# Panariagroup Industrie Ceramiche S.p.A.

# QUARTERLY REPORT
# AS OF MARCH 31st, 2008


Panariagroup Industrie Ceramiche S.p.A.
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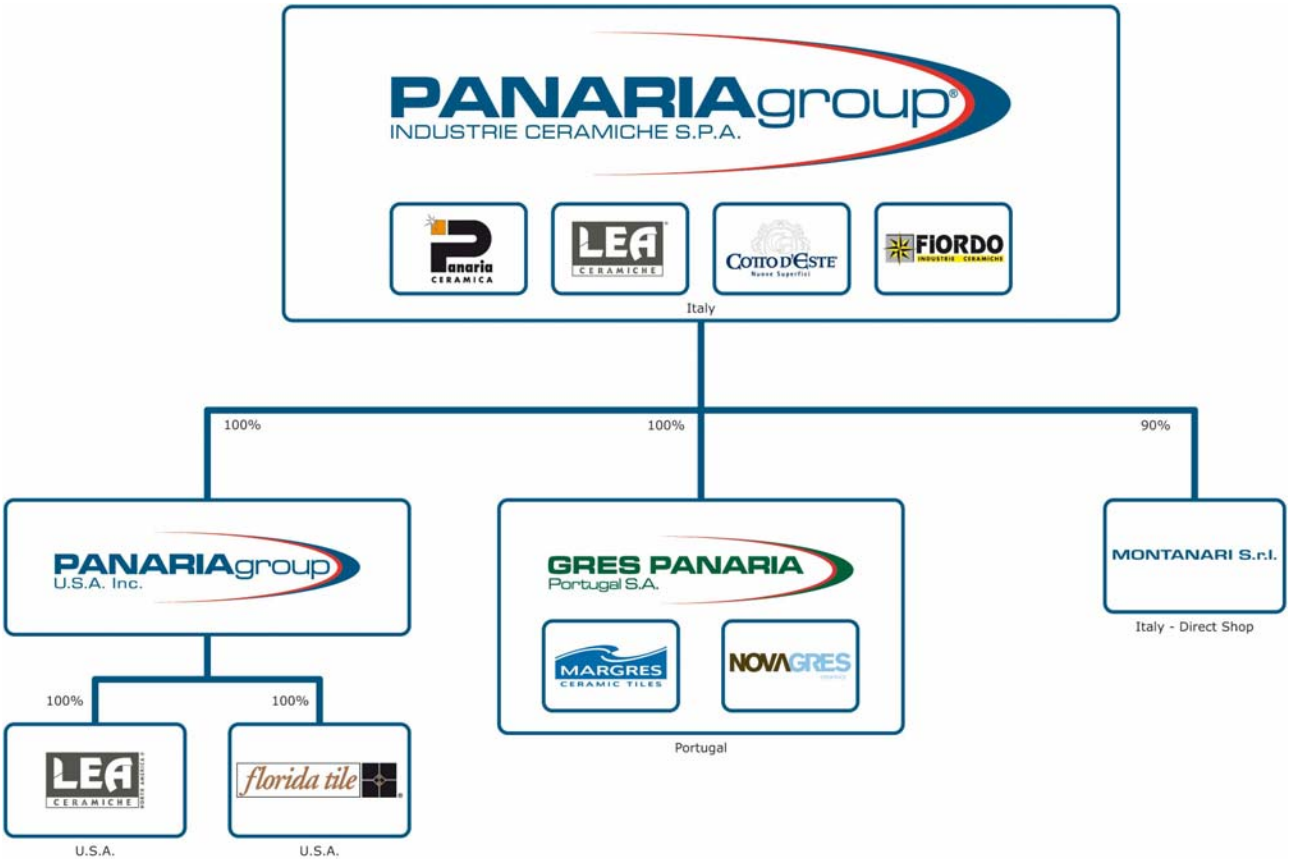
## INDEX

## 1. GROUP STRUCTURE

As of March 31st 2008, the Group was structured as follows:



The Parent Company is **Panariagroup Industrie Ceramiche S.p.A.**, based in Finale Emilia, Modena, Italy, with a fully paid-in share capital of Euro 22,677,645.50.
Panariagroup produces and distributes floor and wall ceramic tiles under 4 distinct brand names: Panaria, Lea, Cotto d'Este and Fiordo. All brands are positioned on the high and deluxe market segment, focused on porcelain grès tiles and sell their product lines both on the domestic as well as on foreign markets.

