

Cinema City International N.V.

Annual Report
for the year ended
31 December 2006

GENERAL INFORMATION

Management Board

Moshe Greidinger
Amos Weltsch
Israel Greidinger

Supervisory Board

Coleman Kenneth Greidinger
Carrie Twist
Frank Pierce
Scott Rosenblum
Peter Weishut
Yair Shilhav

Registered office

Weena 210-212
3012 NJ Rotterdam
The Netherlands

Auditors

KPMG Accountants N.V.
Burg. Rijnderslaan 10-20
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The Netherlands

LETTER FROM THE CEO

To our shareholders

2006 was truly a watershed year in our more than 75 year history.

In December, we completed a very successful initial public offering on the Warsaw Stock Exchange. We floated nearly €90 million of shares on the exchange, which included more than €50 million of new equity capital for the Company.

In addition, 2006 was a record year for growth and profitability for the Cinema City Group. With the benefit of a strong recovery in the international movie theatre market in 2006, we realised record revenues of € 143,791,000 and record EBITDA of € 31,248,000. During the year we continued our aggressive growth strategy with the opening of 4 new theatres, 44 new screens and 2 new IMAX® theatres throughout our territories.

In June 2006, we entered our fifth territory of operation with the opening of the Sofia, Bulgaria, “Mall of Sofia”, a 13 screen modern multiplex including an IMAX® theatre. During the same month, we also opened our first “new generation” 15-screen “Yes Planet” multiplex in Ramat Gan, Israel.

Our theatre operations performed strongly during 2006, supported by a strong supply of movies. Geographically, Poland, which produced the weakest relative results in 2005, performed very well, supported both by a string of well received international movies and a strong local supply. In addition, the new screens the Company opened in Poland during the latter part of 2005 and early 2006, which had their first full year of operations in 2006, helped to increase the positive results and contributed to record breaking results in Poland both in terms of number of admissions and EBITDA.

Our real estate activities continued to contribute strongly to our overall results in 2006. During the year we sold our remaining 25% interest in the Mall of Sofia to a partnership between GE Capital and Quinlan Private, while maintaining our long-term lease of the cinema multiplex and IMAX® theatre on the site. In July 2006, we signed an agreement to acquire, together with our original Mall of Sofia partner, 60% of a Bulgarian company whose main asset is a parcel of land in Plovdiv, Bulgaria. Plovdiv is one of the largest secondary cities in Bulgaria. Similar to the Mall of Sofia project we plan to develop a modern shopping and entertainment center on this parcel, which will include a multiplex theatre. The Company plans to sell the shopping centre while maintaining the multiplex theatre.

In 2006, we continued to expand our ancillary activities with the opening of our DVD distribution company in Hungary. This distribution company is already the exclusive distributor of films and DVDs for two major US studios: Warner Bros and Sony (Columbia).

From a geographic point of view, Central Europe continues to play an increasingly important role in our activities. We remain the largest cinema operator in this region, and we believe we are well positioned for sustainable growth. In addition to an 18 screen modern multiplex we acquired from Kinopolis in January 2007 in Poznań, Poland, which sold more than one million tickets last year, we plan to open four new multiplexes with 32 additional screens in Poland in 2007. In addition to sites under development in both the Czech Republic and Israel, we are developing a “megaplex” project in Budapest, Hungary, which will become our largest theatre to date, with 24 screens and an IMAX® theatre. This project, scheduled to open in the second half of the year, is being built on leased space as part of a new shopping mall and entertainment centre that is now under construction.

During 2007, we also expect to enter Romania, which will become our sixth territory of operation. We recently signed lease agreements for three multiplexes in “key” cities, and currently plan to open at least two of these multiplexes by the end of the year. These three multiplexes are in addition to the leases we previously signed for three multiplex theatres in Bucharest that are scheduled to open in 2008.

LETTER FROM THE CEO

I would like to take this opportunity to express my gratitude to our Cinema City employees for helping make 2006 such a successful year and for their continued hard work and dedication. Now as a public company, we are committed more than ever to continuing our growth and expansion, and we know that our ultimate success will continue to largely depend on the ongoing contribution of each one of them.

