

**VILKYŠKIŲ PIENINĖ**  
**ANNUAL REPORT 2006**

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## INTRODUCTORY REMARK OF GENERAL DIRECTOR G. BERTAŠIUS

2006 has been a year of growth and expansion for Vilkyškių pieninė. The award of the most important event of the year should go to listing company's shares on Vilnius stock exchange. 17th of May, the day, when Vilkyškių pieninė shares showed up on the I-list of Vilnius stock exchange is indeed a memorable moment, which marks a qualitatively new chapter in company's history. During 24th of April - 4th May 2006 10% of company's shares were successfully distributed, in total 935 300 common stock. More than 390 investors chose to participate in the IPO which was 5% oversubscribed.

In line with company plans, the first stage of modernization of cheese production project was completed with the help of EU structural funds financing. Investments into modern technologies meeting the highest EU hygiene requirements are a guarantee of safe production process and highest quality cheese. It also allows further increases in company's production effectiveness, increases in competitiveness both in domestic and foreign markets. The maximum production output increased from 10 thou to 14 thou tons of cheese per year.

The development of the company's product assortment also gives reasons for optimism. In the beginning of 2006, after the acquisition of JSC „Modest“, „Mozzarella“ type cheese became the latest addition to the product line. As „Mozzarella“ cheese types are quite popular among Lithuanian customers, the company is planning further investment into development and expansion of „Mozzarella“ production, keeping in pace with changes in customer habits and attitudes.

Activities in foreign markets have also been very successful during 2006. Exports into Russia alone increased by more than fourfold, and made up a total of total 15% of company's sales. 2006 was a year of breakthrough, when cooperation with partners from Western, Eastern Europe and Scandinavia was further amplified, concurrently new business contacts were made in the new European Union countries. Since this year, the majority of Vilkyškių pieninė production reaches foreign markets not as industrial cheese, but as niche-gourmet, higher value added, and Vilkyškių pieninė branded products.

Company meets 2007 renewed, enlarged, and full of ambitious plans for the future. Being one of the most modern and currently the only fully specialized cheese dairy in Lithuania and having anchored its positions in European markets, Vilkyškių pieninė reached the stage of a mature business. Recent years have been marked as years of rapid growth, however now the time has come to move further through the path of quality, business contacts and well build reputation.

## I. GENERAL INFORMATION

### 1. Reporting period

2006.

### 2. Information about the issuer

Company name	Vilkyškių pieninė
Share capital	9 353 000 LTL
Headquarters	Vilkyškiai, Pagėgių municipality
Phone	8-441 55330
Fax	8-441 55242
E-mail	centras@cheese.lt
Legal form	Public limited company
Registration date and place	10 May 1993
Re-registration date and place	30 December 2005, Register centre Tauragė department
Registration No.	060018
Company code	277160980
Web page	<a href="http://www.cheese.lt">http://www.cheese.lt</a>

### 3. Main activity of issuer

Main activity of Vilkyškių pieninė – production of various types of cheese.

The company also produces butter, butter mixtures, processed cheese and cheese products.

### 4. Availability of the report and related documents

It is possible to get a look at the annual report at the Vilkyškių pieninė headquarters in Vilkyškiai, Pagėgiai municipality, at working days from 8 to 17.

All information, which according to the corresponding law acts must be published publicly, will be published through „Lietuvos Žinios“ newspaper or sent to shareholders via registered mail.

Information about main events in the company will be disclosed via information system of securities trading house, BNS news portal, and other media services.

## 5. Persons, responsible for the presented information

### 5.1 Vilkyškių pieninė:

Vilkyškių pieninė managing director Gintaras Bertašius, phone (8 441) 55330, fax (8 441) 55242.

Vilkyškių Pieninė senior accountant Birutė Bazilienė, phone (8 441) 70423, fax (8 441) 55242.

### 5.2 Consultants:

JSC „Orion securities“, A. Tumėno st. 4 B, LT-01109, Vilnius, phone +370 5 2313833, fax +370 5 2313840.

„Orion Securities“ representative – corporate finance analyst Vilius Maniušis, tel. +370 52 60 39 69.

## 6. Confirmation of the correctness of information.

Vilkyškių pieninė, represented by managing director Gintaras Bertašius and senior accountant Birutė Bazilienė, confirms, that disclosed information in this annual report meets reality, and that there are no un-disclosed facts, which might influence decisions of investors or affect market price of issuer's securities.

Vilkyškių pieninė

Managing director Gintaras Bertašius

.....

Vilkyškių pieninė

Senior accountant Birutė Bazilienė

.....

JSC „Orion securities“ representative

Financial analyst Vilius Maniušis

.....

Annual report prepared in Vilnius, May 2007.

## II. INFORMATION ABOUT SHARE CAPITAL AND ISSUER'S SECURITIES

## 7. Share capital

## Authorized capital

Name of securities	Number of securities	Nominal value, LTL	Total nominal value, Lt	Part of share capital, %
Common stock	9 353 000	1,00	9 353 000	100 %

## Information about prospective increase of share capital

-

## 8. Shareholders

The number of shareholders on the 20th April 2007 was equal to 395. Shareholders, owning more than 5% of total share capital are listed below:

Name, surname	Number of common stocks	Part of share capital, %	Part of votes, %
Gintaras Bertašius (p. c. 36401260554)	6 016 506	64,33	64,33
Martynas Bertašius (p.c. 38701180923)	935 000	9,996	9,996
Gabrielė Bertašiūtė (p.c. 49004101873)	935 000	9,996	9,996

## 9. Characteristics of securities, traded in the stock exchange

Vilkyškių pieninė common stock is traded on Vilnius stock exchange since 17<sup>th</sup> May 2006. ISIN code - LT0000127508.

Securities name- Vilkyškių pieninė common stock. Number of shares - 9 353 000. Nominal value of 1 share: 1,00 LTL.

Period		Price, LTL			Turnover, thou LTL			Total turnover		Capitalization, LTL
From	Until	Max	Min	Last	Max	Min	Last	Shares	Sum, LTL	
2006.05.	2007.04..2	5,82	4,80	5,70	647,8	0	0	531	2	53 310



17	0							126	821 828	000
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10.Information about the shares, which are registered and placed for non-public circulation of securities

-

11.Information about depository receipts issued on the basis of shares

-

12.Main characteristics of debt securities issued into public circulation of securities

-

13.Information about debt securities, which are registered and placed for non-public circulation of securities

-

14.Securitys, which do not certify the participation in the share capital but circulation of which is regulated by the Law on Public Trading, except debt securities

-

### III. INFORMATION ABOUT SECONDARY CIRCULATION OF SECURITIES ISSUED BY THE ISSUER

#### 15. Securities included into trading lists of stock exchanges

The following securities of Vilkyškių pieninė are included into the I-list of Vilnius Stock Exchange (VSE ticker - VPL1L):

Type of securities	Number of securities	Nominal value, LTL	Total nominal value, LTL	ISIN code
Common stock	9 353 000	1,00	9 353 000	LT0000127508

#### 16. Trading in Issuer's securities on stock exchange

Trading in Vilkyškių pieninė common stock on Vilnius stock exchange:

Period	Price (LTL)		Turnover (LTL)	
	max	min	max	min
2006 05 17 - 2006 06 30	5.60	5.25	647,808	0,00
2006 07 01 - 2006 09 30	5.50	5.20	202,990	0,00
2006 10 01 - 2006 12 31	5.30	4.80	360,722	0,00

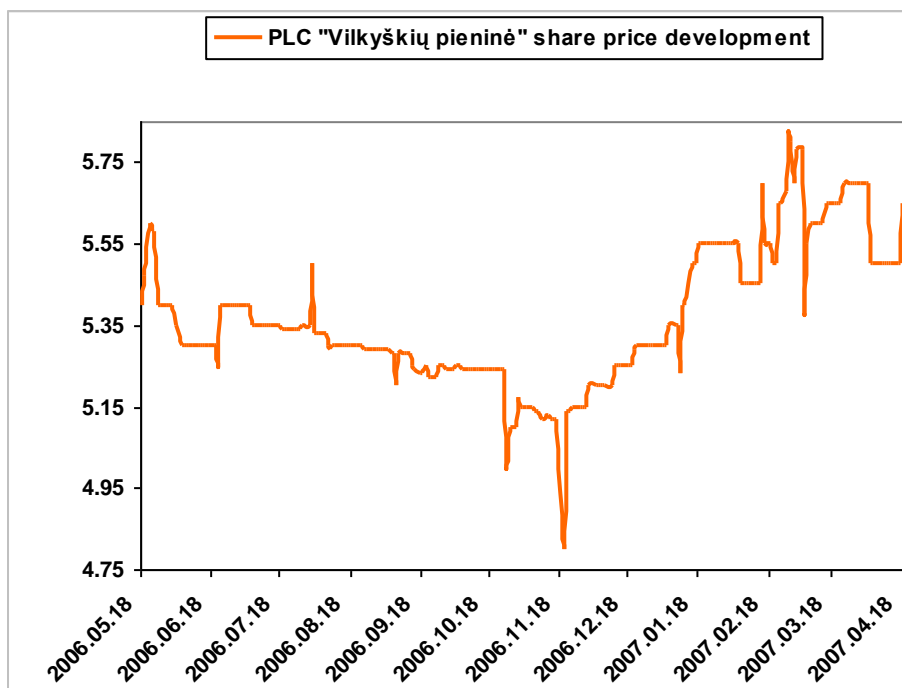
Period	Price (LTL)		Turnover (LTL)	
	max	min	max	min
2006 05 17 - 2006 06 30	0,00	0,00	173,491	919,265
2006 07 01 - 2006 09 30	0,00	0,00	84,050	441,769
2006 10 01 - 2006 12 31	0,00	0,00	137,665	711,659