**Gres Panaria Portugal S.A**., based in Chousa Nova, Ilhavo, Portugal, with a paid-in share capital of Euro 16,500,000.00, is fully owned by Panariagroup Industrie Ceramiche. Gres Panaria Portugal is specialized in white body wall tiles and in porcelain grès products and operates with 2 different brands, Margres and Novagres, both focused on the main European markets.

**Panariagroup USA Inc.**, based in Delaware, USA, with a paid-in capital of USD 54,500,000.00, is fully owned by Panariagroup Industrie Ceramiche S.p.A. The company is the holding for the US market and controls the participations in Florida Tile Inc. and Lea North America LLC.
In the first quarter 2008, Panariagroup Industrie Ceramiche SpA, has performed a capital increase of the subsidiary Panariagroup USA Inc. from USD 45 million to USD 54.5 million.

**Florida Tile Inc.** based in Delaware, USA, with a paid-in capital of USD 15,000,000.00 that is fully owned by Panariagroup USA Inc., manufactures and distributes ceramic tile products in the US market through a directly managed distribution network mainly based on the East Coast.

**Lea North America LLC**, based in Delaware, USA, with a paid-in share capital of USD 20,000, is wholly owned by Panariagroup USA Inc.
The company operates in the marketing and distribution of the Lea brand products in North America.

**Montanari srl,** based in Bologna, Italy, with a paid-in share capital of Euro 48.000, is owned 90% by Panariagroup Industrie Ceramiche. The company is a retail shop of ceramic material.

## 2. CORPORATE BOARDS

### 2.1 Board of Directors

| Name and surname | Office | Place and date of birth |
|---|---|---|
| Giuliano Mussini | Chairman of the Board of Directors | Modena, 10/9/1930 |
| Giovanna Mussini | Deputy chairman of the Board of Directors | Sassuolo (MO), 12/4/1959 |
| Andrea Mussini | Managing Director | Sassuolo (MO), 15/5/1958 |
| Emilio Mussini | Managing Director | Sassuolo (MO), 20/4/1961 |
| Giuseppe Mussini | Managing Director | Sassuolo (MO), 23/11/1962 |
| Paolo Mussini | Managing Director | Sassuolo (MO), 11/2/1958 |
| Giuliano Pini | Managing Director | Modena, 21/5/1952 |
| Marco Mussini | Director | Sassuolo (MO), 21/7/1971 |
| Giovanni Burani(*) | Director | Parma, 20/10/1964 |
| Alessandro Iori(*) | Director | Reggio Emilia, 15/6/1943 |
| Paolo Onofri(*) | Director | Bologna, 11/11/1946 |

(*) Indipendent non-executive director

### 2.2 Board of Statutory Auditors

| Name and surname | Office | Place and date of birth |
|---|---|---|
| Giovanni Ascari | Chairman of the Board of Auditors | Modena, 13/10/1935 |
| Vittorio Pincelli | Standing auditor | Frassinoro (MO), 3/8/1943 |
| Premoli Trovati Stefano | Standing auditor | Milano, 01/12/1971 |
| Corrado Cavallini | Alternate auditor | Sassuolo (MO), 4/1/1971 |
| Massimiliano Stradi | Alternate auditor | Sassuolo (MO), 16/3/1973 |

### 2.3 Independent Auditors

Deloitte & Touche S.p.A.

PANARIAgroup
INDUSTRIE CERAMICHE S.P.A.

