

DIRECTORS' REPORT

on the Operations of Pfleiderer Grajewo S.A. in the period
January 1st – December 31st 2011

FINANCIAL HIGHLIGHTS

	PLN '000		EUR '000	
	Jan 1 2011– Dec 31 2011	Jan 1 2010–Dec 31 2010	Jan 1 2011–Dec 31 2011	Jan 1 2010– Dec 31 2010
Revenue	1,725,231	1,390,388	416,712	347,219
Operating profit	136,205	47,100	32,899	11,762
Profit/(loss) before tax	38,747	(34,770)	9,359	(8,683)
Net profit/(loss) attributable to owners of the parent	33,208	(15,183)	8,021	(3,792)
Net cash from (used in) operating activities	175,404	113,612	42,367	28,372
Net cash from (used in) investing activities	(33,602)	(21,091)	(8,116)	(5,267)
Net cash from (used in) financing activities	(142,084)	(103,517)	(34,319)	(25,851)
Total net cash flow	(282)	(10,996)	(68)	(2,746)
Basic profit/(loss) per share (PLN / EUR)	0.67	(0.31)	0.16	(0.08)
Diluted profit/(loss) per share (PLN / EUR)	0.67	(0.31)	0.16	(0.08)
PLN/EUR average exchange rate			4.1401	4.0044
	PLN '000	PLN '000	EUR '000	EUR '000
	Dec 31 2011	Dec 31 2010	Dec 31 2011	Dec 31 2010
Total assets	1,935,970	1,852,471	438,320	467,760
Liabilities	1,369,489	1,356,297	310,064	342,473
Non-current liabilities	941,509	1,032,164	213,165	260,628
Current liabilities	427,980	324,133	96,898	81,846
Equity	566,481	496,174	128,256	125,287
Share capital	16,376	16,376	3,708	4,135
Number of shares	49,624,000	49,624,000	49,624,000	49,624,000
Book value per share (PLN / EUR)	11.42	10.00	2.59	2.52
PLN / EUR exchange rate as at the reporting date			4.4168	3.9603

GENERAL INFORMATION

The Pfleiderer Grajewo Group is composed of single-division enterprises. The Group's parent is Pfleiderer Grajewo S.A., which conducts its business in Grajewo, a town situated in north-eastern Poland.

The Parent, under its former name of Zakłady Płyt Wiórowych S.A. of Grajewo, was originally registered on July 1st 1994 by the District Court, Commercial Court of Łomża, in the Commercial Register in Section B under entry No. 270. Subsequently, on May 9th 2001, it was registered by the District Court of Białystok, XII Commercial Division of the National Court Register, under entry No. KRS 0000011422. On September 18 2002, the Management Board of Pfleiderer Grajewo S.A. received the decision of the District Court of Białystok to enter the Company's new name in the National Court Register. Accordingly, on September 18th 2002, the Company's former name was changed to Pfleiderer Grajewo S.A. The registered office of Pfleiderer Grajewo S.A. is situated at ul. Wiórowa 1, Grajewo, Poland. The Company shares are publicly traded. In accordance with the Polish Classification of Business Activities, Pfleiderer Grajewo S.A. is registered under No. 1621 Z.

Below are presented the other entities of the Pfleiderer Grajewo Group:

Pfleiderer Prospan S.A. - a joint-stock company entered in the Polish Commercial Register maintained by the District Court of Kalisz under No. RHB 1754, on September 23rd 1997, under the name of Zakłady Płyt Wiórowych Prospan S.A.; and subsequently, on September 17th 2001, registered with the District Court of Łódź-Śródmieście in Łódź, XX Division of the National Court Register, under No. KRS 0000042082.

Industry Identification Number (REGON):	250744416
Tax Identification Number (NIP):	619-17-42-967
Registered office:	ul. Bolesławecka 10, 98-400 Wieruszów, Poland

Pfleiderer OOO – a limited liability company incorporated under the laws of the Russian Federation, registered on January 15th 2003 by the Interregional Inspection No. 3 of the Novgorod District of the Ministry of Duties and Taxes of the Russian Federation.

Uniform Registration Number:	1035301200164
Tax Identification Number:	5310011273
Registered office: 106	Tsentralnaya St, Novgorod Region 173502, Russia

Pfleiderer MDF OOO – a limited liability company incorporated under the laws of the Russian Federation, registered on September 11th 2007 by the Interregional Inspection No. 3 of the Novgorod District of the Ministry of Duties and Taxes of the Russian Federation.

Uniform Registration Number:	1075321005396
Tax Identification Number:	5310014147
Registered office: 106	Tsentralnaya St, Novgorod Region 173502, Russia

Silekol Sp. z o.o. – a company entered into the National Court Register by the District Court of Opole, VIII Commercial Division of the National Court Register of Opole, under entry No. KRS 0000225788 on January 6th 2005.

Industry Identification Number (REGON):	160003017
Tax Identification Number (NIP):	749-19-69-061
Registered office:	ul. Mostowa nr 30 K, 47-220 Kędzierzyn-Koźle, Poland

Pfleiderer MDF Sp. z o.o. – entered in the National Court Register by the District Court of Białystok, XII Commercial Division of the National Court Register in Białystok, under entry No. KRS 174810, on October 9th 2003.

Industry Identification Number (REGON): 330994545
Tax Identification Number (NIP): 719-13-99-317
Registered office: ul. Wiórowa 1, 19-203 Grajewo, Poland

Jura Polska Sp. z o.o. – a company entered into the National Court Register by the District Court of Katowice, Commercial Division of the National Court Register, under entry No. KRS 149282, on November 24th 1999.

Industry Identification Number (REGON): 276746151
Tax Identification Number (NIP): 629-215-85-14
Registered office: ul. Wiórowa 1, 19-203 Grajewo, Poland

Unifloor Sp. z o.o. (in liquidation) - a company entered in the National Court Register by the District Court of Białystok, Commercial Division of the National Court Register, under entry No. KRS 0000237233, on June 29th 2005.

Industry Identification Number (REGON): 200021250
Tax Identification Number (NIP): 719-149-38-49
Registered office: ul. Bolesławiecka 10, 98-400 Wieruszów, Poland

Pfleiderer Services Sp. z o.o. – a company entered into the National Court Register by the District Court of Białystok, XII Commercial Division of the National Court Register in Białystok, under No. KRS 0000247423 on December 20th 2005.

Industry Identification Number (REGON): 200052769
Tax Identification Number (NIP): 719-15-03-973
Registered office: ul. Wiórowa 1, 19-203 Grajewo, Poland

The company has suspended its operations.

Blitz 11-446 GmbH of Neumarkt, Germany – a company entered in the Commercial Register by the Court in Nurnberg, under No. HRB 28 166.

HRB Registry Number: 28 166
Tax Identification Number (NIP): 201/116/21366
Registered office: Ingolstädter Strasse 51, Neumark, Germany

The business of Pfleiderer Grajewo S.A., Pfleiderer Prospan S.A., Pfleiderer MDF Sp. z o.o. and Pfleiderer OOO consists in the manufacture and veneering of wood and wood-based products, impregnation of paper, trade in Poland and abroad, provision of industrial services related to the companies' core business, as well as other services based on the companies' resources. At present, Pfleiderer MDF OOO constructs an MDF board production plant. The other companies provide services and supply raw materials to the Group entities.

Information on the other entities' business profiles and inclusion of the entities in consolidation is presented in the notes to the annual consolidated financial statements.

As at the end of the reporting period, the Management Board of Pfleiderer Grajewo S.A. of Grajewo, the parent, was composed of:

- | | |
|------------------------|-------------------------------------|
| 1. Wojciech Gątkiewicz | - President of the Management Board |
| 2. Rafał Karcz | - Member |
| 3. Dariusz Tomaszewski | - Member |
| 4. Radosław Wierzbicki | - Member |

The same persons comprising the Management Board of the parent also managed the operations of its subsidiary Pfleiderer Prospan S.A. of Wieruszów.

With effect as of February 8th 2011, Johann Bitzi, Vice-President of the Management Board, was removed from office as member of the Pfleiderer Grajewo Management Board.

The table below sets forth the composition of the Management Boards of the other consolidated entities as at December 31st 2011:

	Jura Polska Sp. z o.o.	Pfleiderer MDF Sp. z o.o.	Silekol Sp. z o.o.	Pfleiderer OOO	Pfleiderer MDF OOO
President	Krzysztof Brzostek	Rafał Karcz	Janusz Zowade	Vladimir Vladimirovich Kotenev	Vladimir Vladimirovich Kotenev
Member	Grzegorz Woelke	Dariusz Tomaszewski	Marek Filusch	Tomasz Mika	Tomasz Mika
Member	-	Radosław Wierzbicki	-	Juergen Winkler	Andrzej Valerevich Nicolajev
Member				Dimitry Lobanov	

On October 31st 2011, the Extraordinary General Meeting of Pfleiderer MDF Sp. z o.o. appointed Mr Radosław Wierzbicki as Member of the Management Board.

As at December 31st 2011, Unifloor did not have a Management Board as the company was in the process of liquidation. The company's liquidator is Mr Ryszard Gruszka.

On 23 March 2012 Extraordinary General Meeting recalled Mr. Grzegorz Woelke from the position of Member of Supervisory Board of Jura Polska Sp. z o.o.

As at December 31st 2011, the composition of the Parent's Supervisory Board was as follows:

- | | |
|-------------------------|----------|
| 1. Michael Wolff | Chairman |
| 2. Hans H. Overdiek | Member |
| 3. Jan Woźniak | Member |
| 4. Hans-Joachim Ziems | Member |
| 5. Hans-Kurt von Werder | Member |

On October 17th, Mr Heiko Graeve resigned from the Pfleiderer Grajewo Supervisory Board.

At the Extraordinary General Meeting held on November 24th 2011 Mr Paweł Wyrzykowski was removed from the post of Chairman of the Supervisory Board.

Mr Hans-Joachim Ziems and Mr Hans-Kurt von Werder were appointed as Members of the Supervisory Board.

At a meeting of the Pfleiderer Grajewo Supervisory Board held on December 21st 2011, Members of the Supervisory Board appointed Mr Michael Wolff to the post of Supervisory Board Chairman.

On March 7th 2012, Mr Hans-Joachim Ziems tendered his resignation from the position of a member of Pfleiderer Grajewo S.A.'s Supervisory Board, with effect as of April 10th 2012.

At the Extraordinary General Meeting held on April 10th 2012 Mr Jochen Schapka was appointed as Member of the Supervisory Board.

