Company documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in fair values or cash flows of the hedged item.

Movements in the hedging reserve in equity are also detailed in the statement of changes in equity.

iii) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in profit or loss immediately, together with any changes in the fair value of the hedged item that is attributable to the hedged risk.

Hedge accounting is discontinued when the Company revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. The adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to profit or loss from that date.

iv) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss as part of other expenses or other income.

Amounts deferred in equity are recycled in profit or loss in the periods when the hedged item is recognised in profit or loss. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

Hedge accounting is discontinued when the Group revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss deferred in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was deferred in equity is recognised immediately in profit or loss.

v) Hedges of net investment in foreign operations

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in equity in the foreign currency translation reserve. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

Gains and losses deferred in the foreign currency translation reserve are recognised in profit or loss on disposal of the foreign operation.

Fair value

The fair values of financial assets and financial liabilities are determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices;
- the fair value of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions; and
- the fair value of derivative instruments, are calculated using quoted prices. Where such prices are not available use is made of discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives.

Revenue recognition

Revenue from sales is recognised when earned. Sales of goods are recognised when goods are delivered and title has passed.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Assets held under finance leases are recognised as assets at their fair value. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation under finance leases.

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. 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 years and it further excludes items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

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

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profit against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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 assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover or settle the carrying amount of it assets and liabilities.

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 Company intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax are recognised as an expense or income in the income statement, except when they relate to items credited or debited directly to equity, in which case the tax is also recognised directly in equity, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is taken into account in calculating goodwill or in determining the excess of the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over cost.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of assets, other than land and properties under construction, over their estimated useful lives, using the straight-line method, on the following basis:

Real estate	2–5%
Equipment	5–33%

The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Internally-generated intangible assets – research and development expenditure

Expenditure on research activities and product development is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from development is recognised if, and only if, all of the following conditions are met:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- the intention to complete the intangible asset and use or sell it;
- the ability to use or sell the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical and other resources to complete the development and to use or sell the intangible asset; and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally-generated intangible assets is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally-generated intangible asset can be recognised, development expenditure is charged to income statement in the period in which it is incurred.

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately.

Other intangible assets

Other intangible assets acquired in a business combination are identified and recognised separately from goodwill where they satisfy the definition of an intangible asset and their fair value can be measured reliably. The cost of such intangible assets is their fair value at the acquisition date.

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets acquired separately.

Other intangible assets include licensing agreements, customer contracts and customer relationships.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date the company 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 assets is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing 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 for which the estimates of future cash flows have not been adjusted.

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 recognised immediately in the income statement, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment is treated as a revaluation increase.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost prices of processed inventories are direct material costs, direct wages costs and a proportion of indirect processing costs while cost price for purchased inventories is the actual cost of acquisition. Cost is calculated using the "first in – first out" – basis (FIFO). Net realisable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits 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.

Provision

Provision is recognised when an enterprise has a present obligation as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Pension

The Company's defined benefit plan requires contributions to be made to a separate administrated fund. The amounts charged to operating profit, as part of staff costs, are the current service cost. The interest on pension plan liabilities and the expected return on assets are shown as a net amount of other finance costs or income. Actuarial gains and losses are recognised immediately in equity.

Pension plan assets are measured at fair value and liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a corporate bond of equivalent currency and term to the plan liabilities. The actuarial valuations are obtained at least triennially and are updated at each balance sheet date. The resulting defined benefit asset or liability, net of the related deferred taxation, is included in the balance sheet.

Contributions to other Company pension plans are charged to the profit and loss account, in the period vested. Additional details are given in note 25.

3. Subsidiaries

Subsidiaries at 31 December 2006.

	Place of registration and operation	Interest	Principal activity
Bakkavor London Ltd.	United Kingdom	100%	Management company
Bakkavor Acquisitions Ltd.	United Kingdom	100%	Holding company
Hitchen Foods Ltd.	United Kingdom	100%	Packaging and marketing of fresh produce
Laurens Patisseries Ltd.	United Kingdom	100%	Packaging and marketing of desserts
Bakkavor Jersey Ltd.	Jersey	100%	Holding company
Bakkavor Invest Ltd.	United Kingdom	100%	Holding company
Bakkavor Ltd.	United Kingdom	100%	Holding company
Bakkavor Foods Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
Katsouris Fresh Foods Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
Bakkavor Birmingham Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
Anglia Crown Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
New Primebake Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
Bakkavor Fresh Cook Ltd.	United Kingdom	100%	Preparation and marketing of fresh prepared foods
English Village Salads Ltd.	United Kingdom	95%	Packaging and marketing of fresh produce
International Produce Ltd.	United Kingdom	76%	Packaging and marketing of fresh produce
Cinquième Saison SAS Group	France	100%	Preparation and marketing of fresh prepared foods
Centrale Salades France SAS	France	100%	Preparation and marketing of fresh prepared foods
Crudi SAS	France	100%	Preparation and marketing of fresh prepared foods
Société Bretonne de Légumes Préparés SAS	France	100%	Preparation and marketing of fresh prepared foods
Bakkavor Overseas Ltd.	United Kingdom	100%	Import and exporter of machinery and equipment
Bakkavor Insurance (Guernsey) Ltd.	Guernsey	100%	Insurance and re-insurance
Bakkavor Properties Ltd.	United Kingdom	100%	Property managment
BV Negecos	United Kingdom	100%	Holding company
Geest European Marketing BV	Netherlands	100%	Holding company
Vaco BV	Belgium	100%	Preparation and marketing of fresh prepared foods
Geest (SA) (Pty) Ltd.	South Africa	100%	Preparation and marketing of fresh prepared foods
Bakkavor Asia Ltd.	United Kingdom	100%	Holding company
Bakkavor China Ltd.	United Kingdom	60%	Holding company