# 3. CONSOLIDATED P&L AND BALANCE SHEET

## 3.1 Profit and loss account – First quarter 2007 and 2006

**(in € / 000)**

| CUMULATED | 31/3/2008 | % | 31/3/2007 | % | var. |
|---|---|---|---|---|---|
| **Revenues from sales and services** | **85,769** | **97,97%** | **92,646** | **98,40%** | **(6,877)** |
| Changes in inventories of finished products | 0,861 | 0,98% | 0,484 | 0,51% | 0,377 |
| Other revenues | 0,913 | 1,04% | 1,020 | 1,08% | (0,107) |
| **Value of Production** | **87,543** | **100,00%** | **94,150** | **100,00%** | **(6,607)** |
| Raw, ancillary and consumable materials | (22,320) | -25,50% | (25,366) | -26,94% | 3,046 |
| Services, leases and rentals | (34,045) | -38,89% | (36,236) | -38,49% | 2,191 |
| Personnel costs | (18,281) | -20,88% | (18,225) | -19,36% | (0,056) |
| Changes in inventories of raw materials | 0,103 | 0,12% | (0,259) | -0,28% | 0,362 |
| Other operating expenses | (0,868) | -0,99% | (1,053) | -1,12% | 0,185 |
| **Cost of production** | **(75,411)** | **-86,14%** | **(81,139)** | **-86,18%** | **5,728** |
| **Gross operating profit** | **12,132** | **13,86%** | **13,011** | **13,82%** | **(0,879)** |
| D&A expenses | (4,368) | -4,99% | (3,899) | -4,14% | (0,469) |
| Provisions and impairments | (0,488) | -0,56% | (0,395) | -0,42% | (0,093) |
| **Net operating profit** | **7,276** | **8,31%** | **8,717** | **9,26%** | **(1,441)** |
| Financial income and expense | (2,329) | -2,66% | (1,127) | -1,20% | (1,202) |
| **Pre-tax profit** | **4,947** | **5,65%** | **7,590** | **8,06%** | **(2,643)** |
| Income taxes | (1,902) | -2,17% | (3,442) | -3,66% | 1,540 |
| **Net profit for the period** | **3,045** | **3,48%** | **4,148** | **4,41%** | **(1,103)** |
| **Cash Flow** | **7,901** | **9,03%** | **8,442** | **8,97%** | **(0,541)** |

## 3.2 Reclassified balance sheet

**(in € / 000)**

| | 31/3/2008 | 31/12/2007 |
|---|---|---|
| Inventories | 145,171 | 144,310 |
| Accounts Receivable | 107,924 | 100,510 |
| Other current assets | 8,980 | 11,497 |
| **CURRENT ASSETS** | **262,075** | **256,317** |
| Accounts Payables | (70,707) | (75,063) |
| Other current liabilities | (35,371) | (34,632) |
| **CURRENT LIABILITIES** | **(106,078)** | **(109,695)** |
| **NET WORKING CAPITAL** | **155,997** | **146,622** |
| Goodwill | 13,002 | 13,002 |
| Intangible assets | 3,031 | 3,252 |
| Tangible assets | 97,391 | 96,426 |
| Equity Investments and other financial fixed assets | 0,001 | 0,001 |
| **FIXED ASSETS** | **113,425** | **112,682** |
| Receivables due after the following year | 0,281 | 0,299 |
| Provisions for termination benefits | (6,964) | (7,172) |
| Provisions for risks and charge and deferred taxes | (12,703) | (12,777) |
| Other payables due after the year | (3,919) | (4,743) |
| **ASSETS AND LIABILITIES DUE AFTER THE YEAR** | **(23,305)** | **(24,393)** |
| **NET CAPITAL EMPLOYED** | **246,117** | **234,911** |

| | | |
|---|---|---|
| Short term financial assets | (7,725) | (6,263) |
| Short term financial debt | 68,929 | 56,003 |
| **NET SHORT TERM FINANCIAL DEBT** | **61,204** | **49,740** |
| Mid-long term financial debt | 30,681 | 31,130 |
| **NET FINANCIAL POSITION** | **91,885** | **80,870** |
| Group Shareholders' Equity | 154,232 | 154,041 |
| **SHAREHOLDERS' EQUITY** | **154,232** | **154,041** |
| **TOTAL SOURCES OF FUNDS** | **246,117** | **234,911** |