I would also like to warmly welcome our new shareholders. I look forward to a long and mutually fruitful relationship as we continue to build and grow our company.

And last but not least, I would like to thank our millions of customers, in five countries, who continue to share in our never ending love for the movies. As we say in the movie business... to be continued....

Moshe Greidinger

CEO

18 April 2007

Annual Report for the year ended 31 December 2006

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Supervisory Board report

Supervisory Board report

We take pleasure in presenting the financial statements of Cinema City International N.V. for the financial year 2006, accompanied by the report of the management board. KPMG Accountants N.V. audited the financial statements and issued an unqualified auditor's report. We recommend the shareholders to adopt the financial statements as presented.

We concur with the management board's proposal as taken up on page 92 to allocate the net profit for the year 2006 amounting to EUR 11,738,000 to retained earnings.

Supervision

Towards the end of 2006, in preparation of the listing of the Company at the Warsaw stock exchange, the Company's corporate governance structure was amended in order to comply as much as practically possible with Dutch governance regulations. The Supervisory Board has reviewed the Dutch corporate governance code (the "Code"), and generally agrees with its basic provisions, and has, to the extent possible, approved the implementation of most of the best practice provisions of the Code. For a more detailed description, reference is made to pages 3 to 7 of this Annual Report.

During the meetings of the Supervisory Board that were held in 2006 the following topics were discussed:

- the Company's business strategy;
- the anticipated listing of the Company's shares at the Warsaw stock exchange including the initial public offering of shares in the Company;
- the corporate governance structure of the Company and the implementation of the Code;
- risk management;
- a Management Board remuneration policy including the implementation of a long-term incentive plan.

Audit committee

The roles and responsibilities of the Audit Committee are to supervise, monitor and advise the Management Board and Supervisory Board on all matters related to risk management, audit, control and compliance to relevant financial legislation and regulations. The Audit Committee evaluates the performance of external auditors and related costs.

Appointment committee

The primary responsibility of this committee is to advise the Supervisory Board on matters relating to the nominations of both Supervisory and Management Board members. The Appointment Committee regularly reviews the Supervisory Board profile, its effectiveness and composition. The committee also reviews the performance of the members of the Management Board.

Remuneration committee

It is the primary task of the Remuneration Committee to propose to the Supervisory Board remunerations of the members of the Management Board, including a review and monitoring of the Group's total remuneration policy.

Supervisory Board report

Financial statements

The Management Board has prepared the 2006 financial statements. These financial statements were discussed at a Supervisory Board meeting attended by the auditors, who provided further information on the financial statements and their audit findings.

Composition

On 7 November 2006, the shareholders of the Company approved the appointment of Mr Yair Shilhav as a Supervisory Board director. Mr Shilhav's curriculum vitae is taken in the Chapter "Corporate Governance" on page 5. Mr Shilhav has obtained extensive financial and accounting experience in various professional positions and is therefore considered to qualify as a financial expert in accordance with the Dutch corporate governance code.

18 April 2007

For the Supervisory Board

Coleman Kenneth Greidinger
Chairman

Corporate Governance

Corporate Governance

Governance structure

The Company is a Dutch public company with a listing on the Warsaw stock exchange.

Corporate governance Code in the Netherlands

On the basis of Section 391 of Book 2 of the Dutch Civil Code (Act of 9 July 2004, Stb 370, to amend Book 2, CC) and the Royal Decree of 23 December 2004, public limited liability companies, whose shares – to put it briefly – are listed on a stock exchange, must include a statement in their annual report about their compliance with the principles and best practices of the Tabaksblat Code, published on 9 December 2003 (the ‘Code’).

The Code contains 21 principles and 113 best practice provisions covering the management board, the supervisory board, the shareholders and general assembly, financial reporting, auditors, disclosure, compliance and enforcement. The Code requires Dutch companies that are listed on a government recognised stock exchange, whether in the Netherlands or in any other country, to disclose in their annual reports (commencing with those annual reports for financial years beginning on or after 1 January 2004), whether or not they comply with the provisions of the Code and, if they do not comply, to explain the reasons why.