Pfleiderer Grajewo S.A.'s shareholder structure:

Shareholder structure as at Apr 16 2012	Number of shares	Ownership interest (%)	Number of votes at GM	% of votes at GM
Pfleiderer Service GmbH	32,308,176	65.11%	32,308,176	65.11%
Aviva OFE Aviva BZ WBK	4,928,816	9.93%	4,928,816	9.93%
ING OFE	2,639,144	5.32%	2,639,144	5.32%
Other shareholders	9,747,864	19.64%	9,747,864	19.64%
TOTAL	49,624,000	100.00%	49,624,000	100.00%

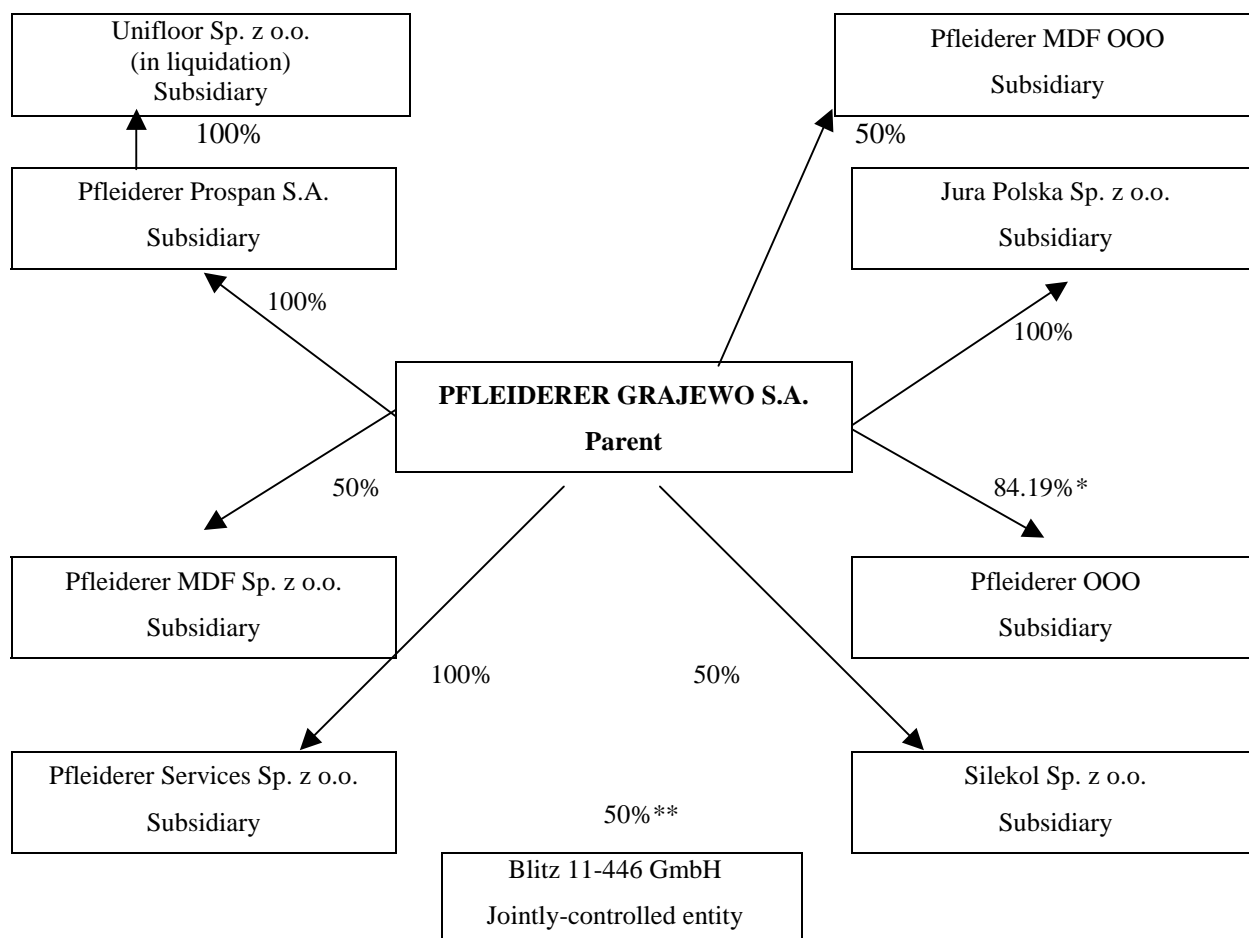
The information on the number of Company shares held by Aviva OFE (former Commercial Union Otwarty Fundusz Emerytalny BPH CU WBK) is sourced from the most recent notification of shareholding change, received by the Company on July 9th 2007.

Information on the number of shares in Pfleiderer Grajewo S.A. held by ING OFE is based on the most recent notification of change in the number of shares held, received by the Company on June 5th 2009.

The number of the Company shares held by its main shareholder, Pfleiderer Service GmbH, did not change during the period under review.

Structure of the Group as at December 31st 2011

Structure of the Group as at December 31st 2011:



1. The main shareholder of Pfleiderer Grajewo S.A. is Pfleiderer Service GmbH, which holds 65.11% of the Company shares.
2. 50% of shares in Pfleiderer MDF Sp. z o.o. is held by Pfleiderer Service GmbH.
3. 50% of shares in Silekol Sp. z o.o. is held by Pfleiderer Holzwerkstoffe GmbH.
4. 50% of shares in Pfleiderer MDF OOO is held by Pfleiderer Schweiz AG.

Pfleiderer Grajewo S.A. (Parent) holds 50% of the shares and votes in subsidiaries Pfleiderer MDF Sp. z o.o., Silekol Sp. z o.o., and Pfleiderer MDF OOO, but it still exercises control over these entities as it has the power to govern their financial and operating policies through the right to appoint and remove from office a majority of the management board members of the entities.

* Pfleiderer Grajewo S.A. holds a call option to repurchase the shares held by the non-controlling shareholder prior to the agreed date. The non-controlling shareholder holds a put option to sell early the shares held in the Parent if the financial agreements executed between the Parent, Pfleiderer OOO and the non-controlling shareholder are breached, or if there is a risk that the shares might not be repurchased by the parent by the agreed date. Accordingly, from the point of view of the parent (Pfleiderer Grajewo S.A.), Pfleiderer OOO is treated as a subsidiary in which Pfleiderer Grajewo S.A. holds 100% of shares. For details, see Note 21.

** Shares in the company Blitz 11-446 GmbH, which is jointly controlled by a Group are taken in consolidated financial statements and are accounted for with the equity method.

Changes in the Group's structure in the reporting period

On December 21st 2011, Pfleiderer Grajewo S.A. and Pfleiderer Service GmbH acquired shares in Blitz 11-446 GmbH of Germany. Each of the companies holds 50% of shares in Blitz 11-446 GmbH. The purchase price paid by Pfleiderer Grajewo S.A. was EUR 14.5 thousand (PLN 65.2 thousand).

External factors with a bearing on the Group's business:

- Broader collaboration with customers, which is based on long-term framework agreements, providing the parties with assurance of stable cooperation and lasting development.
- Customer insolvency risk – the Group monitors the financial liquidity of its customers on an ongoing basis, mitigating the customer insolvency risk by using trade credit insurance.
- Dependence on suppliers – key raw materials purchased by the Group include wood and wood waste, decorative paper, chemical substances, and machine parts. The Group mitigates the related risk by using diversified sources of supplies. Increases in the prices of the raw materials affect the Group as well as its competitors and for this reason do not have an adverse impact on the Group's competitive position.
- Currency risk – the Group does not incur any significant currency risk. It monitors its exposure to exchange-rate fluctuations on an ongoing basis and relies on natural hedging and forward transactions to hedge the risk.
- Seasonality – sales fall in the second quarter of a year. Seasonal changes do not give rise to a significant risk for the Group as lower sales in the period are accompanied by lower purchases of raw materials. The Group's liquidity remains relatively stable over the second quarter.

Internal factors with a bearing on the Group's business:

- Technological process – the technologies employed by the Group result in exposure to fire hazard. To mitigate that risk, the Group uses a number of technical and organisational safeguards. There is no risk of unscheduled process stoppages at the Group, as its plant and equipment is relatively new.
- Debt risk – as the parent of the other Group members, Pfleiderer Grajewo S.A. bears all the burdens related to the financing of investment projects. The debt is monitored on an ongoing basis. To mitigate the liquidity risk, the Group uses a full spectrum of available financial instruments.

Plans and development prospects for 2012

- Focus on the furniture sector and strengthening of the Company's position as a leading full-range supplier for the sector.
- Launch of a new product range on the construction market.
- Launch of the new range of UNICO kitchen worktops on the construction and furnishings markets.
- Launch of new laminated board lines, and a review of quality and technical parameters of selected products in order to respond to customers' requirements.
- Expansion onto European markets.
- Continued investments in Russia.
- Further optimisation of the production processes and cost savings programme.
- Modernisation of the production plant and equipment in order to ensure the highest quality of products and enhancement of production efficiency.
- Promotion of the brand and mission of Pfleiderer as a modern and continuously expanding company, which implements state-of-the-art technologies and respects the natural environment.

1. In 2011, the efforts of Pfleiderer Grajewo S.A. were focused on the following tasks:

1. Optimisation of the production process and optimisation of operating costs
2. Group-wide increase of production and sales volumes
3. Optimisation efforts designed to improve the Group entities' operating efficiency
4. Manufacturing of a new range of products - MFP construction boards
5. Securing of wood supplies
6. Ensuring financial liquidity of the Group
7. Enhancing efficiency and production processes through tight cost control
8. Promoting the Company's image as a financially stable and reliable business partner.
9. Strengthening of Pfleiderer's market position by promoting the Company's brand and vision

2. Financial standing of the Pfleiderer Grajewo Group

The Pfleiderer Grajewo Group finances its operations primarily with bank borrowings. Most of these facilities are long-term borrowings. The bank borrowings are advanced to Pfleiderer Grajewo S.A. or to project vehicles (project finance) i.e. Pfleiderer OOO, Pfleiderer MDF Sp. z o.o., and, in the near future, Pfleiderer MDF OOO.

Additionally, the Group is financed with loans advanced by its shareholders (Pfleiderer AG and Pfleiderer Service GmbH). The loans are primarily used to finance the operations of Pfleiderer MDF OOO in Russia, and, to a lesser extent, Pfleiderer Grajewo S.A. and Pfleiderer MDF Sp. z o.o.

Moreover, the Pfleiderer Grajewo Group supports its operations with a non-recourse factoring programme, whereby it sells insured trade receivables to PEKAO Faktoring Sp. a o.o. The above financing of Pfleiderer Grajewo S.A. and Pfleiderer Prospan S.A. of up to PLN 200m is an off-balance sheet item.