Bakkavör Group hf. also operates a finance branch in Switzerland to govern intercompany long-term liabilities and investments.

Amounts in thousands of GBP

4. Quarterly statements

	Q4 2005	Q1 2006	Q2 2006	Q3 2006	Q4 2006
Net sales	252,170	258,606	298,483	332,939	329,161
Cost of sales	(180,599)	(190,281)	(219,154)	(244,430)	(239,047)
Gross profit	71,571	68,325	79,329	88,509	90,114
Other operating income	12	5	5	4	10
Operating expenses	(50,447)	(49,470)	(46,367)	(56,270)	(59,943)
Share of profit (loss) in associates	(278)	(402)	(178)	(208)	470
Operating profit (EBIT)	20,858	18,458	32,789	32,035	30,651
Net finance costs	(9,764)	(10,452)	(12,888)	(13,922)	(10,098)
Profit before tax	11,094	8,006	19,901	18,113	20,553
Income tax	193	(1,976)	(5,681)	(2,866)	(4,714)
Profit from continuing operations	11,287	6,030	14,220	15,247	15,839
Discontinuing operation, net of tax	0	0	0	0	16,910
Profit for the period	11,287	6,030	14,220	15,247	32,749
EBITDA	28,427	27,307	40,720	40,411	39,324
EBITDA (including discontinuing operation)	28,427	27,307	40,720	40,411	60,623
EBITDA ratio	11.3%	10.6%	13.6%	12.1%	11.9%
EBITDA ratio (including discontinuing operation)	11.3%	10.6%	13.6%	12.1%	18.4%
Working capital provided by operating activities	29,998	18,421	33,177	31,202	59,964
Cash flow from operating activities	53,357	19,433	24,067	51,502	36,498
Free cash generated by operating activities	47,844	12,401	16,555	40,699	23,943

5. Business and geographical segments

The Company operates in seven countries with over 4,500 products in 17 categories.

The following table provides an analysis of the Company's sales by geographical market, irrespective of the origin of the goods/services:

	2006	2005
United Kingdom	1,122,731	669,374
Continental Europe	96,458	52,691
	1,219,189	722,065

The following table provides an analysis of the Company's sale by categories:

	2006	2005
"Hot eating"	488,531	340,199
"Cold eating"	500,547	267,386
Traded produce and Continental Europe	230,111	114,480
	1,219,189	722,065

The following table provides an analysis of the Company's operating profit (loss) by geographical market:

	2006	2005
United Kingdom (excluding discontinuing operation)	112,526	69,236
Continental Europe	1,407	(2,586)
	113,933	66,650

Amounts in thousands of GBP

6. Salaries

Salaries and salary-related expenses paid by the Company are specified as follows:

	2006	2005
Salaries	272,972	179,652
Related expenses	32,351	20,601
	305,323	200,253
Average number of employees	15,888	14,365

	Salary and board fee	Benefits	Bonus	Pension	Shares*
Lýdur Gudmundsson, Chairman	341	68		1	**826,209,416
Ágúst Gudmundsson, CEO	584	153	300	1	**826,209,416
Antonios P. Yerolemou, Board member	25			1	74,534,353
Ásgeir Thoroddsen, Board member	25			1	1,418,164
Erlendur Hjaltason, Board member	19			1	1,192,400
Hreinn Jakobsson, Board member	25			1	1,500,000
Panikos J. Katsouris, Board member	25			1	52,336,471
Gareth Voyle, former CEO of Bakkavor Invest Ltd.	2,051	129	708	32	

No options, warrants or other rights were granted during 2006 and no member of the Board or management holds such rights.

* in Icelandic Króna (ISK) and including are holdings of their spouses, dependent children, and companies owned by them, if any.

** Ágúst Gudmundsson and Lýdur Gudmundsson in total hold control of 826,209,416 shares through Exista B.V. and related parties.