### 3.3 Net financial position

**(in € / 000)**

| | 31/03/2008 | 31/12/2007 |
|---|---|---|
| Securities | - | - |
| Cash and cash equivalents | (7,725) | (6,263) |
| **Short term financial assets** | **(7,725)** | **(6,263)** |
| Due to banks | 68,142 | 55,216 |
| Financial payables to holding companies | - | - |
| Due to other lenders | 0,787 | 0,787 |
| **Short term financial debt** | **68,929** | **56,003** |
| Due to banks | 29,654 | 30,102 |
| Due to other lenders | 1,027 | 1,027 |
| Due to bondholders | - | - |
| **Mid-long term financial debt** | **30,681** | **31,129** |
| **Net Financial Position** | **91,885** | **80,869** |

# 4 NOTES TO THE ACCOUNTS

## 4.1 Accounting standards and criteria

This consolidated quarterly report has been prepared in compliance with art. 82 of the enacting Regulations of Law Decree no. 58 dated February 24th, 1998 governing issuers (Consob Resolutions no. 11971 dated May 14th, 1999 and following amendments), and specifically in keeping with Appendix 3D of said Resolution.

The Group adopted the International Accounting Standard (IFRS), issued by International Financial Accounting Standards Board. The accounting principles used for the preparation of this quarterly report do not differ from those utilized from the introduction of IFRS
The accounting figures do not contain any estimates other than those normally used when preparing a set of annual accounts.

In connection with the US companies of the Group, no significant differences has been found between local accounting principle (US GAAP) and the accounting principle used for the consolidated financial report (IFRS).

The report has not been audited.

The amount contained herein are shown and commented upon in thousand Euro, unless expressly indicated otherwise.

## 4.2 Consolidation scope

The consolidation scope includes:

- **Panariagroup Industrie Ceramiche S.p.A**., Parent Company;
- **Gres Panaria Portugal S.A**., 100% owned;
- **Panariagroup USA Inc.,** 100% owned;
- **Florida Tile Inc.,** 100% owned;
- **Lea North America LLC,** 100% owned;
- **Montanari Srl,** 90% owned;

All the subsidiaries are consolidated on a line by line basis.

With reference to the controlled company Montanari Srl, in consideration of the existence of pre-emptive rights on the remaining 10%, and considering the assertion procedure provided for by the contract, even this percentage has been considered in the Equity of the Group, in accordance with international accounting standards.

The consolidation scope has not changed in the first quarter 2008

## 4.3 Executive report on operations

### Profit and loss analysis

***Profit and Loss – Figure as of March 31st 2008***

***(in € / 000)***

| | 31/3/2008 | % | 31/3/2007 | % | var. € |
|---|---|---|---|---|---|
| **Revenues from sales and services** | **85,769** | **97,97%** | **92,646** | **98,40%** | **(6,877)** |
| **Value of Production** | **87,543** | **100,00%** | **94,150** | **100,00%** | **(6,607)** |
| **Gross operating profit** | **12,132** | **13,86%** | **13,011** | **13,82%** | **(0,879)** |
| **Net operating profit** | **7,276** | **8,31%** | **8,717** | **9,26%** | **(1,441)** |
| **Pre-tax profit** | **4,947** | **5,65%** | **7,590** | **8,06%** | **(2,643)** |
| **Net profit for the period** | **3,045** | **3,48%** | **4,148** | **4,41%** | **(1,103)** |

The quarterly results are the following:

- **Consolidated net sales** amounted to **85.8 million Euros**, down by **7.42%** in comparison with the same period of the previous year.

- **Gross operating profit** amounted to **12.1 million Euros** (13.0 as of March 31st 2007), the **Net operating profit** amounted to **7.3 million Euros** (8.7 as of March 31st 2007) and the **Consolidated net profit** is **3.0 million Euros** (4.1 as of March 31st 2007).

Group revenues in the quarter were mainly influenced by the following factors:

- The slowdown of turnover in the United States, resulting from the continuation of structural crisis of U.S. real estate sector that reported in the first quarter 2008 a contraction in the residential market of 19,1% if compared to the same period of the previous year.