#### 17. Market capitalisation of securities

Capitalisation of Vilkyškių pieninė common stock traded on Vilnius stock exchange:

Period	Number of stocks	Share price (LTL)	Capitalisation (LTL)
2006 06 30	9,353,000	5.40	50,506,200
2006 09 30	9,353,000	5.24	49,009,720
2006 12 31	9,353,000	5.30	49,570,900

Graph of Vilkyškių pieninė share price development from 2006.05.17 until 2007.04.20 is presented below:



18.Trading in Issuer's securities outside the stock exchange

-

19.Information about the buy-back of own shares by the Issuer

-

20.Announcement of the official tender offer

-

21.Issuer's paying agents

-

22.Agreements with intermediaries of public trading in securities

Vilkyškių pieninė has made an agreement with JSC "Orion Securities" (A. Tumėno st. 4, B, LT-01109, Vilnius) on accounting of the Company's securities and related services.

#### IV. INFORMATION ABOUT THE ISSUER'S ACTIVITIES

##### 23. Legal basis for Issuer's activities.

In conducting its business Vilkyškių pieninė follows the Company law, Law on Securities Market, Law on Markets of Financial Instruments, and other laws and legal acts of the Republic Lithuania and Company's By-laws.

##### 24. Membership in associated structures

-

##### 25. Brief company history

JSC Vilkyškių pieninė was established 10 May 1993 in place of an old dairy.

2 November 1993 – water tower, boiler house, and separation room were rebuilt. Since then the company started milk separation activity.

15 June 1994 – cheese room was opened.

July 1995 – butter room was opened.

1997 – production of fermented „Tilžė“ type of cheese was started.

1998 – beginning of production of famous „Gouda“ type of fermented cheese.

1999 – started production of „Žemaičių“ fermented cheese, butter mixture „Saulės vaisės“ and fermented cheese „Tilžiukas“ with fixings, which later during the same year won gold medal in AgroBalt'1999 exhibition, as the best product of the year in Lithuania.

2000 – started „Maasdam“ cheese production.

2001 - „Maasdam“ cheese in AgroBalt'2001 won gold medal. Furthermore, during 2000-2001 3 more types of fermented cheeses were offered for Lithuanian consumers: „Kuršiukas“, „Taupa“ and „Sumuštinis“. During fourteen years of company activities all needed infrastructure for facilitating production has been established: mechanic rooms for cheese production, 50 vehicles, milk freezing equipment, and other.

## 26.Characteristics of the production (services)

Key figures and ratios	2004	2005	2006
Net profit, for 1 share, LTL	0.49	0.46	0.42
Net profit margin (%)	6.09%	4.67%	3.35%
Return on assets (%)	14.64%	11.16%	5.98%
Debt ratio	0.66	0.64	0.63
Debt to assets ratio	1.91	1.77	1.69
Current ratio	1.36	1.65	1.29
Turnover of assets	2.41	2.39	1.79
Book value of 1 share, LTL *	1.15	1.48	2.57
Revenue (thou LTL)	75,102	91,709	115,719
Net profit (loss) (thou LTL)	4,571	4,283	3,874
Assets (thou LTL)	31,215	38,381	64,763
Liabilities (thou LTL)	20,477	24,537	40,709
Equity (thou LTL)	10,738	13,844	24,054
Current assets (thou LTL)	9,889	16,586	25,491
Current liabilities (thou LTL)	7,272	10,023	19,795
Number of shares (thou)	99.5	9,353	9,353

\* Calculations of these ratios use current number of company's shares outstanding.

Issuer specializes in production of cheese – it produces 10 types of cheese, sold with 29 brand names (e.g. “Prūsija”, “Memel Blue”). The company also produces butter, butter mixtures, processed cheese and cheese products.

Below, the main figures best characterizing the production of Issuer, are presented.

Procurement of raw milk (recalculated into base fatness)	2002	2003	2004	2005	2006	2006 (consolidated)
Procured milk, tons	63.235	69.809	88.100	94.852	122.016	126.707
Procured milk, thou LTL	28.838	28.608	46.491	56.180	73.134	75.592
Price of procured milk, LTL/t	456,0	409,8	527,7	592,3	599,4	596,6

Over last five year Vilkyškių pieninė produced following amounts:

Amount of produced products, tons	2002	2003	2004	2005	2006	2006 (consolidated)
Fermented cheese	5.461	5.974	7.489	8.293	10.204	10.341

Butter	448	1.450	1.555	1.247	587	587
Cream	-	-	551	2.090	4.831	4831

The details of Vilkyškių pieninė production sold over the last five years:

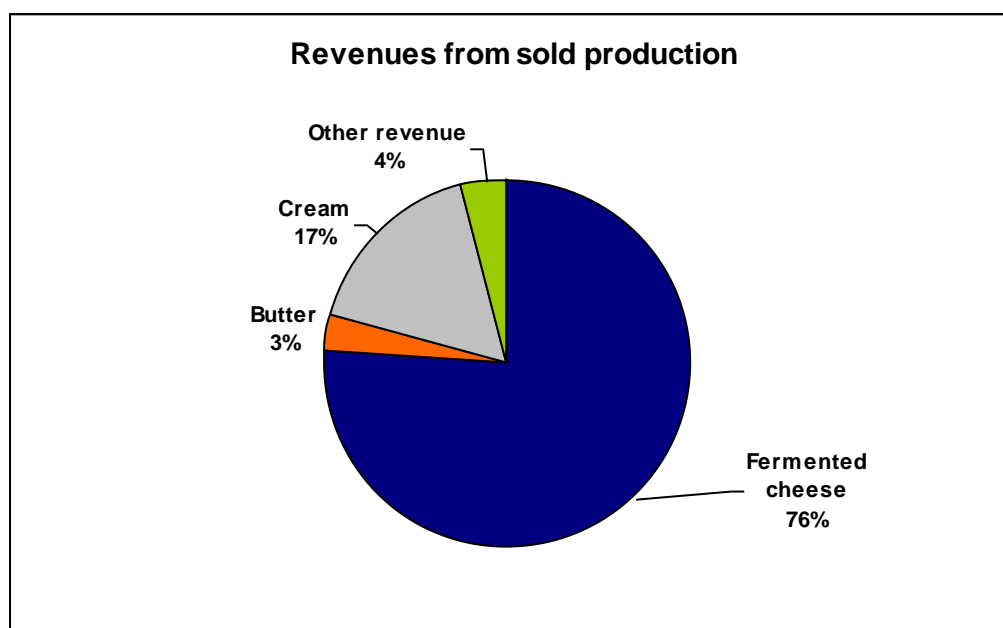
Amounts of sold production, tons	2002	2003	2004	2005	2006	2006 (consolidated)
Fermented cheese	5.799,5	6.385,7	7.338,1	7.968,7	9471,6	9619,8
Butter	539,5	1.297,8	1.547,1	1.379,5	607,8	607,8
Cream	-	-	551	2090	4831	4831

Vilkyškių pieninė revenues from production sales were the following:

Revenues of sold production, thou LTL	2002	2003	2004	2005	2006	2006 (consolidated)
Fermented cheese	43.649	46.774	63.038	71.391	86.491	88.175
Butter	2.735	6.749	9.278	8.287	3.502	3.502
Cream	-	-	2.630	8.893	19.454	19.454
Other revenue	179	475	156	3.138	2.105	4.622
<b>Total revenue</b>	<b>46.563</b>	<b>53.998</b>	<b>75.102</b>	<b>91.709</b>	<b>111.552</b>	<b>115.719</b>

The average prices of Vilkyškių pieninė production sold over the last five years were the following:

Average prices of sold production, LTL/t	2002	2003	2004	2005	2006	2006 (consolidated)
Fermented cheese	7.552	7.398	8.606	8.959	9.132	9.162
Butter	5.070	5.200	5.997	6.703	5.762	5.762
Cream	-	-	4.773	4.255	4.027	4.027



On the February 22<sup>nd</sup>, 2006 PLC „Vilkyškių pieninė“ received 3,45 mLTL European Union structural funds grant, to be used to fulfill EU requirements, and for modernisation of the production base: development of technology to allow the remake of whey from cheese production into whey butter, protein concentrate, and lactose concentrate. After the completion of this investment plan, it will be possible to start the realization of whey products.