7. Fees to Auditors

	2006	2005
Audit of financial statements	283	290
Review of interim financial statement	170	16
Other services	1,013	1,564
	1,466	1,870

8. Net finance costs

	2006	2005
Interest income	2,325	2,792
Dividend	9	0
Interest expenses and exchange rate adjustments	(49,694)	(31,061)
	(47,360)	(28,269)

Amounts in thousands of GBP

9. Income tax

	2006	2005
Current tax	17,936	10,502
Deferred tax (note 18)	1,690	(4,454)
	19,626	6,048

Reconciliation of effective tax rate:

	2006		2005	
Profit before tax	66,573		38,381	
Discontinuing operation, before tax	21,299		0	
	87,872		38,381	
Tax calculated at domestic tax rate	15,817	18.0%	6,909	18.0%
Effect of different tax rates of other jurisdictions	7,254	8.3%	2,301	6.0%
Tax effect of expenses that are not deductible	1,524	1.7%	308	0.8%
Tax exempt revenues	29	0.0%	(92)	(0.2%)
Equity transactions effecting taxes	0	0.0%	(1,290)	(3.4%)
Permanent differences for tax purposes	(1,085)	(1.2%)	260	0.7%
Utilisation of previously unrecongised tax losses/tax asset not recognised	(3,900)	(4.4%)	800	2.1%
Tax incentives not recognised in the income statement	0	0.0%	(1,300)	(3.4%)
Adjustments in respect of prior years	400	0.5%	(1,731)	(4.5%)
Other changes	(413)	(0.5%)	(117)	(0.3%)
	19,626	22.3%	6,048	15.8%

10. Discontinued operation

A fire, as previously disclosed, at the Barton site destroyed substantial part of the facility. The decision was made not replace the assets in question or other assets affected as result of the fire. The operation was therefore discontinued in this facility. The insurance claim reimbursement, in excess of book value, amounts to GBP 21.3 million.

Insurance reimbursement in excess of book value	21,299
Tax expense	(4,389)
	16,910

11. Earnings per share

The calculation of earnings per share is based on the following data:

	2006	2005
Net profit for the 12 months ended 31 December attributable to shareholders	67,617	31,986
Total average number of shares outstanding during the period (in million)	1,960	1,615
Earnings per share (GBP pence)	3.4	2.0

Amounts in thousands of GBP

12. Goodwill and other intangible assets

	Goodwill	Licensing agreements	Customer contracts	Total
Cost at 1 January 2006	560,225	333	5,165	565,723
Additions and assessment changes in fair value during the year	147,781	0	1,639	149,420
Amortisation during the year	0	(333)	(882)	(1,215)
At 31 December 2006	708,006	0	5,922	713,928
Carrying amount:				
At 31 December 2006	708,006	0	5,922	713,928

The Company tests goodwill annually for impairment, or more frequently if there are indications that goodwill might be impaired.

The recoverable amounts of the cash generating units are determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rates, growth rates and expected changes to selling prices and direct costs during the period. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the cash generating units. The growth rates are based on industry growth forecasts. Changes in selling prices and direct costs are based on past practices and expectations of future changes in the market.

The Company prepares cash flow forecasts based on actual operating results and derived from the most recent financial budgets approved by management for the next five years. Cash flows for future periods are extrapolated using a 2 per cent growth rate. This rate does not exceed the average long-term growth rate for the relevant markets. A pre-tax discount rate of 12 per cent has been used in discounting the projected cash flows.

Licensing agreements and customer contracts have finite useful lives, over which the assets are amortised. These intangible assets will be amortised on a straight line basis over their useful lives.

The amortisation charge for each period is recognised as expense on the following basis:

Licencing agreements	18 months
Customer contracts	4–10 years

13. Property, plant and equipment

	Real estate	Equipment	Total
Cost at 1 January 2006	57,177	257,084	314,261
Accumulated depreciation at 1 January 2006	(5,733)	(40,630)	(46,363)
Book value at 1 January 2006	51,444	216,454	267,898
Acquisitions	13,230	22,572	35,802
Additions in 2006	8,677	31,202	39,879
Disposals in 2006	(811)	(598)	(1,409)
Depreciated 2006	(3,422)	(34,147)	(37,569)
Exchange differences	(423)	(420)	(843)
Book value at 31 December 2006	68,695	235,063	303,758

Insurance value of property, plant and equipment at year end amounts to GBP 744.7 million.

Depreciation and impairment in the Income Statement is specified as follows:

	2006	2005
Depreciation included in Cost of sales in the Income Statement	24,509	16,331
Depreciation included in Operating expenses in the Income Statement	7,301	3,098
Impairment included in Discontinued operation in the Income Statement	5,759	0
	37,569	19,429

Amounts in thousands of GBP

14. Interest in joint ventures and associates

Joint ventures and associates at 31 December 2006.

	Place of registration and operation	Interest	Principal activity
Geest QV Ltd.	United Kingdom	55.0%	Marketing of fresh produce
Creative Food Group Ltd.	China	40.0%	Produce and manufactures salad products
Fram Foods hf.	Iceland	30.5%	Manufactures consumer packaged seafood

15. Inventories

	31.12. 2006	31.12. 2005
Raw material and packaging	30,076	22,493
Work in progress	979	1,101
Finished goods	4,712	8,245
	35,767	31,839

Insurance value of inventories at the end of the period amounts to GBP 31.2 million.