The Company acknowledges the importance of good corporate governance. The Management Board and Supervisory Board have reviewed the Code, and generally agree with its basic provisions, and have, to the extent possible, implemented and subsequently applied most of the best practice provisions of the Code in its corporate governance structure and Articles of Association. Save as disclosed below, the Company complies with the Code. The Code recognises that non-compliance of a specific Best Practice Provision is not in itself objectionable but indeed may be justified under certain circumstances.

In certain respects where the provisions of the Code conflict with Polish law or Polish corporate governance requirements, the Company has determined that it will comply with the Polish requirements rather than the provisions of the Code in view of the fact that the Company is solely listed on a Polish stock exchange and the majority of its public shareholders are expected to be based in Poland. The following is a description of the deviations from the provisions of the Code:

- Best Practice Provision II.2.7 of the Code states that severance payments may not exceed the annual salary. Employment contracts of the members of the Management Board, which were entered into before the Code was developed, provide severance payments that exceed the annual salary. The employment contracts are considered to be in line with standard company policy and the Supervisory Board intends to honour this contractual commitment and is of the view that a deviation from the Code is justified.
- Best Practice Provision III.2.1 of the Code prescribes that the Supervisory Board consists of independent persons, except for one. The Company currently has two non-independent members of the Supervisory Board, which is a deviation from the Code. However, the current composition of Supervisory Board is consistent with Polish corporate governance guidelines.

Corporate Governance

In view of the foregoing considerations and justifications, the Company makes the following statement.

Statement referred to in Section 3 of the Decree of 23 December 2004, Stb 747, determining the further requirements concerning the contents of annual reports

In the year under review, the Company did not comply fully with the provisions of the Code, nor does it intend to fully comply with these during the current or the next financial year.

The Extraordinary General Meeting of Shareholders held on 24 November 2006 approved the corporate governance policy and framework of Cinema City International N.V., including the structure of the remuneration of management under article 2:135 of the Dutch Civil Code. The corporate governance policy and the framework will once again be placed on the agenda for the General Meeting of Shareholders, in order to allow the shareholders to discuss and exchange views upon the issue with the Management Board and Supervisory Board.

Corporate governance Code in Poland

On 15 December 2004, the WSE management board and the WSE supervisory board adopted corporate governance rules of the WSE contained in the Best Practices in Public Companies in 2005 (the “WSE Corporate Governance Rules”). The WSE Corporate Governance Rules reflect the achievements in this field at both national and international level and apply to companies listed on the WSE, irrespective of whether such companies are incorporated in Poland or outside of Poland. The WSE Corporate Governance Rules consist of five general principles and 48 best practice provisions relating to shareholders’ meetings, management boards, supervisory boards and relations with third parties and third party institutions. The WSE Corporate Governance Rules impose on companies listed on the WSE an obligation to disclose in their annual reports, whether or not the companies comply with those principles and provisions and, if they do not comply, to explain the reasons why.

Compliance with WSE Corporate Governance Rules is voluntary. Companies listed on the WSE are required, however, to give reasons justifying non-compliance or partial compliance with any rule. The Company intends, to the extent practicable, to comply with all principles of the WSE Corporate Governance Rules. However, certain principles will apply to the Company only to the extent allowed by Dutch law. In particular, as Dutch law does not provide for elections of the Supervisory Board’s members by separate groups of shareholders, the Company’s internal regulations do not and will not include provisions on group elections (Rule 6). No reports will be provided by the Supervisory Board member delegated by a group of shareholders (Rule 30) because Dutch law does not provide for delegation of a board member by a group of shareholders.

Detailed information on the Company’s compliance with the WSE Corporate Governance Rules as well as additional explanations regarding partial compliance with certain principles of the WSE Corporate Governance Rules due to their incompatibilities with Dutch law, are included in the full text of the Company’s statement regarding the compliance with the WSE Corporate Governance Rules which was filed with the WSE in December 2006 together with the Company’s WSE listing applications and is available on the Internet on the Company’s website (www.cinemacity.nl).

