Financial statements **2006**

DRIVEN BY DRIVES

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Board of directors' report

Board of directors' report 1 January–31 December 2006

Year 2006

During 2006 Vacon continued its profitable growth in the AC drive market. The company strengthened its market position, increased its revenues and improved its profit. The earnings per share for the fiscal year was EUR 1.04.

According to Vacon's estimations, the AC drive market grew by some seven to nine per cent in 2006. High energy prices and increasing automation boosted the total market. Demand for AC drives is very strong at the moment and the outlook for 2007 is positive.

Vacon raised its market share on all continents. The company's factory in China started to make a profit during the first half of the year. The business outlets established in India, Australia and Thailand coupled with the factory in China form a strong foundation for developing Vacon's business in Asia. The cooperation agreement signed in November with multinational Converteam opens up the market for example in the oil and gas industries.

During the past year the company expanded its product range up to 5 MW. Development work on next generation products continued as planned.

The company's profitability improved despite the rise in global market prices for certain materials such as copper and steel.

Global position

In 2006 69.6 % of Vacon's revenues came from Europe (71.1 % in 2005), 20.3 % (19.4 %) from North America, 8.5 % (7.8 %) from Asia and Australia and 1.6 % (1.7 %) from elsewhere. Vacon's sales in Asia and Australia grew 35 %. The main factor in this growth was China. The investments made in developing the sales network in this area are expected to strengthen Vacon's market position in the future. Revenues in North America rose 30 % mainly through brand label customers. Growth in Europe was 22 %.

Vacon's revenues by distribution channel in 2006 were as follows: own direct sales 41 % (41 %), distributors 13 % (15 %), machine and equipment manufacturers 24 % (22 %), and brand label customers 22 % (22 %). Orders received by the Group in 2006 totalled EUR 197.4 (156.7) million. The Group's order book at the end of the year stood at EUR 29.7 (18.8) million.

Record profit and strong balance sheet

Consolidated revenues in 2006 rose 24.3 % to EUR 186.4 million (EUR 149.9 million in 2005). The parent company Vacon Plc had revenues of EUR 159.9 million. The consolidated profit before taxes was EUR 22.7 (17.7) million and the profit for the financial period was EUR 16.1 (12.2) million. Earnings per share (EPS) rose to EUR 1.04 (0.79). Key factors in the growth in revenues and profit were Vacon's extensive, competitive product offering and the strengthening of the Group's own sales network and of production operations.

The Group's cash flow from operations was EUR 15.1 (9.7) million positive. The Group was able to finance its growth from income. The consolidated balance sheet total was EUR 86.9 million. Vacon's equity ratio remained almost unchanged at 61.7 % (56.8 %). Net gearing was -16.6 % (-18.3 %). The return on investment increased to 45.1 % (40.8 %), and the return on equity was 33.7 % (30.5 %).

Key figures:

	2006	**2005**	**2004**
Revenues, MEUR	186.4	149.9	128.6
Operating profit, MEUR	23.1	18.1	15.9
Operating profit, % of revenues	12.4	12.1	12.4
Return on equity, %	33.7	30.5	31.3
Equity ratio, %	61.7	56.8	56.2

Strategy

Vacon continues with its strategy of profitable growth. Vacon has the determination and the ability to grow as a global AC drive supplier. Vacon stands out from its main competitors by focusing one hundred per cent on AC drives.

The company's financial targets are annual growth in revenues of 15–20 % and achieving an operating profit (EBIT) of more than 14 % of revenues by 2010. Vacon has also set a target for return on equity (ROE) of more than 30 %. Growth is expected to take place mainly organically. Vacon aims to achieve these targets by strengthening the company's main operations on all continents, improving the product offering and making it more customer-oriented, and increasing investments in the customer interface.

The company's strategic choices are focusing on AC drives, strengthening the competitive edge through product leadership, a multi-channel sales network, and flexible, efficient operating methods. These are all being implemented globally, as close as possible to the customer.

The core competences are product development, product and application know-how, customer relations management, logistics and mass customization. Vacon aims at more comprehensive global management for major customers. In accordance with Vacon's international production strategy, products are customized as close as possible to the customer. Vacon is establishing a product development unit at the factory in China. This is to ensure that products are suitable for customers in this particular market area.

It is the policy of Vacon's Board of Directors to propose for approval by the Annual General Meeting a dividend consistent with the company's financial performance. The goal is to pay a dividend of about 50 % of the profit for the period. The level of dividend takes into account the financing required to expand operations.

Changes in corporate structure

During 2006 Vacon established subsidiaries in Australia and India. The company also opened a branch office in Bangkok, Thailand and closed the branch office in Singapore. These investments are expected to improve customer service and to boost growth in Vacon's sales in Asia already in 2007. After these additions Vacon's own sales network comprises 14 sales companies and two representative offices.

Vacon's holding in the Group's subsidiary Vacon Traction fell from 90 % to 19 % in a transaction in April 2006. Vacon Traction is not part of the Group's core business. In accordance with its strategy Vacon is focusing 100 % on AC drives. The transaction had no significant impact on the Group's result.

The associated companies Verteco Oy and Rotatek Finland Oy became part of a larger holding company through a share exchange towards the end of 2006, when Vacon's holding in the resulting holding company fell below 20 %. This arrangement had no impact on the Group's result.

Foreign branch offices

The company has branch offices in the United Arab Emirates and in Thailand.

Investments

Gross investments by the Group during 2006 totalled EUR 8.5 (6.6) million. Expenditure focused mainly on information systems, R &D testing systems and the new production line at Vacon's factory in Suzhou, China.

Financial instruments valued at fair value

Foreign currency forward contracts are valued in the financial statements at fair value. The principles used for this are described in more detail in the Accounting Principles and the Notes to the Financial Statements.

Preferred capital notes

The company has repaid all the preferred capital notes and the interest on them during the financial year.

Personnel structure and changes in organization

The number of Vacon personnel increased by 98 during 2006. At the end of December the Group employed 675 (577) people, of whom 447 (376) were in Finland and 228 (201) in other countries. The average number of personnel during 2006 was 618 (533). To even out the production load the Group makes use of contract labour, on average 58 (40) persons in 2006.

The number of personnel by function is as follows: sales and marketing 44 (50) %, production 39 (33) %, R&D 13 (13) %, and administration 4 (4) %. The average age of personnel was 35 (35) years. The average length of employment was 4.1 (4.1) years. Some 27 (26) % of personnel were women and 73 (74) % men. Personnel turnover was 7 (5) %.

Vacon restructured its corporate organization in February 2006. The restructuring aims to enhance the implementation of the strategy, speed up decision making, raise efficiency and improve cooperation between the different functions. Vacon now has a two tier management team structure. The Vacon Management Team meets monthly and its main tasks include defining strategic policies and monitoring and safeguarding the company's financial performance. In addition the company has an expanded management team, Vacon Extended Management Team, which meets 4-6 times a year and focuses on implementing the strategy and developing uniform operations for the Group worldwide.

Compensation

Vacon has a bonus scheme covering all personnel that uses different indexes for each function. The indexes used include the Group's revenues, operating profit, working capital and delivery reliability.

In January 2005 Vacon's Board of Directors decided to initiate a share bonus scheme to provide long-term motivation and commitment for the Group's management and key personnel. The share bonus scheme lasts three years. The Board decides each year on targets for revenues, result and turnover of working capital for each year, and these determine the size of the bonus in accordance with the terms of the scheme.

The total amount of salaries and other compensation in the financial year was EUR 25.3 (21.4) million.

Human resources management

Vacon's human resource strategy, which is derived from the company's business strategy, summarizes the priorities in human resources management. These are being a leader, performance management, internal communications and total wellbeing. Vacon's vision, strategy and values set the direction for all work activities. Vacon's people-oriented management stresses the importance of interactive skills, which are essential for creating good working conditions. Performance management aims at strengthening the company's strategy-based, goal-oriented operations. Everyday management is another important element in performance management. It is not just the professional skills of personnel that are important but also their mental, physical and social wellbeing.

Personnel development, skills development

Leadership has become an important area in the company's human resources strategy. The role of the Vacon manager is to coach. One of the steps taken by Vacon is to start specialist vocational education in management. New supervisory staff have also been trained using the 'supervisor's toolbox' course.

Development discussions are being extended to all personnel. The actual level achieved is almost 90 %. These discussions are used to set individual targets and action supporting the strategy, identify development needs and assess success in the previous period. The Management Team monitors the implementation of development discussions regularly.

Skills and training

Skills development is part of performance management. The training projects in the past year focused on supervisor activities, sales training, initial training and language training, and on training to support application information system projects.

Recruitment

Recruitment has been active during the past year. New personnel were taken on in all functions. Vacon also encouraged job rotation and about 30 people changed jobs within the company.

Wellbeing at work

The focus in the total wellbeing programme varies from year to year. In 2006 the theme was social wellbeing. To maintain mutual trust between the company and personnel it is necessary to pay attention to working conditions, job contents and the work of supervisory staff. The personnel survey conducted each year with an external research organization reveals the current situation and gives ideas for improving wellbeing at Vacon. The results of the 2006 job satisfaction survey show that employees consider Vacon to be a good employer. They are also aware of the company's goals. The survey results are used to draw up action plans for the individual departments.

Equal opportunities

Vacon has had an equal opportunities plan in use for some time and it is updated each year.

The assessment of the situation regarding equal opportunities at the work place required by the new equal opportunities act was carried out as soon as the new act came into force. The assessment examined how women and men were placed in different jobs and examined the differences in salaries between women and men.

Business principles relating to environmental aspects and environmental management systems

The products manufactured by Vacon, AC drives, save energy and play a part in achieving the objectives of sustainable development. Vacon's goal is to improve the ecofriendliness of its products throughout their lifecycle.

Vacon has an environmental management system certified by SGS-FIMKO that meets the requirements of the ISO 14 001 standard. The company is committed to identifying and complying with environmental legislation and regulations that affect its operations and is continuously developing its operations in this area. Vacon aims in all its activities to choose raw materials, working methods and processes that cause the minimum harm to the environment. The company arranges regular training to maintain the environmental skills of personnel. Environmental issues are not separate functions at Vacon but through the operations system belong to all areas of the company's business. The system creates the conditions for the company to achieve environmental goals and meet environmental requirements.

Major environmental aspects and improvements made

Vacon uses the Design for Environment check list in the concept phase of product design, which helps make more efficient use of materials and resources and minimize the use of substance that harm the environment. The check list also complies with the EU's ROHS directive (on the restriction of the use of certain hazardous substances in electrical and electronic equipment).

Level of environmental protection considering the nature and scope of operations

The company's normal operations do not pollute water or the soil. Vacon Group's production consumed about 8,600 m^3 of water in 2006. Vacon Group's production consumed about 9,700 MWh of energy in 2006.

The recycling of various waste is organized efficiently at the company's business locations. In 2006 more than 13 tonnes of production electronic waste was recycled and more than 200 tonnes of other waste such as paper and wood.

Board Report in relation to other environmental reporting

The Annual Report published by the company contains a corporate responsibility section that includes a part on the environment.

Research and development

R&D costs during the year were EUR 12.6 (10.8) million, or 6.7 % of the Group's revenues (7.2 %).

The company aims to bring new innovative products on to the market in the next few years. The product selection in the high-power equipment sector was expanded in 2006 from 3 MW to 5 MW. Expanding the power range increases Vacon's total offering in the low-voltage sector and is part of the Group's product leadership approach. Vacon unveiled the first of its new generation AC drives to customers during 2006.

Other events during the year

Multinational system supplier Converteam and AC drive manufacturer Vacon signed a global cooperation agreement. Under the agreement Vacon will supply AC drives to Converteam globally. The agreement is important for Vacon since it opens up the market for example in the growing oil and gas industries.

In January Vacon reopened its Chinese factory after a move to new premises with a floorspace of more than 5,000 m2 in Suzhou. The increase in production capacity is in response to the growth in demand mainly in the Asian and Far Eastern market. The extensions to the factory in Finland were commissioned in June in Vaasa. The extensions have a total floor area of about 7,100 m2. About half of this is used by Vacon and the remainder by DHL, which provides logistics services for Vacon.

Shares and shareholders

Vacon has a share capital of EUR 3,059,000, and this is divided into 15,295,000 fully paid shares. According to its Articles of Association, Vacon has a minimum share capital of one million (1,000,000) euros and a maximum share capital of four million (4,000,000) euros. Vacon has one share series with the trading code VAC1V. The share has a nominal value of EUR 0.20, and each share entitles the holder to one vote at the general meeting of shareholders.

In April 2006 parent company paid a dividend of EUR 6.2 million, or EUR 0.41 per share (52 % of the earnings per share in the 2005 financial year). During 2006 a total of 4,439,458 shares – 29 % of the share stock – with a value of EUR 101.0 million were traded on the stock exchange. The highest share price during the year was EUR 26.99 and the lowest EUR 17.70. The closing price on the last day in 2006 was EUR 26.1 and the company had a market capitalization of EUR 397.1 million. Vacon had 3,731 registered shareholders according to the shareholder register updated on 31 December 2006. The number of nominee registered shares and shares registered outside Finland totalled 27.5 % of the total share stock.

Own shares

Vacon's Annual General Meeting of Shareholders on 6 April 2006 authorized the Board of Directors to decide to purchase and dispose of the company's own shares. The Board did not exercise this authorization during 2006. On the basis of authorization in 2004, on 31 December 2006 Vacon Plc held a total of 81,572 of its own shares at an average price of EUR 12.39. Purchasing of the company's own shares has no major impact on the distribution of ownership or voting rights in the company. In consequence of the purchasing of the company's own shares, the number of shares with ownership and voting rights was 15,213,428 at the end of 2006.

Board of Directors and President

The members of the Board of Directors until the Annual General Meeting were Pekka Ahlqvist, Jari Eklund, Kalle Heikkinen, Mauri Holma, Jan Inborr and Veijo Karppinen. The AGM on 6 April 2006 re-elected the six members of the old Board of Directors, namely Pekka Ahlqvist, Jari Eklund, Kalle Heikkinen, Mauri Holma, Jan Inborr and Veijo Karppinen. The term of office for Board members continues until the end of the following Annual General Meeting of Shareholders. At its organization meeting after the AGM the Board re-elected Jan Inborr as its chairman and Veijo Karppinen as vice chairman. Stefan Wikman is secretary to the Board. Vacon's President throughout the financial year was Vesa Laisi. Heikki Hiltunen was appointed Executive Vice President as from 9 February 2006.