16. Other financial assets

Trade and other receivables:

	31.12. 2006	31.12. 2005
Nominal value of trade receivables	142,767	129,333
Allowance for doubtful accounts	(3,131)	(4,822)
Pension asset (note 25)	17,700	7,500
Other receivables	64,131	48,040
	221,467	180,051

The directors consider that the carrying amount of trade and other reveivables approximates their fair value.

Cash and cash equivalents:

Bank balances and cash comprise cash and short-term deposits. The carrying amount of these assets approximate their fair value.

Amounts in thousands of GBP

17. Share capital

Share capital is registered in Icelandic króna (ISK) and is 2,157,888,219 ISK as required by the articles of association. At year end, the company's own shares amounted to 1,154,000 ISK.

Total share capital at year end according to the financial statements was GBP 14.9 million, as follows:

Total share capital	14,932
Own shares	(8)
	14,924

Changes in share capital are as follows:

Share capital at 1 January 2006	10,813
Changes during the year	4,111
Share capital at 31 December 2006	14,924

18. Deferred income tax asset and liability

	Deferred tax asset	Deferred tax liability	Total
At 1 January 2006	2,080	(24,957)	(22,877)
Arising on acquisition	0	(2,358)	(2,358)
Computed income tax for the year 2006	1,582	(21,208)	(19,626)
Income tax payable in 2006	135	17,801	17,936
Deferred tax movement associated with pension asset movement	0	(2,515)	(2,515)
Income tax asset (liability) at 31 December 2006	3,797	(33,237)	(29,440)

19. Dividends

The Annual General Meeting of Bakkavör Group, held on 24 March 2006, resolved to pay a dividend of 25% of nominal share value to shareholders. This corresponds to ISK 0.25 per share. Dividends were paid on 25 April 2006.

20. Non-current liabilities

	31.12. 2006
Borrowings in GBP	711,856
Borrowings in USD	3,678
Current maturities of non-current liabilities	(33,094)
	682,440

The borrowings are repayable as follows:

2007	33,094
2008	34,482
2009	161,172
2010	330,013
2011	155,757
Later	1,016
	715,534

Borrowings in total of GBP 542.3 million are secured over certain of land and buildings of the Company.

Amounts in thousands of GBP

21. Derivative financial instruments

The Company utilises currency derivatives to hedge significant future transactions and cash flows. At the balance sheet date, the total notional amount of outstanding forward exchange contracts to which the Company is committed amounts to GBP 26.0 million.

The Company uses interest rate swaps to manage its exposures to interest rate movements on its bank borrowings. At the balance sheet date, the total notional amount of outstanding interest rate swaps amounts to GBP 411.5 million.

22. Mortgages and commitments

Operating lease commitments

The future minimum lease payments under non cancellable operating leases are as follows:

	31.12. 2006
Not later than 1 year	10,531
Later than 1 year and not later than 5 years	28,942
Later than 5 years	57,162
	96,635

Capital commitments

Capital expenditure contracted for, but not provided for in these accounts, amounted to GBP 7.8 million.

Purchase commitments

The Company has purchase commitments for the next 12 months to guarantee supply and price in the amount of GBP 8.7 million.

23. Contingent liabilities

There are a number of legal claims or potential claims against the Company, the outcome of which cannot at present be foreseen. Provision has been made for all liabilities which are expected to materialise.

At 31 December the Company has granted its subsidiaries and associates guarantees amounting to GBP 25.3 million.

Amounts in thousands of GBP

24. Acquisitions

The following table sets out the book values of the identifiable assets and liabilities acquired and their fair value to the Company:

	Laurens Patisseries Ltd.	New Primebake Ltd.	Other acquisitions	Total
Tangible assets	25,835	4,695	5,272	35,802
Inventories	999	819	2,544	4,362
Debtors	10,795	2,720	3,331	16,846
Cash	0	162	0	162
Total assets	37,629	8,396	11,147	57,172
Bank loans	(8,099)	0	0	(8,099)
Bank overdrafts	(1,706)	0	(1,105)	(2,811)
Taxation	(1,468)	(1,062)	709	(1,821)
Other creditors	(9,076)	(5,233)	(14,950)	(29,259)
Deferred taxation	(2,070)	(288)	0	(2,358)
Total liabilities	(22,419)	(6,583)	(15,346)	(44,348)
Net assets	15,210	1,813	(4,199)	12,824
Joint venture reclassified	0	0	3,178	3,178
Goodwill	115,614	16,708	16,465	148,787
Other intangible assets	0	1,639	0	1,639
	130,824	20,160	15,444	166,428
Satisfied by:				
Shares issued	30,000	0	0	30,000
Direct costs relating to acquisition	824	600	194	1,618
Cash consideration	100,000	19,560	3,250	122,810
	130,824	20,160	3,444	154,428

Net cash outflows and deferred payments in respect of the acquisition comprises of:

	Laurens Patisseries Ltd.	New Primebake Ltd.	Other acquisitions	Total
Cash consideration	(100,824)	(20,160)	(3,444)	(124,428)
Cash at bank and in hand acquired	(1,706)	162	(1,105)	(2,649)
Deferred payments	0	0	(12,000)	(12,000)
	(102,530)	(19,998)	(16,549)	(139,077)

In accordance with the relevant IFRS standard, the Company has carried out an assessment of the fair value of the assets and liabilities of each of the businesses and companies acquired in 2006. This assessment has established the fair values of the tangible assets as well as the intangible assets and inventories. The difference between the sum of the fair values less liabilities and the purchase price paid is accounted as goodwill at the time of acquisition, and is subject to an annual impairment test. The assessments have been carried out with the assistance of outside experts.