The Company makes all efforts to comply with all principles of both the Dutch Code and the WSE Corporate Governance Rules and to enforce such corporate structure that ensures the Company’s transparency to the most possible extent. The Company believes that its efforts are appreciated by its stakeholders and will support the Company’s growth and its reliability.

Corporate Governance

General Meeting of Shareholders

The annual General Meeting of Shareholders shall be held within six months after the end of the financial year to deal with, among other matters: (i) the annual report; (ii) adoption of the annual accounts, (iii) discussion of any substantial changes in corporate governance; (iv) discussion of remuneration policy board of managing directors, (v) granting of discharge to the board of managing directors for the management over the past financial year (vi) discussion of remuneration supervisory board, (vii) granting of discharge to the Supervisory Board for the supervision over the past financial year, (viii) policy on additions to reserves and dividends and (ix) adoption of the profit appropriation.

Other General Meetings of Shareholders shall be held as often as the Management Board or the Supervisory Board deems necessary. Shareholders representing in the aggregate at least one-tenth of the Company's issued capital may request the Management Board or the Supervisory Board to convene a General Meeting of Shareholders, stating specifically the business to be discussed.

Supervisory and management boards

The Company has a two-tier corporate governance structure, consisting of a (executive) management board (the "Management Board") and a (non executive) supervisory board (the "Supervisory Board"). The day-to-day management and policy-making of the Company is vested in the Management Board, under the supervision of the Supervisory Board. There are currently three members of the Management Board whose names are set out below. The Supervisory Board supervises the Management Board and the Company's general course of affairs and the business it conducts. It also supports the Management Board with advice. In performing their duties the Supervisory Board members must act in accordance with the interests of the Company and the business connected with it.

Supervisory Board

The Articles of Association provide that the Company shall have a Supervisory Board consisting of at least three and at most six persons of which at least two Supervisory Directors shall be independent. Supervisory Directors are appointed by the General Meeting of Shareholders for a period of four years. After holding office for the first period of four years, Supervisory Directors are eligible for re-election for two additional terms of four years each. The General Meeting of Shareholders shall establish the remuneration for each Supervisory Director.

Supervisory Board Committees

The Supervisory Board is supported by three committees:

- the audit committee;
- the appointment committee;
- the remuneration committee.

These committees are composed from members of the Supervisory Board with relevant experience. All committees operate under the overall responsibility of the Supervisory Board, in accordance with the best practice stipulations of the Code.

Corporate Governance

Composition of the Supervisory Board

Coleman Greidinger (1 January 1924)

An Israeli citizen, Coleman Greidinger was appointed as a member of the Supervisory Board in 2004, is the current Chairman of the Supervisory Board and a member of the Audit Committee. He founded Israel Theatres Limited in 1958 and has been Managing Director of Israel Theatres Limited and affiliated companies since that time. He was also a President of Variety Israel, serves as a member of the International Board of Variety Clubs and is a member of the board of governors of the Hebrew University in Jerusalem and the board of governors of the Technion University in Haifa. He is the father of Moshe and Israel Greidinger. His current term as Supervisory Director expires in June 2008.

Yair Shilhav (12 October 1958)

Yair Shilhav was appointed as a member of the Supervisory Board in November 2006, and is the Chairman of the Audit Committee. Since 2004, Mr Shilhav has been the owner of a business consulting office. Between 2000 and 2003, he was a member of the executive directory committee of the audit firm, Somekh Chaikin, a member of KPMG (“Somekh Chaikin”). Between 1995 and 2003, he was the head of the Haifa branch of Somekh Chaikin, of which he was partner from 1990 to 2003. Prior to becoming a partner at Somekh Chaikin, he was head of the professional and finance department of the same firm. He was also the head of the accountancy faculty at Haifa University between 1998 and 2002. His current term as Supervisory Director expires in November 2010.