Auditors

In accordance with the decision of the Annual General Meeting, the company's auditors are the authorized public accountants KPMG Oy Ab and the principal auditor appointed by them is Pekka Pajamo, APA.

Risk management

Vacon has carried out an extensive survey of risks and examines its risk management every year. Several potential risks have been defined on Vacon's risk map, which may have an impact on future profitability and development. The most significant risks are listed here:

- The risk that Vacon's products or operations cause injury or damage to the personnel or property of customers or third parties and thus endanger the continuation of their business operations.
- The risk that Vacon's R&D fails or is delayed in its development projects for new products or that products are unable to meet new customer requirements in terms of a product's performance or price/quality ratio.
- The risk that an unexpected harmful event endangers the delivery capability of Vacon's factory in Vaasa.
- The risk that, due to an unexpected harmful event, their financial situation or their problems with capacity, Vacon's main suppliers, component and software suppliers, are unable to supply their products on time and in accordance with agreed quality criteria.
- The risk that, during the production process and testing, a quality defect is not noticed in a product, its components or software, resulting in a major increase in quality costs or the recall of all the supplied products.
- The risk that continuous competition and R&D investments by competitors in the frequency converter market cause greater selling price erosion than anticipated or even the loss of key Vacon customer accounts.
- The risk that as demand rises the global market prices for certain materials and components rise more sharply than expected.

The company's risk management policy is presented in more detail in the Risk Management section in the Notes to the 2006 Financial Statements.

Events after end of year

No major events have taken place after the end of the financial year.

Prospects for the near future

No significant changes have taken place in Vacon's market prospects. The state of the market is expected to remain favourable in 2007. The high level of energy prices and the growth in investments in automation boost the AC drive market. Based on market surveys Vacon estimates that the AC drive market is growing at an annual rate of 7–9 %.

Vacon's market share is rising in all major market areas. AC drive demand is forecast to increase in Europe and North America by more than 5 % and in Asia by much more than 10 %, with China and India the engines of growth. Investments in the growing markets in Asia and Russia will strengthen Vacon's global market position.

Vacon considers that potential risks to its financial performance in 2007 are possible problems that material suppliers may have with capacity, sharp changes in exchange rates, and increasing problems with the availability of key components.

The order intake has been strong during the final months of 2006 and the first month of 2007. Vacon forecasts that revenues in 2007 will grow by 15–20 % and that profitability will improve from 2006.

Board proposal for distribution of profit

At the end of the financial year the distributable equity of the parent company stands at EUR 37.7 million. The Board of Directors proposes to the Annual General Meeting of Shareholders to be held on 28 March 2007 that a dividend of EUR 0.65 per share be paid from the parent company's profit for the financial year 2006 of EUR 12.5 million and the remainder of the profit for the year be transferred to retained earnings. According to this proposal, a total of EUR 9.9 million would be paid in dividend.

No major changes have occurred in the company's financial position after the end of the financial year. The company's liquidity is good and in the opinion of the Board the proposed distribution of profit does not place the company's solvency at risk.

Consolidated financial statements

Key figures

	IFRS 2006	IFRS 2005	IFRS 2004	FAS 2003	FAS 2002
Per share data					
Earnings per share, EUR	1.04	0.79	0.71	0.50	0.43
Equity per share, EUR	3.42	2.78	2.39	2.11	1.78
Dividend per share, EUR *)	0.65	0.41	0.35	0.55	0.17
Dividend payout ratio % *)	62.57	52.12	49.31	109.32	39.60
Effective dividend yield % *)	2.5	2.3	3.0	5.6	2.3
Price/earnings ratio	25.1	22.2	16.6	19.5	17.2
Share price development					
Lowest during the year, EUR	17.70	11.85	9.95	6.70	5.60
Highest during the year, EUR	26.99	17.50	11.99	10.65	11.60
Closing price at end of year, EUR	26.10	17.50	11.78	9.80	7.40
Average price for the year, EUR	22.60	14.68	11.00	8.95	9.68
Market capitalization, MEUR	397.10	266.00	180.00	148.50	112.11
Trading volume, share	4,439,458	5,693,881	3,427,027	4,231,544	4,599,195
Trading volume, %	29.2	37.5	22.6	27.9	30.4
Adjusted average number of shares during the financial year **)	15,209,303	15,203,147	15,186,805	15,150,000	15,150,000
Number of shares at end of year **)	15,213,428	15,199,740	15,282,200	15,150,000	15,150,000

*) The 2006 dividend is the Board of Directors' proposal to the Annual General Meeting.
**) The average number of shares during the year was 15,209,303. The total number of shares outstanding was 15,213,428.

	IFRS 2006	IFRS 2005	IFRS 2004	FAS 2003	FAS 2002
Group's financial ratios					
Revenues, MEUR	186.4	149.9	128.6	112.3	97.5
Increase in revenues, %	24.3	16.6	14.5	15.2	7.7
Operating profit, MEUR	23.1	18.1	15.9	11.8	9.9
Increase in operating profit, %	27.6	13.8	N/A	19.2	-4.8
Operating profit as % of revenues	12.4	12.1	12.4	10.5	10.2
Profit before taxes, MEUR	22.7	17.7	15.9	11.7	9.8
Profit before taxes as % of revenues	12.2	11.8	12.4	10.4	10.1
Return on equity, %	33.7	30.5	31.3	26.1	26.2
Return on investments, %	45.1	40.8	38.6	31.7	30.4
Interest-bearing net liabilities, MEUR	-8.8	-7.9	-10.6	-6.2	-0.8
Net gearing (%)	-16.6	-18.3	-28.9	-19.1	-3.0
Equity ratio (%)	61.7	56.8	56.2	55.8	51.7
Gross capital expenditure, MEUR	8.5	6.6	4.6	4.8	4.7
Gross capital expenditure as % of revenues	4.6	4.4	3.6	4.3	4.8
Research and development costs, MEUR	12.6	10.8	9.8	8.9	7.1
Research and development costs as % of revenues	6.7	7.2	7.6	7.9	7.3
Personnel at the end of the period	675	577	469	436	426
Order book, MEUR	29.7	18.8	12.0	12.3	15.5

Calculation of key figures

Earnings per share =	$\dfrac{\text{Profit for the financial year attributable to equity holders of the parent company}}{\text{Adjusted average number of shares}}$
Equity per share =	$\dfrac{\text{Equity attributable to the equity holders of the parent company}}{\text{Adjusted average number of shares at the end of the year}}$
Dividend per share =	$\dfrac{\text{Dividend for the financial year}}{\text{Adjusted number of shares at end of year}}$
Dividend payout ratio =	$\dfrac{\text{Dividend for the financial year x 100}}{\text{Profit for the period attributable to equity holders of the parent company}}$
Effective dividend yield =	$\dfrac{\text{Dividend per share x 100}}{\text{Adjusted closing share price at end of year}}$
Price/earnings ratio =	$\dfrac{\text{Adjusted closing share price at end of year}}{\text{Earnings per share}}$
Return on equity =	$\dfrac{\text{Profit for the financial year x 100}}{\text{Shareholders' equity (incl. minority interest), average of the beginning and end of the year}}$
Return on investment =	$\dfrac{\text{(Profit before taxes + interest and other financial expenses) x 100}}{\text{Balance sheet total - non-interest-bearing liabilities, average of the beginning and end of the year}}$
Equity ratio =	$\dfrac{\text{Shareholders' equity (incl. minority interest) x 100}}{\text{Balance sheet total – advances received}}$
Net gearing =	$\dfrac{\text{(Interest-bearing liabilities – cash, bank balances and financial assets)}}{\text{Shareholders' equity (incl. minority interest)}}$
Research and development costs =	Research and development costs recorded in the income statement (including costs covered with subsidies) and capitalized development expenses
Market capitalization =	Number of shares outstanding at end of year x closing share price
Trading volume =	$\dfrac{\text{Number of shares traded during the year}}{\text{Adjusted average number of shares}}$

Consolidated income statement (IFRS)

EUR thousands	Note	Jan 1–Dec 31, 2006	%	Jan 1–Dec 31, 2005	%
Revenues	3,4	**186,449**	**100.0**	**149,928**	**100.0**
Other operating income	5	250		197	
Change in inventories of finished goods and work in progress		1,469		978	
Materials and services		-97,117		-76,382	
Employee benefit costs	7	-31,968		-26,876	
Depreciation and amortization	8	-4,213		-3,783	
Other operating expenses	6	-31,793		-25,993	
Operating profit		**23,077**	**12.4**	**18,069**	**12.1**
Financial income	10	294		185	
Financial expenses	10	-699		-371	
Share of results in associated companies		0		-220	
Profit before taxes		**22,672**	**12.2**	**17,663**	**11.8**
Income taxes	11	-6,557		-5,511	
Profit for the financial year		**16,115**	**8.6**	**12,152**	**8.1**

EUR thousands	Note	Jan 1–Dec 31, 2006	%	Jan 1–Dec 31, 2005	%
Attributable to:					
Equity holders of the parent company	12	15,799		11,959	
Minority interest		316		193	
Earnings per share for profit attributable to the equity holders of the parent company:	12				
Basic earnings per share (EUR)		1.04		0.79	
Diluted earnings per share (EUR)		1.04		0.79	

Consolidated balance sheet (IFRS)

EUR thousands	Note	Dec 31, 2006	%	Dec 31, 2005	%
Assets					
Non-current assets					
Goodwill	13	1,479		1,725	
Development costs	13	1,625		1,949	
Intangible assets	13	4,684		1,985	
Property, plant and equipment	14	13,261		13,610	
Other investments	17	1,359		1,070	
Loan receivables	18	566		498	
Deferred tax assets	11	1,099		1,002	
Other receivables		238		168	
		24,311	28.0	22,007	29.0
Current assets					
Inventories	19	11,737		9,176	
Trade and other receivables	20	37,813		33,222	
Cash and cash equivalents	21	13,026		11,560	
		62,576	72.0	53,958	71.0
Total assets		**86,887**	**100.0**	**75,965**	**100.0**

EUR thousands	Note	Dec 31, 2006	%	Dec 31, 2005	%
Equity and liabilities					
Equity attributable to equity holders of the parent company					
Share capital	22	3,059		3,059	
Share premium		4,966		4,966	
Other reserves		48		32	
Own shares		-1,171		-1,171	
Translation difference		-117		-67	
Fair value reserve	23	61		-106	
Retained earnings		45,161		35,601	
		52,007	59.9	42,314	55.7
Minority interest		954	1.1	499	0.7
Total equity		52,961	61.0	42,813	56.4
Non-current liabilities					
Deferred tax liabilities	11	1,219		697	
Employee benefits	25	678		590	
Interest-bearing liabilities	26	1,828		1,960	
		3,725	4.3	3,247	4.3
Current liabilities					
Trade and other payables	27	25,610		25,976	
Income tax liabilities		1,509		1,391	
Provisions	28	652		790	
Interest-bearing liabilities	26	2,430		1,748	
		30,201	34.8	29,905	39.4
Total liabilities		33,926	39.0	33,152	43.6
Total equity and liabilities		**86,887**	**100.0**	**75,965**	**100.0**

Consolidated cash flow statement (IFRS)

EUR thousands	Jan 1–Dec 31, 2006	Jan 1–Dec 31, 2005
Cash flow from operating activities:		
Profit for the financial year	**16,115**	**12,152**
Adjustments:		
Depreciation	4,213	3,783
Share of results in associated companies		220
Financial income and expenses	405	186
Taxes	6,557	5,511
Other adjustments	-53	47
	27,237	21,899
Changes in working capital:		
Change in inventories	-2,629	-2,442
Change in non-interest-bearing receivables	-2,964	-9,491
Change in non-interest-bearing liabilities	-78	4,833
	-5,671	-7,100
Interest received	240	181
Interest paid	-348	-209
Other financial items	-195	-37
Taxes paid	-6,133	-5,084
Cash flow from operating activities	**15,130**	**9,650**
Cash flow from investing activities:		
Investments in tangible and intangible assets	-6,942	-6,436
Proceeds from the disposal of tangible and intangible assets	472	258
Loans granted	-1,365	
Other investments	-490	-182
Change in long-term loan receivables		178
Proceeds from the disposal of other investments	270	29
Cash flow from investing activities	**-8,055**	**-6,153**

EUR thousands	Jan 1–Dec 31, 2006	Jan 1–Dec 31, 2005
Cash flow from financing activities:		
Share issue	143	
Proceeds from long-term borrowings	437	1,185
Repayments on long-term loans	-170	-856
Proceeds from short-term borrowings	5,000	
Repayments on short-term loans	-4,251	-1,271
Repurchase of own shares		-1,021
Financial leasing payments	-320	-311
Dividends paid	-6,337	-5,320
Cash flow from financing activities	**-5,498**	**-7,594**
Change in liquid funds	**1,577**	**-4,097**
Liquid funds at beginning of period	11,560	15,524
Translation differences of liquid funds	-111	133
Liquid funds at end of period	13,026	11,560

Consolidated statement of changes in equity

EUR thousand	Attributable to equity holders of parent company								Minority interest	Total equity
	Share capital	Share premium	Other restricted reserves	Own shares	Translation difference	Revaluation fund	Retained earnings	Total		
Shareholders' equity on Dec 31, 2004	3,059	4,966	28	-150	-276	0	28,924	36,551	304	36,855
Cash flow hedging:										
Hedging result allocated to equity						-106		-106		-106
Hedging result carried to income statement								0		0
Translation difference					209			209		209
Recognized taxes							-6	-6		-6
Other changes			4				44	48		48
Net income recorded directly in equity	**0**	**0**	**4**	**0**	**209**	**-106**	**38**	**145**	**0**	**145**
Profit for the financial year							11,959	11,959	193	12,152
Total income and expenses recorded for the year	**0**	**0**	**4**	**0**	**209**	**-106**	**11,997**	**12,104**	**193**	**12,297**
Dividends paid							-5,320	-5,320		-5,320
Share repurchase				-1,021				-1,021		-1,021
Equity on Dec 31, 2005	**3,059**	**4,966**	**32**	**-1,171**	**-67**	**-106**	**35,601**	**42,314**	**499**	**42,813**

EUR thousand	Attributable to equity holders of parent company								Minority interest	Total equity
	Share capital	Share premium	Other restricted reserves	Own shares	Translation difference	Revaluation fund	Retained earnings	Total		
Cash flow hedging:										
Hedging result allocated to equity						61		61		61
Hedging result carried to income statement						106		106		106
Translation difference					-104			-104		-104
Gains/losses from hedging net investment					54			54		54
Recognized taxes							6	6		6
Other changes			16				92	108	-11	97
Net income recorded directly in equity	**0**	**0**	**16**	**0**	**-50**	**167**	**98**	**231**	**-11**	**220**
Profit for the financial year							15,799	15,799	316	16,115
Total income and expenses recorded for the year	**0**	**0**	**16**	**0**	**-50**	**167**	**15,897**	**16,030**	**305**	**16,335**
Dividends paid							-6,337	-6,337		-6,337
Minority interest in new subsidiaries								0	150	150
Equity on Dec 31, 2006	**3,059**	**4,966**	**48**	**-1,171**	**-117**	**61**	**45,161**	**52,007**	**954**	**52,961**

Notes to the consolidated financial statements

1. General information

Vacon Plc is a Finnish public corporation that has been established in accordance with the laws of Finland. The company's domicile is in Vaasa. The Vacon Group is a global company providing a comprehensive set of AC drives and related services. Vacon Plc and its subsidiaries focus exclusively on AC drives.