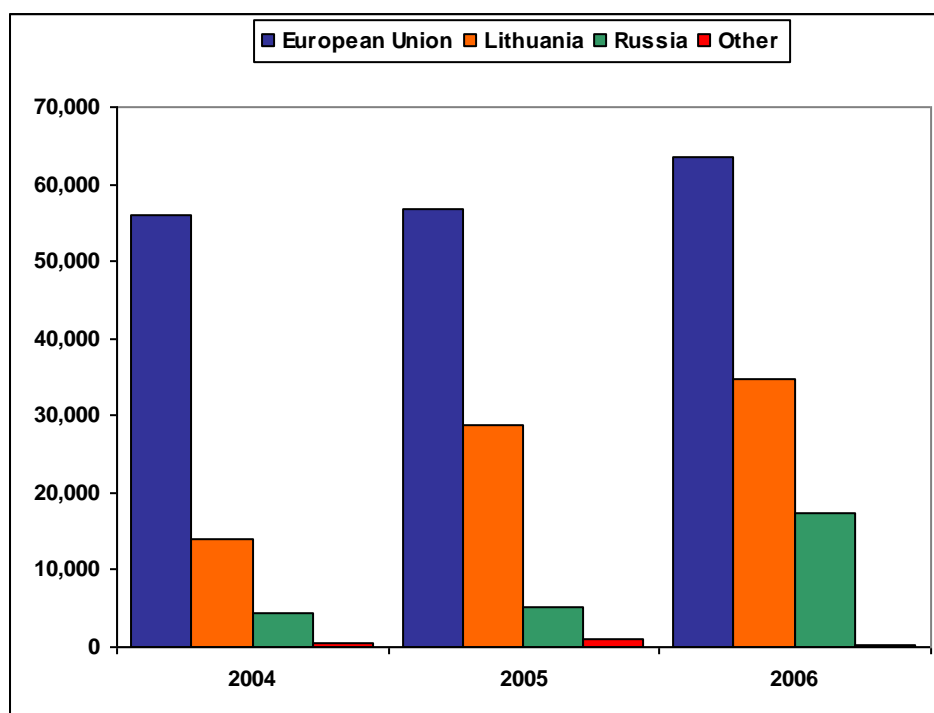
2006 – acquisition of control share package of JSC „Modest“ allowed broadening of Issuer’s product assortment with “Mozzarella” types of cheese.

Currently Issuer is waiting for another structural fund grant from EU equalling 2,12 mLTL. By supplementing the grant with own capital the process of milk collection, cheese production and packaging lines will be modernized.

## 27.Sales markets

Vilkyškių pieninė revenue breakdown by geographical segments over last three years:

Revenue by segment, (thou LTL)	2004	2005	2006
European Union	56,059	56,863	63,559
Lithuania	13,998	28,718	34,713
Russia	4,440	5,148	17,310
Other	605	980	137
<b>Total revenue:</b>	<b>75,102</b>	<b>91,709</b>	<b>115,719</b>



In the short run the company plans to penetrate Danish and Swedish dairy markets.

In Russia Vilkyškių pieninė realizes its production by long term contract, short term contracts in EU countries, and medium term and long term contracts in domestic market.

## 28. Procurement

The main raw material used in production is milk. The largest milk suppliers are Lithuanian companies, individual farmers, and other agricultural companies.

Other raw materials are usually bought in Lithuania.

Equipment is sometimes bought from abroad using 1 year or longer contracts.

Vilkyškių pieninė constantly procures raw milk and sometimes ready-made production from its peers and competitors in Lithuania including: JSC „Marijampolės pieno konservai“, PLC „Rokiškio sūris“ and PLC „Pieno žvaigždės“.

## 29. Real estate and other fixed assets

Vilkyškių pieninė changes in fixed assets statement:

Thousand Lit	Land and buildings	Machinery and equipment	Other tangible assets	Construction in progress	Total
<b>Cost</b>					
Balance as at 1 January 2005	9 448	18 417	5 415	27	33 307



Acquisitions	1 002	1 256	2 244	749	5 251
Disposals		73	378		451
Balance as at 31 December 2005	10 450	19 600	7 281	776	38 107
Balance as at 1 January 2006	10 450	19 600	7 281	776	38 107
Acquisitions through business combination	980	265	241	0	1 486
Acquisitions	469	3 777	2 593	1 303	8 142
Revaluation	8 158				8 158
Disposals	-28	-377	-637	0	-1 042
Reclassification	-1 089	96	1 914	-921	0
Balance as at 31 December 2006	18 940	23 361	11 392	1 158	54 851
<b>Depreciation and impairment</b>					
Balance as at 1 January 2005	1 447	8 383	3 585		13 415
Depreciation for the year	411	2 616	596		3 623
Disposals	0	-73	-345		-418
Balance as at 31 December 2005	1 858	10 926	3 836	0	16 620
Balance as at 1 January 2006	1 858	10 926	3 836		16 620
Depreciation for the year	478	1 578	865		2 921
Disposals	-4	-377	-310		-691
Reclassification	-163	-386	549		0
Revaluation	-2 125				-2 125
Balance as at 31 December 2006	44	11 741	4 940	0	16 725
<b>Carrying amounts</b>					
As at 1 January 2005	8 001	10 034	1 830	27	19 892
As at 31 December 2005	8 592	8 674	3 445	776	21 487
As at 1 January 2006	8 592	8 674	3 445	776	21 487
As at 31 December 2006	18 896	11 620	6 452	1 158	38 126

Vilkyškių pieninė owned tangible assets:

Type of building	Area, sq. m.
<b>Main buildings:</b>	
1. Production administrative building	1884,72 sq. m
2. Cheese production building	373,1 sq. m
3. Cheese ripenning building	1855,72 sq. m.
4. Cheese salting building	492,57 sq. m.
5. Boiler house	48,4 sq. m
6. Substation	57,2 sq. m
7. Automatic control building (cleaning equipment)	121,75 sq. m
8. Freezing room	406,15 sq. m.

**Main buildings in Tauragė:**

1. Administrative building	779,02 sq. m
2. Production building	2665,81 sq. m
3. Concrete storehouse	500,35 sq. m
<b>4. Mechanical workshop</b>	721,49 sq. m
5. Transformer house	83 sq. m
6. Skaudvilė room	1217,69 sq. m
7. Freezing station	861,54 sq. m
<b>Eržvilkas dairy bulding</b>	<b>154,80 sq. m</b>

### 30. Risk factors, associated with the Issuer's activities

Main risk factors, associated with the Issuer's activities:

#### **Risk factors related to the company's business**

- The main Company's activity is milk processing (production of fermented cheese). The main factors creating business risk are possible changes in the raw materials (milk) markets, directly or indirectly related to the business of Vilkyškių pieninė and likely to affect Company's cash flows and operating results
- The Company is specializing in the production of cheese. The largest part of revenues is received from sales of cheese and cheese products. Due to this reason the company's revenue and profit is sensitive to the negatives changes in the demand or prices of cheese (market risk). The price of cheese can also be negatively affected by stiffening competition in the international and local markets.
- The main raw material used by the company is the cow milk. The supply of milk for milk processing companies of the EU is restricted by the national milk quotas. The restrictions on the supply raw materials may cause a shortage in raw milk and thus lead to an increase in the price of milk. Such changes could negatively affect Company's cash flows and operating results.
- Production of fermented cheese is a time consuming process which can take from 1 up to 3 months. Such production specifics does not allow quick reaction to the rapid changes in the cheese market and thus could negatively affect Company's cash flows and operating results.
- Company's business (especially raw milk collection) is a labor intensive process. Shortage in labor force and growth in salaries can negatively affect Company's growth potential and operating results.
- Company's credit risk is connected to the trade debtors. Risk that business partners would not meet their financial obligations is regulated by established controlling procedures. Credit risk connected to the liquid assets held in banks is limited as the Company works only with the biggest Lithuanian banks (mainly with AB "SEB Vilniaus bankas"). On 31 December 2006 debt to asset ratio was

equal to 0.59. The interest rate of all the major loans is connected to the EURIBOR level. On 31 December 2006 the remaining loans to credit institutions were equal to 21,601 thousand LTL. Loans are denominated in EUR. The pay-back of the loans is going on according to the agreements, with no overdue payments.

- Currency exchange risk. Operations with foreign currency are evaluated in LTL according to the exchange rate of operation date. Cash and liabilities denominated in foreign currency are evaluated in LTL using exchange rate of the balance sheet formation date. Gain or loss due to currency exchange fluctuation is reported in the profit and loss account. The main part of Company's income is received in EUR. There are no such foreign currency transactions which could significantly affect Company's financial results due to exchange rate fluctuation.

### Risk factors related to the industry

- Agriculture in European Union (including milk production) is a highly regulated sector. A price level of raw milk is regulated through limitation of supply to processing companies and final consumers, using interventional purchases of milk products and by application of tariff for imported and subsidies for exported EU milk products. The World Trade Organization and other organizations supporting free trade are persuading EU to decrease the regulation level in agriculture sector. The liberalization of milk market could decrease the price of the raw milk as well as processed products and reduce current export subsidies thus increasing competition from non-EU countries. Such factors can negatively affect Company's cash flows and operating results.

Milk products are produced using raw materials of animal origin. Such cattle infections as Mad Cow disease can negatively affect supply of raw milk and decrease the demand for milk products. Such changes would negatively affect Company's cash flows and operating results.