The internal financing in the Pfleiderer Grajewo Group comprises loans advanced by Pfleiderer Grajewo S.A. to its subsidiaries: Pfleiderer OOO, Pfleiderer MDF OOO, and Silekol Sp. z o.o., as well as issues and purchases of short-term notes (commercial papers). The notes are usually issued by Pfleiderer Grajewo S.A., and acquired by Pfleiderer Prospan S.A. and Silekol Sp. z o.o.. The issuance programme and the loans are designed to provide financing to all of the Group's entities and optimise cash management within the Group.

3. Staff and remuneration at the Pfleiderer Grajewo Group.

As at December 31st 2011, all companies of the Group employed 1,639 personnel, including the management personnel and staff working under managerial contracts or appointed by the Supervisory Board. The employment structure as at the last day of the reporting period was as follows:

Employees	Dec 31 2011	Dec 31 2010
- direct production employees	801	765
- indirect production employees	393	419
- administration, office and other employees	445	434
Total	1,639	1,618

Employment at Group companies:

Company	Headcount in 2011	Employees directly involved in production	Employees indirectly involved in production	Administration, office and other employees
PFLEIDERER GRAJEW O S.A.	583	282	121	180
Pfleiderer Prospan S.A.	428	235	94	99
Pfleiderer OOO Russia	361	117	153	91
Pfleiderer MDF OOO Russia	5	0	0	5
Jura Polska Sp. z o.o.	26	10	0	16
Silekol Sp. z o.o.	84	40	25	19
Pfleiderer MDF Sp. z o.o.	152	117	0	35
Total	1,639	801	393	445

Remuneration of the members of the Pfleiderer Grajewo Management Board, including bonuses paid for the period January 1st – December 31st 2011 was as follows:

1.	President of the Management Board	- Wojciech Gątkiewicz	PLN 735 thousand
2.	Member	- Rafał Karcz	PLN 369 thousand
3.	Member	- Dariusz Tomaszewski	PLN 456 thousand
4.	Member	- Radosław Wierzbicki	PLN 460 thousand

The same persons serve on the Management Board of Pfleiderer Prospan S.A. The remuneration of the members of the Management Board of Pfleiderer Prospan S.A. for the same period was as follows:

5.	President of the Management Board	- Wojciech Gątkiewicz	PLN 735 thousand
6.	Member	- Rafał Karcz	PLN 369 thousand
7.	Member	- Dariusz Tomaszewski	PLN 456 thousand
8.	Member	- Radosław Wierzbicki	PLN 453 thousand

The managerial contract with Mr Rafał Karcz, member of the Management Board, contains a provision entitling Mr Karcz to a one-off severance pay equal to one month's remuneration if the contract is terminated by notice.

The managerial contract between Pfleiderer Prospan S.A., the Company's related entity, and Mr Dariusz Tomaszewski, member of the Management Board, contains a provision entitling Mr Tomaszewski to a one-off severance pay equal to one month's remuneration if the contract is terminated by notice.

The managerial contract with Mr Wojciech Gątkiewicz, President of the Management Board, in effect as of January 1st 2012, provides for a six-month notice period.

The remuneration paid to the members of the Supervisory Board of Pfleiderer Grajewo S.A. for the period January 1st – December 31st 2011 amounted to PLN 48 thousand and was paid only to Mr Jan Woźniak.

Supervisory board members at the other Group companies did not receive any remuneration in the reporting period.

As at December 31st 2011, the members of the Management and Supervisory Boards of Pfleiderer Grajewo S.A. had no outstanding debt under any loan agreements with the Company. At Pfleiderer Prospan S.A., as at December 31st 2011 Mr Dariusz Tomaszewski was the only member of the Management Board, who had outstanding debt of PLN 26 thousand, resulting from a loan taken out in 1997 from the Privatisation Fund to finance the purchase of Prospan shares.

4. Number of Pfleiderer Grajewo S.A. shares held by the management staff of Pfleiderer Grajewo S.A.

As at the date of this report the holdings of the Management Board members were as follows:

- Wojciech Gątkiewicz, President of the Management Board, held 5,400 Company shares,
- Rafał Karcz, Member of the Management Board, held 3,472 Company shares,
- Mr Dariusz Tomaszewski, Member of the Management Board, held 4,108 Company shares;
- Mr Radosław Wierzbicki, Member of the Management Board, held 2,000 Company shares.

As at the date of this report, Mr Jan Woźniak, Member of the Supervisory Board, held 10,000 shares in Pfleiderer Grajewo S.A.. The other members of Pfleiderer Grajewo S.A.'s Supervisory Board did not hold any shares in the Company.

Mr Paweł Wyrzykowski held 4,800 shares in Pfleiderer Grajewo S.A. as at December 31st 2010.

Under the stock option scheme operated by Pfleiderer AG, the parent of the Pfleiderer Group, members of the Management Board of Pfleiderer Grajewo S.A. were entitled to acquire options for shares in the Pfleiderer Group's parent directly from Pfleiderer AG. The options were valued with the Black-Scholes model, assuming a three-year vesting period. As at December 31st 2011, the value of options granted to the members of the Pfleiderer Grajewo Management Board was as follows:

- Mr Wojciech Gątkiewicz, President of the Management Board – PLN 0
- Mr Rafał Karcz, Member of the Management Board – PLN 31.1 thousand
- Mr Dariusz Tomaszewski, Member of the Management Board – PLN 20.2 thousand
- Mr Radosław Wierzbicki, Member of the Management Board – PLN 15.6 thousand.

5. Production volume and structure

In 2011 and 2010, the production volumes of the four main product groups at the three Polish companies of the Group (Pfleiderer Grajewo S.A., Pfleiderer Prospan S.A. and Pfleiderer MDF Sp. z o.o.) and at the Russian subsidiary were as follows:

		Dec 31 2011	Dec 31 2010
Gross production of raw chipboards	thousand m ³	1,519.3	1,469.7
Melamine-faced chipboards	thousand m ²	52,230.8	51,690.1
Raw MDF boards	thousand m ³	223.9	206.8
Lacquered MDF boards	thousand m ²	24,158.1	24,356.0

In 2011, the production of raw and melamine-faced chipboard increased slightly. In 2011, the Group did not use its production capacity in full.

Compared with 2010, 2011 saw an 8% increase in the production of raw MDF board and a slight decrease in production of lacquered MDF board.

6. Sales volume and structure

Revenue reported by all Group companies in 2011 was PLN 1,725,231 thousand, up by 24% year on year.

The Group's export sales in 2011 improved significantly, having increased by 33% year on year. At the Parent, exports to countries east of Poland and to the EU countries accounted for 39% of total sales, up by 15% on 2010.

The table below present an analysis of revenue by products, goods, materials, and services.

By product group	Jan 1–Dec 31 2011	%	Jan 1–Dec 31 2010	%
Revenue from sales of products	1,618,043	93.79%	1,302,774	93.70%
Chipboard	1,165,266	67.54%	954,807	68.67%
MDF boards	230,945	13.39%	183,171	13.17%
Adhesive resins	150,518	8.72%	102,561	7.38%
Other	71,314	4.13%	62,235	4.48%
Revenue from sales of materials	5,348	0.31%	3,875	0.28%
Revenue from sales of merchandise	78,211	4.53%	65,341	4.70%
Revenue from sales of services	23,629	1.37%	18,398	1.32%
Total	1 725 231	100.00%	1 390 388	100.00%

Quantitative sale of the main products of the Pfleiderer Grajewo as follows

By product group (in thousand m ³)	2011	2010
Chipboard	891.3	876.0
MDF boards	64.5	59.2
Total quantitative sale	955.8	935.1

The furniture industry continues to be the most important sector for Pfleiderer Grajewo Group as it accounts for 90% of its total sales. The Group takes steps to more effectively place its products on the interior design market. On the other hand, it focuses its efforts on expanding its presence on the

construction market, which is becoming increasingly more attractive for chipboard manufacturers in Poland.

The long-term sales strategy of the Pfeiderer Grajewo Group is based on three key distribution channels:

1. Sales to industrial customers
2. Sales to the Pfeiderer Partner dealership network (PP network)
3. Export sales

The Group's sales data comprises sales of Pfeiderer Grajewo S.A., Pfeiderer Prospan S.A., and Pfeiderer MDF Sp. z o.o. The Group's sales by distribution channels in 2010–2011 were as follows:

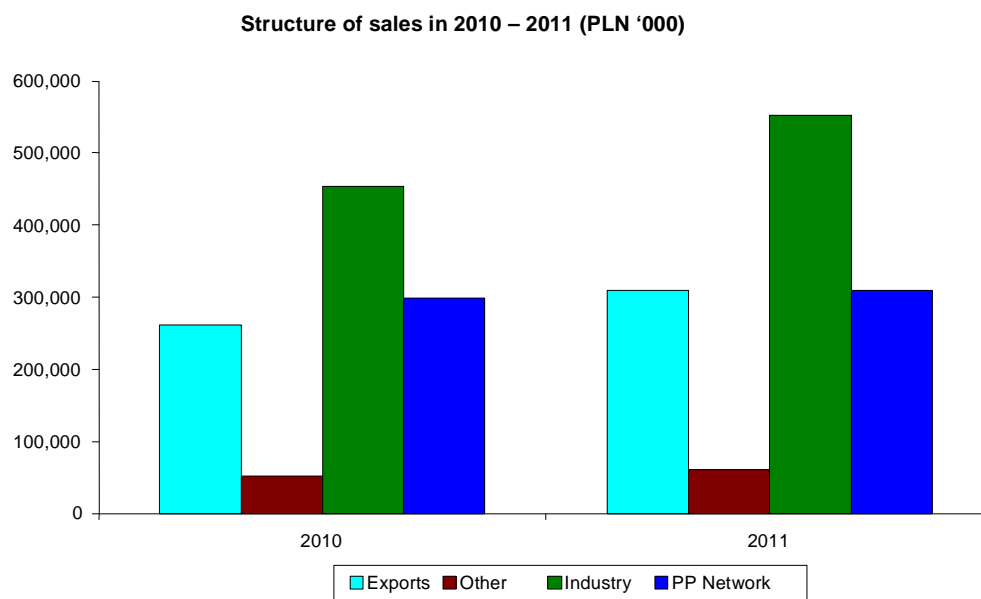


Fig. Sales structure in 2010–2011 (PLN '000)

In the Polish market, direct sales to large and medium-sized furniture producers and the Pfeiderer Partner network continued to represent the most important distribution channels. Compared with the previous year, in 2011 direct sales to medium-sized and large furniture producers rose by 22% in value terms, while sales to the Pfeiderer Partner wholesale network increased by 4% in value terms. Export sales increased by 19% in the reporting period. Sales through other distribution channels rose by 18%.