- The further depreciation of the Us dollar; it has to be remarked, that the average exchange in the first quarter of 2008 has been **1.473 Usd/Eur** while in the first three months of 2007 the average exchange rate was **1.311 USD / Eur**. (+ 12.2%)

- Lower shipping days in March 2008 on the Italian market, as a result of the Easter holiday (last year the Easter holidays fell in April), have implied a decrease in turnover, especially on the Italian market

The reduction in sales has implied a correspondence reduction in the margin in absolute value while maintaining the index of profitability equal to **13.86%** aligned with that of the first quarter of last year (**13.82%**)

The effect of exchange rate trend on European Business Unit of Panariagroup, if compared to the same period of the previous year, is a turnover decrease (and consequently an operating profit decrease) of Euro **0.4 million**, and a worsening of the financial result due to foreign exchange losses amounting to Euro **0.7 million**. The total effect on Pre-tax profit amounted to Euro **1.1 million**.

The following table reproduces the results as of March 31st 2008 of the European Business Units without considering the negative effect of the dollar exchange rate trend. It shows a positive result in line with the same period of the previous year.

| | 31/3/2008 | % | 31/3/2007 | % |
|---|---|---|---|---|
| **Revenues from sales and services** | **72,212** | **100,00%** | **73,906** | **100,00%** |
| **Gross operating profit** | **12,596** | **17,44%** | **13,109** | **17,74%** |
| **Net operating profit** | **8,399** | **11,63%** | **9,141** | **12,37%** |
| **Pre-tax profit** | **6,969** | **9,65%** | **8,318** | **11,25%** |
| **Net profit for the period** | **4,690** | **6,49%** | **4,877** | **6,60%** |

For a better comprehension, it has to be noted that the European Business Unit is composed by Italian companies Panariagroup Industrie Ceramiche SpA, Montanari Srl and the Portuguese company Gres Panaria Portugal SA, while Us Business Unit is represented by the consolidated financial statement of Panariagroup USA Inc. (that includes Florida Tile Inc. and Lea and North LLC)

As previously reported, the FY 2008 confirms the good profitability of the European Business Units (Italy and Portugal) of the Group, which, net of currency exchange effect, generated a gross operating profit higher than **17%** on the net sales. On the contrary the US Business Unit is still penalized by the structural crisis of the internal market.

## Revenues

The **Net sales** reported a fall of **7.8%** going from 92.7 million Euros as of March 31st 2007 down to 85.8 million Euros as of March 31st 2007 (- 6.9 million Euros).

The European companies realised a decrease of about **2.8 %,** almost entirely attributable to the Italian market.

**<u>Main reference markets</u>**

The three main reference areas are the European market, the Italian market and the US market.

Sales in **European markets** are essentially in line with last year; the only significant changes worthy of note are the excellent performance of French market (+8.9% equal to +0.7 million Euros) and the slowdown in the German market (-13.2% equal to -0.6 million Euros).
The Group continue to have a positive outlook of expected growth for 2008 in the European market
The incidence of the European markets on the total turnover on the consolidated turnover is around 44%.

The **Italian market** with a total turnover of 28.3 million Euros, (representing 32% on the consolidated turnover), is declined of about 7% if compared with the same quarter of 2007; this decrease is partly attributable to fewer shipping days of March due to stops during the Easter holidays (in particular the sales in March 2008 decreased of about 13%, if compared to the same month of 2007) and partly to a general climate of caution in the property sector even in the wake of the recession that has invested the U.S. market and financial markets in general.
On this market, expectations of the group for the coming months are of substantial alignment with the results of last year.

The incidence of the **US market** on the consolidated turnover is around 19%.

The first quarter 2008 confirms the structural crisis of the US Real Estate industry: according to the last U.S. Census Bureau research, sales of new homes on the residential sector have suffered a contraction of 19.1% if compared to the same period of the previous year.
In this scenario, the European companies of the Group registered a decrease of sales in dollars of about 10%, while U.S. companies Florida Tile and Lea North America lost about 16% if compared to 2007.

The revenues from US included in the Group consolidated financial statement as of March 31st 2008, fell of 15,22% if express in Us dollars; furthermore if we consider the unfavourable effect of the exchange rate, the total sales in Euro declined of more than 24%.