As permitted by IFRS 3 *Business combinations* the assessment of the fair value of the net assets is provisional up to one year from the date of acquisition.

All acquisition have been accounted for by applying the purchase method.

If the acquisition of Laurens Patisseries Ltd. had been completed on the first day of the financial year, the Company's operating profit for the period would have been GBP 5.1 million higher.

If the acquisition of New Primebake Ltd. had been completed on the first day of the financial year, the Company's operating profit for the period would have been GBP 1.1 million higher.

If other acquisitions had been completed on the first day of the financial year, the Company's operating profit for the period would have been GBP 1.4 million lower .

The operations of all acquired companies are integrated into the Company's current structure from the date of acquisition, information on results after date of acquisition until Balance Sheet date are therefore not available.

Amounts in thousands of GBP

25. Pension

The Company operates a number of pension schemes in the UK and overseas. These schemes are either trust or contract based and have been set up in accordance with appropriate legislation. The assets of each of the pension schemes are held separately from the assets of the Company.

In the UK, the two main schemes, one a defined contribution scheme and the other a funded defined benefit scheme are open to employees joining the Company (full time or part time).

Pension costs charged in arriving at profit on ordinary activities before taxation were:

	2006
UK defined benefit plan net charge	(1,900)
UK defined contribution plan net charge	(467)
Overseas net charge	(226)
	(2,593)

No amounts were owed at the year end for the defined contribution scheme.

Defined benefit scheme

The valuation used for IAS 19 disclosures has been used upon the latest full actuarial valuation at 31 March 2004 and updated by the actuaries to take account of the requirements of IAS 19 in order to assess the assets and liabilities of the scheme at 31 December 2006.

The fair value of the scheme's assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the scheme's liabilities, which are derived from cash flow projections over long periods and thus are inherently uncertain, were:

	31.12.2006	
	Expected rate of return	Estimated bid value
UK equities	8.0%	83,200
Overseas equities	8.0%	33,900
Corporate bonds	5.1%	19,000
UK government bonds	4.6%	6,400
Property	6.2%	14,100
Cash	4.0%	1,700
		158,300
Present value of scheme liabilities		(140,600)
Surplus in scheme		17,700
Related deferred taxation liability		(5,300)
Net pension asset		12,400

The assumptions used by the actuary are the best estimates chosen from a range of possible actuarial assumptions which, due to the timescale covered, may not necessarily be borne out in practice.

	31.12.2006
Rate of increase in salaries	4.5%
Rate of increase for pensions in payment and deferred pensions	3.0%
Expected return of scheme assets	7.3%
Discount rate	5.2%
Inflation assumption	3.0%

Amounts in thousands of GBP

The amount charged to the Company's operating profit under IAS 19 of 1.6 million is analysed as follows:

	2006
Current service cost	(4,700)
Interest on pension scheme liabilities	(6,400)
Expected return on assets in the pension scheme	9,500
	(1,600)

Analysis of the amount recognised in the income statement:

	2006
Gain on assets	4,900
Experienced gain on liabilities	200
Gain on change of assumptions (financial and demographic)	4,100
Actuarial gain	9,200

Analysis of the movement in the surplus/(deficit) in the scheme during the year:

	2006
Surplus in the scheme at 1 January 2006	7,500
Contributions paid	2,600
Current service cost	(4,700)
Net financial return	3,100
Actuarial gain	9,200
Surplus in the scheme carried forward	17,700

History of experienced gains and losses:

	2006
Surplus between actual and expected return on scheme assets	4,900
% of scheme asset at the end of the year	3.1%
Experience gain on scheme liabilities	200
% of scheme liabilities at end of the year	0.1%
Actuarial gain recognised in statement of recognised income and expense	9,200
% of scheme liabilities at the end of the year	6.5%

26. Other matters

The Company has a GBP 55 million multi currency credit revolving facility (RCF). At 31 December GBP 27.9 million were available against the RCF.

The Company has purchased a business interruption insurance to the amount of GBP 1,098 million.

Amounts in thousands of GBP

27. Related party transactions

The following transactions were carried out with related parties:

Tjarnargata 35 ehf.

Rent:	2006
Tjarnargata 35 ehf.	47

Tjarnargata 35 ehf. is owned by Ágúst Gudmundsson, CEO and Lýdur Gudmundsson, Chairman of the Board of Bakkavör Group hf.