### Debt and loan structure of the Issuer:

Credit institution	Ref.	Loan amount	Interest rate	Balance at 31 12 2006	Balance at 31 12 2005
			6monthLIBOR+1,3		
AB SEB Vilniaus Bankas	a)	11 998	%	10 998	11 727
AB Snoro Bankas	b)	2 072	6monthLIBOR +1,75%	1 692	2 072
AB Snoro Bankas	c)	345	6monthLIBOR +1,75%	0	345
Nordic Environment Finance Corporation (NEFCO)	d)	691	3%	115	345
			6 month.LIBOR+1,3		
AB SEB Vilniaus Bankas	e)	7 078	%	3 972	0
AB SEB Vilniaus Bankas credit line	f)	4 005	6 month LIBOR+1,3%	3 307	0
AB DnB Nord bankas	g)	600	3 month VILIBOR+2.7%	600	-
Finance lease liabilities				1 563	1 296
Total liabilities				22 247	15 785
Less: current part				-5 567	-2 575
Total long-term part of current liabilities				16 680	13 210

All interest rates of the loans are connected to the EUR LIBOR interest rate.

Repayment of loans proceeds according to the timetable without any delayed payments.

31. Termination or reduction of production, which has had a material impact on the Issuer's results during the last two fiscal (business) years

-

32. Patents, licenses, contracts

8 May 2000 – received a license export to the EU.

14 October 2004 – the inspected production lines meet the requirements and Vilkyškių pieninė is certified to produce for the Russian market.

18 May 2004 – obtained EU veterenarian certificate for Vilkyškių pieninė Tauragė room.

33. Litigation and arbitration

-

34. Personnel

Average wage rate according to a particular job group:

Department	2004		2005		2006	
	Average number of employees	Average wage rate	Average number of employees	Average wage rate	Average number of employees	Average wage rate
Administration	34	2408,8	32	2643,79	44	3070,39
Operating personnel	60	826,53	59	818,79	54	1183,88
Transportation	72	1051,13	67	854,89	75	1348,00
Milk collection department	100	658,17	104	361,15	116	942,14
Production	204	788,48	140	706,19	213	908,70
<b>Total:</b>	<b>470</b>	<b>1042,5</b>	<b>402</b>	<b>879,44</b>	<b>502</b>	<b>1220,75</b>

35. Investment policy

Name of the company	JSC „Modest“
---------------------	--------------

Headquarters	Jeruzalės st. 16, Vilnius
Address of the factory	Bagaslaviškis village, Gelvonai municipality, Širvintos district
Activity	Milk collection, remake, realization
Share capital	26,000 common stocks denominated in 1 LTL.
Net profit (loss)	- 172,234 LTL
Quick ratio	2.56
Debt to assets ratio	0.8

Vilkyškių pieninė controls 88,73% of JSC „Modest“ shares.

Main Vilkyškių pieninė investments over last 3 years:

During 2004 and 2005 no large investments, which exceeded 10 percent of Issuer's share capital have not been carried out.

Over 2006 cheese room was modernized using 3.487,6 thou LTL: a loan of 2.927 thou LTL and own funds of 560,6 thou LTL.

### 36. Competitors

Vilkyškių pieninė estimated the market share in domestic market to be around 15%, which means a fourth place behind producers like PLC „Rokiškio sūris“, PLC „Pieno Žvaigždės“, and PLC „Žemaitijos pienas“. One of the direct competitors of Vilkyškių pieninė is PLC „Marijampolės pieno konservai“, which over 2006 had revenues of 206.15 mLTL.

In foreign markets Vilkyškių pieninė competes with domestic producers, which have an advantage of smaller transportation costs. However Vilkyškių pieninė compensates this by offering higher value added line of cheese products.

### 37. Dividends paid

During 2002 and 2003 there were no dividend payments.

Dividend payments over last 3 years:

Dividends	2002	2003	2004	2005	2006
Dividends (LTL)	0	0	1,177,000	2,500,000	2,057,660
Dividends for 1 share (LTL)*	0	0	0.13	0.27	0.22
Number of shares	99,500	99,500	99,500	9,353,000	9,353,000

\*This ratio is calculated using the existing number of shares.

## V. FINANCIAL STATUS

## 38. Financial reports

Vilkyškių pieninė unconsolidated balance sheets for last 3 years:

Thousand Lit	2006	2005	2004
<b>Assets</b>			
Property, plant and equipment	36 567	21 487	19 892
Intangible assets	28	196	283
Deferred tax assets	1 381	0	0
Long-term receivables	551	112	1 151
<b>Total non-current assets</b>	<b>38 527</b>	<b>21 795</b>	<b>21 326</b>
Prepayments for investments	0	350	0
Inventories	13 434	8 427	6 160
Trade and other receivables	10 704	6 768	3 624
Cash and cash equivalents	832	1 041	105
<b>Total current assets</b>	<b>24 970</b>	<b>16 586</b>	<b>9 889</b>
<b>Total assets</b>	<b>63 497</b>	<b>38 381</b>	<b>31 215</b>
<b>Equity</b>			
Share capital	9 353	9 353	9 353
Reserves	9 683	705	466
Retained earnings	5 156	3 786	919
<b>Total Equity</b>	<b>24 192</b>	<b>13 844</b>	<b>10 738</b>
<b>Liabilities</b>			
Interest-bearing loans and leasing liabilities	16 656	13 210	11 731
Capital grants	1 441	0	0
Deferred tax liabilities	2 793	1 304	1 474
<b>Total non-current liabilities</b>	<b>20 890</b>	<b>14 514</b>	<b>13 205</b>
Interest-bearing loans and leasing liabilities	4 945	2 575	536
Income tax payable	359	1 037	237
Trade and other amounts payable	13 111	6 411	6 499
<b>Total current liabilities</b>	<b>18 415</b>	<b>10 023</b>	<b>7 272</b>
<b>Total liabilities</b>	<b>39 305</b>	<b>24 537</b>	<b>20 477</b>
<b>Total equity and liabilities</b>	<b>63 497</b>	<b>38 381</b>	<b>31 215</b>

Vilkyškių pieninė consolidated balance sheet (acquisition of subsidiary carried out only in 2006):

Thousand Lit	2006
<b>Assets</b>	
Property, plant and equipment	38 126
Intangible assets	1 061
Deferred tax assets	23
Long-term receivables	62
<b>Total non-current assets</b>	<b>39 272</b>
Prepayments for investments	0
Inventories	13 543
Trade and other receivables	11 057
Cash and cash equivalents	891
<b>Total current assets</b>	<b>25 491</b>
<b>Total assets</b>	<b>64 763</b>
<b>Equity</b>	
Share capital	9 353
Reserves	9 683
Retained earnings	4 967
<b>Total equity attributable to equity holders of the Company</b>	<b>24 003</b>
<b>Minority interest</b>	<b>51</b>
<b>Total equity</b>	<b>24 054</b>
<b>Liabilities</b>	
Interest-bearing loans and leasing liabilities	16 680
Capital grants	1 441
Deferred tax liabilities	2 793
<b>Total non-current liabilities</b>	<b>20 914</b>
Interest-bearing loans and leasing liabilities	5 567
Income tax payable	361
Trade and other amounts payable	13 867
<b>Total current liabilities</b>	<b>19 795</b>
<b>Total liabilities</b>	<b>40 709</b>
<b>Total equity and liabilities</b>	<b>64 763</b>

Vilkyškių pieninė unconsolidated profit and loss statements for last 3 years:

Thousand Litas	2006	2005	2004
<b>Revenue</b>	111 551	91 709	75 102
Cost of sales	-98 775	-80 173	-63 488
<b>Gross profit</b>	12 776	11 536	
Other operating income, net	76	27	44
Distribution expenses	-1 652	-1 422	-1 612
Administrative expenses	-5 182	-4 345	-4 182
<b>Results from operating activities</b>	6 018	5 796	5 864
Financial income	91	20	161
Financial expenses	-985	-619	-814
<b>Net financing costs</b>	-894	-599	-653
<b>Profit before income tax</b>	5 124	5 197	5 211
Income tax expense	-1 040	-914	-640
<b>Profit for the period</b>	4 084	4 283	4 571

Vilkyškių pieninė consolidated profit and loss statement (acquisition of subsidiary carried out only in 2006):

Thousands Litas	2006
<b>Revenue</b>	115 719
Cost of sales	-102 262
<b>Gross profit</b>	13 457
Other operating income, net	87
Distribution expenses	-1 921
Administrative expenses	-5 788
<b>Results from operating activities</b>	5 835
Financial income	73
Financial expenses	-1 025
<b>Net financing costs</b>	-952
<b>Profit before income tax</b>	4 883
Income tax expense	-1 009
<b>Profit for the period</b>	3 874
Attributable to:	
Equity holders of the company	3 905
Minority interest	-31
<b>Profit for the period</b>	3 874
Basic earnings per share (in Litas)	0,42

Vilkyškių pieninė unconsolidated cash flow statements for last 3 years:



Thousand Lit	2006	2005	2004
<b>Cash flows from operating activities</b>			
Net profit	4 084	4 283	4 571
Adjustments:			
Depreciation	2 597	3 623	3 181
Amortization	191	159	141
Part of capital subsidies recognized as income	-140	0	0
Impairment of non-current assets	45	0	0
Result of disposal of tangible non-current assets	-2	-71	-27
Interest expenses, net	894	599	653
Income tax expense	1 040	914	640
<b>Cash flows from ordinary activities before changes in the working capital</b>	<b>8 710</b>	<b>9 507</b>	<b>9 159</b>
Change in inventories	-5 007	-2 267	-1 413
Change in receivable amounts	-2 605	-2 105	1 303
Change in trade and other payable amounts	6 000	-389	-2 080
	7 098	4 746	6 969
Paid / received interest, net	-915	-563	-895
Income tax paid	-1 792	-285	-6
<b>Cash flows from operating activities</b>	<b>4 391</b>	<b>3 898</b>	<b>6 068</b>
<b>Cash flows from investing activities</b>			
Acquisition of property, plant and equipment	-6 331	-3 662	-3 667
Acquisition of intangible assets	-23	-72	-175
Proceeds on sale of property, plant and equipment	264	104	57
Investment in subsidiary, net of cash acquired	-1 031	-350	0
Loans provided	-489	0	0
Interest received	21	0	0
<b>Net cash flow from investing activities</b>	<b>-7 589</b>	<b>-3 980</b>	<b>-3 785</b>
<b>Cash flows from financing activities</b>			
Loans received	11 828	3 156	1 714
Repayment of borrowings	-6 233	-230	-4 118
Payment of finance lease liabilities	-1 106	-757	-497
Dividends paid	-1 800	-1 177	0
Capital grants received	300	0	0
<b>Net cash from financing activities</b>	<b>2 989</b>	<b>992</b>	<b>-2 901</b>
Change in cash and cash equivalents	-209	936	-618
Cash and cash equivalents at 1 January	1 041	105	727
<b>Cash and cash equivalents at 31 December</b>	<b>832</b>	<b>1 041</b>	<b>105</b>

Vilkyškių pieninė consolidated cash flow statement (acquisition of subsidiary carried out only in 2006):

Thousand Lit	2006
<b>Cash flows from operating activities</b>	
Net profit	3 874
Adjustments:	
Depreciation	2 921
Amortization	191
Part of capital subsidies recognized as income	-140

Impairment of non-current assets	45
Result of disposal of tangible non-current assets	-9
Interest expenses, net	952
Income tax expense	1 009
<b>Cash flows from ordinary activities before changes in the working capital</b>	<b>8 843</b>
Change in inventories	-5 116
Change in receivable amounts	-2 959
Change in trade and other payable amounts	6 756
	7 524
Paid / received interest, net	-951
Income tax paid	-1 782
<b>Cash flows from operating activities</b>	<b>4 791</b>
<b>Cash flows from financing activities</b>	
Loans received	-7 778
Repayment of borrowings	-23
Payment of finance lease liabilities	271
Dividends paid	-971
Capital grants received	-8 501
<b>Cash flows from financing activities</b>	
Loans received	12 428
Repayment of borrowings	-6 233
Payment of finance lease liabilities	-1 135
Dividends paid	-1 800
Capital grants received	300
<b>Net cash from financing activities</b>	<b>3 572</b>
Change in cash and cash equivalents	-150
Cash and cash equivalents at 1 January	1 041
<b>Cash and cash equivalents at 31 December</b>	<b>891</b>

Vilkyškių pieninė unconsolidated changes in equity statements for last 3 years:

Thousand Litas	Share capital	Revaluation reserve	Compulsory reserve	Retained earnings	Total equity
At 1 January 2004	9 353		466	- 3 652	6 167
Net profit for 2004				4,571	4,571
Transfer to reserves			0		
Dividends				0	0
At 31 December 2004			466		10 738
At 1 January 2005	9 353		466	919	10 738
Net profit for 2005				4,283	4,283
Transfer to reserves			239	-239	0
Dividends				-1,177	-1,177
At 31 December 2005	9 353		705	3 786	13 844
At 1 January 2006	9 353		705	3 786	13 844
Net profit for 2006				4 084	4 084

Increase of value of PPE*		8 764			8 764
Transfer to reserves			214	-214	0
Dividends				-2 500	-2 500
At 31 December 2006	9 353	8 764	919	4 967	24 003

Vilkyškių pieninė consolidated changes in equity statement for 2006:

Thousand Lit	Share capital	Revaluation reserve	Compulsory reserve	Retained earnings	Total equity
At 1 January 2006	9 353	0	705	3 786	13 844
Net profit for 2006				3 905	3 905
Increase of value of PPE*		8 764			8 764
Transfer to reserves			214	-214	0
Dividends				-2 500	-2 500
Losses not recognized in the income statement				-10	-10
At 31 December 2006	9 353	8 764	919	4 967	24 003

\*The increase in value of property, plant and equipment represents the revaluation of buildings, net of related deferred tax, amounting to 1,564 thou LTL.

### 39. Comments of Financial Statements

Contents of main positions during the reporting period, and the changes and underlying reasons behind them are explained in the audit report attached to this prospectus.

### 40. Report prepared by the Issuer's Board

The annual report of the company is prepared in compliance with the requirements of the Republic of Lithuania financial reporting law article number 24, requirements of the Republic of Lithuania consolidated company accounts reporting law article number 9, according to the rules of the Republic of Lithuania securities law article number 21 and the Republic of Lithuania public companies law article number 34. According to the requirement of the Republic of Lithuania securities law article number 21 part 3 and „AB Vilniaus vertybinių popierių birža“ trading rules paragraph number 20.5, Company discloses how it complies with the corporate governance code for the companies listed on the Vilnius Stock Exchange.

#### 1. Unbiased overview of the business group's financial state, activities and development, description of the risk factors faced by the group

The main Vilkyškių Pieninė business activity is the production of cheese, melted and smoked cheese, butter products. The Company is specializing in the making of fermented cheese; butter products, sour cream and melted cheese are produced in order to efficiently exploit Company's production capacities.

During year 2006 company has purchased 122 thousand tons of basic fat level milk (increase by 28.7% if compared with 2005) and produced 10,204 tons of fermented cheese (increase by 23 %). The biggest challenge during the period of 2006 was the rise of raw milk prices. Since 2005 the price of raw milk has increased by 1.2% and reached the level of approximately 599.4 LTL per liter. Despite the growth of the raw milk prices, company managed to achieve profit before taxes similar as in 2005 (5.1 million LTL during 2006).

The previous financial year is also exceptional due to the fast growth in exports – during 2006 Vilkyškių pieninė has sold 1696 tons of cheese to Russian market and reached the sales turnover of 17.3 million LTL (15% of total company's sales during 2006). Comparing with 2005, the amount of exported cheese has increased by more than 4 times.

The most important events for Vilkyškių pieninė in 2006:

2006.01.12 – Vilkyškių pieninė has acquired 80.24% of PLC “Modest” shares. Acquired enterprise produces fresh dairy products and “Mozzarella” type cheese. It is planned to modernize technological base of the company and concentrate business activities on the production of “Mozzarella” type cheese.

2006.05.04 – during the period of 2006.04.24-2006.05.04 Vilkyškių pieninė has successfully distributed 10% of company's shares on Vilnius Stock Exchange.

On 11 July 2006 the Company has signed an agreement with the National Paying Agency concerning EU structural funds support of 3.45 million LTL to be provided for Vilkyškių pieninė. The funds will be used for modernization of production processes: to technologically upgrade the cheese production line and implement new whey processing project. The total value of the whole project is over 7.63 million LTL. Support from EU accounts to 45% of the whole project value.

Investments into modern processing technologies will allow significant increases in production efficiency, improvements in quality control, and minimization of generated waste. Approximately half of the provided funds has been already used for the modernization of cheese production line. Installed equipment meets the highest EU hygiene requirements, as now the whole cheese production process is fully automated.

The remaining part of the funds is allocated for the acquisition of whey processing equipment. The Company is planning to start whey processing already by the end of 2007.

On 10 August 2006 JSC “Modest” has signed an agreement with the National Paying Agency regarding EU structural funds support of 2.1 million LTL to be allocated for

the company. The support will be used for the modernization of production processes – company is planning to install new raw milk processing equipment and modern “Mozzarella” type cheese production – packaging line, and upgrade specialized milk and dairy products transport fleet. Implementation of this EU supported project will allow increasing competitiveness and operating efficiency of JSC “Modest” as well as expanding assortment of high value-added dairy products. In addition to that, modernization of company’s production processes will enable JSC “Modest” to export its products to EU countries.

Despite successful business activity, company faces specific risk factors affecting its operations.