Arthur F. Pierce (4 April 1930)

Arthur Pierce was appointed as a member of the Supervisory Board in 2004 and, as of November 2006, has been a member of the Remuneration Committee and the Appointment Committee. From 1996 to the present time, he has worked as a consultant providing services related to the international motion picture distribution. Between 1954 and 1972, Mr. Pierce held various executive positions with Columbia Pictures International, Paramount Pictures International and Cinema International Corporation. From 1972 to 1993, he served as Vice President of Europe for Warner Brothers Theatrical Distributions. From 1993 to 1996, he served as Senior Vice President for European Theatrical Distributions, Time Warner Entertainment. Mr. Pierce currently serves as Director of Luna Productions, Limited, a UK subsidiary of New Regency Productions, Inc., and as President of Frank Pierce Partners, International Theatrical Representation. He received his B.A. and M.A. from Boston College in the United States.. His current term as Supervisory Director expires in June 2008.

Scott. S. Rosenblum (4 October 1949)

Scott Rosenblum was appointed as a member of the Supervisory Board in 2004, was appointed Chairman of the Remuneration Committee and of the Appointment Committee in November 2006 and is also a member of the Audit Committee. He is licensed as a lawyer and admitted to the New York Bar Association. For the past ten years he was a partner in the law firm of Kramer Levin Naftalis & Frankel LLP, New York, and was Managing Partner between 1994 and 2000. He is currently a director of Escala Group, Inc and Temco, Inc. He is also legal adviser to Israel Theatres limited Ltd., the indirect shareholder of the Company. His current term as Supervisory Director expires in June 2008.

Caroline M. Twist (25 January 1956)

Caroline Twist was appointed as a member of the Supervisory Board in 2004 and, as of November 2006, has been a member of the Remuneration Committee. Between 1978 and 1984, Ms Twist worked as a manager in ABC/Thorn EMI cinemas in the UK. From 1984 to 1988, she served as West End Regional Manager / New Projects Manager for C.I.C. Theatres in the U.K. From 1989 until now, Ms Twist has held various managerial positions, with PACER CATS, a leading supplier of computerised ticketing systems, both in the United States and Europe. Her current term as Supervisory Director expires in June 2008.

Corporate Governance

Peter J. Weishut (31 July 1935)

Peter Weishut was appointed as a member of the Supervisory Board in 2004 and, as of November 2006, has been a member of the Appointment Committee. Between 1969 and 1997, Mr Weishut worked as a director in Akzo Nobel in the Netherlands and Japan. From 1997 to 1999, he served as Management Consultant for Rafino, producer of pet foods, in the Netherlands. Between 1999 and 2001, Mr Weishut was the treasurer of a foundation celebrating the 400-year relationship between the Netherlands and Japan. His current term as Supervisory Director expires in June 2008.

Management Board

The management of the Company is entrusted to the Management Board under the supervision of the Supervisory Board. The Articles of Association provide that the Management Board shall consist of two or more managing directors. Managing directors are appointed by the General Meeting of Shareholders. The Management Board shall meet as often as a managing director requests a meeting. All resolutions by the Management Board shall be adopted by an absolute majority of the votes cast.

The Management Board as a whole is responsible for the day-to-day management, including comprehensive risk management control, financing and regulatory compliance. Cinema City International N.V. and its operating companies are organised along clear functional reporting lines. Throughout the Group, corporate and operating accountabilities, roles and responsibilities are in place.

Composition of the Management Board:

Moshe J. (Mooky) Greidinger (12 December 1952)

Moshe J. (Mooky) Greidinger was appointed Chief Executive Officer of the Company in 1984. Mr Greidinger joined the Company in 1976. Since 1984, he has held executive positions with the Company with substantially the same responsibilities as he presently maintains. Mr Greidinger has also served as a director and Deputy Managing Director of Israel Theatres Limited since 1983 and Co-Chairman of the Cinema Owners Association in Israel since August 1996. He is the brother of Israel Greidinger and the son of Coleman Greidinger. His current term as Managing Director expires in June 2008.

Amos Weltsch (28 February 1950)

Amos Weltsch joined the Company in 1980 at which time he was appointed Chief Operating Officer of the Company. Since that time, Mr Weltsch has held executive positions with the Company with substantially the same responsibilities as he presently maintains. He has also held various senior management positions with Israel Theatres Limited and affiliated companies since 1980. From 1974 to 1978, he was a manager at L. Glickman Building Materials, and from 1978 to 1980, a managing director of Eitan Cement Limited. His current term as Managing Director expires in June 2008.