Katsouris Brothers Ltd.; Katsouris family; AP Yerolemou and Others

Sales of goods and services:	2006
Katsouris Brothers Ltd.	100

Purchases of goods and other services:	
Katsouris Brothers Ltd.	5,889
Katsouris family	147
	6,036

Rent:	
AP Yerolemou and Others	141

Katsouris Brothers Ltd. is amongst others owned by Panikos J. Katsouris and Antonios P. Yerolemou, Board members of Bakkavör Group hf.

AP Yerolemou and Others is amongst others owned by Panikos J. Katsouris and Antonios P. Yerolemou, Board members of Bakkavör Group hf.

Joint ventures

Sales of goods and services:	2006
Sales to joint ventures	1,206

Purchases of goods and other services:	
Purchases from joint ventures	316

The above transactions were carried out on commercial terms

28. Events after the Balance Sheet date

There have been no material post Balance Sheet events which would require disclosures or adjustment to the 31 December 2006 Consolidated Financial Statements.

The Consolidated Financial Statements were approved by the Board of Directors and authorised for issue on 31 January 2007.

Amounts in thousands of GBP

Glossary of general terms

This glossary of some specific financial and business terms used in this year's report is not exhaustive and many of the definitions have been interpreted from a Bakkavör Group perspective and so may not be pertinent to other businesses or countries.

ACNielsen
An international marketing research firm.

Actuarial valuation
Professional assessment of the funding position of a company's pension scheme, based on assumptions regarding future events (including average lifespan of members, returns on the different investment types etc).

All-China Women's Federation
An organisation of women set up in 1949 to represent and safeguard the rights and interests of women.

Amortisation
Depreciation of an intangible asset – the cost of goodwill spread over the number of years which are judged to benefit.

Associate / Associated company
Entity over which Bakkavör Group has significant influence and that is neither a subsidiary nor a joint venture. Significant influence means the power to participate in the financial and operating policy decisions of the investee but not to have control or joint control over those policies.

Basis point
One hundredth of a percentage point (0.01%), used in quoting movements in interest rates or yields on securities.

Book value
The net value of assets or liabilities (cost, less any amounts written off) held in the books of account at a point in time.

Bond
A certificate of debt issued to raise funds. Bonds typically pay a fixed rate of interest and are repayable at a fixed future date.

British Retail Consortium (BRC)
Trade association representing retailers in the UK.

CAGR (Compound Annual Growth Rate)
The year-over-year growth rate over a specified period of time.

Capital commitment
The situation where a company has contractually agreed to undertake some capital expenditure before the period end, but the money has not yet been spent nor the asset received.

Capital expenditure (Capex)
Payment for acquisition of a longer-term asset, e.g. buildings, machinery.

Cash flow
A measure of the actual cash generated by the business rather than accounting profit. Free cash generated by operating activities is defined as the amount of cash generated after meeting all its obligations for interest, tax and after investments in tangible assets.

Competition Commission
An independent UK public body established by the Competition Act 1998. It conducts in-depth inquiries into mergers, markets and the regulation of the major regulated industries. www.competition-commission.org.uk

Consumer Price Index (CPI)
A basket of goods/services whose price is calculated monthly and which provides a broad measure of the level of inflation.

Continuing
Describes the ongoing element of a company's results and excludes the results of disposed or discontinued activities.

Corporate governance
The code of conduct by which the Group is directed and controlled.

CNY
Chinese yuan. The ISO currency code for the China Renminbi (RMB).

Datamonitor
Business information company, specialising in industry analysis.

Deferred tax
See Income tax.

Depreciation
The systematic allocation of the depreciable amount of an asset over its useful life. For an intangible asset, this is generally referred to as amortisation.

Derivatives
Financial instruments (for Bakkavör Group, mainly foreign currency forward contracts) to hedge risks associated with foreign currency fluctuations.

Dividends
The proportion of a company's profits paid to shareholders, usually declared as a dividend per share.

Earnings
Profit available to ordinary shareholders, after all operating expenses, interest charges, taxes and preference dividends have been deducted.

Earnings per share (EPS)
Earnings divided by the number of ordinary shares in issue.

EBIT
Earnings (as above) Before Interest and Tax.

EBITDA
Earnings (as above) Before Interest, Tax, Depreciation and Amortisation.

Effective tax rate (%)
See Income tax.

Equity ratio
Used to describe the relationship between debt and equity. Calculated by dividing the company net debt by the shareholders' equity.

Ethical Trading Organisation (ETI)
An alliance of companies, non-governmental organisations and trade unions working to promote and improve the implementation of corporate codes of practice which cover supply chain working conditions. www.ethicaltrade.org

European Commission
The European Commission (formally the Commission of the European Communities) is the executive body of the European Union. www.europa.eu.

Eurostat
The Statistical Office of the European Communities (Eurostat).

Executive Directors
Board Directors who are also full-time employees of the company and have management responsibility.