2. Accounting principles for the consolidated financial statements

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS), applying the IAS and IFRS standards in force on 31 December 2006 as well as the SIC and IFRIC interpretations. International Financial Reporting Standards refer to the standards and their interpretation to be applied in the community as provided in the Finnish Accounting Act and the provisions issued on the basis of this act, and in regulation (EC) No 1606/2002 of the European Parliament and of the Council on the application of international accounting standards. Notes to the consolidated financial statements have also been prepared in accordance with Finnish accounting and Community legislation.

Vacon adopted the IFRS standards on January 1, 2004 until which date the reporting was conducted in accordance with the Finnish Accounting Standards (FAS). For the transition, Vacon applied the First-Time Adoption of IFRS standard, which allows certain transitional exceptions for the retrospective application of individual standards. The most significant exception applied was using the FAS-compliant financial statement carrying amounts as the consolidated goodwill carrying amounts in the IFRS transition balance sheet.

Financial statement information is presented in thousand euros and it is based on the original acquisition cost unless otherwise stated in the accounting principles below.

The Group has applied the following revised standards as from 1 January 2006:

- Amendment to IAS 19 Employee Benefits – Actuarial Gains and Losses, Group Plans and Disclosures. The amendment has increased the amount of information given in the Notes. Adopting the amendment to the standard only has an impact on the Notes to the Consolidated Financial Statements, since the Group has not changed its accounting practice for actuarial gains and losses.
- Amendment to IAS 39 Financial instruments (Cash flow hedges of forecast intragroup transactions). Applying the amendment does not have any significant impact on the 2006 result.
- Amendment to IAS 21 The Effects of Changes in Foreign Exchange - Net Investment in a Foreign Operation. Applying the amendments does not have any significant impact on the 2006 result.

Estimates

When preparing the IFRS-compliant consolidated financial statements, the company's management is required to make estimates and assumptions. These affect the amount of assets, liabilities, income and expenses to be recorded. The estimates and assumptions are based on historical experience and other justifiable assumptions that are believed to be reasonable under the circumstances that serve as the foundation for assessing the items entered in the financial statements. The final figures may differ from these estimates. The estimates concern the feasibility of realizing certain assets, the period of useful economic life for tangible and intangible assets, the setting of provisions relating to the business operations, goodwill and deferred tax assets. For goodwill, the anticipated income and interest rate used in testing for impairment contain estimates. The estimate of future taxable income creates a basis for stating deferred tax assets.

Principles of consolidation

The consolidated financial statements include the parent company and all companies in which the parent company has the majority of votes or other controlling interest. The financial results of subsidiaries acquired or established during the year are consolidated from the date of acquisition or establishment. The consolidated financial statements have been prepared using the acquisition cost method. The identifiable assets and liabilities of acquired companies have been measured at fair value at the time of acquisition. The difference between the price paid for the company and its net assets measured at fair value constitutes goodwill. As allowed by IFRS 1, acquisitions made before the adoption of IFRS have not been adjusted to comply with IFRS principles; instead, they remain at the FAS compliant values at the time of adoption.

Intra-group business transactions, receivables, liabilities, non-realized margins and intra-group profit distribution have been eliminated in the consolidation. Profit for the period is divided into the parent company owners' interest and minority interest. Minority interest is presented as an individual item under shareholders' equity. In the consolidated financial statements, the changes in group companies' accumulated depreciation have been divided into change in deferred taxes and profit for the period. In the consolidated balance sheet, accumulated depreciation difference has been divided into deferred taxes and non-restricted equity.

Associated companies, in which Vacon has 20 to 50 % of the voting rights or in which Vacon exercises significant influence but has no controlling interest, have been consolidated using the equity method. In accordance with this method, the Group's share of the associated companies' results is included in the consolidated income statement. In the consolidated balance sheet, the Group's share of the accumulated results since the acquisition of the company has been presented as a part of the investment made in the associated company. If Vacon's share of the associated company's losses exceeds the carrying amount of the investment, the investment will be recorded in the balance sheet at nil value and losses in excess of that value will be ignored unless the Group has obligations towards the associated companies. If the Group has other long-term investments that in fact are part of an investment company's net investment in the associated company, losses will be allocated to these investments after the share investment has been booked at nil value.

The joint venture Vacon Americas LLC has been consolidated according to the Group's ownership. During the financial period the joint venture had no personnel.

Foreign currency items

The figures concerning the financial performance and position of the Group's business units are measured in the currency that is the main currency in the business environment of each unit ("business currency"). The consolidated financial statements are presented in euros, which is the business and presentation currency of the Group's parent company.

Zao Vacon Drives, which operates in Russia, uses the euro as its business currency since goods purchases are made from the parent company mainly in euros. In addition a large part of the Russian subsidiary's costs are tied to the euro or the US dollar.

Transactions carried out in foreign currencies have been recorded in the business currency at the exchange rate on the transaction date. On the balance sheet date, monetary items denominated in foreign currencies are valued at the exchange rate at the year-end. Translation differences from business transactions have been entered in sales and purchases translation differences, and translation differences from interest-bearing liabilities and receivables have been included in their net amounts in financial income and expenses. Translation differences from loans receivable in foreign currencies that are part of foreign net investment have been recorded in translation differences in consolidated shareholders' equity. Translation differences for foreign currency loans that have been specified to hedge foreign net investment have also been recorded in shareholders' equity.

The income statements of Group companies whose business currency or financial statement currency is not the euro, have been translated into euros using the average rate for the financial year, and balance sheets using the rate on the balance sheet date. Translation differences arising from the different exchange rates used in the income statement and balance sheet have been recorded in the Group's shareholders' equity. Translation differences arising from applying the acquisition cost method and the resulting currency exchange rates have also been recorded as a separate item in the Group's shareholders' equity.

The cash flows of foreign subsidiaries have been translated into euros at the average monthly exchange rates.

Financial instruments

Vacon has applied the IAS 39 and IAS 32 standards since January 1, 2005.

Financial assets have been classified in accordance with IAS 39 as follows: assets booked at fair value affecting the result, liabilities and other receivables. Assets booked at fair value affecting the result include cash assets and other short-term investment, such as bank deposits. Loans and other receivables include assets other than derivative assets that involve fixed or definable payments and that are not quoted on the active markets.

This item includes accounts receivable and other loan receivables resulting from commercial activities. Loans and other receivables have been measured at amortized cost less any write-down, and in the balance sheet they are included in short- or long-term loan receivables depending on their maturity.

Investments in other companies (Group ownership and voting rights less than 20 %) have been measured at fair value except in cases where fair value could not be determined. In these cases, they have been presented at acquisition cost.

Interest-bearing liabilities are classified as other liabilities. Loans are measured at fair value on the basis of the consideration received in connection with the original recognition, after which the loans are recorded at amortized cost using the effective interest rate method.

Derivative contracts are originally booked at acquisition cost, which matches their fair value. In subsequent financial statements derivative contracts are measured at fair value. Publicly quoted market prices and rates as well as generally used measurement models are used to define the fair value of derivatives. The information and assumptions used in the measurement models are based on verifiable market prices and values. The fair values of derivative contracts expiring within a year are shown in the balance sheet under short-term receivables or liabilities, and contracts with longer maturity under long-term receivables or liabilities.

The Group applies IAS 39 -compliant hedge accounting for cash flow hedging with respect to operative currency exposure. In this case the Group, when initiating hedge accounting, documents the relationship between the item to be hedged and the hedging instrument, the method used to measure effectiveness, and the hedging strategy in accordance with the Group's risk management policy, so that these meet all IAS 39 requirements for hedge accounting. The hedging instruments used are forward exchange contracts. For those hedging relationships that meet the hedge accounting criteria, the effective portion of the change in the fair value of the hedging instrument is recorded in shareholders' equity and any remaining ineffective portion is recorded affecting the result. The cumulative change in fair value, which is entered in shareholders' equity, is recorded as affecting the result at the moment the anticipated cash flow is recorded in the income statement.

If the derivative instruments do not meet the criteria for hedge accounting specified in IAS 39, the change in the fair value of the derivative instrument is recorded immediately affecting the result.

Goodwill and other intangible assets

The goodwill generated from business acquisitions consists of the difference between acquisition cost and identifiable net assets measured at fair value. Goodwill has been allocated to cash generating units. Goodwill and intangible assets with an unlimited economic life, if there are any, are tested annually for impairment.

Testing for impairment is made by comparing the amount of recoverable cash to its balance sheet value. A unit's recoverable amount is determined from cash flow predictions discounted to their present value. The discount rate used in the calculation is based on the business unit's return on equity requirement. The ROE requirement comprises three components: the risk-free interest in each country, the general risk premium in the share market, and the beta coefficient, which measures the level of risk of operations. The discount rate used is defined so that the equity structure is debt-free. The discount rate used in calculation is also defined before taxes. More information about the sensitivity of the amount of recoverable cash to changes in the assumptions used is given in Note 13.

As allowed by the IFRS 1, acquisitions made before the adoption of IFRS have not been adjusted to comply with IFRS principles; instead, they remain at the FAS compliant values.

Other intangible assets include software licenses, computer programs and subscription fees. These are measured at original acquisition cost and amortized on a straight-line basis over their economic life, which can range between five and eight years.

Any subsequent expenses associated with intangible assets will be capitalized only if it is likely that the future financial benefit will flow to the company and if the acquisition cost can be reliably determined. Otherwise the costs are recognized as expenses as they are incurred.

Research and development costs

Research and development costs are recognized as expenses as they are incurred. Development costs that meet the criteria specified in IAS 38 are recorded in intangible assets and amortized over their effective life span but no later than in five years. Capitalized expenses include direct material costs, labor costs and related overheads.

A product designed to replace an existing product remains in the research stage until it has been tested and found feasible in prototype testing and is therefore likely to become available for sale later. After that it moves on to the development stage and the expenses are capitalized in the balance sheet.

Expenses related to products developed for new product ranges are not capitalized since the future benefits of such products are difficult to estimate. The expenses for products developed for a specific customer are also not capitalized.

Property, plant and equipment

Machinery and equipment represent the largest component of property, plant and equipment. In the balance sheet these are measured at original acquisition cost less accumulated depreciation.

Ordinary maintenance and repair costs are booked as expenses at the time they are incurred. Significant modernization and improvement investments are capitalized and depreciated over the remaining economic life of the related main asset.

Property, plant and equipment are depreciated on a straight-line basis over their economic life.

The depreciation schedule for property, plant and equipment is as follows:

Machinery and equipment	4–15 years
Other tangible assets	5–10 years

Gains or losses from the disposal of property, plant and equipment are recorded in the income statement.

Impairment

The carrying amount of assets is assessed on each balance sheet date to identify potential impairment. If there are any elements suggesting impairment, the recoverable amount of the asset is estimated to be the higher of the net sales price or the value in use. Impairment is recognized if the carrying amount exceeds the recoverable amount.

Leases

Leasing agreements where the Group has an essential part of the risks and benefits inherent in ownership are classified as finance leases. At the start of the agreement, these are entered in the balance sheet under assets in the amount that equals the fair value of the asset at the start of the agreement, or the fair value of minimum leases if lower. The leasing fees are divided into financial expenses and loan repayment. Financial expenses are allocated to financial periods during the leasing period so that the interest rate for the remaining debt will be the same for each financial period. The corresponding leasing liabilities less financial expenses are included in interest-bearing liabilities. The interest rate portion of financing is recognized in the income statement during the leasing period. Assets leased under a financial leasing agreement are depreciated according to plan over their economic life.

Leasing agreements that are not finance leases constitute operating leases. These fees will be recognized as expenses in equal amounts over the leasing period.

Inventories

Inventories are entered in the balance sheet at the lower of the acquisition cost or the net realizable value. As from 1 June 2006 the acquisition cost has been determined using the FIFO method. Previously the acquisition cost was determined using the weighted average cost method. This change has a very small impact on the Group's result. The opening balances in the year have not been adjusted because the impact on them is not significant.

The acquisition cost of finished goods and work in progress includes raw materials, direct salaries and other direct expenses as well as the appropriate share of indirect production costs, excluding interest expenses. Net realizable value is the estimated sales price in ordinary activities less the costs associated with the sale of products.

Trade and Other Receivables

Trade and other receivables are recognized at original value. Uncertain receivables are assessed on the basis of the risk involved in individual items. Credit losses are recorded as expenses in the income statement.

Cash and Cash Equivalents

Cash and cash equivalents include cash and bank and other liquid investments with a maturity of less than three months. Balances in credit accounts are included in current liabilities.