The breakdown of sales by Panariagroup's major markets is:

**Revenues by geographical area** (gross of costumer incentives) (amounts in thousand euros)

| *rk* | *Nazione* | *31/03/2008* | *31/03/2007* | *var.* | *%* |
|---|---|---|---|---|---|
| **1** | ITALY | 28.334 | 30.557 | (2.223) | -7,3% |
| **2** | USA | 16.095 | 21.350 | (5.255) | -24,6% |
| **3** | FRANCE | 8.940 | 8.215 | 725 | 8,8% |
| **4** | PORTUGAL | 8.866 | 9.117 | (251) | -2,8% |
| **5** | BELGIUM | 4.863 | 4.871 | (8) | -0,2% |
| **6** | GERMANY | 4.132 | 4.763 | (631) | -13,3% |
| **7** | HOLLAND | 3.376 | 3.588 | (212) | -5,9% |
| **8** | UNITED KINGDOM | 1.244 | 1.224 | 20 | 1,6% |
| **9** | SWITZELAND | 986 | 1.071 | (85) | -8,0% |
| **10** | GREECE | 954 | 1.079 | (125) | -11,6% |
| | OTHERS | 10.012 | 8.974 | 1.038 | 11,6% |
| | **TOTAL** | **87.802** | **94.809** | **(7.007)** | **-7,4%** |

As previously stated, the table remarks the dynamics of the main markets of Panariagroup

The data shows a decline in the U.S. and Italian markets and a substantial maintenance of European markets.

The emerging economies (Eastern Europe, Middle and Far East) represent an important market opportunity for our Group. These countries, traditionally oriented on low-end products, have increased their demand for the "made in Italy" and high-end products.

The total turnover in these areas has been Euros 6.3 million, with an increase of about 1.2 million Euros (+24% compared to 2007); in particular, we highlight the excellent results achieved in Russia, Poland, Cyprus and Israel.

Regarding the individual brand, **Cotto d'Este** and **Margres** registered good performance growth while the other European brand **Panaria**, **Lea**, **Fiordo** and **Novagres** registered a slight decline over the previous year.

At the contrary the Us business unit registered a pronounced negative performance under the persistence of the structural crisis of Us real estate sector.

The product types distributed by the Group are: the porcelain gres (the core business of Panariagroup), the white body wall tiles, the single-fired floor tiles (exclusively of Florida Tile).
The Florida Tile brand sells also non ceramic material.

The breakdown of sales by product class is:

**Revenues by type of product (gross of customer incentives)** (in thousand euro)

| *Type of product* | *31/03/2008* | *31/03/2007* | *var.* | *%* |
|---|---|---|---|---|
| Porcelain gres | 73.227 | 74.427 | (1.200) | -1,61% |
| % | 83,4% | 78,5% | | |
| White body wall tiles | 8.253 | 10.343 | (2.090) | -20,20% |
| % | 9,4% | 10,9% | | |
| Single-fired floor tiles | 790 | 3.477 | (2.687) | -77,27% |
| % | 0,9% | 3,7% | | |
| Non ceramic Material | 5.532 | 6.562 | (1.030) | -15,70% |
| % | 6,3% | 6,9% | | |
| ***Total*** | **87.802** | **94.809** | **(7.007)** | **-7,4%** |

The sales of “Porcelain gres” are those that have registered the lowest decrease in turnover; while, at the contrary, the higher decrease is referred to “Single-fire floor tiles” that are almost exclusively related to Florida Tile. This drop on sales come from the ongoing process in the American controlled company of conversion of all single fire product lines (previously purchased from third parties) into porcelain gres product lines in order to exploit the new American porcelain production line installed in the second half of last year.

The decrease of “White body wall tiles” is mainly determined by a strong decrease in Florida Tile, where this type is typically reserved to large distributors.

The “non ceramic material” is related to products sold by Florida Tile only, supplied to complete tiles’ sale, such as natural stones and laying and fixing tile materials.

**Operating results**

Despite the heavy weakening of Dollar against Euro and the persistence of the crisis in the important US market, the Group maintains a good level of Operating result.

The **Gross operating profit** totalled **12.1 million Euros**, represents 13.86% of the Value of Production (13.82% as of March 31st 2007).