FESE (Federation of European Securities Exchanges)
The foremost aim of FESE is to represent and promote the common interests of securities exchanges in Europe. www.fese.be

Financial Supervisory Authority (FSA)
Icelandic state authority whose role is to ensure that the activities of parties (e.g. financial institutions) subject to supervision are in accordance with laws and regulations and consistent with sound and proper business practices. www.fme.is

Food Standards Agency (FSA)
An independent UK Government department set up by an Act of Parliament in 2000 to protect the public's health and consumer interests in relation to food. www.food.gov.uk

Functional currency
A company's working currency. For Bakkavör Group, GBP.

GBP
Pound sterling. The UK's official currency.

GDP
Gross Domestic Product.

GfK
A worldwide market research organisation.

Goodwill
The excess of the cost of acquisition over the company's interest in the fair value of the identifiable assets and liabilities at the date of acquisition.

Hedging
Reducing exposure to risk of loss resulting from fluctuations in exchange rates, commodity prices, interest rates etc. Typical tools include forward foreign exchange contracts and interest rate swaps.

IGD (Institute of Grocery Distribution)
Research organisation for the UK food and grocery industry. www.igd.com

Impairment
Impairment write-downs are made when the carrying amount of an asset or a cash generating unit exceeds the higher of the estimated value in use and the fair value less costs of disposal.

IMRG
Internet Measurement Research Group - industry body for global e-retailing. www.imrg.org

Income tax
The tax on company profits or losses. This is influenced by the tax rate applicable to the size of the company and the level of profits and any differences between accounting treatment and tax treatment. This gives rise to the effective tax rate, which expresses tax payable as a percentage of profit. Deferred tax relates to the tax that may be payable in future as a result of the differences between accounting treatments and tax treatments adopted to date.

International Financial Reporting Standards (IFRS)
Set of accounting standards, currently issued by the International Accounting Standards Board (IASB). Many of the standards forming part of IFRS are known by the older name of International Accounting Standards (IAS).

International Labour Organisation (ILO)
The United Nation's specialised agency which seeks the promotion of social justice and internationally-recognised human and labour rights. www.ilo.org

International Obesity Taskforce (IOTF)
The IOTF is a research-led think tank and advocacy arm of the International Association for the Study of Obesity. www.iotf.org

ISK
Icelandic Króna. Iceland's official currency.

Joint venture
Contractual arrangement whereby a company and other parties undertake an economic activity that is subject to joint control, i.e. the strategic financial and operating policy decision relating to activities requires the unanimous consent of the parties sharing control.

Leatherhead Food International
An international research, information and training centre for the food and drinks industry.

LIBOR
London Inter Bank Offered Rate – the rate of interest at which banks will lend in the inter-bank market.

Liquidity
The proportion of cash or cash equivalents in a company's assets. For shares, the ability to trade on an open market.

Management Board
Bakkavör Group's executive operational team.

Market capitalisation
Value at current market prices of a company's share capital. Calculated by multiplying current share price by the number of shares in issue.

Minority interests
Subsidiary undertakings which are not 100%-owned by the parent company.

Mintel
Global supplier of consumer, media and market research.

Net debt
The excess of the company's borrowings over its cash and liquid resources.

Non-government organisation (NGO)
Any local, national, or international organisation whose members are not employed by a government.

NOREX Alliance (NOREX)
An alliance between the Nordic and Baltic exchanges in Denmark, Finland, Estonia, Iceland, Norway, Latvia and Sweden giving single access to the Nordic and Baltic equity markets. www.norex.com

OFT (Office of Fair Trading)
UK's competition authority which enforces consumer protection law and competition law, reviews proposed mergers and conducts market studies. www.oft.gov.uk

OMX The Nordic Exchange
Bakkavör Group is listed on OMX The Nordic Exchange, formerly Iceland Stock Exchange, acquired by OMX the Nordic Exchange in October 2006. www.icex.is

ONS (Office for National Statistics)
The government department that provides UK statistical and registration services. www.statistics.gov.uk

Organic growth
Growth achieved by increasing the scale of business by internal activities as opposed to acquiring other established businesses.

Price sensitive information (PSI)
Any information which if in the public domain could cause the share price to move.

Quick ratio
A measure of a company's liquidity and ability to meet its obligations. Quick ratio (or acid test ratio) is obtained by subtracting inventories from current assets and then dividing by current liabilities.

Record date
The date on which a shareholder should be entered on the company's share register to qualify for a dividend payment.

Renminbi (RMB)
The currency of the People's Republic of China, the basic unit of which is the yuan (CNY).

Retail Price Index (RPI)
A basket of goods/services whose price is calculated monthly and which provides a broad measure of the level of inflation.

SAXESS
Electronic trading system used on the OMX Exchanges (Copenhagen, Stockholm, Helsinki, Iceland, Tallinn, Riga and Vilnius Stock Exchanges).

Shareholder value
The value a company generates for shareholders in terms of both dividends and growth in the company's share price.

Subsidiary/Subsidiary undertaking
Businesses in which all or the majority of their share is owned and where management control can be exercised.