Relative to 2010, the shares of the individual distribution channels in the structure of total sales changed. Share of direct sales to medium-sized and large furniture producers saw an increase from 42.6% to 44.8%, share of export sales went up from 24.4% to 25.1%, while the share of sales through other distribution channels rose from 4.9% to 5.0%. The share of sales to the Pfeiderer Partner wholesale network declined from 28.1% to 25.1%.

7. Procurement

In 2011, both Polish and Russian plants purchased raw wood from traditional sources, located in close proximity to the plants.

The share of individual product groups in total supplies varied slightly between the plants due to their different production profiles, local markets, or the current pricing of various raw materials.

In Poland, forest wood represented 51.6% of all supplies, while by-products of the wood processing industry accounted for 48.4% of the total. The share of recycled raw materials in total supplies

remained at a level similar to 2010, and was 5.4%. Supplies of wood from Poland prevailed, and represented 74.5% of total purchases.

In Russia, the share of round timber decreased slightly and accounted for 69%, while the share of wood processing waste rose to 31% of total purchases. Nearly all wood supplies (above 80%) came from the Novgorod area.

8. Economic and financial data

The cost of raw materials and energy used continues as the dominant component in the cost structure of the Group companies. Additionally, the cost of contracted services accounts for a significant portion of the costs incurred by the companies. This follows from the fact that certain auxiliary functions were outsourced and certain types of services were contracted from external companies, as well as from a gradual growth of transport costs related to the sale of products and supplies of raw materials. Finance expenses are an increasingly important component of the income statement, especially in the case of the parent. This is due to the large capital expenditure made by the Group. Other items were not materially changed relative to the previous periods.

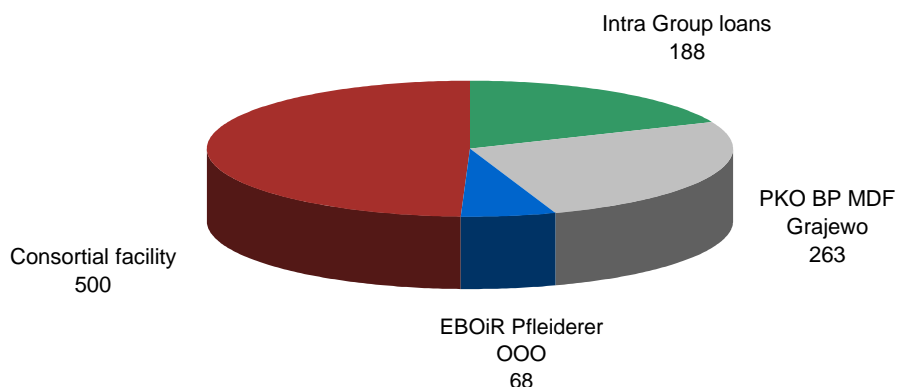
In 2010 and 2009, the Group recorded the following sales margins:

	Jan 1–Dec 31 2011	Jan 1–Dec 31 2010
<u>Net profit/loss</u>		
Revenue	2.25%	(2.50%)
	Jan 1–Dec 31 2011	Jan 1–Dec 31 2010
<u>Net profit/loss (attributable to owners of the parent)</u>		
Revenue	1.92%	(1.09%)

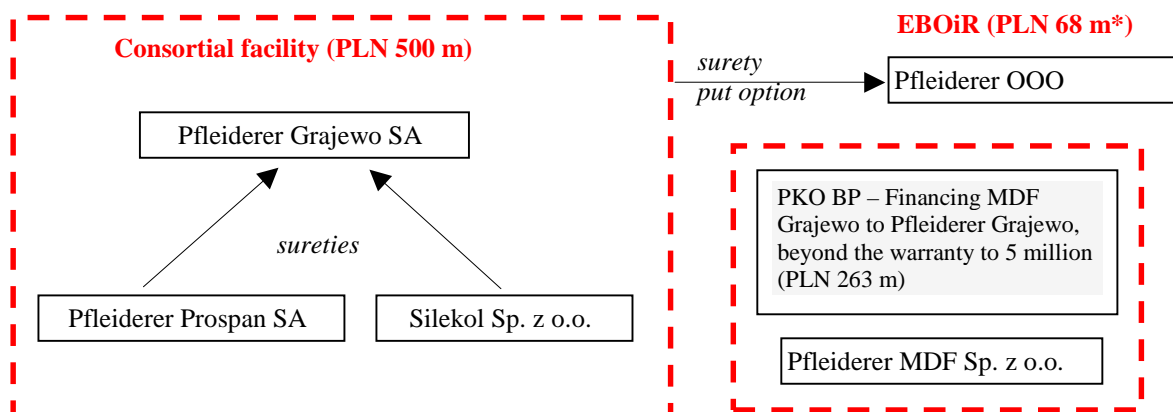
9. Use of bank borrowings

PLNm	Dec 31 2011
Debt under bank borrowings	831
Intra-Group loans	188
Cash	20
Net debt under bank borrowings	811

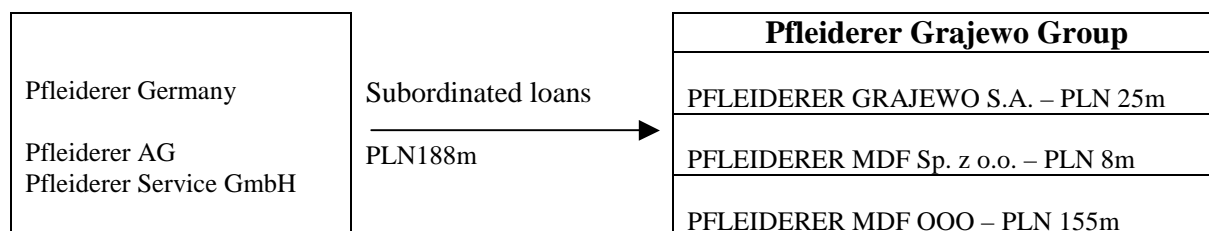
Debt structure at the Pfeiderer Grajewo Group



Financing of the Pfeiderer Grajewo Group



Financing of the Pfeiderer Grajewo Group by Pfeiderer Germany



Financing of the Pfeiderer Grajewo Group by Pfeiderer Germany is based exclusively on subordinated loans. All advanced loans are subordinated to bank borrowings, and must not be repaid prior to the bank borrowings, and banks treat them as equity. In addition, no sureties or guarantees are outstanding between Pfeiderer Germany and the Pfeiderer Grajewo Group.

Syndicated credit facility agreement

On March 16th 2010, Pfleiderer Grajewo S.A. (Parent) and its subsidiaries Pfleiderer Prospan S.A. and Silekol Sp. z o.o. executed a PLN 700m credit facility agreement with a bank syndicate. The credit facility has been used to repay the Company's outstanding debts.

The bank syndicate comprised the same institutions which have so far provided funding to the Company, i.e. Bank PEKAO S.A. (syndication agent), Bank Zachodni WBK S.A., BRE Bank S.A. Fortis Bank Polska S.A., and Bank Gospodarki Żywnościowej S.A.

The new credit facility extended to the Company under the agreement is split into two tranches:

- PLN 530,000,000 Tranche A, in the form of a non-revolving facility to be used to repay the outstanding debt owed by the Company and its subsidiaries to the Banks;
- PLN 170,000,000 Tranche B, in the form of a working capital revolving facility to be used to repay the outstanding debt owed by the Company and its subsidiaries to the Banks and to finance the Company's day-to-day operations.

The repayment deadline for Tranche A is December 30th 2013, while Tranche B is to be repaid two years after execution of the credit facility agreement. Furthermore, under Tranche B bank guarantees and letters of credit may be issued.

Repayment of the credit facility is secured by:

- mortgages over the Company's and the Subsidiaries' real estate, on which production facilities are located, up to the amount of PLN 1,400m;
- registered pledges over assets owned by the Company and the Subsidiaries (pledge over a business), up to the amount of PLN 1,050m;
- financial and registered pledge over the Group's shares in the Subsidiaries; the pledge covers 100% of the shares in Pfleiderer Prospan S.A. and 50% of the shares in Silekol Sp. z o.o.;
- financial and registered pledge over the Group's bank accounts;
- assignment by way of security of the Group's plant and equipment intended to be used for the purpose of the MDF project in Russia.

Additionally, an agreement creating a pledge over Pfleiderer Grajewo S.A.'s shareholding in Pfleiderer MDF OOO is to be executed and the scope of security to be created over Pfleiderer MDF OOO's assets is to be established. At present, the agreed date for the performance of the obligations specified above is May 31st 2012.

Under the agreement, the subsidiaries will be jointly and severally responsible for the liabilities assumed by the Company as the borrower.

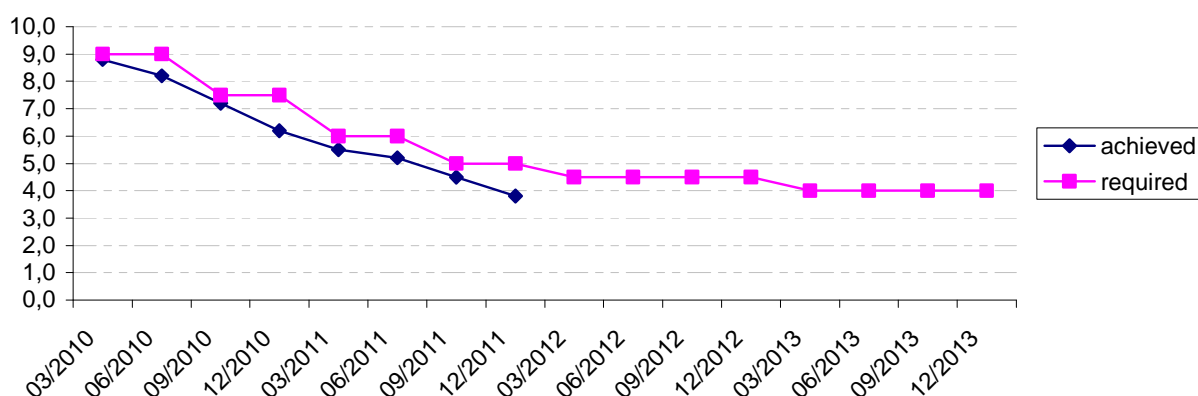
The credit facility agreement contains financial covenants concerning the required level of certain financial ratios, which are based on consolidated financial data of the Pfleiderer Grajewo Group. These ratios are related to:

- financial debt to EBITDA
- total equity to total assets,
- current assets to current liabilities,
- debt-service coverage ratio,

As at December 31st 2011, all bank covenants were complied with.