Pension Schemes

In Group companies, pension schemes are arranged in different ways depending on the pension legislation and practices of the country in question. As a rule, the pension arrangements represent contribution plans. In addition, the pension schemes of some foreign subsidiaries represent defined benefit plans.

Payments for contribution plans are recorded as expenses for the period to which they are allocated. The present value of defined benefit plans is determined using a method based on an anticipated benefit unit, and the assets covered by the arrangement have been measured at fair value on the balance sheet date. Actuarial gains and losses are recorded in the income statement during the average remaining years of employment of the personnel participating in the plan to the extent that it exceeds 10 % of the present value of the defined benefit plan or the higher fair value of the assets covered by the plan. At the time of transition on 1 January 2004 all actuarial gains and losses were recorded under shareholders' equity.

Revenues

Sales are recognized in connection with the transfer of ownership-related risks and benefits to the buyer. Usually sales are recognized at the date of delivery. Sales adjustment items include cash discounts as well as exchange rate profits and losses on sales.

In accordance with IAS 11, long–term projects are partially recognized as income for the financial period in cases that involve fixed-price contracts the outcome of which can be reliably assessed. The percentage-of-completion required in long-term projects is determined from the proportion of the costs to date of the estimated total costs of the project, ie the cost-to-cost method. If it is likely that the overall costs of the project will exceed the overall income, the expected losses are recognized as expenses immediately.

Operating profit

The concept of operating profit is not defined in IAS 1: Presentation of financial statements. The Group has defined it as follows: Operating profit is the net sum of revenues plus other operating income less purchase costs adjusted with the change in inventories of finished goods and work in progress and the expenses arising from production for own use, less employee benefit costs, depreciation, amortization and any impairment losses, and other operating costs. All other income statement items except those mentioned above are shown beneath operating profit. Exchange differences are included in the operating profit provided that they originate in items related to business operations; otherwise they are recorded under financial items.

Subsidies

Subsidies received from the State or other parties are recognized as income in the income statement, with matching expenses recorded. Subsidies are recorded as deductions from the corresponding expenses. Subsidies associated with tangible and intangible assets are deducted from the asset acquisition price and the net acquisition cost is capitalized in the balance sheet.

Equity compensation benefits

The Group has a share bonus scheme that offers key personnel the opportunity to receive company shares in three earning periods of one calendar year as a reward for achieving their personal targets. The earning periods are the calendar years 2005, 2006 and 2007. The share bonus has been recorded as an expense and as an increase in shareholders' equity. The amount recorded as expenses during the earning period has been determined on the basis of market values on the day the shares have been awarded. The terms of the share bonus scheme are given in more detail in Note 24 'Share-based payments'.

Provisions

Items related to contracts and their effective obligations that are likely to require financial resources are recorded in the balance sheet as provisions, if their amount can be reliably assessed. These items currently include only warranty provisions and any negative project margins. The anticipated future warranty costs of delivered products are recorded as warranty provisions. Realized warranty costs, with changes in warranty liability taken into account, are recorded in the income statement in the period during which they incur.

Income taxes

Taxes in the consolidated income statement include the Group companies' taxes paid and accrued corresponding to the financial result for the period based on taxable income calculated in accordance with each company's local tax regulations, adjustments to taxes from previous financial periods, and changes in deferred taxes.

The recorded deferred tax assets and liabilities include the temporary differences between the Group companies' taxes and the balance sheet, as well as differences arising in connection with Group elimination. To calculate deferred tax assets and liabilities, the tax rate used is the following year's tax rate approved for the country in question on the balance sheet date. The most significant tax assets and liabilities consist of tax losses carried forward, appropriations, fixed assets, financial instruments and Group eliminations.

Deferred tax assets from tax losses carried forward are recorded in cases where it is likely that the loss can be used against the taxable income in future financial years. Deferred tax liabilities are recorded in full.

Applying new and amended IFRS standards and interpretations in 2007 or later

During 2007, the Group will adopt the following new and amended standards and interpretations issued in 2005 and 2006:

- IFRS 7 Financial Instruments: Disclosures
- Amendment to IAS 1 Presentation of Financial Statements – Capital Disclosures

The Group estimates that the new standard and interpretation will mainly affect the notes to the consolidated financial statements.

- IFRIC 8 Scope of IFRS 2
- IFRIC 9 Reassessment of Embedded Derivatives
- IFRIC 10 Interim Financial Reporting and Impairment

The Group estimates that the new interpretations will not have any effect on the Group's future financial statements.

In 2009 the Group will adopt IFRS 8 Operating Segments issued in 2006. The Group is examining the impact of the standard on the figures presented in the financial statements.

3. Segment Information

Vacon Group's reporting is based primarily on business segments and secondarily on geographic segments.

Vacon has one business segment, which is AC drives. Figures for the primary segment are equal to the figures for the entire Group. Vacon's operations are organized in the following functions: Products and Markets, Production, Research & Development, Finance and Administration, Human Resources, IT and Process Development, and Corporate Development. To ensure that the organisation is customer-oriented, operations are controlled by customer segments that are called business areas. These business areas are: Component Customers, Solutions Customers, OEM and Brand Label Customers, and Service and After-Market Services.

The secondary geographic segment is divided into four sales areas:
Europe, North America, Asia and Australia, and other countries. Revenues are distributed by customers, assets and investments by geographic location.

Geographic segments in 2006, EUR thousand	Europe	North America	Asia and Australia	Others	Group
Revenues	129,699	37,915	15,799	3,036	186,449
Segment's assets	78,812	411	7,664	0	86,887
Investments	7,892	0	646	0	8,538
Geographic segments in 2005, EUR thousand					
Revenues	106,556	29,120	11,609	2,643	149,928
Segment's assets	71,548	458	3,959	0	75,965
Investments	4,962	0	1,656	0	6,618

4. Long-term projects

Consolidated revenues include EUR 1,320 thousand worth of income recognized from long-term projects in 2006 (EUR 1,902 thousand in 2005).

The consolidated income statement includes EUR 1,088 thousand worth of income from long-term projects in progress on Dec 31, 2006 (EUR 1,207 thousand on Dec 31, 2005). The balance sheet includes advance payments in the amount of EUR 1,027 thousand for long-term projects in progress on Dec 31, 2006 (EUR 1,205 thousand Dec 31, 2005).

5. Other operating income

EUR thousand	2006	2005
Rental income	173	102
Proceeds from the disposal of assets	77	34
Others	0	61
Total	250	197

6. Other operating expenses

EUR thousand	2006	2005
Delivery costs and commissions	6,024	4,677
Sales and marketing costs	6,276	5,456
Rental costs	4,532	3,611
Administrative costs	7,581	5,524
Other costs	7,380	6,725
Total	31,793	25,993

7. Employee benefit costs

EUR thousand	2006	2005
Salaries	24,705	21,141
Share bonuses granted paid in shares	120	60
Share bonuses granted paid in cash	439	168
Pensions		
Defined benefit plans	149	155
Contribution plans	3,902	3,152
Other indirect personnel costs	2,653	2,200
Total	31,968	26,876

	2006	2005
Office personnel	424	385
Factory personnel	194	148
Average number of personnel	618	533

8. Depreciation, amortization and impairment charge

EUR thousand	**2006**	**2005**
Depreciation by asset		
Intangible assets		
Development costs	910	863
Intangible rights	580	356
Other intangible assets	101	71
Total	1,591	1,290
Property, plant and equipment		
Machinery and equipment	2,622	2,436
Other tangible assets	0	6
Total	2,622	2,442
Impairment charge by asset		
Development costs	0	32
Intangible rights	0	19
Total	0	51
Total depreciation, amortization and impairment charge	4,213	3,783

As of January 1 2004, goodwill has not been amortized.

9. Research and development costs

The income statement includes research and development costs recorded as expenses of EUR 11,931 thousand in 2006 (EUR 10,237 thousand in 2005).

10. Financial income and expenses

EUR thousand	**2006**	**2005**
Interest income	228	143
Exchange rate gains	24	4
Other financial income	42	38
Total	294	185
Interest expenses	-351	-229
Exchange rate losses	-193	0
Other financial expenses	-155	-142
Total	-699	-371
Total financial income and expenses	-405	-186

Items above operating profit include exchange rate differences of EUR 121 thousand (EUR -250 thousand in 2005).

11. Income taxes

EUR thousand	2006	2005
Taxes based on the taxable income for the financial year	-6,146	-5,322
Taxes on the previous year	-22	0
Deferred taxes	-389	-189
Total	-6,557	-5,511
Profit before taxes	22,672	17,663
Taxes calculated in accordance with domestic tax rate	5,895	4,592
Impact of foreign subsidiaries´ differing tax rates	481	694
Tax-free income	-21	-19
Non-deductible expenses	177	112
Impact of the change in tax rate	0	59
Unrecorded deferred tax assets from taxable losses	34	0
Taxes on previous year	-22	0
Other items	13	73
Taxes in the income statement	6,557	5,511

Deferred tax assets and liabilities

EUR thousand	2006	2005
Net deferred tax liability is allocated in the balance sheet as follows		
Deferred tax assets	1,099	1,002
Deferred tax liability	-1,219	-697
	-120	305

Gross change in deferred taxes recorded in balance sheet:	2006	2005
Deferred taxes Jan 1	305	454
Items entered in income statement	-389	-189
Translation differences	-4	3
Items entered in shareholders' equity	-32	37
Deferred taxes Dec 31	-120	305

Change in deferred tax assets and liabilities during financial year

2006	Jan 1	Items entered in income statement	Items entered in share-holders' equity	Translation differences	Dec 31
Deferred tax assets:					
Employee benefits	20	-3			17
Provisions	206	-206			0
Tax losses carried forward	407	-91			316
Internal margin from inventories	575	151			726
Other temporary differences	37	94	-32		99
Total	1,245	-55	-32	0	1,158
Deferred tax liabilities:					
Property, plant and equipment	86	28			114
Capitalized intangible assets	225	124			349
Employee benefits	0				0
Accumulated depreciation difference	629	182		4	815
Total	940	334	0	4	1,278
Deferred taxes, net	305	-389	-32	-4	-120

2005	Jan 1	Items entered in income statement	Items entered in share-holders' equity	Translation differences	Dec 31
Deferred tax assets:					
Employee benefits	14	6			20
Provisions	0	206			206
Tax losses carried forward	547	-140			407
Internal margin from inventories	586	-11			575
Other temporary differences	0		37		37
Total	1,147	61	37	0	1,245
Deferred tax liabilities:					
Property, plant and equipment	61	25			86
Capitalized intangible assets	92	133			225
Employee benefits	12	-12			0
Accumulated depreciation difference	528	104		-3	629
Total	693	250	0	-3	940
Deferred taxes, net	454	-189	37	3	305

EUR 0.04 million in tax assets relating to confirmed losses will become void during the next five years, the remainder by 2015. The balance sheet contains EUR 0.3 million in deferred tax assets in a company which had a loss-making financial result in the current financial year. Recording these deferred tax assets is based on forecast results that show that it will be possible to utilise the deferred tax assets.

12. Earnings per share

Basic earnings per share are calculated by dividing the profit attributable to the equity holders of the parent by the weighted average number of shares outstanding during the year. At the end of financial years 2006 and 2005, the Group had no diluting instruments.

EUR thousand	2006	2005
Profit attributable to the equity holders of the parent company	15,799	11,959

Number of shares	2006	2005
Weighted average number of shares during the year	15,209,303	15,203,147
Basic earnings per share (EUR/share)	1.04	0.79
Diluted earnings per share (EUR)	1.04	0.79

13. Intangible assets

EUR thousand	Goodwill	Development costs	Intangible rights	Other intangible assets	Total 2006	Total 2005
Acquisition cost Jan 1	1,725	6,597	3,196	601	12,119	11,381
Increases		642	3,514	48	4,204	1,681
Decreases	-246	-671	-522	-7	-1,446	-177
Transfers between items			160	-55	105	-45
Translation differences			-4	-30	-34	44
Acquisition cost Dec 31	1,479	6,568	6,344	557	14,948	12,884
Accumulated amortization Jan 1		-4,648	-1,617	-195	-6,460	-5,910
Accumulated amortization from decreases and transfers		615	222	48	885	31
Amortization for the financial year		-910	-580	-101	-1,591	-1,290
Impairment charge					0	-51
Translation differences			2	5	7	-5
Accumulated amortization Dec 31		-4,943	-1,973	-243	-7,159	-7,225
Carrying amount Dec 31, 2006	1,479	1,625	4,371	341	7,789	
Carrying amount Dec 31, 2005	1,725	1,949	1,579	406		5,659

Impairment testing of goodwill in cash-generating units

Goodwill is tested annually in accordance with IFRS. Vacon Group goodwill has been allocated to five cash-generating units. Allocating and testing goodwill at the level of cash-generating units also helps to plan and monitor the Group's operations.

Impairment of goodwill is tested by comparing the recoverable amount of cash of a cash-generating unit with its balance sheet value. The unit's recoverable amount is determined from its cash flow projections discounted to their present value. The cash flows in turn are based on the five year forecast drawn up by the unit's management. The forecast take into account only the unit's organic growth. The basis used for calculating long-term growth is annual growth of two per cent.

The Group's godwill is divided among five business units (Netherlands, Spain, Italy, Sweden and German). According to the annual impairment tests the recoverable amounts of the cash-generating units exceed their corresponding balance values, so the tests have not resulted in the recognition of impairment losses. The forecast 30% reduction in operating profit would not create a need for writedowns in any of the tested units.

Goodwill has been allocated to the following cash-generating units:

EUR thousand	2006	2005
European sales companies	1,479	1,479
Others	0	246
Total	1,479	1,725

Main assumptions used in impairment testing:

	2006	2005
Growth in revenues (p.a., five year forecasts)	10–16%	10–20%
Pretax discount rate	10.0–13.4%	10.09–14.74%
Long-term growth	2%	2%
Goodwill allocated, 1000 EUR	1,479	1,725
Carrying value, 1000 EUR	17,778	15,717
Result of impairment test (recoverable amount vs. carrying value)	Exceeds clearly	Exceeds clearly

Changes in the company's markets, the global economy and interest rates are reflected in the growth and profitability forecasts for the business units and in the related risk and requirements for returns. The assumptions made for the impairment tests are based on the management view of the coming financial periods on the closing date. The forecasts and assumptions have been drawn up to carry out impairment tests. The forecasts and other assumptions are reviewed constantly and can change.