TNS Worldpanel (Taylor Nelson Sofrès)
Global market information group. www.tnsinfo.com

WHO (World Health Organisation)
A specialised agency of the United Nations that acts as a coordinating authority on international public health.

Working capital
The cash that the business has tied up in funding day to day operations – this includes the value of the stock it holds, the amount owed to it in trade debts by customers less any amounts that are funded by our suppliers/creditors in the form of our trade debts to them.

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Product definitions

Convenience salads
As a rule of thumb, these salads do not contain salad leaves and are 'dressed' e.g. with vinaigrette, mayonnaise or other sauces. Traditional convenience salads are potato salad and coleslaw. Some of our newer salads include pasta, rice, couscous, cracked bulgur wheat, beans and lentils. These salads are usually served as accompaniments but are also popular as lunchtime snacks.

Desserts
We specialise in premium desserts such as carrot cake, cheesecakes, fruit tarts, crumbles and trifles. Following our recent acquisitions we now make profiteroles, cream cakes, chocolate eclairs, sundaes, scones, doughnuts ...

Dips
Dips are sauces suitable for dipping! Dips generally come in two key formats: single pots of the most popular flavours and 'multipacks'– typically four smaller portions for parties. Dips can be vegetable-based such as guacamole (avocado) and salsa (fresh tomatoes and chilli peppers) or made with mayonnaise or sour cream flavoured with fresh ingredients (e.g. cheese and chive; garlic and onion). Traditional Mediterranean recipes include taramasalata (made with cod roe), tzatziki (made with fresh cucumber) and houmous (made with chick peas).

Dressings
Our fresh dressings range has been developed to complement our leafy salads. Recipes include traditional French vinaigrette, honey and mustard, balsamic vinegar and garlic, and yoghurt and mint.

Ethnic snacks
Our ethnic snacks include traditional snacks and accompaniments such as Chinese spring rolls and dim sum or Indian bhajis, samosas and pakoras.

Leafy salads
These salads are predominantly mixes of different salad leaves. The leaves are carefully selected for flavour, colour and texture and are cut, washed, dried and packed so that the salad is ready to eat. Bakkavör Group sources over 40 different varieties of salad leaves and fresh herbs. For salad recipe ideas log on to: www.bringonthesalads.com or: www.watercress.co.uk for recipes that include watercress, one of the 'super foods' that we sell.

Pasta
We specialise in making unfilled pasta which can be split into two main groups: long and short shapes. Long shapes include spaghetti, linguine, tagliatelle and fettuccine. Short shapes include fusilli (bows), spirale (twists), ricciole (curls) and penne (quills).

Pizza
Whatever the type of base or range (thin or thick, Italian or American) the most popular pizza is cheese and tomato. However, our fresh pizzas are now topped with a huge variety of ingredients: smoked salmon, sundried tomatoes, chorizo, marinaded olives, bell peppers, artichokes, prosciutto and a whole host of different cheeses. (Bakkavör Group alone buys over 30 different types of cheese).

Prepared fruit
Fruit salads make great lunchtime snacks or healthy desserts. Most of our salads are fruit mixes and include mango, various types of melon, passion fruit, pineapple, kiwi, apple, citrus, blueberries, grapes, etc.

Prepared vegetables
Most of our prepared vegetable products are ready to reheat in the oven or microwave – or on the BBQ. We also have a range of prepared potatoes.

Ready meals
Ready meals are pre-cooked complete meals or accompaniments. The majority of these products are for one or two persons although there are also larger packs for families. In the UK, the most popular ready meal cuisines are Indian, traditional British and Italian, followed by Oriental.

Our extensive range includes recipes from around the world: prawn creole with rice, chicken with goat's cheese and peppers, beef in plum sauce, Thai yellow chicken and prawn laska, coq au vin, chicken karai balti, BBQ ribs, and Lincolnshire sausages with mushrooms and gravy.

Ready to cook meals
Ready to cook meals are essentially 'ready meals' with the key difference that many of the ingredients are still raw, i.e. the meal has to be cooked rather than just reheated.

Soups and sauces
Tomato and basil, carrot and coriander, broccoli and stilton are popular fresh soup recipes throughout the year. In winter, we also launch seasonal specials such as spicy parsnip, pea and ham, Scotch broth, pumpkin and ginger; and in summer, minted pea, asparagus, watercress and gazpacho.

Most of our sauces are developed especially to eat with pasta and include traditional Italian recipes. We also make fresh sauces for stir fries.

Speciality bread
Our breads are chilled, pre-cooked breads filled or topped with fresh butter, mixed mainly with garlic or cheese. The main style of bread we bake is baguettes but we also top Italian-style breads with olives, herbs and sun-dried tomatoes. The breads need to be put into the oven to finish off the baking and are best served warm.

Stir fries
Take a wok or a heavy-based frying pan, heat up some oil and stir in some fresh vegetables and bean sprouts for a healthy meal or accompaniment. We grow our own bean sprouts and then add fresh colourful prepared vegetables to take away the chore of chopping.

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