The Group monitors the ratios on an ongoing basis and, based on its short-term financial plans, analyses the risk of failure to meet the ratios.

Development of net financial debt to EBITDA ratio.



In 2011, Pfeiderer OOO financed its working capital with a bank borrowing in the form of an overdraft facility contracted with ZAO RaiffeisenBank, which was repaid in full on September 30th 2011.

Moreover, Pfeiderer OOO of Russia was advanced an investment loan by the European Bank for Reconstruction and Development, repayable in instalments by October 11th 2013. The original facility amount was EUR 35m. The debt outstanding under the facility as at December 31st 2011 was EUR 7.8m.

In performance of the agreement with the EBRD, in Q2 2007 Pfeiderer OOO issued, and the EBRD subscribed for, new shares worth EUR 7m. The agreement provides for the Bank's equity involvement until June 19th 2012. Thereafter, the shares will be sold to Pfeiderer Grajewo S.A., which has a call option to repurchase the shares held by the Bank at any time prior to the agreed date. The EBRD holds a put option enabling it to sell the shares before December 28th 2010 if the financing agreements concluded by the Company and Pfeiderer OOO with the EBRD are breached and if there arises the risk that the shares may not be purchased by the agreed deadline. The financial cost of the transaction, following from the difference between the purchase price and the selling price of the shares, will be equal to annual interest expense under the facility.

In 2011, Pfeiderer MDF Sp. z o.o. was using bank borrowings. As at December 31st 2011, Pfeiderer MDF Sp. z o.o. was a party to the following credit agreements:

1. Investment loan of PLN 227m from PKO BP S.A. repayable by July 15th 2016.
2. Credit facility of up to PLN 57m, repayable by June 30th 2013. As at December 31st 2011, the debt under the facility was PLN 35.7m.

As at December 31st 2011, Pfeiderer MDF Sp. z o.o. utilised PLN 263m under the facilities.

Pfeiderer Prospan S.A. and Silekol Sp. z o.o. had no debt under bank borrowings.

For information on interest rates applicable to the credit agreements, see Section 21 of the consolidated financial statements.

As at December 31st 2011, the debt outstanding under the bank borrowings taken out by the Group totalled PLN 831m.

As at December 31st 2011, the Group companies did not have any borrowings other than those described above.

10. Feasibility of Pfleiderer Grajewo Group's investment plans for 2011

The Group's capex in 2011 amounted to PLN 34 m (including PLN 12,6m for the construction of the MDF Plant in Novgorod).

PFLEIDERER GRAJEWO S.A.

Operating investments in 2011: planned expenditure – PLN 7.7m; actual expenditure – PLN 6.0m.

The largest project planned for 2011 was the panel processing solution (project value: PLN 3.8m), which was postponed from 2010. Ultimately, the Company spent PLN 0.14m more on the project in 2011, primarily due the higher than budgeted EUR/PLN exchange rate in the second half of the year.

The remaining capital expenditure of PLN 2.2m was spent on smaller projects scheduled for 2011. The difference between planned and actual expenditure is a result of substituting purchase of three pieces of specialist wood loading equipment with long-term leases.

PFLEIDERER PROSPAN S.A.

Operating investments in 2011: planned expenditure – PLN 5.0m; actual expenditure – PLN 4.4m.

A taping machine with a capacity of 50t/h and forming stations were the largest projects planned for 2011 (rescheduled from 2010), completed at a cost of PLN 2.3m (within budget). Other large projects included a power supply line (actual expenditure: PLN 0.8m, planned: PLN 1.0m) and closing of a landfill (actual expenditure: PLN 0.6m, planned: PLN 0.8m). The remaining capital expenditure of PLN 0,7m was spent on smaller projects planned for 2011 and the high pressure taping machine project, which was launched ahead of schedule.

SILEKOL Sp. z o.o.

Operating investments in 2011: planned expenditure – PLN 2.3m; actual expenditure – PLN 1.4m.

The expenditure of PLN 1.4m covered mostly other minor projects (e.g. melamine handling system, glue warehouse upgrade and loading station for melamine and formalin). The construction of a steam superheater (PLN 0.7m), scheduled for 2011, was cancelled due to execution in 2012 of a comprehensive steam management project (approved in 2011).

PFLEIDERER MDF Sp. z o.o.

Operating investments in 2011: planned expenditure – PLN 2.8m; actual expenditure – PLN 2.1m.

The largest project in 2011 was a grinder for bark and oversized biomass components (PLN 0.7m). The company spent PLN 1.1m on the project.

Other capital expenditure of PLN 1.0m covered chiefly minor replacement projects, among which the most important ones were: a biomass shed (PLN 0.2m, within budget) and a heat exchanger (PLN 0.2m, within budget).

OOO PFLEIDERER

Operating investments in 2011: planned expenditure – PLN 5.6m; actual expenditure – PLN 5.7m.

The largest expenditure in 2011 involved purchase of a set of diamond rollers (PLN 0.6 m), air conditioning stations (PLN 0.5m), a production line cooling system (PLN 0.4m) and process a wastewater pretreatment plant (PLN 0.9). The expenditure of PLN 4.6m covered mostly other minor operating projects.

11. Marketing activities in 2011

The marketing efforts of Pfleiderer Grajewo S.A. and the Group companies in 2011 included:

Promotion of the Pfleiderer brand and mission

“OUR MISSION STATEMENT: We foster partnership in development and building common value, and strive to ensure functional and sustainable wood-based solutions for your home.”

The Pfleiderer brand

- Creation of a positive image of the Pfleiderer brand among all stakeholders;
- Pfleiderer – a reliable business partner offering attractive prospects for growth;
- Professionalism, responsibility and credibility of the management staff;
- Consistent internal and external communication.

Corporate objectives

- Positive financial result at all levels of the P&L in 2011;
- 10% margin on new products;
- Improved customer service – customer segmentation;
- Increased focus on products generating higher margins;
- Sector diversification.

Marketing objectives

- Development of the Premium brands and products;
- Finding new applications for the existing product mix;
- Using all possible opportunities for strong entry onto local markets;
- Creating new quality of dealership network;
- Developing new communication channels at Pfleiderer
- Implementing trade and marketing standards for serving new markets and customers.

Product policy

First of all, Pfleiderer Grajewo S.A. took steps to optimise its product portfolio and continued search for new markets. The Company put a lot of effort into further development of its product mix.

Pricing

The continued efforts to withdraw from the commodity segment of the furniture industry require the Company to take broader look at its offering. Apart from items exposed to significant price pressures, the group also includes many products with a potential for better margins.

In interior design, the Company entered the market with high-end products. The customers expect good quality and they are also ready to bear higher costs connected.

The offer for the construction industry includes Premium brand products. However, the Group also entered the market for lower-priced items, i.e. shuttering board.

Distribution strategy

Over the years, the duality of services rendered for the furniture industry has proven to be an efficient system and may now be considered optimal.

The Group needs to put yet more effort into improving the distribution system in the interior design sector.

New communication/distribution channels/; increasing the Company's presence on the interior design market through cooperation with the following partner groups:

- design and architecture studios,
- kitchen studios,
- entities offering interior design products and accessories,
- innovative and non-mainstream furniture manufacturers,
- Pani Kowalska (communications).

The situation on the construction market requires the Company to take further steps aimed at building a base of loyal distributors. In order to effectively reach customers with our offering, it is necessary to create dedicated distribution channels, tailored to the needs of particular market segments.

Communications policy

Our extensive communications efforts effectively conveyed information about the Company, its products and values to all target groups. Depending on the form of interaction between Grajewo Pfleiderer and the target groups (e.g. type of application of our products or of business relations), the communications process is based on different criteria and promotes relevant values.

From the point of view of the target groups, such messages may be broken down into those addressed to end users and business partners. These areas of communication may often overlap.

The customer dimension - "Pfleiderer as a partner providing functional and sustainable wood-based solutions for your home"

- Differentiation of Pfleiderer's products from those offered by our competitors;
- Building strong product distinctiveness and characteristics;
- Communications based on products' strengths and possible applications.

The business dimension - "Pfleiderer as a partner in development and building common value"

- Building Pfleiderer's position as an industry leader;
- Promoting the Company's image as an innovative and experienced partner introducing new solutions to the market;
- Promoting the Company's image as a financially stable partner focused on business growth.

12. Material related-party transactions in 2011

Information on material transactions executed with related parties in 2010 is provided in Note 29 in the Supplementary Notes to the Group's annual consolidated financial statement

In 2011, the Company did not execute any related-party transactions other than on an arms' length basis.

13. Management of Pfleiderer Grajewo Group's financial resources in 2011

In 2011, Pfleiderer Grajewo S.A. financed its operations chiefly with bank borrowings and, to a certain extent, issues of notes acquired by Pfleiderer Prospan S.A.

As at December 31st 2011, the par value of the parent's debt under notes in issue totalled PLN 295m. Short-term bonds are issued order to optimise the management of financial liquidity within the Pfleiderer Grajewo Group, to decrease Company's external debts and to finance it's current business activities. As at the same date its debt under bank borrowings was PLN 500m, under put option PLN 38.6m, totally PLN 538.6m.

On March 16th 2010, Pfleiderer Grajewo S.A. (Parent) and its subsidiaries Pfleiderer Prospan S.A. and Silekol Sp. z o.o. executed a PLN 700m credit facility agreement with a bank syndicate. The credit facility has been used to repay the Company's outstanding debts.

Credit facility from March 16th 2010 extended to the Company under the agreement is split into two tranches:

- PLN 530,000,000 Tranche A, in the form of a non-revolving facility to be used to repay the outstanding debt owed by the Company and its subsidiaries to the Banks;
- PLN 170,000,000 Tranche B, in the form of a working capital revolving facility to be used to repay the outstanding debt owed by the Company and its subsidiaries to the Banks and to finance the Company's day-to-day operations. . Company's debt under Tranche B amounted to PLN 20m. As at December 31st 2011 repayment date of Tranche B was scheduled for March 16th 2012. On March 15th 2012 an annex to the Credit Facility Agreement of March 16th 2010 was signed. The annex extended the repayment date for Tranche B, previously scheduled for March 16th 2012. Consequently, the full amount of Tranche B (PLN 170,000,000) falls due on March 16th 2013. Furthermore, under Tranche B bank guarantees and letters of credit may be issued.