### **Risk factors related to the company’s business**

- The main Company’s activity is milk processing (production of fermented cheese). The main factors creating business risk are possible changes in the raw material (milk) markets, directly or indirectly related to the business of Vilkyškių pieninė and likely to affect Company’s cash flows and operating results
- The Company is specializing in the production of cheese. The largest part of revenues is received from sales of cheese and cheese products. Due to this reason company’s revenues and profit is sensitive to the negatives changes in the demand or prices of cheese (market risk). The price of cheese can also be negatively affected by the competition in international and local market.
- The main raw material used by the company is the cow milk. The supply of milk for milk processing companies of the EU is restricted by the national milk quotes. The restriction of raw material supply can cause a shortage in raw milk and thus increase in the price of milk. Such changes could negatively affect Company’s cash flows and operating results.
- Production of fermented cheese is a time consuming process which can take from 1 up to 3 months. Such production specifics does not allow quick reaction to the rapid changes in the cheese market and thus could negatively affect Company’s cash flows and operating results.
- Company’s business (especially raw milk collection) is a labor intensive process. Shortage in labor force and growth in salaries can negatively affect Company’s growth potential and operating results.
- Company’s credit risk is connected to the trade debtors. Risk that business partners would not meet their financial obligations is regulated by established controlling procedures. Credit risk connected to the liquid assets held in banks is limited as the Company works only with the biggest Lithuanian banks (mainly with AB “SEB Vilnius bankas”). On 31 December 2006 debt to asset ratio was equal to 0.59. The interest rate of all the major loans is connected to the EURIBOR level. On 31 December 2006 the remaining loans to credit institutions were equal

to 21,601 thousand LTL. Loans are denominated in EUR. The pay-back of the loans is going on according to the agreements, with no overdue payments.

- Currency exchange risk. Operations with foreign currency are evaluated in LTL according to the exchange rate of operation date. Cash and liabilities denominated in foreign currency are evaluated in LTL using exchange rate of the balance sheet formation date. Gain or loss due to currency exchange fluctuation is reported in the profit and loss account. The main part of Company's income is received in EUR. There are no such foreign currency transactions which could significantly affect Company's financial results due to exchange rate fluctuation.

### Risk factors related to the industry

- Agriculture in European Union (including milk production) is a highly regulated sector. A price level of raw milk is regulated through limitation of supply to processing companies and final consumers, using interventional purchases of milk products and by application of tariff for imported and subsidies for exported EU milk products. The World Trade Organization and other organizations supporting free trade are persuading EU to decrease the regulation level in agriculture sector. The liberalization of milk market could decrease the price of the raw milk as well as processed products and reduce current export subsidies thus increasing competition from non-EU countries. Such factors can negatively affect Company's cash flows and operating results.
- Milk products are produced using raw materials of animal origin. Such cattle infections as Mad Cow disease can negatively affect supply of raw milk and decrease the demand for milk products. Such changes would negatively affect Company's cash flows and operating results.

## 2. The analysis of the business group's financial and non-financial activities results. Information related to personnel and business environment issues

During 2006 sales revenues of the business group reached 115.8 million LTL. The group's profit before taxes amounted to 4.88 million LTL.

The main indicators of Vilkyškių pieninė company's and group's financial results for year 2006 (if not indicated differently, in thousands of LTL):

	2006		2005		2004	
	Company	Group	Company	Group	Company	Group
Sales revenues	111 551		91 709	-	75 102	-
Cost of goods sold	98 775		80 173	-	63 937	-
Gross profit	12 776		11 535	-	11 614	-
Net profit	4 084		4 283	-	4 788	-
Net profit margin, %	3.66%		4.67%	-	6.38%	-

During the first half of 2006 company has generated 203 thousands LTL as earnings before taxes (EBT). Compared with the same period in 2005, the EBT has decreased by 80%. Due to decreased prices of cheese (-3.4%) and sour-cream (-7.3%), Vilkyškių pieninė has respectively lost 1.15 m. LTL and 0.57 m. LTL as sales revenues. As a result, gross profit margin decreased from 11.6% to 8.4%. A larger decrease was avoided due to smaller raw milk price, which has declined by 1.3%.

EBT for the first 9 months of 2006 has decreased by 42% if comparing with the same period during 2005. Due to smaller prices of cheese and sour-cream company has lost respectively 1.1 m. LTL and 1.0 m. LTL. Despite the fact that cheese prices in the 3<sup>rd</sup> quarter have come back to the level of 2005, Company's gross profit margin has decreased from 14% to 11%. The profit margin was additionally pulled down by growing personnel and energy expenses.

After cheese prices have reached the level of 2005 in the 3<sup>rd</sup> quarter, during the last quarter, which was the most successful in 2006, Vilkyškių pieninė has generated 4.5 million LTL of gross profit.

Comparing with 2005 annual gross profit margin has declined from 12.6% to 11.45%. Besides decreasing prices of realized production, profitability was also negatively affected by implemented modernization of technological Company's base and non-recurring expenses associated with Vilkyškių pieninė shares enlistment on the Vilnius stock exchange. Due to these factors Company's expenses during 2006 has increased by 20%.

The profitability of subsidiary company JSC "Modest" has declined due to the decision to specialize in the production of "Mozzarella" type of cheese and partly discontinuing production of fresh dairy products.

During the reporting period the number of Vilkyškių pieninė employees has increased from 451 to 502.

On 31 December 2006 544 people were employed by the business group.

### **3. Information links and additional explanation of consolidated accounts data**

There are no additional explanations.

### **4. Important events after the end of the reporting period**

There have been no important events after the end of financial year 2006.

### **5. The plans and forecasts of the business group's activities**



In 2007 the Company is planning to increase its sales revenues up to 135 million LTL and earn 5 m. LTL of net profit. Growth is expected due to the current investments and acquisition of JSC "Modest".

The new whey processing project is planned to be implemented during 2007 at the main company's production site in Vilkyškiai. Part of the project is financed by EU structural funds.

## 6. Information about business group's research and development activities

In 2006 the Company continued rapid investment into expansion of production capacities and modernization of production processes. In order to increase product assortment, Vilkyškių pieninė in January 2006 Company has acquired JSC „Modest“, which specializes in the production of „Mozzarella“ type cheese. 7.63 million LTL was invested into modernization of cheese production line and development of whey processing project. Part of current and planned investment projects is financed by EU structural funds.

## 7. Number and nominal value of parent company's shares owned by the company, its subsidiaries and delegated persons who are acting on their own

There are no such shares.

## 8. When company is using financial tools and when it is important for valuation of business group's assets, shareholder equity, liabilities, financial state and operating results, financial risk management goals are disclosed, as well as employed major transactions insurance tools, for which insurance transactions accounting is applicable, as well as group's price, credit, liquidity, and cash flow risks

In 2006 company has entered into floating to fixed interest rate swap agreement paying the fixed leg. The total amount agreed in the contract is 3.2 million EUR. Fixed interest rate is 3.55%, limit for the floating interest rate is 4.75%.

The main indicators of Company's credit and liquidity risks:

Indicator	2006 12 31	2005 12 31
Debt to assets ratio	0,59	0,64
Liquidity ratio	1,36	1,62
Current ratio	0,63	0,77

## 9. Information about parent company's branch offices

Parent company currently has no branch offices.

## 10. Corporate governance disclosure form for listed companies

Vilkyškių pieninė in compliance with the Republic of Lithuania securities law article 21 paragraph 3 and AB „Vilniaus vertybinių popierių birža“ (VVPB) trading rules paragraph 20.5 discloses how the Company meets the requirements of the corporate governance code for companies listed on Vilnius Stock Exchange.

The company discloses how it meets each principle of the corporate governance code. Disclosure is provided as confirmation, which means that company meets, partially meets or doesn't meet the requirements of the specific principle of the corporate governance code.

### Principle I: Basic Provisions

**The overriding objective of a company should be to operate in common interests of all the shareholders by optimizing over time shareholder value**

Company confirms that it meets the requirements of the principle I. The recommendations of the paragraph 1.1 are partially met as Company constantly discloses information related to the development strategy and other activities related to the maximization of shareholders value using its internet web page (<http://www.suris.lt/investuotojams/>), BNS news agency reports.

### Principle II: The corporate governance framework

**The corporate governance framework should ensure the strategic guidance of the company, the effective oversight of the company's management bodies, an appropriate balance and distribution of functions between the company's bodies, protection of the shareholders' interests.**

Company confirms that partially meets the requirements of principle II. Company has a collegial management body - management board, and two managing employees of administration: the chairman of the board and a senior accountant. Supervisory board as a collegial supervisory body is not present. The supervision of company's activities and management is performed by the management board.

The Company is not meeting the recommendation of the article 2.3 - currently the single collegial body is not a supervisory but management body, simultaneously performing supervisory function.

The Company is partially meeting the recommendation of the article 2.5 regarding the sufficient number of the members in the collegiate body - currently there are 4 members in the management board was leaving a probability that a single member can dominate while taking decisions.

The company is not meeting recommendation of the article 2.7, as the chairman of the board is at the same time the director of the company. The other members of the board are responsible for ensuring that decisions taken are fair and unbiased.

**Principle III: The order of the formation of a collegial body to be elected by a general shareholders' meeting**

**The order of the formation a collegial body to be elected by a general shareholders' meeting should ensure representation of minority shareholders, accountability of this body to the shareholders and objective monitoring of the company's operation and its management bodies.**

Currently it is not possible to fully evaluate how the Company meets the requirements of the principle III, as there has not yet been any general meeting of the shareholders, during which the collegial bodies are elected.

The company is meeting the recommendation of the paragraph 3.4 as all the members of the management board have the essential competences needed for the execution of the assigned duties and are responsible for the management of the main production processes (technical, raw materials planning, and sales coordination).