14. Property, plant and equipment

EUR thousand	Machinery and equipment	Advance payments and construction in progress	Other tangible assets	Total 2006	Total 2005
Acquisition cost Jan 1	23,858	2,014	125	25,997	21,300
Increases	3,489		18	3,507	4,768
Decreases	-443	-949	-2	-1,394	-116
Transfers between items	73		-73	0	-89
Translation differences	-127	-3		-130	134
Acquisition cost Dec 31	26,850	1,062	68	27,980	25,997
Accumulated depreciation Jan 1	-12,322	0	-65	-12,387	-10,126
Accumulated depreciation from decreases and transfers	214		65	279	186
Depreciation for the financial year	-2,622		0	-2,622	-2,442
Translation differences	11			11	-5
Accumulated depreciation Dec 31	-14,719	0	0	-14,719	-12,387
Carrying amount Dec 31, 2006	12,131	1,062	68	13,261	
Carrying amount Dec 31, 2005	11,536	2,014	60		13,610

Property, plant and equipment include assets acquired through financial leasing agreements.

2006, EUR thousand	Machinery and equipment	Total
Acquisition cost	1,325	1,325
Accumulated depreciation	-634	-634
Carrying amount	691	691

2005, EUR thousand	Machinery and equipment	Total
Acquisition cost	1,325	1,325
Accumulated depreciation	-423	-423
Carrying amount	902	902

15. Investments in associates

EUR thousand	2006	2005
Carrying amount Jan 1	0	93
Income from associates		19
Increase		0
Decrease		-112
Carrying amount Dec 31	0	0

The associated companies Verteco Oy and Rotatek Finland Oy became part of a larger holding company through a share exchange towards the end of 2006, when Vacon's holding in the resulting holding company fell below 20 %. This arrangement had no impact on the Group's result.

16. Joint ventures

	Interest %
Vacon Americas LLC, Milwaukee, United States	50

The consolidated financial statements include a share of the joint venture's assets, liabilities, income and expenses that matches the Group's ownership. The company had no operations in the financial years 2006 and 2005.

EUR thousand	2006	2005
Current assets (100%)	822	915
Net assets	822	915
Income	2	3
Expenses	0	0
Profit for the financial year	2	3

17. Other investments

	2006		2005	
EUR thousand	Balance sheet value	Fair value	Balance sheet value	Fair value
Shares in investment fund	1,002	1,002	816	816
Available-for-sale financial assets	357	357	254	254
Total	1,359	1,359	1,070	1,070

18. Loan receivables

	2006		2005	
EUR thousand	Balance sheet value	Fair value	Balance sheet value	Fair value
Long-term				
Loan receivables from associates	0	0	406	406
Other loan receivables	566	566	92	92
Total	566	566	498	498

19. Inventories

EUR thousand	2006	2005
Materials and consumables	4,478	3,387
Finished goods	7,259	5,789
Total	11,737	9,176

Inventories have been written down by EUR 132 thousand to accommodate for nonmarketable assets in 2006 (EUR 109 thousand in 2005). Nonmarketability deductions primarily cover spare parts and replacement units.

20. Trade and other receivables

EUR thousand	2006	2005
Trade receivables	33,497	30,207
Receivables from associates	0	428
Other loan receivables	1,197	0
Other receivables	1,881	1,493
Prepaid expenses and accrued income	1,238	1,094
Total	37,813	33,222

21. Cash and cash equivalents

EUR thousand	2006	2005
Cash and bank	13,026	10,034
Other financial assets	0	1,526
Total	13,026	11,560

22. Notes relating to shareholders' equity

	Number of shares	Number of own shares	Share capital EUR	Own shares EUR	Share premium reserve EUR	Total EUR
Jan 1, 2005	15,295,000	-12,800	3,059,000	-149,865	4,966,488	7,875,623
Purchases of own shares Jan 3–Feb 15, 2005		-82,460		-1,021,147		-1,021,147
Dec 31, 2005	15,295,000	-95,260	3,059,000	-1,171,012	4,966,488	6,854,476
Shares issued as share bonus April 21, 2006		13,688				
Dec 31, 2006	15,295,000	-81,572	3,059,000	-1,171,012	4,966,488	6,854,476

Vacon's share capital is EUR 3,059,000 divided into 15,295,000 fully paid shares. As stated in the Articles of Association, the minimum capital is one million (1,000,000) euro and maximum capital is four million (4,000,000) euro. Vacon has one share series. Each share has a nominal value of EUR 0.20 and each share confers one vote at the shareholders' meeting.

Under the authorization given at the shareholders' meeting on March 25, 2004, the company has repurchased 95,260 of its own shares. 13 688 shares were issued as a share bonus on 21 April 2006, after which the company holds 81 572 of its own shares.

23. Fair value reserve

EUR thousand	Cash flow hedging
Jan 1, 2005	0
Cash flow hedging recorded in equity	142
Cash flow hedging carried from equity to the income statement	0
Deferred taxes	-36
Dec 31, 2005	**106**
Cash flow hedging recorded in equity	82
Cash flow hedging carried from equity to the income statement	-106
Deferred taxes	-21
Dec 31, 2006	**61**

24. Share-based payments

At its meeting in January 2005, Vacon Plc's Board of Directors decided to introduce a share bonus scheme as a part of Vacon Group's key personnel incentive scheme. The purpose of the bonus scheme is to establish a shared set of objectives for shareholders and key personnel to increase the company's value, and to enhance key personnel commitment and offer them a competitive ownership-based bonus scheme.

The share bonus scheme offers key personnel the opportunity to receive company shares for three earning periods equalling one calendar year as a reward for achieving their personal targets. The earning periods are calendar years 2005, 2006 and 2007.

The Board of Directors makes decisions annually to determine the key personnel to be included in the scheme and their maximum bonuses. The maximum bonus is expressed in a number of shares. The maximum number of Vacon Plc shares to be disposed of under the incentive scheme is 80,400 shares for three earning periods. Additionally, the sum required to pay the taxes and other tax-like charges associated with the distributed shares at the time of distribution shall be provided in cash. Those included in the share bonus scheme are also entitled to any dividend accumulated during the earning period. The proportion of the maximum bonus to be distributed to key personnel depends on how well personal targets have been met during the earning period. These targets are linked to the group's strategic objective – namely, profitable growth – the indicators of which are revenue, operating profit and working capital to revenue ratio.

Any bonuses payable on the basis of the share bonus scheme will be paid as a combination of shares and cash in the year following the earning period. Shares distributed as a bonus must remain in the recipient's possession for two years after the earning period. If the recipient's employment is terminated during this two-year period, the shares must be returned to the group. An exception may be made subject to a decision of Vacon Plc's Board of Directors.

The target group comprises Vacon Group's key personnel as determined by the Board of Directors. Those included in the target group must have an employment contract with a Vacon Group company that is effective until further notice. Being included in the target group for the share bonus scheme does not affect the other terms and conditions of an employee's employment contract.

The share bonus scheme features three earning periods equalling one calendar year, beginning on 1 January 2005, 1 January 2006 or 1 January 2007, and ending on 31 December of the same year. The payable bonus will be determined by the end of April following the end of the earning period and it will depend on how well personal targets have been met. If the company's financial period is changed before 31 December 2007, the Board of Directors will be entitled to change the earning period correspondingly.

Nature of arrangement: Share bonus scheme	**2006–2008 2006**	**2005–2007 2006**	**2005–2007 2005**
Date of issue	Jan 28, 2005	Jan 28, 2005	Jan 28, 2005
Implementation	Shares and cash	Shares and cash	Shares and cash
Maximum number of shares offered as share bonus during the earning period, share	26,000	22,814	26,800
Share price at time of issue, EUR	12.25	12.25	12.25
Agreed earning period (no. of years)	1	1	1
Agreed period (years) for prohibition on transfer after the earning period	2	2	2
Share price on valuation date, EUR	26.10	23.52	17.50
Assumed participation	91%	100%	91%
Realisation of profit-based terms and conditions in the earning year	70%	58%	60%
No. of shares issued under the scheme	18,200	13,688	16,080
Value of shares being issued on valuation date, EUR thousand	475	322	281
Share to be paid in cash (for taxes) calculated with the value on balance sheet date and assumed dividend, EUR thousand	754	500	537
Total cost of shares issued based on value at the time of issue, EUR thousand	223	168	197
Total cost of the share bonus scheme, EUR thousand	977	668	734
Share value adjusted with anticipated participation, EUR thousand	203	168	179
Consolidated income statement includes 1/3 of the sum in employee benefits and increase in shareholders' equity, EUR thousand	68	52	59
Remaining amount to be recognized in future financial years after taking the anticipated participation into consideration, EUR thousand	135	56	120
Amount to be paid in cash adjusted with anticipated participation, EUR thousand	690	500	489

Nature of arrangement: Share bonus scheme	2006–2008 2006	2005–2007 2006	2005–2007 2005
Consolidated income statement includes 1/3 of the sum in employee benefits and liabilities, EUR thousand	258	181	168
Remaining amount to be recognized in future financial years after taking the anticipated participation into consideration, EUR thousand	432	151	321
Costs from the share bonus system recorded during the period as employee benefits EUR thousand	326	233	228

The amount recognized as cost from the share bonus scheme during the financial year was based on real financial profit and the probability at which the conditions based on result will be met. During the year, these conditions were met. The amount payable in cash changes until the handover of the shares, after which the allocations on remaining years will be final.

25. Employee benefits

The Group has different pension arrangements to cover employee pension security in different parts of the world. Pension security is based on each country's local legislation and standard practices. In Finland, pension security is largely provided in accordance with the Employees' Pensions Act. In some countries, supplementary pensions complement the pension security.

EUR thousand	2006	2005
Reconciliation of the employee benefit related to assets and liabilities		
Current value of unfunded obligations	412	309
Current value of funded obligations	814	524
Fair value of assets	-467	-210
Non-recorded actuarial gains (-) or losses (+)	-81	-33
Net liabilities in the balance sheet	678	590
Distributed in the balance sheet as follows:		
Employee benefit assets	-508	-243
Employee benefit liabilities	1,186	833
Net liabilities in the balance sheet	678	590

EUR thousand	2006	2005
Defined benefit pension costs in the income statement are determined as follows:		
Labour costs during the year	-109	-131
Interest expenses	-36	-32
Expected income from assets covered by the arrangements	6	8
Total	-139	-155
Changes in the current value of the liability are as follows:		
Liability at start of year	834	675
Current service cost	314	131
Interest cost	38	29
Actuarial gains (-) and losses (+)	0	-2
Total	1,186	833
Changes in the fair values of plan assets are as follows:		
Fair value of plan assets at start of year	-243	-159
Anticipated return	-6	-6
Actuarial gains (-) and losses (+)	-1	-22
Payments by employer to scheme	-258	-56
Fair value of plan assets at end of year	-508	-243

Plan assets are invested in bonds.

Key actuarial assumptions	2006	2005
Discount rate, %	4.00–4.60	4.25–4.5
Expected return on assets, %	5	5
Assumed future payrise, %	2–3	3
Assumed increase in pensions, %	1–2	1–2

The Group forecasts that it will pay EUR 0.2 million to defined benefit pension plans in 2007.

26. Interest-bearing liabilities

EUR thousand	2006	2005
Long-term		
Loans from financial institutions	1,828	1,675
Preferred capital notes	0	33
Finance lease liabilities	0	252
Total	1,828	1,960
Short-term		
Loans from financial institutions, following year's instalments	178	873
Finance lease liabilities, following year's instalments	252	320
Following year's instalments on preferred capital notes	0	289
Other loans	2,000	266
Total	2,430	1,748

Instalments	Loans from financial institutions	Finance lease liabilities	Other loans
2007	178	252	2,000
2008	748	0	0
2009	624	0	0
2010	456	0	0

Finance lease liabilities, EUR thousand	2006	2005
Finance lease liabilities mature as follows:		
In less than a year	255	333
In more than one year but less that five years	0	255
In more than five years	0	0
Total minimum rents	255	588

Finance lease liabilities, EUR thousand	2006	2005
Current value of minimum rents:		
In less than a year	252	320
In more than one year but less that five years	0	252
In more than five years	0	0
Total current value of minimum rents	252	572
Non-accrued financial expenses	3	17

Preferred capital notes

The 2005 financial statements contained preferred capital notes of EUR 289,746 received by the parent company from certain shareholders and preferred capital notes of EUR 32,554 received by Vacon Traction from Tekes. Both preferred capital notes were paid off during 2006.

27. Trade and other payables

EUR thousand	2006	2005
Trade payables	14,675	16,429
Other current liabilities	3,041	2,216
Interest payable and other financial liabilities	36	40
Allocations from employee benefits	5,685	5,358
Other accrued expenses and deferred income	2,173	1,933
Total	25,610	25,976

28. Provisions

EUR thousand	Warranty provision
Jan 1, 2006	790
Increases in provisions	652
Used provisions	-790
Dec 31, 2006	652

The Group issues a warranty for its products. Any defects discovered during the warranty period will be repaired at the company's expense or the customer will be provided with a corresponding product. Warranty provision is based on experience of faulty products in earlier years. The warranty provision is expected to be used in the year following its issue.

29. Risks and risk management

Risk management supports Vacon's growth

Vacon Group's risk management is part of the management process for the company's business operations. Risk management aims to ensure that the risks relating to business operations have been thoroughly surveyed and are effectively controlled. The goal is to minimize any damage arising from the risks and to identify the risks in managing the business. Risk management activities aim to ensure profitable growth for the company.