Israel Greidinger (14 April 1961)

Israel Greidinger joined the Company in 1994 and was appointed Chief Financial Officer of the Company in 1995. Since that time he has held executive positions with the Company with substantially the same responsibilities as he presently maintains. Mr Greidinger has also served as a director of Israel Theatres Limited since 1994. From 1985 to 1992, Mr Greidinger served as Managing Director of C.A.T.S. Limited (Computerised Automatic Ticket Sales), a London company, and from 1992 to 1994, he was President and Chief Executive Officer of Pacer C.A.T.S., Inc. He is the brother of Moshe Greidinger and the son of Coleman Greidinger. His current term as Managing Director expires in June 2008.

Remuneration Report

Remuneration Report

Introduction

The Extraordinary General Meeting of Shareholders held on 24 November 2006, upon recommendation of the Supervisory Board, approved the Company's remuneration policy which sets forth the terms of remuneration of the members of the Management Board. The same General Meeting approved a long-term incentive plan for members of the Management Board and other key personnel of the Company and its subsidiaries. The remuneration for the Supervisory Board was also adopted at the same General Shareholders' Meeting.

Remuneration Policy

The objective of the Company's remuneration policy is to provide a compensation programme that allows the Company to attract, retain and motivate qualified people who have the character traits, skills and background to successfully lead and manage the Company. The remuneration policy is designed to reward members of the Management Board and other key personnel for their contribution to the success of the Company.

Governance

The General Meeting of Shareholders approves all aspect of the remuneration policy for the Management Board. The General Meeting of shareholders further determines the remuneration of the Supervisory Board. Compensation of both the Supervisory Board and Management Board is reviewed regularly. The Supervisory Board has a dedicated Remuneration Committee.

Remuneration of the Management Board

Employment contracts

The three members of the Company's Management Board have three-year employment contracts that terminate in December 2007 and are automatically renewed by the year periods unless notice of termination is given by either party. It also includes a non-compete clause that requires the Managing Director to refrain from any activity that is competitive to the Company's activity for a period of twelve months after termination of employment. These persons are paid under contractual agreements that provide a monthly base salary indexed to the Israeli consumer price index and annual participation in a bonus pool with the other Management Board members. Forum Film (Israel), the Company's 50% subsidiary, covers 100% of the portion of the bonus pool derived from Forum Film (Israel) profits and 33% of the monthly based salaries to Mr. Moshe Greidinger and Mr. Israel Greidinger.

In addition, under the terms of the employment contracts, the members of the Management Board are entitled to a car, contribution to a severance fund, contribution to a statutory provident fund, a EUR 175 per diem payment for business travel days and reimbursement of reasonable business expenses, including payment of reasonable telephone bills. The members of the Management Board are not entitled to any benefits on termination of his employment except for a severance payment. For Messrs Moshe Greidinger and Israel Greidinger, the severance payment is equal to their monthly base salaries at the time of termination, multiplied by the number of years of employment by the Company. For Mr Weltsch, the severance payment is equal to the greater of: (a) the statutory amount accumulated in his policy account for severance pay and (b) his monthly base salary at the time of termination, multiplied by the number of years of his employment by the Company.

Remuneration Report

Long-term incentive plan

Towards the end of 2006, a new long-term incentive plan (the “Plan”) was implemented. The persons eligible for participation in the Plan are the employees of the Group, including the members of the Management Board. Under the Plan, both option rights to acquire shares in the Company and cash bonuses may be granted to the participants.

The grant of options to Management Board members and other personnel has a maximum of 930,000 newly issued or repurchased shares. The Supervisory Board is authorised to determine, with the participation of at least one independent member of the Supervisory Board, the exact terms of any stock or stock-based incentive scheme. The actual grant of share options is disclosed in the Notes to the Consolidated Financial Statements.

Remuneration of the Supervisory Board

Each Supervisory Board member receives an annual remuneration of EUR 8,500 and EUR 1,500 per attendance at meetings or EUR 750 if attendance is by telephone.