The company is collecting and disclosing all the information about the member of collegial body, their professional education, qualification, interest conflicts in compliance with the recommendations of the paragraph 3.2. Information is disclosed in periodical reports. Members of the board are constantly participating in various courses and seminars during which they are informed about essential changes in the law regulating Company's activities. In addition to that, reports of board members' business trips are disclosed according to internal Company's rules.

The Company is not meeting the recommendations of the article 3.6 as one of the members of the management board can not be held as an independent member according to the paragraph 3.7 - Company's management board member is a controlling shareholder of the Company. The board does not receive a separate salary, they are compensated as Company's employees.

**Principle IV: The duties and liabilities of a collegial body elected by the general shareholders' meeting**

**The corporate governance framework should ensure proper and effective functioning of the collegial body elected by the general shareholders' meeting, and the powers granted to the collegial body should ensure effective monitoring of the company's management bodies and protection of interests of all the company's shareholders.**

The Company confirms that partially meets the requirements of the requirements of the principle V.

The management board analyzes, evaluates annual financial accounts and presents it to the general shareholder meeting.

The members of the management board did participate in the board meeting and devoted sufficient amount of time for the assigned duties.

The company is meeting the recommendations of the paragraphs 4.7-4.14 as in February 2006 the board has formed the Nomination and remuneration committee and signed its statute.

The main goal of the Nomination and remuneration committee - provide recommendations for the bodies or persons of the Company who are responsible for nomination and election of management bodies members and executive employees and to ensure transparent policy and principles of salaries for management bodies and executive employees. The committee is providing support for the management board on: (i) election and nomination of the director or other executive officers, and (ii) on the determination of the salary size for the members of the board, director and other executive employees.

In March 2006 management board of the Company has formed Audit committee and signed its statute.

The main goal of the Audit committee is the supervision of the Company's financial audit process and presentation of the accounting and financial information for the interested parties. The committee assists Company's management board on the issues of: (i) the quality and coherence of financial, accounting and other related documents, (ii) qualification, independence and appropriateness of an independent auditor, and (iii) execution of internal control.

#### **Principle V: The working procedure of the company's collegial bodies**

**The working procedure of supervisory and management bodies established in the company should ensure efficient operation of these bodies and decision-making and encourage active co-operation between the company's bodies.**

The Company confirms that it partially meets the requirements and recommendations of the principle V. the meeting of the Company's collegial management body (management body) are taking place on pre-set frequency and according to the pre-designed work plans. Each member of the body is able to review the material of each meeting before the day of the meeting. When informing about the meetings, material to be discussed is provided in advance. Usually the work plan

of the meeting is not being changed, unless during the meeting, when all the members of the board are participating, the different decision is taken and there is enough information for the effective discussion of an additional issue. Issues to be discussed during the board meeting as the as the reports on the decisions taken are prepared by the director of the company, members of the boards, special groups assigned by the board, which can include addition specialist-non-employees of the Company.

Recommendations of the paragraph 5.4 can not be applied to the Company as the supervisory collegial body is not being formed.

#### **Principle VI: The equitable treatment of shareholders and shareholder rights**

**The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. The corporate governance framework should protect the rights of the shareholders.**

The Company confirms that partially meets the requirement and recommendations of the principle VI. Equity of the company is formed from common stock shares, which provides the owner with the same material and non-material rights.

The place and date of the company's meeting is set in a way that ensures equal participation possibilities for each shareholder. Each shareholder can participate personally or delegate his/her rights to another person and require in-advance voting on the issues announced on the work plan of the meeting. In such a case in-advance voting bulletins are formed.

Company is presenting the reports of general meeting decisions on the Company's webpage in compliance with relevant regulations and laws.

#### **Principle VII: The avoidance of conflicts of interest and their disclosure**

**The corporate governance framework should encourage members of the corporate bodies to avoid conflicts of interest and assure transparent and effective mechanism of disclosure of conflicts of interest regarding members of the corporate bodies.**

Company confirms that it meets all the requirements and recommendations of the principle VII.

#### **Principle VIII: Company's remuneration policy**

**Remuneration policy and procedure for approval, revision and disclosure of directors' remuneration established in the company should prevent potential conflicts of interest and abuse in determining remuneration of directors, in**

**addition it should ensure publicity and transparency both of company's remuneration policy and remuneration of directors.**

The Company is not meeting the requirements of this principles regarding public disclosure of the salary policy report. Company acts in accordance of its policy that salaries and bonuses system as well as other transactions related to employment are not disclosed publicly and considered as commercial secret.

#### **Principle IX: The role of stakeholders in corporate governance**

**The corporate governance framework should recognize the rights of stakeholders as established by law and encourage active co-operation between companies and stakeholders in creating the company value, jobs and financial sustainability. For the purposes of this Principle, the concept "stakeholders" includes investors, employees, creditors, suppliers, clients, local community and other persons having certain interest in the company concerned.**

Company confirms that it meets all the requirements and recommendations of the principle IX.

#### **Principle X: Information disclosure and transparency**

**The corporate governance framework should ensure that timely and accurate disclosure is made on all material information regarding the company, including the financial situation, performance and governance of the company.**

Company confirms that it meets all the requirements and recommendations of the principle X.

#### **Principle XI: The selection of the company's auditor**

**The mechanism of the selection of the company's auditor should ensure independence of the firm of auditor's conclusion and opinion.**

The Company confirms that it meets the requirements and recommendations of the principle XI. The management board of the Company suggests the candidature of the independent auditing company for the general shareholder meeting; auditing company is confirmed by the general shareholder meeting, thus it can be state that Company meets the recommendation of the paragraph 11.2. The candidature of the auditing company and of a specific auditor has been approved by the Securities exchange commission on 3 January 2007.

#### **41. Audit related information**

Vilkyškių pieninė was audited by JSC "KPMG Baltics" audit company.

PLC "KPMG Baltics" company code 111494971, Vytauto st. 12, LT-08118, Vilnius.

Financial accountability consists of a consolidated balance sheet of December 31 2006, consolidated profit and loss statement for the financial year, consolidated statement on changes in equity and consolidated cash flow statement together with notes to the consolidated financial statements and consolidated annual report.

Auditor's report has been signed on the 4th of April 2007 on behalf of „KPMG Baltics“ by Leif Rene Hansen, Danish State Authorised Public Accountant, and Rokas Kasperavičius, Lithuanian Certified Auditor.

## INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF VILKYŠKIŲ PIENINĖ

We have audited the accompanying consolidated financial statements of Vilkyškių Pieninė, which comprise the consolidated balance sheet as at 31 December 2006, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a consolidated summary of significant accounting policies and other explanatory notes, set out on pages 5-35.

### **Management's responsibility for the consolidated financial statements**

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

### **Auditor's responsibility**

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

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

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



## Opinion

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

## Report on legal and other regulatory requirements

Furthermore, we have read the consolidated Annual Report for the year 2006 set out on pages 36-46 of the consolidated Annual Accounts and have not noted any material inconsistencies between the financial information included in it and the consolidated financial statements for the year ended 31 December 2006.

Klaipėda, 4 April 2007

KPMG Baltics, JSC

Leif Rene Hansen  
Danish State Authorised  
Public Accountant

Rokas Kasperavičius  
Lithuanian Certified  
Auditor

## VI. INFORMATION ABOUT THE MANAGING BOARD OF THE ISSUER

## 42. Members of the managing bodies

Structure of the board:

Name, Surname	Education, occupation	Position	Start of cadence	End of cadence	Beginning of work in Vilkyškių pieninė
Gintaras Bertašius	Higher education, engineer-mechanic	Chairman of the board, general director	2006 01 30	2010 01 30	Since 1993 Vilkyškių pieninė
Sigitas Trijonis	Higher education, engineer-mechanic	Member of the board, technical director	2006 01 30	2010 01 30	Since 1993 Vilkyškių pieninė
Rimantas Jancevičius	Further education, zoo-technician	Member of the board, director of purchases	2006 01 30	2010 01 30	Since 1996 Vilkyškių pieninė
Ramūnas Šniepis	Higher education, engineer	“Snoras” bank, director of Tauragė department	2007 04 20	2010 01 30	1997 - “Litimpeks bank” director of Tauragė department, 1999 - “Hermis bank” director of Tauragė department 2000 - 2007 “Snoras” bank director of Tauragė department
Vaidotas Juškys (ex-member of the board)	Higher education, IT engineer	Member of the board, director of commerce	2006 01 30	2007 04 20	Since 1994 Vilkyškių pieninė

Administrative employees:

Name, Surname	Education, occupation	Position	Start of career
Gintaras Bertašius	Higher education, engineer-mechanic	Chairman of the board, general director	2006 01 01*
Birutė Bazilienė	Higher education, accountancy	Chief accountant	1994 06 27
Rūta Žiliutė	Higher education, finance	Substitute of chief	2000 05 01

		accountant	
Rimantas Jancevičius	Further education, zoo-technician	Member of the board, director of purchases	1996 01 02
Sigitas Trijonis	Higher education, engineer-mechanic	Member of the board, technical director	1993 09 01
Vilija Milaševičiūtė	Higher education, economist	Economist-analyst	2000 05 01
Rita Juodikienė	Higher education, administration of IT	IT engineer-programmer	2002 09 23
Asta Aukštakalnienė	Higher education, law	Jurist	2000 09 21

\*Such a date due to reorganization of the company into PLC. Is working in the company since 1993 05 10.