During 2005 Vacon Plc carried out an extensive survey of risks, led by an expert in risk management, and on the basis of this survey the company revised its risk management policy. In accordance with this policy, as part of the 2006 strategy processes the risk survey was updated. Vacon has defined several potential risks that may have an impact on future profitability and development. The most significant of these are:

- The risk that Vacon's products or operations cause injury to the personnel or damage to the property of customers or third parties and thus endanger the continuation of their business operations.
- The risk that Vacon's R&D fails or is delayed in its development projects for new products or the products fail to meet new customer requirements in terms of a product's performance or price/quality ratio.
- The risk that an unexpected harmful event endangers the delivery capability of Vacon's factory in Vaasa.
- The risk that, due to an unexpected harmful event or their financial situation or their problems with capacity, Vacon's main suppliers, component and software suppliers, are unable to supply their products on time and in accordance with agreed quality criteria.
- The risk that, during the production process and testing, a quality defect is not noticed in a product, its components or software, resulting in a major increase in quality costs or the recall of all the supplied products.
- The risk that continuous competition and R&D investments by competitors in the frequency converter market cause greater selling price erosion than anticipated or even the loss of key Vacon customer accounts.
- The risk that as demand rises the global market prices for certain materials and components rise more sharply than expected

A few risks are examined and analyzed separately below.

Risk management is pro-active

Vacon Group's risk management is proactive and aims to take all possible risks into account. The underlying principle is that risk management is spread throughout all levels of the organization. Each employee is encouraged to look out for risks, to assess them and to tell about them. Employees are expected to report any risks either to their immediate superior or to the Group's Vice President, Finance and Control.

The company's risk policy is explained to the entire personnel and also forms part of the initial training for new employees. Employers are provided with more information about risk management for example on the Group's intranet site.

The objectives of risk management are safe products and operating methods

Vacon has defined six objectives in its risk management policy and all decision-making aims at these:

1. Ensuring the safety of the personnel of Vacon, its customers and third parties.
2. Ensuring the safety and high quality of the company's products and operating methods.
3. Complying with local and international law, regulations and recommendations.
4. Ensuring awareness of risks and that they are taken into account in decision-making.
5. Ensuring the continuity of business operations and sustainable growth.
6. Protecting Vacon's brand and reputation.

Risk management is assessed every year

Risk management processes are reviewed annually as part of the strategy process.

The company's Board of Directors approves the risk management operating policies to be used and is aware of the key risks to the company. Vacon's Management Team assesses risk management, revises if necessary risk reporting, and reports to the Board on the company's key risks. Three main criteria are used to assess risks: the seriousness of the risk, the probability of the risk, and the current level of risk management for each identified risk.

The company's VP, Finance and Control, monitors and develops risk management procedures. In addition he supports the introduction of risk management and monitors risk reporting. He is also responsible for ensuring that Vacon's risk management complies with the company's corporate governance principles.

Managing business risks

Administrative risk

Vacon has operations throughout the world, with subsidiaries or branch offices in 16 countries and production in Finland and China. For this reason it is important that the Group has clear administrative guidelines. The company has defined the Group's administrative guidelines with different functions that have different tasks and duties. The objective of these is to ensure that all major matters and decisions are consistent and in line with the company's objectives.

Risks relating to business operations, sales and result

The risks relating to markets, products, customers, goods suppliers and components are monitored regularly as part of normal business processes. These risks are also assessed and monitored as part of the Group's strategy processes.

Customer credit risks

Credit risks relating to commercial operations are primarily the responsibility of the operative units. A credit policy has been defined for the sales organization that governs the delivery and payment terms granted to customers, how these are monitored, and the collection of payment. The parent company's finance function is a centralized provider of services relating to customer finance and monitors payment terms and the security demanded to ensure they comply with the principles of the finance policy.

Country risk is continuously monitored and limits are set to grant credit in areas where the political or financial situation is unstable. Some 90 % of the Group's receivables are from OECD countries, which represent a low country risk. This figure is expected to fall by a few percentage points in the next few years as new sales companies are set up.

Supplier risk

Vacon is dependent for its materials and components on its suppliers and their ability to supply products at the right time and in accordance with agreed quality criteria. On average 55 % of the Group's total costs are for components and materials, see table 'Costs and Revenues'. Coupled with the ability of suppliers to expand their own capacity, this can form a risk for Vacon.

For the sake of efficient logistics and the investments made, it is essential that suppliers are able to meet quality and environmental requirements and supply goods at the right time. For this reason, suppliers, their products and other services are monitored regularly. All the company's suppliers are audited at least once every two years.

Asset and liability risks

Vacon Plc aims to prevent damage with pro-active risk management action. It is particularly important to protect production plants. Vacon Plc has taken out global insurance schemes against property, business interruption, transport and liability risks. The Group's parent company administers all the global insurance schemes relating to the company's operations. Management of other insurance is spread among the different companies.

Management of finance risks

Finance risks

The finance function at the Group's parent company's is solely responsible for Vacon Plc's internal and external financing and for management of finance risks. It is responsible for the Group's liquidity, for ensuring sufficient financing, and for managing interest rate, currency and counterparty risks. The objective is to provide cost-effective financing for the Group's companies and reduce fluctuations in the result using various financing options.

Foreign exchange risk

The company has its own business operations in 16 countries. The group supplies its products and services through partners to a total of more than 100 countries. This means that the Group is exposed to foreign exchange risks arising from exports and imports, from internal transactions, financing for non-Finnish subsidiaries, and currency-denominated shareholders' equity.

The Group's biggest currency risks, however, arise from exports and imports. The Group's biggest invoicing currency, apart from the euro, is the US dollar, which accounts directly or indirectly for some 29% of the Group's invoicing. The other invoicing currencies are the Swedish krona, the Norwegian krone and the British pound. Together these account for some 10 % of the Group's invoicing. Currency linked purchases in the Group account for some 15% of revenues (all the above currencies).

In accordance with the Group's finance policy, money transactions between the Group's parent company and subsidiaries are made in the internal unit of accounting. This being the case, transaction risk focuses almost entirely on the Group's parent company and the Group's non-Finnish subsidiaries are not exposed to any significant transaction risk. In accordance with the Group's finance policy, binding delivery and purchase contracts are hedged in full. In addition, forecast currency-denominated cash flows in the parent company are hedged for six months for about 70 % of the estimated cash flow. The hedging instruments used are foreign exchange forwards.

The most significant exchange rate risks relating to investments come from the equity of the subsidiaries in Sweden, Norway, Great Britain, Australia, India and China and of the joint venture in the USA.

Changes in exchange rates can also cause a company's result to rise or decline, when the income statements and balance sheets of the above companies are translated into euro in the consolidated financial statements. The Group hedges selectively against exchange rate risks by using foreign currency loans. The Group's Board of Directors decides on the hedging policy.

Interest rate risk

Changes in the level of market interest rates and margins can affect the Group's financing costs, the income from financial investments and the valuation of financial derivative instruments. The

Group's net gearing and balance structure are such that interest rate risk is low. The Group hedges against interest rate risks through its choice of interest rate periods for loans. The Group held no open interest rate swaps at the balance sheet date. The Group's Board of Directors decides on the hedging policy.

Liquidity risk

The Groups aims to continually assess and monitor the amount of financing required by operations, so that the Group has sufficient liquid funds to finance operations and to repay loans as they mature. The Group maintains immediate liquidity with cash management solutions such as Group accounts and bank credit facilities. The amount of unused credit facilities on 31 December, 2006 was EUR 28.3 million. Surplus liquid funds are invested in partner banks. Liquid funds on 31 December 2006 totalled EUR 13.0 million.

Counterparty risks for financing operations

When the Group invests cash funds and enters into derivatives contracts, it only accepts as counterparty partner banks that are specified in the finance policy, meet credit-worthiness terms and are approved by the Board of Directors.

Costs and Revenues, 1 January – 31 December, 2006

	% of total costs	% of revenues
Materials	55%	49%
Services	3%	2%
Delivery costs and commission	4%	3%
Employee benefit related costs	19%	17%
Sales and marketing costs	4%	3%
Leases	3%	2%
Administrative costs	5%	4%
Other income and costs	4%	4%
Depreciation	3%	2%
Total	100%	88%

30. Derivative agreements to which hedge accounting has been applied

EUR thousand	Positive fair value	Negative fair value	Net fair value	Nominal value
2005				
Cash flow hedging				
Forward exchange contracts	20	-340	-320	17 468
2006				
Cash flow hedging				
Forward exchange contracts	193	-56	137	14 855

31. Operating leases

EUR thousand	2006	2005
Minimum rents for irrevocable operating leases:		
In one year	4,216	3,801
In more than one and less than five years	9,369	9,213
In more than five years	1,311	1,842
Total	14,896	14,856

32. Collateral and contingent liabilities

EUR thousand	2006	2005
For own debt/commitment		
Guarantees	1,075	1,198
Collateral given on behalf of associates		
Guarantees	0	382
Collateral given on behalf of others		
Guarantees	704	519

33. Other commitments

EUR thousand	2006	2005
Financial commitment in capital investment funds	1,494	1,681

34. Related party transactions

Vacon Group has a related party relationship with its associated companies, Board members, the parent company's President and CEO, the Management Team and their immediate family, and companies in which the said persons have a controlling interest or in which they exercise significant control.

The Group's control in its parent company and subsidiaries is as follows:	Group holding (%)	Group votes (%)
Parent company Vacon Plc, Vaasa, Finland		
Vacon GmbH, Essen, Germany	100.00	100.00
Vacon Benelux B.V., Gorinchem, the Netherlands	100.00	100.00
Vacon SpA, Reggio Emilia, Italy	100.00	100.00
Vacon Drives Ibérica S.A., Manresa, Spain	100.00	100.00
Vacon Drives (UK) Ltd, Leicestershire, Great Britain	70.00	70.00
Vacon AB, Solna, Sweden	100.00	100.00
Vacon AT Antriebssysteme GmbH, Leobersdorf, Austria	70.00	70.00
Vacon Americas LLC, Milwaukee, United States	50.00	50.00
ZAO Vacon Drives, Moscow, Russia	100.00	100.00
Vacon France SAS, Saint Pierre du Perray, France	70.00	70.00
Vacon AS, Holmestrand, Norway	80.00	80.00
Vacon Benelux NV/Sa, Heverlee, Belgium	100.00	100.00
Vacon Suzhou Drives Co. Ltd., Suzhou, China	100.00	100.00
Vacon Drives & Control Pvt Ltd, Chennai, India	100.00	100.00
Vacon Pacific Pty Ltd, Melbourne, Australia	75.00	75.00

Management cash-based employment benefits:	2006	2005
EUR thousand		
Salaries and other short-term benefits	1,899	1,551
Post-employment benefits	390	345
Share-based benefits	764	57
Total	3,053	1,953

	2006	2005
Management salaries and fees		
Laisi Vesa, President and CEO	457	262
Hiltunen Heikki, Executive Vice President	393	
Board members:		
Inborr Jan-Erik, Chairman	50	43
Ahlqvist Pekka	25	22
Eklund Jari	25	22
Heikkinen Kalle	25	22
Holma Mauri	25	22
Karppinen Veijo, Vice Chairman	25	22
Total	1,025	413

The retirement age of the parent company's President and CEO is 60 years.

Related party transactions with associates:	2006	2005
EUR thousand		
Sale of goods	0	779

Financial statements for the parent company

Income statement for the parent company (FAS)

EUR thousand	Note	Jan 1–Dec 31, 2006	%	Jan 1–Dec 31, 2005	%
Revenues	2	**159,936**	**100.0**	**129,690**	**100.0**
Change in inventories of finished goods and work in progress		794		886	
Other operating income		189		133	
Materials and services					
Materials and consumables					
Purchases during the financial year		-88,077		-70,218	
Change in inventories		706		693	
External services		-4,012		-2,901	
		-91,382	**-57.1**	**-72,426**	**-55.8**
Personnel expenses	3	-21,415		-17,776	
Depreciation and amortization	6	-3,237		-2,988	
Other operating expenses		-27,025		-22,823	
Operating profit		**17,860**	**11.2**	**14,696**	**11.3**
Financial income and expenses	7	-358		183	
Profit before appropriations and taxes		**17,501**	**10.9**	**14,879**	**11.5**
Appropriations	8	-712		-363	
Income taxes	9	-4,331		-3,998	
Profit for the financial year		**12,458**	**7.8**	**10,518**	**8.1**

Balance sheet for the parent company (FAS)

Assets, EUR thousand	Note	Dec 31, 2006	%	Dec 31, 2005	%
Fixed assets					
Intangible assets	10				
Development costs		282,		1,015	
Intangible rights		4,040		1,505	
Other long-term expenditure		49		34	
		4,371	5.9	2,554	3.7
Tangible assets	11				
Machinery and equipment		9,150		8,478	
Other tangible assets		42		37	
Construction in progress		930		1,999	
		10,122	13.6	10,514	15.4
Investments	12				
Investments in Group companies	13	5,868		5,645	
Receivables from Group companies		4,272		4,583	
Investments in associates				759	
Receivables from associates				645	
Other investments		1,313		1,054	
Other receivables		610		134	
		12,063	16.2	12,820	18.8
Total fixed assets		26,556	35.8	25,888	38.0
Current assets					
Inventories					
Materials and consumables		3,120		2,414	
Finished goods		3,331		2,536	
		6,451	8.7	4,950	7.3
Short-term receivables	14				
Trade receivables		32,684		28,449	
Loan receivables		1,197			
Other receivables		1,540		1,275	
Prepaid expenses and accrued income	15	675		604	
		36,096	48.6	30,328	44.5
Cash and cash equivalents		5,148		6,941	
Total current assets		47,696	64.2	42,219	62.0
Assets		**74,252**	**100.0**	**68,107**	**100.0**

Liabilities, EUR thousand	Note	Dec 31, 2006	%	Dec 31, 2005	%
Equity	16,17				
Share capital		3,059		3,059	
Share premium		4,966		4,966	
Retained earnings		25,266		20,980	
Profit for the financial year		12,458		10,518	
Total equity		45,749	61.6	39,523	58.0
Accumulated appropriations					
Depreciation difference	18	2,899	3.9	2,186	3.2
Liabilities	19				
Long-term liabilities					
Preferred capital notes				290	
Loans from financial institutions		1,828		1,676	
		1,828	2.5	1,965	2.9
Short-term liabilities					
Loans from financial institutions		2,179		872	
Advances received		361		290	
Trade payables		13,799		15,687	
Other current liabilities		546		676	
Provisions		652		790	
Accrued expenses and deferred income	20	6,240		6,117	
		23,776	32.0	24,433	35.9
Total liabilities		25,604	34.5	26,398	38.8
Total equity and liabilities		**74,252**	**100.0**	**68,107**	**100.0**

Cash flow statement for the parent company (FAS)

EUR thousand	Jan 1–Dec 31, 2006	Jan 1–Dec 31, 2005
Cash flow from operating activities:		
Profit for the financial year	**12,458**	**10,518**
Adjustments:		
Depreciation	3,237	2,988
Financial income and expenses	358	-183
Appropriations	712	363
Taxes	4,331	3,998
Other adjustments	-204	121
	20,893	17,805
Changes in working capital:		
Change in non-interest-bearing receivables	-4,366	-9,841
Change in inventories	-1,501	-1,579
Change in non-interest-bearing liabilities	-1,541	4,318
	-7,408	-7,102
Interest received	334	278
Interest paid	-264	-152
Dividends received	750	500
Other financial items	-36	11
Taxes paid	-4,554	-3,593
Cash flow from operating activities	**9,715**	**7,747**
Cash flow from investing activities:		
Investments in tangible and intangible assets	-4,923	-3,920
Proceeds from the disposal of tangible and intangible assets	260	
Loans granted	-1,365	-1,129
Other investments	-801	-153
Repayments on loan receivables	312	693
Proceeds from the divestiture of other investments	270	29
Cash flow from investing activities	**-6,248**	**-4,480**

EUR thousand	Jan 1–Dec 31, 2006	Jan 1–Dec 31, 2005
Cash flow from financing activities:		
Share repurchases		-1,021
Withdrawals (+) and instalments (-) of long-term loans	158	366
Increase (+) or decrease (-) in short-term financing	1,104	-1,533
Increase (+) or decrease (-) in preferred capital notes	-290	
Dividends paid	-6,232	-5,320
Cash flow from financing activities	**-5,260**	**-7,508**
Change in liquid funds	**-1,793**	**-4,241**
Liquid funds at the beginning of the period	6,941	11,182
Liquid funds at the end of the period	5,148	6,941

Notes to the financial statements for the parent company

1. Accounting principles for financial statements

General accounting principles
The financial statements of Vacon Plc have been prepared and presented in accordance with the Finnish Accounting Standards (FAS) and other laws and regulations in force in Finland.