As at December 31st 2011, liabilities under borrowings contracted by subsidiary Pfleiderer MDF Sp. z o.o. stood at PLN 263m. Pfleiderer MDF Sp. z o.o. contracted an investment loan from PKO BP S.A., to be repaid in instalments by July 15th 2016. As at December 31st 2011, the debt under the loan was PLN 227.0m. Also, Pfleiderer MDF Sp. z o.o. was advanced by PKO BP S.A. a PLN 57m multi-purpose credit facility repayable by June 30th 2013. As at December 31st 2011, the debt outstanding under this facility was PLN 35,713 thousand.

As at December 31st 2011, Pfleiderer Prospan S.A. and Silekol Sp. z o.o. utilised PLN 0m under bank borrowings.

Pfleiderer OOO financed its operations with bank borrowings, advanced by the European Bank for Reconstruction and Development. As at December 31st 2011 the debt outstanding under the facility was PLN 29.4m (EUR 7.8m), debt is repayable in instalments by October 11th 2013.

In 2011, Pfleiderer OOO financed its working capital with a bank borrowing in the form of an overdraft facility contracted with ZAO RaiffeisenBank, which was repaid in full in September 2011.

In performance of the agreement with the EBRD, in Q2 2007 Pfleiderer OOO issued, and the EBRD subscribed for, new shares worth EUR 7m. The agreement provides that the EBRD will retain its capital commitment until June 19th 2012. Thereafter, the shares will be sold to Pfleiderer Grajewo S.A.. Pfleiderer Grajewo S.A. has a call option allowing it to repurchase the shares held by the Bank at any time before the abovementioned date. The EBRD holds a put option to allowing it to early sell the shares in the event of a default under the financing agreements executed by the Company and Pfleiderer OOO

with the EBRD or if there is a risk that the shares will not be repurchased by the agreed deadline. The financial cost of the transaction, following from the difference between the purchase price and the selling price of the shares, will be equal to annual interest expense under the loan.

The Parent has an outstanding loan advanced by Pfleiderer Services GmbH to finance its current business activities. As at December 31st 2011 the debt amounted to PLN 24.9m. The debt is to be repaid by June 30th 2014.

Pfleiderer MDF OOO financed the construction of a plant in Russia with loans advanced to it by Pfleiderer Grajewo S.A. (loan in RUR) and Pfleiderer AG (loan in EUR).

In 2011, Pfleiderer Grajewo SA granted two loans to Pfleiderer MDF OOO of the total amount of RUR 82,182 thousand. Interest of loans is MOSPRIME + margin. In addition, Pfleiderer AG in 2011 Pfleiderer MDF OOO granted four loans for a total of EUR 5,450 thousand. Interest of loans is EUROIBOR + margin. All these loans are the subordinated debts to credit granted by banks to the Pfleiderer Grajewo S.A. As at December 31st 2011, the debt outstanding under the loans advanced to Pfleiderer MDF OOO by Pfleiderer AG amounted to EUR 154.6m.

Pfleiderer MDF Sp. z o.o. was using loans advanced by related entities of Pfleiderer Grajewo S.A. and Pfleiderer Service GmbH, under which as at December 31st 2011 it had drawn PLN 0.4m and PLN 8.4m, respectively. The loans were advanced to finance the company's business activity. The agreements provide for the repayment of the whole debt on July 16th 2016.

On February 8th 2011, the share capital of Pfleiderer MDF Sp. z o.o., a subsidiary, was increased by PLN 35,278 thousand. The new shares were acquired by the existing shareholders of Pfleiderer Grajewo S.A. (PLN 17,639 thousand-worth of shares) and Pfleiderer Service GmbH (PLN 17,639 thousand-worth of shares). As agreed upon on February 25th 2011, the share capital increase was effected through debt set-off by converting debt under loans advanced by Pfleiderer Grajewo S.A. and Pfleiderer Service GmbH into equity.

As at December 31st 2011, Silekol Sp. z o.o. had an outstanding loan of PLN 16.3m advanced by Pfleiderer Grajewo S.A. Silekol Sp. z o.o will repay the debt on January 5th 2013.

As at December 31st 2011, the Group's net debt under bank borrowings and other debt instruments was PLN 1,019m.

For detailed information on all liabilities under bank borrowings and other debt instruments as well as contingent liabilities and security instruments as at December 31st 2011, see Note 21 and Note 28, respectively, of the consolidated financial statements of the Pfleiderer Grajewo Group.

14. Financial instruments

Overview of the financial instruments

a) Forward transactions

Forward transactions included purchase of foreign currency at a predetermined rate. In 2011, the Company used forward transactions to hedge its currency risk related to business transactions (product exports).

The Group had no unsettled forward contracts as at December 31st 2011.

According to IAS 39, if a cash flow hedge is effective, the effective portion of the gain or loss on the hedging instruments should be recognised in equity under other comprehensive income, whereas the ineffective portion of the gain or loss on the hedging instruments should be recognised as current period's profit or loss.

The other Group companies did not enter into any transactions on derivative instruments.

b) Guarantees, sureties and security provided by the Group

As at December 31st 2011, the Group had the following contingent liabilities and security:

1. Mortgage over real estate and registered pledge over plant and equipment

A mortgage on real estate and a registered pledge over plant and equipment serve as security for an investment loan granted to Pfleiderer MDF Sp. z o.o. by PKO Bank Polski S.A. on January 15th 2007. It is a special purpose facility contracted to finance the construction of the new MDF board production plant in Grajewo. A mortgage on real estate secures a liability up to PLN 356,860 thousand. The registered pledge over plant and equipment secures liabilities up to PLN 450,000 thousand and has been created over a floating group of assets owned by Pfleiderer MDF Sp. z o.o. (floating charge). The pledge is reviewed on a quarterly basis to take account of any changes in the company's movable property (plant and equipment, vehicles). As at December 31st 2011, the Group's debt under the facility totalled PLN 227.0m.

2. Mortgage on real estate located at ul. Wiórowa, Grajewo and registered pledge over assets

A mortgage of up to PLN 80,000 thousand created on the real estate located at ul. Wiórowa, Grajewo, on which the MDF plant is situated, serves as security for a multi-purpose credit facility for the total amount of PLN 57,000 thousand, granted to Pfleiderer MDF Sp. z o.o., a member of the Pfleiderer Group, by PKO Bank Polski S.A. on August 29th 2007.

The pledge was created under an agreement on registered pledge over assets, dated July 30th 2010, concluded between Pfleiderer MDF Sp. z o.o. and Powszechna Kasa Oszczędności Bank Polski S.A. of Warsaw. The pledge, with the maximum security amount of PLN 83,163,000, was created for the benefit of Powszechna Kasa Oszczędności Bank Polski S.A. to secure claims under a PLN 57,000,000 multi-purpose credit facility granted to Pfleiderer MDF Sp. z o.o. by Powszechna Kasa Oszczędności Bank Polski S.A. on the basis of an agreement of August 29th 2007. The pledge was created in connection with the extension of the term of the working capital loan by three years, until June 30th 2013. The same assets are also encumbered with a pledge created earlier for the benefit of Powszechna Kasa Oszczędności Bank Polski S.A. in connection with an investment loan agreement of January 15th 2007.

As at December 31st 2011, the Group's debt under the facility totalled PLN 35.7m.

3. Security for claims under the credit agreement concluded on March 16th 2010 with Bank PEKAO S.A., Bank Zachodni WBK S.A., BRE Bank S.A., Fortis Bank Polska S.A. and Bank Gospodarki Żywnościowej S.A.

On March 25th 2010, Pfleiderer Grajewo S.A. ("the Parent") and its subsidiaries Pfleiderer Prospan S.A. and Silekol Sp. z o.o. ("the Subsidiaries") executed security agreements and documents granting security with respect to the debt arising under the credit facility agreement concluded on March 16th 2010 with Bank PEKAO S.A., Bank Zachodni WBK S.A., BRE Bank S.A., Fortis Bank Polska S.A. and Bank Gospodarki Żywnościowej S.A. ("the Banks"). They provide in particular for:

- creation of contractual blanket security mortgages over the Parent's and the Subsidiaries' real estate on which production facilities are located, up to the maximum amount of PLN 1,400m;
- creation of registered pledges over assets owned by the Parent and the Subsidiaries (pledge over a business), up to the maximum amount of PLN 1,050m,
- creation of registered and financial pledges over amounts credited to bank accounts;
- assignment of rights under insurance agreements by way of security;
- assignment by way of security of the Company's interest in co-ownership of plant and equipment intended to be used for the purposes of the MDF project in Russia;
- creation of financial and registered pledges over the Parent's shares in the Subsidiaries; the pledge covers 100% of the shares in Pfleiderer Prospan S.A. and 50% of the shares in Silekol Sp. z o.o.

Furthermore, on March 25th 2010, the Company, the Subsidiaries and the Banks executed an agreement with the European Bank for Reconstruction and Development (the "EBRD"), which provides financing to Pfleiderer OOO of Russia under the credit facility agreement of December 27th 2005. Under the agreement, the parties agreed upon the scope of the security to be created over the Company's and the Subsidiaries' assets. Pfleiderer Prospan S.A. and Silekol Sp. z o.o. joined the following agreements executed between Pfleiderer Grajewo S.A. and the EBRD:

- guarantee agreement securing the EBRD's claims under the credit facility extended to Pfleiderer OOO; and
- put/call option agreement concerning Pfleiderer OOO shares.

In order to secure the EBRD's claims under the guarantee agreement and the put/call option agreement, on March 25th 2010 the Company and the Subsidiaries executed agreements and documents whereby:

- establishment of contractual joint ceiling mortgages over the Company's and the Subsidiaries' real estate, on which production facilities are located, up to the amount of EUR 70.5m;
- creation of registered pledges over assets owned by the Company and the Subsidiaries (pledge over a business), up to the amount of EUR 79.5m.

In 2010 the following agreements were also concluded to secure the repayment of liabilities to the EBRD by Pfleiderer OOO under the credit agreement of December 27th 2005:

- agreement creating a pledge over movable property of Pfleiderer OOO;
- mortgage on real estate owned by Pfleiderer OOO, on which the plant is situated;
- agreement creating a pledge over the shares held by the Company in Pfleiderer OOO. The pledge was established over one share in Pfleiderer OOO's share capital, representing 84.1913% of the company's share capital and conferring the right to 84.1913% of the total vote at Pfleiderer OOO's general meeting.

As at December 31st 2011, the Group had not issued any sureties.

c) Shareholdings

For details concerning holdings of shares see Note 12 – "Investments in related entities" to the annual consolidated financial statements.

On December 22nd 2011, Pfleiderer Grajewo S.A. and Pfleiderer Service GmbH acquired shares in Blitz 11-446 GmbH of Germany. Each of the companies holds 50% of shares in Blitz 11-446 GmbH. The purchase price paid by Pfleiderer Grajewo S.A. was EUR 14.5 thousand (PLN 65.2 thousand).