## Vilkyškių pieninė list of managing bodies for 20 April 2007

Name	Surname	Personal code	Position held	Number of Vilkyškių pieninė shares held
Gintaras	Bertašius	36401260554	Chairman of the board, general director	6 016 506
Sigitas	Trijonis	36403310012	Member of the board, technical director	425 538
Rimantas	Jancevičius	36203241541	Member of the board, director of purchases	1 985
Ramūnas	Šniepis	35510220537	Member of the board, "Snoras" bank, director of Tauragė department	0
Arvydas	Zaranka	36608280042	Director of production	1 923
Birutė	Bazilienė	45206090918	Chief accountant	12

JSC „Modest“ information about director and chief accountant:

	<b>Albertas Šlėderis</b>	<b>Ina Papinigienė</b>
Personal code	35312060938	46406241530
Start of career	1994-09-15	1992-04-08
Total wage for 2006	27459,14	14414,08
Salary 2006	19858,48	9729,86
Education	Higher	Higher
Profession	Zoo-engineering	Accountancy

Board of JSC „Modest“:

	<b>G.Bertašius</b>	<b>A.Zaranka</b>	<b>A.Šlėderis</b>
Personal code	36401260554	36608280042	35312060938
Start of career	2006-09-04	2006-09-04	2006-09-04

## Information about participation in other companies:

Name	Surname	Personal code	Position held	Other information: shares held, participation in other companies	Shares held of Vilkyškių pieninė
Gintaras	Bertašius	36401260554	Chairman of the board, general director	Shareholder of "Šilgaliai" (1 divvy) Chairman of the board of JSC "Modest"	6 016 506
Sigitas	Trijonis	36403310012	Member of the board, technical director	-	425 538
Rimantas	Jancevičius	36203241541	Member of the board, director of purchases	-	1 985
Ramūnas	Šniepis	35510220537	Member of the board, "Snoras" bank, director of Tauragė department	-	-
Arvydas	Zaranka	36608280042	Director of production	Member of the board of JSC "Modest"	1 923
Birutė	Bazilienė	45206090918	Chief accountant	-	12

Salaries of the members of managing bodies over last 3 years:

**Salaries of the managing bodies Vilkyškių pieninė 2004-2006**

	2004		2005		2006	
	Charged	Disbursed	Charged	Disbursed	Charged	Disbursed
G. Bertašius	97837,72	63879,39	110547,96	72013,95	121951,08	83435,09
B. Bazilienė	52960,32	35041,68	75134,10	49622,35	75619,17	52248,54
R. Jancevičius	73979,20	48581,20	82654,08	54834,06	91172,64	62617,54
V. Juškys	71313,90	46915,77	82606,61	54131,46	90890,70	62486,76
S. Trijonis	72359,53	46870,39	82280,45	53922,73	90414,74	62177,81
A. Zaranka	42770,47	28636,33	65896,26	43436,84	91709,81	63016,51

There is no information about the previous conviction for crimes against property, agricultural order, and finance of the members of managing bodies.

#### 43. Information about remunerations and loans to members of managing bodies

-

#### 44. Transactions with related parties

-

## VII. RECENT EVENTS IN ISSUER'S ACTIVITIES

### 45. Recent events in issuer's activities

The sales of the company for April 2007 amounted to 5.98 million LTL (1.73 million EUR) - 8.8% decrease comparing to April 2006. The sales of the company for last 12 months (May 2006 - April 2007) amounted to 117.6 million LTL (34 million EUR) - 18% increase comparing to the same period last year (May 2005 - April 2006). The sales of the company for period January - April 2007 amounted to 32.73 million LTL (9.48 million EUR) - 22.7% increase comparing to the same period last year.

Company informs that Board member Vaidotas Juskyš presented resignation letter. Resignation date April 20, 2007.

The sales of the company for February 2007 amounted to 8.64 million LTL (2.5 million EUR) - 35.4% increase comparing to February 2006. The sales of the company for last 12 months (March 2006 - February 2007) amounted to 117.87 million LTL (34.14 million EUR) - 23.5% increase comparing to the same period last year (March 2005 - February 2006). The sales of the company for period January - February 2007 amounted to 18.33 million LTL (5.31 million EUR) - 52.62% increase comparing to the same period last year.

The sales of the company for January 2007 amounted to 9.69 million LTL (2.81 million EUR) - 72% increase comparing to January 2006.

The sales of the company for last 12 months (February 2006 - January 2007) amounted to 115.68 million LTL (33.5 million EUR) - 24.7% increase comparing to the same period last year (February 2005 - January 2006).

### 46. Material events in issuer's activities

Lithuanian cheese producer Vilkyškių pieninė increased its 9 month revenues to LTL 78.1 million (EUR 22.6 million), up by 19% year over year. Profit before taxes in first half a year was LTL 2 818 thousand (EUR 816 thousand). Company's nine month profit before taxes was 42% lower than a year ago. According to G. Bertašius, due to the lower cheese and cream prices during the first half a year, company lost respectively LTL 1.1 million (EUR 0.32 million) and LTL 1.0 million (EUR 0.29 million) in revenues. Despite the cheese price increase back to the last year's level during the 3rd quarter, gross profit margin decreased to 11% from 14% a year ago. Gross profitability was also decreased by higher than expected growth in labor and energy costs. Due to the lower than planned 9 months results, Vilkyškių pieninė reviews downwards its 2006 profit plan to LTL 5.2 million (EUR 1.5 million) profit before taxes. 2007 business plans will be reviewed till the end of January, 2007.

Despite the lower than expected 9 months results, company is planning high revenue growth and modernization in the future. Currently company is undergoing the second phase of LTL 7.63 million (EUR 2.21 million). Worth investment program part of which (LTL 3.45 million (EUR 1 million)) is financed from the EU subsidy funds. Investment program is also planned for the modernization of JSC Modest, which is controlled by Vilkyškių pieninė. On August 10, 2006 company signed EU support agreement, according to which it will receive LTL 2.12 million (EUR 0.61 million) EU support for its LTL 4.83 million (EUR 1.4 million) investment program. Lithuanian cheese producer Vilkyškių pieninė increased its half-year revenues to LTL 44.2

million (EUR 12.8 million), up by 31% year over year. Profit before taxes in first half a year was LTL 203 thousand (EUR 59 thousand).

Due to the production line modernization and onetime expenses related to the initial public offering, operating costs increased by 27%. Company's first half a year profit before taxes reached LTL 203 thousand (EUR 59 thousand) and was 80% lower than a year ago. Therefore company is not considering reviewing annual profit forecasts earlier than the end of the third quarter.

In 2006 Vilkyškių pieninė is planning to reach LTL 113 million (EUR 32.73 million) in revenues and LTL 6.2 million (EUR 1.8 million) in net profit. In 2007 company expects revenues to increase up to LTL 126 million (EUR 36.49 million) and net profit up to LTL 8.3 million (2.4 million). Currently cheese maker is undergoing LTL 7.63 million (EUR 2.21 million) investment program, LTL 3.45 million (EUR 1 million) of which is financed through the EU funds.

Company "Modest", owned by Vilkyškių pieninė, will receive the EU support of 2.1 million Litass (0.61 mEUR). JSC "Modest", owned by one of the most modern Lithuanian cheese producers Vilkyškių pieninė, will receive the support of the EU Structural Funds of over 2.1 million LTL (0.61 mEUR). For these funds the company is planning to streamline the production capacity - to implement new milk processing technologies and modern „Mozzarella“ cheese production-packaging line, moreover to renew the park of the means of transportation of special milk and milk products.

Company Vilkyškių pieninė has acquired 80.24 percent of the shares of JSC "Modest", operating in Širvintos region, in the beginning of this year. According to the audited data, the income of Vilkyškių pieninė in 2005 amounted to 91.708 million Litass (26.56 mEUR), i.e. 22.1 percent more than in 2004, when it reached 75.101 million Litass (21.75 mEUR). Net profit of the company last year amounted to 4.28 million LTL (1.24 mEUR).

#### 47. Business strategy and its foreseen changes during the next financial (economic) year

At the end of last year Vilkyškių pieninė ordered a customer opinion survey, results of which showed that cheese market has high growth potential in Lithuania, as it does in whole Europe. According to those results, a brief outline of nearest future plans for 2007 is provided below.

- At the beginning of June whey remake project will be completed.
- New technological line will process whey into whey concentrate, which is highly demanded in European markets.
- Further modernization of equipment will allow higher quality of production, and will decrease production costs.
- Several steps of technological processing will be automated, decreasing the number of employees, and increasing company's competitiveness.
- The company will go on with the strategy of broadening the assortment of higher value added gourmet types of cheese, and expanding exports to Baltic States, Scandinavia, Russia, and new European Union countries.



- Finally, Quality Management System ISO 9001:2000, and Food Safety Management System ISO 22000:2005 will be implemented.

The company will follow its business culture, as dictated by main Vilkyškių pieninė values, which are reliability, flexibility, and competence.