When preparing the financial statements, the company's management is required by the regulations in force and good accounting practice to make assessments and assumptions that affect the valuation and allocation of the financial statement items. Although the assessments are based on the latest available information, the final figures may differ from these assessments.

Revenues
Sales are recognized in connection with the transfer of ownership-related risks and benefits to the buyer. Usually sales are recognized at the date of delivery. Sales adjustment items include cash discounts as well as exchange rate profits and losses on sales.

Long-term projects are partially recognized as income for the financial period in cases that involve fixed-price contracts the outcome of which can be reliably assessed. The percentage-of-completion required in long-term projects is measured from the share of the to-date costs of the estimated total costs of the project, ie with the cost-cost method. If it is likely that the overall costs of the project will exceed the overall income, the expected losses are recognized as expenses immediately.

Foreign currency items
Business transactions in foreign currencies are recorded at the exchange rates on the transaction date. Receivables and payables on the balance sheet date are measured at the average exchange rate on the balance sheet date. Exchange rate differences associated with sales and purchases are recorded as adjustments to these items. Exchange rate gains and losses related to financial operations are recorded under financial income and expenses.

Preferred capital notes
The parent company had no preferred capital notes at the end of 2006. The 2005 preferred capital notes were transferred in accordance with the requirements of the new Finnish Companies Act from equity to a liabilities item.

Derivative contracts
Foreign currency items are hedged with forward contracts. Open foreign currency hedging instruments are measured at fair value on the balance sheet date and recorded under sales adjustment items in the income statement. The accounting principles for the consolidated financial statements contain more details about the use of financial instruments.

Pension arrangements
Statutory and supplementary pension obligations are covered through payments to pension insurance companies and recorded as determined by periodical actuarial calculations prepared by those institutions.

Leasing and rental liabilities
Leasing payments are treated as rentals. Unpaid leasing and rental fees are recorded under leasing and rental liabilities in the notes to the parent company financial statements.

Research and development costs
Research and development costs are recorded under expenses. Before 2004, the parent company has capitalized major projects that have met the requirements of the 50/1998 decision of the Finnish Ministry of Trade and Industry. Capitalized development expenses are amortized during their effective life span but no later than in five years. R&D grants received are entered as deductions under the relevant items.

Income taxes
The company's taxes include taxes paid and accrued corresponding to the financial result for the period based on taxable income calculated in accordance with Finnish tax regulations, and adjustments to taxes from previous financial periods.

Fixed assets and depreciation
Fixed assets are measured in the balance sheet at their original acquisition cost less accumulated planned depreciation. Planned depreciation is calculated on a straight-line basis on the original acquisition cost, based on the estimated useful economic life. The depreciation schedule in accordance with the consolidated accounting principles is as follows:

Intangible assets	5–8 years
Machinery and equipment	4–15 years
Other tangible assets	5–10 years

Investments
Investments are measured at acquisition cost. When disposing of a long-term asset, the difference between sales price and current balance sheet value is recognized as expense or income.

Investments in subsidiaries are measured at acquisition cost in the balance sheet. Investments in associated companies are presented as other investments in the balance sheet. Associated companies include companies in which Vacon has either directly or indirectly more than 20 % but less than 50 % of the voting rights.

Inventories
Inventories are measured at the acquisition cost or the net realizable value, whichever is lower. As from 1 June 2006 the acquisition cost has been determined using the FIFO method. Previously the acquisition cost was determined using the weighted average cost method. This change has a very small impact on the parent company's result. The acquisition cost of finished goods and work in progress includes raw materials, direct salaries and other direct expenses as well as the appropriate share of indirect production costs, excluding interest expenses. When applying the lowest value principle, the value is based on the estimated sales price in ordinary activities less the costs associated with the sale of products.

Dividends and own shares

Dividends proposed by the Board of Directors are not recorded in the financial statements until they have been approved by the Annual General Meeting.

When purchasing the company's own shares, the amount paid for them, including direct purchase costs, is recorded as a decrease in shareholders' equity.

2. Revenues

EUR thousand	2006	2005
Revenues by market area		
Europe	106,509	86,472
North America	37,626	28,929
Asia and Australia	12,765	11,711
Others	3,036	2,578
Total	159,936	129,690
Projects recognized using the percentage-of-completion method		
Revenue recognized as income	937	1,245
Accumulated revenue from uncompleted projects	818	1,385
Amount not recognized as income from uncompleted projects	316	350

3. Personnel costs

EUR thousand	2006	2005
Wages and salaries		
Salaries of President, his deputy and members of the Board of Directors	-1,025	-413
Other wages and salaries	-16,036	-13,820
Total	-17,061	-14,233
Other indirect personnel costs		
Pension costs	-2,852	-2,331
Other personnel costs	-1,502	-1,212
Total	-4,354	-3,543

Salaries and fees of the President, his deputy and Board members are presented in note 34 to the Consolidated Financial Statements.

4. Average number of personnel

	2006	2005
Office personnel	232	212
Factory personnel	174	146
Total	406	358

5. President's pension commitments

The retirement age of the parent company's President and CEO is 60 years.

6. Depreciation and amortization

EUR thousand	2006	2005
Intangible assets	-1,300	-1,090
Tangible assets	-1,938	-1,898
Total	-3,237	-2,988
Total planned depreciations	-3,237	-2,988

7. Financial income and expenses

EUR thousand	2006	2005
Dividend income		
From Group companies	745	500
Total	745	500
Interest income and other financial income		
From long-term investments in Group companies	210	179
From others	135	99
Total	344	278
Write-down of long-term investment		
Group companies	-47	-388
Associated companies	-1,098	0
Others	-2	0
Total	-1,146	-388
Interest expenses and other financial expenses		
From others	-302	-207
Total	-302	-207
Total financial income and expenses	-358	183

8. Appropriations

EUR thousand	2006	2005
The difference between planned depreciation and depreciation presented for taxation	-712	-363

9. Income tax

EUR thousand	2006	2005
Direct taxes for current year	-4,532	-3,993
Direct taxes for previous years	206	0
Other taxes and similar payments	-5	-5
Total	-4,331	-3,998

10. Intangible assets

EUR thousand	Development costs	Intangible rights	Other long-term expenditure	Total 2006	Total 2005
Acquisition cost Jan 1	4,966	2,848	140	7,955	7,299
Increases		3,263	44	3,307	656
Decreases		-190		-190	0
Acquisition cost Dec 31	4,966	5,922	184	11,072	7,955
Accumulated amortization Jan 1	-3,952	-1,343	-107	-5,402	-4,310
Amortization for the financial year	-732	-539	-29	-1,300	-1,091
Accumulated amortization Dec 31	-4,684	-1,882	-135	-6,701	-5,401
Carrying amount Dec 31, 2006	282	4,040	49	4,371	
Carrying amount Dec 31, 2005	1,015	1,505	34		2,554

11. Tangible assets

EUR thousand	Machinery and equipment	Advance payments and construction in progress	Other tangible assets	Total 2006	Total 2005
Acquisition cost Jan 1	19,077	1,999	37	21,113	17,861
Increases	2,680	930	5	3,615	3,252
Decreases	-70	-1,999		-2,069	0
Acquisition cost Dec 31	21,687	930	42	22,659	21,113
Accumulated depreciation Jan 1	-10,599			-10,599	-8,700
Accumulated depreciation on decreases	6			6	0
Depreciation for the financial year	-1,944			-1,944	-1,899
Accumulated depreciation Dec 31	-12,537	0	0	-12,537	-10,599
Carrying amount Dec 31, 2006	9,150	930	42	10,122	
Carrying amount Dec 31, 2005	8,478	1,999	37		10,514

12. Investmets

EUR thousand	Shares in Group companies	Shares in associates	Other investments	Total 2006	Total 2005
Shares Jan 1	5,645	759	1,054	7,458	7,722
Increases	610		260	870	153
Decreases	-340	-759		-1,098	-29
Write-down	-47		-2	-48	-388
Carrying amount Dec 31	5,868	0	1,313	7,181	7,458

EUR thousand	Receivables from Group companies	Receivables from associates	Other receivables	Total 2006	Total 2005
Receivables Jan 1	4,583	645	134	5,362	4,911
Increases	493		170	663	1,145
Decreases and transfers between items	-804	-340		-1,144	-693
Carrying amount Dec 31	4,272	305	304	4,881	5,362
Total investments Dec 31				12,063	12,820

13. Shareholdings

	Parent votes %	Parent holding %
Group companies		
Vacon GmbH, Essen, Germany	100.00	100.00
Vacon Benelux B.V., Gorinchem, the Netherlands	100.00	100.00
Vacon SpA, Reggio Emilia, Italy	100.00	100.00
Vacon Drives Ibérica S.A., Manresa, Spain	100.00	100.00
Vacon Drives (UK) Ltd, Leicestershire, Great Britain	70.00	70.00
Vacon AB, Solna, Sweden	100.00	100.00
Vacon AT Antriebssysteme GmbH, Leobersdorf, Austria	70.00	70.00
Vacon Americas LLC, Milwaukee, United States	50.00	50.00
ZAO Vacon Drives, Moscow, Russia	100.00	100.00
Vacon France SAS, Saint Pierre du Perray, France	70.00	70.00
Vacon AS, Holmestrand, Norway	80.00	80.00
Vacon Benelux NV/Sa, Heverlee, Belgium	99.00	99.00
Vacon Suzhou Drives Co. Ltd., Suzhou, China	100.00	100.00
Vacon Drives & Control Pvt Ltd, Chennai, India	100.00	100.00
Vacon Pacific Pty Ltd, Melbourne, Australia	75.00	75.00

14. Short-term receivables

EUR thousand	2006	2005
Receivables from Group companies		
Trade receivables	16,761	13,676
Total	16,761	13,676
Receivables from others		
Trade receivables	15,923	14,773
Short-term loan receivables	1,197	0
Other receivables	1,540	1,275
Prepaid expenses and accrued income	675	604
Total	19,335	16,652
Total short-term receivables	36,096	30,328

15. Key items included in prepaid expenses and accrued income

EUR thousand	2006	2005
Projects recognized based on their percentage of completion	66	153
Subsidies	25	329
Share bonus receivables	153	0
Others	431	122
Total	675	604

16. Equity

EUR thousand	2006	2005
Share capital Jan 1	3,059	3,059
Share capital Dec 31	3,059	3,059
Share premium Jan 1	4,966	4,966
Share premium Dec 31	4,966	4,966
Retained earnings Jan 1	31,498	27,321
Dividends paid	-6,232	-5,320
Share repurchase	0	-1,021
Retained earnings Dec 31	25,266	20,980
Profit for the financial year	12,458	10,518
Total shareholders' equity	45,749	39,523

17. Distributable profit funds

EUR thousand	2006	2005
Retained earnings	25,266	20,980
Profit for the financial year	12,458	10,518
Total	37,724	31,498

18. Accumulated appropriations

In the parent company, accumulated depreciation difference accounts for the accumulated appropriations.

19. Liabilities

EUR thousand	2006	2005
Long-term liabilities		
Interest-bearing		
Loans from financial institutions	1,828	1,676
Preferred capital notes	0	290
Total	1,828	1,965
Total long-term liabilities	**1,828**	**1,965**
Short-term liabilities		
Interest-bearing		
Loans from financial institutions	2,179	872
Liabilities to Group companies	97	299
Total	2,276	1,171
Non-interest-bearing		
Advances received	361	290
Trade payables	13,235	15,110
Trade payables to Group companies	564	577
Other short-term liabilities	449	377
Warranty provisions	652	790
Accrued expenses and deferred income	6,080	6,117
Accrued debts to Group companies	160	0
Total	21,501	23,261
Total short-term liabilities	**23,776**	**24,432**
Interest-bearing liabilities	4,104	3,137
Non-interest-bearing liabilities	21,501	23,261
Total liabilities	25,604	26,398

Preferred capital notes

The 2005 financial statements included preferred capital notes of EUR 289,746 received from certain shareholders. The notes were paid off during 2006.