On December 22th 2011, a newly established SPV, Blitz 11-446 GmbH ("Pfleiderer SPV"), purchased components of the production line manufactured by Dieffenbacher and designed to be assembled at the MDF/HDF board production plant in Russia. The value of those components is EUR 53,842,497.01 (PLN 239,265,288.20). The components were purchased in a non-cash transaction and the Pfleiderer Group incurred no expenses related to the purchase. As a result of the transaction, two companies of the Pfleiderer Group, Pfleiderer SPV and Pfleiderer MDF OOO, hold the ownership rights to the entire production line manufactured by Dieffenbacher and designed to be assembled at the MDF/HDF board production plant in Russia.

In order to execute the transaction, on December 22nd 2011 the parent and Pfleiderer AG executed an annex to the agreement of July 2nd 2009 concerning financial collateral under the contract for delivery of the MDF/HDF production line ("the Delivery Contract") concluded between Dieffenbacher and Pfleiderer MDF OOO.

Under the annex, the parent transferred onto Pfleiderer AG a 50% interest in joint ownership of the machinery supplied under the Delivery Contract ("the Parent's Interest in the Machinery"). The Company's Interest in the Machinery was subsequently transferred onto Dieffenbacher and eventually onto Pfleiderer SPV. The value of the Parent's Interest in the Machinery is EUR 17,013,900.00 (PLN 75,606,368.82 PLN).

Moreover, prior to the execution of those transactions the Parent's Interest in the Machinery was released from security created for the benefit of the banks providing financing to the Parent, i.e. Bank PEKAO S.A., Bank Zachodni WBK S.A., BRE Bank S.A., BNP Paribas Bank Polska S.A. and Bank Gospodarki Żywnościowej S.A. The release was made in exchange for an assignment by way of security, performed on December 22nd 2011, of the ownership right to the machinery purchased by Pfleiderer SPV. The assignment by way of security secures the repayment of 50% the bank borrowing granted to the parent and 50% of bank borrowings granted to Pfleiderer AG.

Shares in Blitz 11-446 GmbH were accounted for with the equity method in the consolidated financial statements.

15. Financial risks related to the Company's operations

a) Objectives and methods of financial risk management adopted by the Pfleiderer Grajewo Group

The Group manages all types of financial risk described below, which may have a significant effect on its operations in the future. In its risk management process, the Group focuses on the following risk types:

- credit risk,
- currency risk,
- liquidity risk,
- interest rate risk.

The objective behind credit risk management is to reduce the Group's losses which could follow from customers' insolvency. This risk is mitigated with the use of receivables insurance and factoring services.

The objective of currency risk management is to minimise losses arising out of unfavourable changes in foreign exchange rates. The Group monitors its currency position from the point of view of cash flows. To manage its currency risk, it first relies on natural hedging and where necessary uses forward contracts. The time horizon adopted for position monitoring and hedging transactions is up to 12 months.

The objective of financial liquidity management is to protect the Group against insolvency. This objective is pursued through regular projection of debt levels in a five-year horizon, and arrangement of appropriate financing.

The Group is exposed to credit risk, interest rate risk and currency risk in the ordinary course of business. Financial derivatives are used to hedge the risk related to exchange rate fluctuations and changes in interest rates.

b) Credit risk

Transactions which expose the Pfleiderer Grajewo Group companies to credit risk concern trade receivables. The credit risk related to trade receivables is limited, as the customer base is very wide and the risk is highly diversified. Therefore, the credit risk concentration is insignificant. Moreover, the Group operates a strict receivables management policy, whereby the risk of customer insolvency is mitigated through the use of trade credit insurance and recourse factoring. In 2011, over 90% of the Group's trade receivables were secured in this way. In the event of insolvency of customers who have insurance coverage, the compensation is paid by the insurer. Each customer has a trade credit limit (usually covered by an insurance limit).

c) Interest rate risk

The Group holds funds in bank accounts and has liabilities under bank borrowings. The interest rate risk is related to interest payments under borrowings with floating interest rates. The Group does not hedge the interest rate risk.

d) Currency risk

As at the date of the financial statements, exposure to currency risk under foreign-currency borrowings existed only at Pfleiderer OOO of Russia in connection with a euro-denominated bank borrowing, and at Pfleiderer MDF OOO and the Parent in connection with euro-denominated loans advanced by related entities. The other Group companies are not exposed to currency risk under foreign-currency loans.

Foreign currency transactions relate both to purchases of raw materials and sale of goods. Therefore, in the event of any exchange rate fluctuations the resulting foreign exchange gains and losses are offset to some extent. Furthermore, the Group makes investment expenditure in foreign currencies, and therefore it monitors its foreign currency positions on an ongoing basis and hedges open positions – first, through natural hedging (that is through carefully selecting currencies for contracts), and second, through forward transactions. The Group monitors its currency risk exposure in terms of cash flows rather than profit or loss.

In 2011, the Pfleiderer Grajewo Group entered into a number of EUR/PLN forward contracts to hedge against currency risk related to planned trade transactions. The Group had no unsettled forward contracts as at December 31st 2011.

Furthermore, Pfleiderer Grajewo S.A. is exposed to currency risk resulting from RUB-denominated loans extended to Pfleiderer OOO and Pfleiderer MDF OOO.

e) Price risk associated with financial instruments

The Group is not exposed to any material price risk associated with financial instruments.

f) Risk of material cash-flow disruptions

The Group companies are protected against any material cash-flow disruptions thanks to significant credit facilities available at any time. Material cash-flow disruptions are also unlikely due to customer diversification. All extraordinary expenditure is always planned well ahead and accounted for in the liquidity management process.

g) Liquidity risk

The Group monitors its liquidity position on an on-going basis, both with respect to short-term liquidity (a few days forward) and long-term liquidity (a few years forward).

	Current ratio	Quick ratio	Average collection period	Average payment period	Inventory turnover ratio
	$\frac{\text{Current assets}}{\text{Current liabilities}}$	$\frac{\text{Current assets} + \text{inventories}}{\text{Current liabilities}}$	$\frac{\text{Average trade and other receivables}}{\text{Net sales revenue: 360}}$	$\frac{\text{Average trade and other liabilities}}{\text{Net sales revenue: 360}}$	$\frac{\text{Average inventory}}{\text{Net sales revenue: 360}}$
31.12.2011	0,98	0,41	33 days	53 days	44 days
31.12.2010	1,13	0,57	39 days	60 days	45 days

As at December 31st 2011, the Pfleiderer Grajewo Group had debt under bank borrowings in the amount of PLN 830.6m and under other borrowings in the amount of PLN 188m; it also had an unused credit facility of PLN 161m. Most of these liabilities were long-term credit limits. In addition, the Group holds cash in the amount of PLN 20m.

The availability of credit facilities depends on meeting certain ratios set by banks, based on consolidated financial data. The ratios include primarily:

- financial debt to EBITDA ratio
- total equity to total assets,
- current assets to current liabilities,
- debt-service coverage ratio

Pursuant to the PLN 700,000 thousand credit facility agreement executed on March 16th 2010 with a bank syndicate (“the Credit Facility Agreement”), a breach by Pfleiderer AG, Pfleiderer Grajewo S.A.'s indirect parent, of its credit facility agreements would constitute a breach under the Credit Facility Agreement.

In connection with a series of events relating to legal and economic situation PAG, in 2010, there was a breach of Pfleiderer AG of its loan agreements. Pfleiderer Grajewo Group obtained waivers from its financing banks, whereby the banks waived their rights to terminate the credit facility agreement with the Group due to the breach of credit agreements by Pfleiderer AG.

On May 12th 2011, Pfleiderer AG reported that it had reached an agreement with its financing banks regarding key elements of the financial restructuring and debt refinancing plan. The terms of the agreement required an approval of the agreement by Pfleiderer AG's share- and stakeholders. Some non-controlling shareholders and holders of hybrid bonds have appealed against the resolutions granting the approvals to competent courts. As a result of verdict of Higher Regional Court, Frankfurt/Main from March 27th 2012 the debt relief and recapitalization of the company that had been planned within the scope of the restructuring plan is now no longer possible by this means. On 28 March 2012 Pfleiderer AG in Neumarkt filed an application for insolvency. According to the information provided by Pfleiderer AG, the Management Board of Pfleiderer AG filed a request to open insolvency proceedings and has requested to act as debtor in possession. The Management Board, supervised by a judicial administrator, will continue managing and restructuring the company.

According to the best knowledge of the Board of Pfleiderer Grajewo agreements concluded between the PAG and its banks were not uttered in connection with PAG application for insolvency. Moreover, according to the best knowledge of the Board of Pfleiderer Grajewo PAG application for insolvency is not a breach of Pfleiderer Grajewo credit agreement.

In the opinion of the Pfleiderer Grajewo Management Board, the potential declaration of Pfleiderer AG's bankruptcy will not adversely affect the Pfleiderer Grajewo Group's day-to-day operations. The Group companies are fully independent in terms of operations, have their own procurement systems and sales channels. The Pfleiderer Grajewo Group holds separate loan agreements securing funding of its day-to-day operations.

In case that current situation of the ultimate parent Pfleiderer AG has resulted in a violation of Pfleiderer Grajewo credit agreement in the opinion of the Pfleiderer Grajewo Management Board, the likelihood of failing to obtain relevant waivers from its creditors is low.

The Group monitors the ratios on an ongoing basis and, based on its short-term financial plans, analyses the risk of failure to meet the ratios.

16. Court proceedings

There are no court, arbitration or administrative proceedings pending with respect to any liabilities or claims of the Group companies, whose value would represent 10% or more of the Parent's equity.

17. Corporate governance

Appointment and removal of the management staff

Pursuant to the Company's Articles of Association, the Management Board members are appointed by the Company's Supervisory Board. The Articles of Association and resolutions of the Company's General Meeting do not provide for any special powers for the Management Board members with respect to making decisions on the issue or repurchase of shares.

Description of operation governing bodies

The Management Board comprises at least 2 members. The term of office lasts five years, members of the Management Board are appointed for the common term of office. The Supervisory board appoints the President of the Management Board and on the President motion, other Board Members. In the scope of Company management, the Management Board exercises all its powers, except for the rights reserved by the law or by the Company Statute to the other Company's governing bodies. The Management Board's procedure of conducting and all the cases that can be mandated to its members are precisely described in the Management Board regulations, adopted by the Management Board and approved by the Supervisory Board.