The containment of certain cost components is mainly due to the following factors and considerations:

- Decrease in purchases of finished goods registered in particular in the American controlled company Florida Tile
- Internalization of some production phases such as cutting, polishing, lapping, etc, previously outsourced to external suppliers
- Maintenance of rationalization and research policies already adopted in 2007 aimed to a reformulation of bodies and glazes
- Energy costs in the first quarter 2008 grew by only 5.1%, despite the significant increase in the cost of oil, thanks to favourable existing contractual conditions.

The **Net operating profit**, that equals to 7.3 million Euros, is 8.3% of the Value of Production (9.3% as of of March 31st 2007).

The total amount of Depreciation increased, in absolute terms, of about 0.5 million Euros, mainly depending to the depreciation rate on the new production line built in 2007 in the American plant of Lawrenceburg

The increase in financial costs, which rose from 1.1 million Euros as of March 31st 2007 to 2.3 million Euros as of March 31st 2008, reflects the combination of the following factors: the negative exchange differences arising from collections in Dollar (equal to 0.7 million Euros) and the increase of the financial rates and the average Net Financial Position of the period (higher estimated financial charges of about 0.5 million Euros)

The tax charge for the first quarter 2008 is equal to 1.9 million Euros (38.4% tax rate), declining over the same period of the previous year.

The **Net profit** amounts to 3.0 million Euros, 3.5% of the Value of Production.

## Financial and balance sheet highlights

***Balance Sheet***

***(in € / 000)***

| | 31/3/2008 | 31/12/2007 |
|---|---|---|
| **Net Working Capital** | **155,997** | **146,622** |
| **Fixed assets** | **113,425** | **112,681** |
| **Assets / Liabilities due after year** | **(23,305)** | **(24,393)** |
| **NET CAPITAL EMPLOYED** | **246,117** | **234,910** |
| **Net Financial Position** | **91,885** | **80,869** |
| **Shareholders' equity** | **154,232** | **154,041** |
| **TOTAL SOURCES OF FUNDS** | **246,117** | **234,910** |

**Net working capital**

The Net Working Capital increased in the quarter of about 9.4 million Euros, as a result of the increase of accounts receivables due to seasonal factors.

**Investments**

The level of Fixed assets increased from the beginning of the year of about 0.7 million Euros.

The increase is due to:

- The net investments of the period, amounting to approximately 5.1 million Euros: these investments are related for 1.8 million Euros to technical investments in the production plants, while the remaining 3.3 million Euros are referred to the purchase of an industrial land in Portugal considered strategically important for its proximity to the Aveiro plant and to the main roadways; this investment could be utilized for the rationalisation of the existing logistic and productive structures.
- The depreciation of the period of 4.4 million Euros.

**Net financial position**

**Financial cash flow**
*(thousands euro)*

| | **31/03/2008** |
|---|---|
| **Net financial position - beginning** | **(80.869)** |
| Net Profit | 3.045 |
| D & A | 4.368 |
| Net Variation Provisions | (282) |
| **Internal operating Cash flow** | **7.131** |
| Change in net working capital | ((9.375) |
| Dividend distribution | 0 |
| Net Investments | (5.112) |
| Montanari acquisition | 0 |
| Other movements | (3.660) |
| **Net financial position - final** | **(91.885)** |

The Net Financial Position reports a negative balance of 91.9 million Euros, with a negative variation from the beginning of the year of about 11 million Euros. This increase is due to the increase in net working capital, to the purchase of the Portuguese land and to the purchase of company's own shares.

## 5. OPERATIONAL OUTLOOK FOR THE GROUP

Trusting in the European markets-resistance, in the maintenance of the good economic performance we are continuing to perform in these markets and in the reinforcement of the market development on Emerging countries we confirm confidence to be able in the coming months to mitigate the adverse effects arising from the persistent crisis in the Us market aiming to the realignment with the good results achieved over last year.

## 6. NOTEWORTHY EVENTS AFTER THE BALANCE SHEET DATE

We have to remark the change of the brand name Novagés in Love Ceramic Tiles.
As already successfully happened with the Portuguese brand Margrés (formerly Maronagrés), the purpose of this change is to raise the visibility of the brand and to set it on a more prestigious market segment.