20. Key items included in accrued expenses and deferred income

EUR thousand	2006	2005
Salaries including social security costs	4,016	4,027
Taxes	745	968
Interest	43	40
Others	1,436	1,082
Total	6,240	6,117

21. Currency derivatives

EUR thousand	2006	2005
Forward contracts		
Fair value	137	-321
Nominal value	14,855	17,468

Derivative contracts are used only for hedging against currency risks. The contracts mentioned above were open on the balance sheet date.

22. Collateral and contingent liabilities

EUR thousand	2006	2005
Guarantees		
On behalf of Group companies	702	702
On behalf of others	704	901
Total	1,406	1,603
Amounts payable under leasing agreements		
Payable in the following financial year	1,182	1,144
Payable later	1,218	751
Total	2,400	1,895
Payable amounts on rental agreements		
Payable in the following financial year	2,077	2,086
Payable later	6,077	8,249
Total	8,154	10,335
Other commitments		
Financial commitments	1,494	1,681
Total	1,494	1,681

Signatures for the Board of Directors' Report and financial statements

Vaasa, 8 February 2007

Jan Inborr
Chairman

Pekka Ahlqvist

Jari Eklund

Kalle Heikkinen

Mauri Holma

Veijo Karppinen

Vesa Laisi
President and CEO

Auditors' report

Translation

To the shareholders of Vacon Plc

We have audited the accounting records, the report of the Board of Directors, the financial statements and the administration of Vacon Plc for the period January 1 – December 31, 2006. The Board of Directors and the Managing Director have prepared the consolidated financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, containing the consolidated balance sheet, income statement, cash flow statement, statement on the changes in equity and notes to the financial statements, as well as the report of the Board of Directors and the parent company's financial statements, prepared in accordance with prevailing regulations in Finland, containing the parent company's balance sheet, income statement, cash flow statement and notes to the financial statements. Based on our audit, we express an opinion on the consolidated financial statements, as well as on the report of the Board of Directors, the parent company's financial statements and the administration.

We conducted our audit in accordance with Finnish Standards on Auditing. Those standards require that we perform the audit to obtain reasonable assurance about whether the report of the Board of Directors and the financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the report and in the financial statements, assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation. The purpose of our audit of the administration is to examine whether the members of the Board of Directors and the Managing Director of the parent company have complied with the rules of the Companies Act.

Consolidated financial statements

In our opinion the consolidated financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a true and fair view, as defined in those standards and in the Finnish Accounting Act, of the consolidated results of operations as well as of the financial position.

Parent company's financial statements, report of the Board of Directors and administration

In our opinion the parent company's financial statements have been prepared in accordance with the Finnish Accounting Act and other applicable Finnish rules and regulations. The parent company's financial statements give a true and fair view of the parent company's result of operations and of the financial position.

In our opinion the report of the Board of Directors has been prepared in accordance with the Finnish Accounting Act and other applicable Finnish rules and regulations. The report of the Board of Directors is consistent with the consolidated financial statements and the parent company's financial statements and gives a true and fair view, as defined in the Finnish Accounting Act, of the result of operations and of the financial position.

The consolidated financial statements and the parent company's financial statements can be adopted and the members of the Board of Directors and the Managing Director of the parent company can be discharged from liability for the period audited by us. The proposal by the Board of Directors regarding the disposal of the profit is in compliance with the Companies Act.

Vaasa, February 8, 2007
KPMG OY AB

(Signed)
Pekka Pajamo
Authorized Public Accountant

Shares and shareholders

Share capital and shares

Vacon has a share capital of EUR 3,059,000 divided into 15,295,000 fully paid shares. According to the Articles of Association, the minimum share capital is EUR 1 million (1,000,000) and maximum share capital is EUR 4 million (4,000,000). Vacon has one share series. Each share has a nominal value of EUR 0.20, and each share entitles the holder to one vote at the general meeting of shareholders.

Redemption of shares

A shareholder whose holding of all company shares or of the voting rights conferred by the shares reaches or exceeds 33 1/3 % or 50 % is obliged on demand by other shareholders to redeem the shares of such shareholders in the manner prescribed in the Articles of Association.

Authorizations held by the Board of Directors

The Annual General Meeting held on April 6, 2006 authorized the Board of Directors to decide on the purchasing and disposal of the company's own shares. The authorization will be valid until April 5, 2007. The number of shares that may be purchased and disposed of shall be no more than 764,750, which represents 5 % of the registered share capital and total voting rights at the time of the shareholders' meeting. Shares may be purchased for the purpose of developing the capital structure of the company, to be used in the financing of business acquisition or other transactions, or for the purpose of otherwise being transferred or canceled. The company's own shares may also be purchased to be used in key personnel incentive schemes, or to be used as payment of salaries or fees. The purchase of own shares will reduce the company's distributable retained earnings. Cancellation of the shares requires a separate resolution by a shareholders' meeting to reduce the company's share capital.

The Board of Directors shall decide on the disposal price of the shares and on the principles used to determine the price, and the shares may be disposed of for consideration other than cash, or otherwise on specific terms and conditions or by using the right of set-off.

The Board holds no authorization to issue new shares, convertible bonds or bonds with warrants.

Own shares

Under the authorization given at the AGM of March 25, 2004, the Board of Directors decided to purchase a maximum of 200,000 company shares in public trading. The purchase of shares began on December 27, 2004. At the end of 2006, the company held a total of 81,572 of its own shares.

Shareholdings of the Board of Directors and Management Team

On December 31, 2006, members of the Board of Directors of Vacon Plc held a total of 557,420 shares, or 3.6 per cent of the company's share stock. The President and CEO and other members of the Management Team held a total of 455,640 shares, or 3.0 % of the company's share stock and voting rights.

Market capitalization and trading

The shares of Vacon Plc have been quoted on the Helsinki Exchanges since December 14, 2000. Vacon's company code on the Helsinki Exchanges is VAC and its trading code is VAC1V. Each share carries one vote. New shares entitle holders to dividend for the period during which they were subscribed. Other shareholder rights are applicable from the date the increase in share capital was registered in the Trade Register. The shares have been entered in the book-entry securities system. During 2006, a total of 4,439,458 company shares with a value of EUR 101.0 million were traded on the stock exchange. The highest share price during the year was EUR 26.99 and the lowest EUR 17.70. The closing price on the last day of 2006 was EUR 26.10 and the company's market capitalization was EUR 397.1 million.

Incentive schemes

Vacon has an incentive scheme for all personnel. In January 2005, Vacon's Board of Directors decided to set up a share bonus scheme to ensure the long-term motivation and commitment of the Group's management and key personnel. The duration of the share bonus scheme is three years. The Board of Directors will set annually the revenue, profit and working capital turnover objectives that will determine the amount of the reward in accordance with the terms and conditions of the stock option scheme.

Dividend policy

The dividend policy adopted by Vacon's Board of Directors is to propose a dividend that is in line with the company's financial performance. The goal is to distribute approximately 50 per cent of the period's net profit in dividends. When determining the dividend, the financing required for the growth of operations is taken into consideration. Vacon's Board of Directors has decided to propose to the Annual General Meeting to be held on March 28, 2007 that a dividend of EUR 0.65, or 63 per cent of the Group's earnings per share, be paid for 2006.

Shareholders

At the end of 2006, Vacon had 3,731 registered shareholders. The largest shareholder was Ahlström Capital Oy, which held 15.0 % of the shares. The number of nominee registered shares and those registered by foreigners totaled 27.5% of the shares.

Private persons owned 32.7% of the shares. Up-to-date information on Vacon's share price and ownership structure is available on Vacon's website at www.investors.vacon.com.

Distribution of shareholding

	Holdings	%	Number of shares	%
By number of shares held				
Number of shares				
1–500	2,916	78.2	628,550	4.1
501–1 000	381	10.2	310,095	2.0
1 001–5 000	273	7.3	616,181	4.1
5 001–10 000	57	1.5	428,535	2.8
10 001–50 000	64	1.7	1,327,745	8.7
Over 50 000	40	1.1	11,983,894	78.4
Total	3,731	100.0	15,295,000	100.0
By shareholder group				
Corporations			3,160,954	20.7
Banks and insurance companies			1,539,156	10.1
Nominee-registered and foreign shareholders			4,211,543	27.5
Non-profit and public sector institutions			1,378,257	9.0
Households			5,005,090	32.7
Total			15,295,000	100. 0

Major shareholders Dec 31, 2006	No. of shares	% of shares
Ahlström Capital Oy	2,297,996	15.0
Tapiola Mutual Pension Insurance Company	584,500	3.8
Vaasa Engineering Oy	436,433	2.9
Koskinen Jari	356,350	2.3
Holma Mauri	347,171	2.3
Tapiola Group companies	325,300	2.1
Ehrnrooth Martti	325,070	2.1
Niemelä Harri	309,840	2.0
Investment Fund ABM Amro Finland	234,480	1.5
Karppinen Veijo	209,349	1.4
Nominee registered and in foreign ownership	4,211,543	27.5
Others	5,656,968	37.0
Total	15,295,000	100.0
Vacon Plc's own shares	-81,572	
Number of shares outstanding	15,213,428	

Information for investors

Annual General Meeting

The Annual General Meeting of Vacon Plc will be held at 3.00 pm on Wednesday, 28 March 2007 at the company's head office at Runsorintie 7, Vaasa, Finland.

Shareholders wishing to attend the Annual General Meeting must be registered on 16 March 2007 in the company's list of shareholders maintained by the Finnish Central Securities Depository and shall notify the company not later than 4.00 pm (Finnish time) on 21 March 2007. Shareholders are requested to give their name, address, telephone number and date of birth when informing the company of their attendance. This can be done by telephone to Johanna Koskinen on +358 201 212 528, by fax +358 201 212 208, by e-mail johanna.koskinen@vacon.com or by mail to Vacon Plc, Johanna Koskinen, Runsorintie 7, 65380 Vaasa, Finland. Any letters of authorization should be sent to the above address by the date for notification.

Share register

Shareholders are requested to inform the book-entry securities register where they have their book-entry securities account of any changes in address, name or holdings.

Payment of dividends

The Board of Directors proposes to the Annual General Meeting that a dividend of EUR 0.65 per share be paid for the 2006 financial year. The dividend approved by the AGM will be paid to shareholders who are registered on the record date in the company's list of shareholders maintained by the Finnish Central Securities Depository. The record date for the dividend payment is 2 April 2007 and the proposed payment date for the dividend is 11 April 2007.

Financial reports in 2007

Vacon is publishing three interim reports in 2007 as follows:

– January-March: 26 April 2007 at 10.00 am
– January-June: 2 August 2007 at 10.00 am
– January-September: 25 October 2007 at 10.00 am

The reports can be seen immediately after publication on Vacon's website at www.investors.vacon.com. The website also contains other material for investors.

Investor relations

The objective of Vacon's investor communications is to provide the financial markets with information about Vacon's strategies, operations and business environment so as to form as accurate a picture as possible of Vacon as an object for investment.

Responsibility for investor relations at Vacon:

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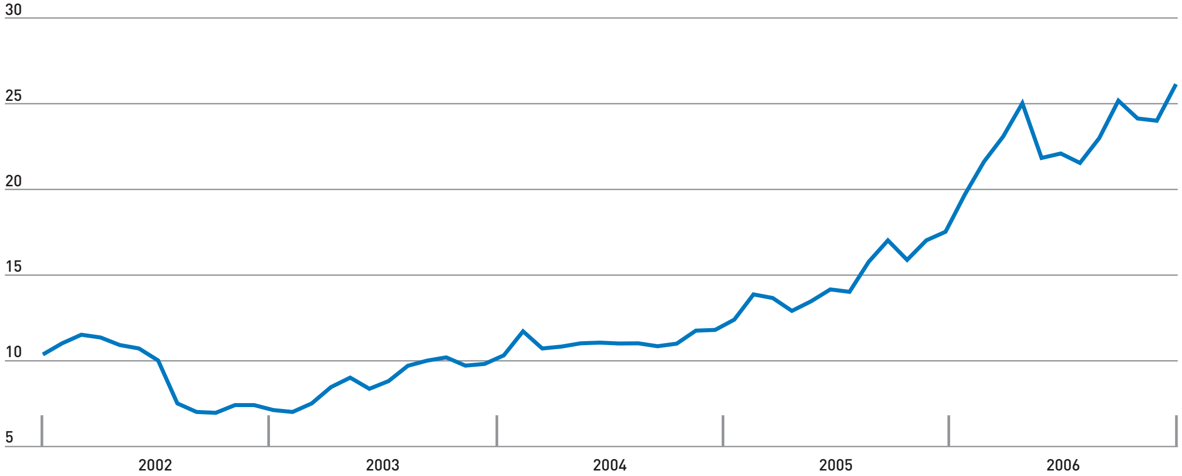
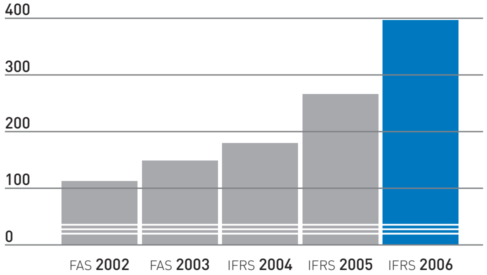
Share data

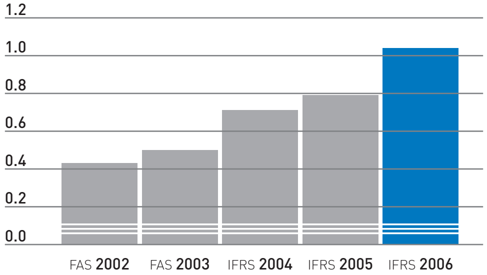
Share quotations 2002–2006



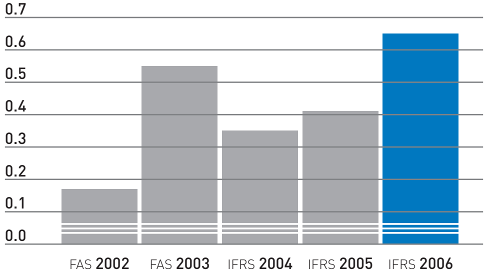
Market capitalization, MEUR



Earnings per share, EUR



Dividend by share, EUR *)



*) The 2006 dividend is the Board of Directors' proposal to the Annual General Meeting.

www.vacon.com