The Supervisory Board is appointed by Shareholders. The Supervisory Board comprises 5, 7 or 9 members. The term of office lasts five years, members of the Supervisory Board are appointed for the common term of office. The Supervisory board supervises the Company's activities. The rights and duties of Supervisory Board are described in the Company Statute and law, including Code of Commercial Companies. The Supervisory Board adopts its regulations, describing detail procedure of supervisory Board conducting.

Amendments to the Articles of Association of the Company

The Articles of Association of the Parent are amended in line with the procedure specified in the Commercial Companies Code. No special provisions with respect to this practice are set forth in the Articles of Association of the Parent.

Proceedings of the General Meeting of the Company

The General Meetings of the Parent has the powers specified in the Commercial Companies Code and the Articles of Association. The proceedings of the General Meeting are governed by the Articles of Association and the Rules of Procedure of the General Meeting, available on the Company's web site.

Company shares

The Company did not issue any shares granting special control powers. In addition, there are no limitations on the exercise of voting rights attached to the shares issued by the Company. Also, there exist no rights related to the securities issued by the Company which would be separate from the ownership of the securities.

Neither the Company's Articles of Association nor any other of its internal regulations provide for any limitations on transfer of the Company shares. Therefore, transfer of ownership of the Company shares is subject only to the limitations imposed by the applicable laws and the stock-exchange regulations.

Financial statements of the Parent and the Group

The Parent's financial statements are prepared by a separate organisational unit. All financial statements are reviewed, verified and approved at several levels at the Company, eliminating the risk related to financial reporting.

The Pfleiderer Grajewo Management Board declares that the Company complies with the corporate governance rules contained in "Best Practices of WSE-Listed Companies" as appended to the WSE Supervisory Board resolution No. 20/1287/2011, dated October 19th 2011, save for the following rule:

Rule III.6

At least two members of the Supervisory Board should meet the criteria of being independent from the company and entities with significant connections with the company. The independence criteria should be applied under Annex II to the Commission Recommendation of February 15th 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board. Irrespective of the provisions of point (b) of the Annex, a person who is an employee of the company, its subsidiary or an associated company cannot be deemed to meet the independence criteria described in the Annex. In addition, a relationship with a shareholder precluding the independence of a member of the Supervisory Board as understood in this rule is an actual and significant relationship with any shareholder who has the right to exercise at least 5% of all votes at the General Meeting.

The Company does not comply with the rule. Instead, it ensures that an independent member serves on the Supervisory Board as specified below:

In accordance with the Company's Articles of Association, at least one member of the Supervisory Board comprising five persons, two members of the Supervisory Board comprising seven persons and three members of the Supervisory Board comprising nine persons are independent members who satisfy the following criteria:

- they are not members of the governing bodies of Pfleiderer Grajewo S.A.'s parent or of such parent's subsidiaries,
- they are not employed by Pfleiderer Grajewo S.A.'s parent or by such parent's subsidiaries,
- they are not relatives (a spouse, direct descendant or direct ascendant) of a member of the governing bodies of Pfleiderer Grajewo S.A. or Pfleiderer Grajewo S.A.'s parent.

In line with the Company's Articles of Association, as at the date of the corporate governance statement, the Supervisory Board is composed of five persons, including one member meeting the independence criteria specified above.

18. The Auditor

The separate and consolidated financial statements are audited and reviewed on the basis of the decision made by the General Meeting on June 23rd 2010 on selection of an entity qualified to audit financial statements. Pursuant to the resolution, the following auditor was appointed:

KPMG Audyt Spółka z o.o. spółka komandytowa
ul. Chłodna 51
00-867 Warszawa, Poland

The financial statements were audited pursuant to the agreement executed between KPMG and the Company. The agreement of July 11th 2011 provided for a review of interim separate and consolidated financial statements of Grajewo S.A. and the Grajewo Group for a fee of PLN 154,400. The second agreement of October 3rd 2011 covered a review of the Group's interim report for the period January 1st–September 30th 2011. The fee payable to KPMG was PLN 52,800. The most recent agreement with KPMG for the review of accounting books, dated January 5th 2012, provided for the audit of the annual separate financial statements of Pfleiderer Grajewo S.A., the audit of the annual consolidated financial statements of the Pfleiderer Grajewo Group for the financial year ended December 31st 2010, prepared in accordance with the IFRS, as well as an audit of the Group's annual report. The fee due to KPMG under the agreement is PLN 236,000. The agreement also covered an audit of relevant procedures.

The fee for the audits specified above amounted to PLN 443,200 (PLN 390,400 thousand for the previous financial year).

19. Audit Committee

All duties of an audit committee were assigned to the Pfleiderer Grajewo Supervisory Board.

20. Non-recurring events affecting the Pfleiderer Grajewo Group's financial performance

No non-recurring events which might affect the Pfleiderer Grajewo Group's financial performance occurred in 2011.

21. Changes in the composition of the Parent's Management Board

With effect from February 8th 2011, Johann Bitzi, Vice-President of the Management Board, was removed from office as member of the Pfleiderer Grajewo Management Board.

22. Changes in the composition of the Parent's Supervisory Board

On October 17th, Mr Heiko Graeve resigned from the Pfleiderer Grajewo Supervisory Board.

At the Extraordinary General Meeting held on November 24th 2011 Mr Paweł Wyrzykowski was removed from the post of Chairman of the Supervisory Board.

Mr Hans-Joachim Ziems and Mr Hans-Kurt von Werder were appointed as Members of the Supervisory Board.

At a meeting of the Pfleiderer Grajewo Supervisory Board held on December 21st 2011, Members of the Supervisory Board appointed Mr Michael Wolff to the post of Supervisory Board Chairman.

On March 7th 2012, Mr Hans-Joachim Ziems tendered his resignation from the position of a member of Pfleiderer Grajewo S.A.'s Supervisory Board, with effect as of April 10th 2012.

At the Extraordinary General Meeting held on April 10th 2012 Mr Jochen Schapka was appointed as Member of the Supervisory Board.

23. Other activities of the Company

Events subsequent to the end of the reporting period

On January 31st 2012, Pfleiderer Grajewo S.A. received a notification dated January 27th 2012 from Wojciech Gątkiewicz, President of the Management Board. In the notification, Mr Gątkiewicz, acting pursuant to Art. 160 of the Act on Trading in Financial Instruments of July 29th 2005, notified the Company that in 2011 he acquired Company shares with a total value of up to EUR 5,000. 2,400 ordinary bearer shares were acquired at prices ranging from PLN 8.10 to PLN 8.78 per share in ordinary session transactions concluded on the Warsaw Stock Exchange on August 29th and September 6th 2011.

On March 7th 2012, Mr Hans-Joachim Ziems tendered his resignation from the position of a member of Pfleiderer Grajewo S.A.'s Supervisory Board, with effect as of April 10th 2012.

On March 15th 2012, an annex was signed to the Credit Facility Agreement of March 16th 2010 executed by Pfleiderer Grajewo S.A. as the lender, Pfleiderer Prospan S.A. and Silekol Sp. z o.o. as other obligors under the agreement and a syndicate of financing banks comprising: Bank Polska Kasa Opieki S.A., Bank Zachodni WBK S.A., BRE Bank S.A., Bank Gospodarki Żywnościowej S.A. and BNP Paribas Bank Polska S.A. (formerly Fortis Bank Polska S.A.). Under the annex, the repayment date for Tranche B, previously scheduled for March 16th 2012, was extended. Consequently, the full amount of Tranche B (PLN 170m) falls due on March 16th 2013.

On 23 March 2012 Extraordinary General Meeting recalled Mr. Grzegorz Woelke from the position of Member of Supervisory Board of Jura Polska Sp. z o.o.

On 28 March 2012 Pfleiderer AG in Neumarkt filed an application for insolvency.

According to the information provided by Pfleiderer AG, the Management Board of Pfleiderer AG filed a request to open insolvency proceedings and has requested to act as debtor in possession. The Management Board, supervised by a judicial administrator, will continue managing and restructuring the company.

Pfleiderer AG is the parent of the Pfleiderer Group. It is a holding company, which does not conduct any operating activities. Pfleiderer AG employs 10 staff. The bankruptcy petition was filed exclusively with respect to Pfleiderer AG and does not involve the Pfleiderer AG Group's subsidiaries which continue their day-to-day operations unaffected.

The Pfleiderer Grajewo Group companies have not issued any sureties for Pfleiderer AG's liabilities.

The Company's direct shareholder is Pfleiderer Service GmbH in Neumarkt, however, the bankruptcy petition does not cover Pfleiderer Service GmbH.

Pfleiderer AG is not a direct shareholder in any of the Pfleiderer Grajewo Group companies.

In the opinion of the Pfleiderer Grajewo Management Board, the potential declaration of Pfleiderer AG's bankruptcy will not adversely affect the Pfleiderer Grajewo Group's day-to-day operations. The Group companies are fully independent in terms of operations, have their own procurement systems and sales channels. The Pfleiderer Grajewo Group holds separate loan agreements securing funding of its day-to-day operations.

on April 2nd 2012 Company and its subsidiary undertaking Pfleiderer Prospan S.A. received a notification of initiation of anti-trust proceedings by the President of the Office of Competition and Consumer Protection ("UOKiK") dated March 30th 2012 on the conclusion by Kronospan Szczecinek Sp.

z o.o., Kronospan Mielec Sp. z o.o., Kronopol Sp. z o.o., Pfleiderer Grajewo S.A. and Pfleiderer Prospan S.A. an agreement restricting competition on the domestic chipboard and fibreboard market.

The information obtained indicates that the case files are just currently created from the material gathered during the investigation. Pfleiderer Grajewo SA and a subsidiary of Pfleiderer S.A. are currently waiting for an opportunity to review case files. Units were given 14 days' notice for explanations. At this stage, the Board of Pfleiderer Grajewo and Pfleiderer basis of the available information is not able to quantify the risk.

At the Extraordinary General Meeting held on April 10th 2012 Mr Jochen Schapka was appointed as Member of the Supervisory Board.

Extraordinary General Meeting held on April 10th 2012 adopted resolution on a consent for extension of a duration of the debt bearing securities issue programme in a form of bonds by June 30th, 2017.

24. 2012 performance forecast

Given the current economic climate, the Group will refrain from publishing its forecast for 2012 until the market volatility subsides and the Polish market of furniture manufacturers becomes more stable.

**Pfleiderer Grajewo Management Board
and Pfleiderer Prospan S.A.**

Grajewo, April 16th 2012

Wojciech Gątkiewicz
President of the Management Board

Rafał Karcz
Member of the Management Board, Chief
Financial Officer

Dariusz Tomaszewski
Member of the Management Board, Sales Director

Radosław Wierzbicki
Chief Operating Officer