Directors' report

Directors' report

General

Introduction

Cinema City International N.V. (the "Company"), incorporated in the Netherlands, is a subsidiary of I.T. International Theatres Ltd. ("ITIT" or "parent company"). The Company (and together with its subsidiaries, the "Group"), is principally engaged in the operation of entertainment activities in various countries including: Poland, Hungary, Czech Republic, Bulgaria and Israel. The Company, through related entities, has been a family operated theatre business since 1929. In December 2006, the Company completed a successful initial public offering of its shares on the Warsaw Stock Exchange, having sold about 10 million primary shares and close to 8 million secondary shares at an offering price of PLN 19.3 (EUR 5.05) per share, giving the Company a post-money market capitalisation of approximately EUR 256 million. The Company's headquarters and principal place of business are located in Rotterdam, the Netherlands.

Company overview

The Company is the largest operator of multiplex cinemas in Central Europe and is currently operating 335 screens in 35 cinemas in Poland, Hungary, the Czech Republic and Bulgaria. The Company has significant expansion plans for Central Europe, mainly in Poland, and is also in initial stages of development in Bulgaria and Romania. In addition to Central Europe, the Company is one of the two leading motion picture exhibitors in Israel, operating 131 screens in 23 cinemas throughout the country. The Company has historically benefited from its relationships with international film companies, having acted as the exclusive motion picture distributor for Walt Disney Company ("Disney") in Israel for the past forty years and, more recently, in Poland and Hungary. The Company also maintains an exclusive arrangement with the IMAX corporation to develop IMAX® theatres in Poland, the Czech Republic, Hungary, Bulgaria and Romania.

Business strategy

The Company's strategic objectives are to enhance its position as a leading operator of multiplex cinemas in Central Europe through continued expansion in Poland, Hungary, the Czech Republic, Bulgaria and Romania, and to maintain its position as a leading motion picture exhibitor in Israel. The Company plans to continue to design and operate multiplex theatres, which it believes will promote increased attendance and maximise space and operating efficiencies through improved utilisation of theatre capacity and reduced labour costs. In conjunction with its movie exhibition business, the Company is also active in other movie related activities, including film distribution and, to a smaller extent, video retail. The Company plans to continue developing its film related activities, mainly in Central Europe, and believes these operations will continue to play a key roll in achieving the Company's targets. In addition, in conjunction with its expansion in Central Europe, the Company has invested in the development of commercial real estate projects associated with its theatres in a number of locations in Central Europe and intends, opportunistically, to continue to do so.

Directors' report

Economy and business developments during the year

Economic environment

Economy

The positive economic trends in Central Europe are stabilising.

- The disposable income in each country represents the purchasing power of the consumer for among other things, cinema entertainment. The Company believes that an increase in the disposable income will increase admissions in the existing cinemas as well as average spending in the cinemas.
- The strengthening of most of the local currencies against the euro, during the past few years, shows that these countries are closing the economic gap with Western European countries.

The Company believes the development of the economies in Central Europe will help its development plans in the region.

Cinema market

While the demand is growing mainly in line with the economic status of the market, the Company believes that the low supply of good quality cinemas is the main reason for the underdeveloped market. The multiplex screens density in the Company's markets of operation in Poland, Hungary, Czech Republic and Bulgaria and soon in Romania in comparison to the density to the western European countries is considered to be relatively low.

This allows expansion of multiplexes, which should increase admissions in the mentioned countries.

Competitive environment

Poland

Cinema City is the clear leader in the Polish movie exhibition market. In 2006, the Company had a 28% share of the total market as measured by admissions (not including the IMAX® theatres) and a 38% share of multiplex admissions. Moreover, the Company has a dominant position in Warsaw, accounting currently for over one third of the box office market in Poland, with a 65% market share of admissions.

Apart from being the market leader in the movie exhibition industry in Poland, Cinema City controls the leading cinema advertising sales house, New Age Media, and is a major film distributor through Forum Film Poland, a wholly-owned subsidiary of Cinema City. Forum Film Poland is the exclusive distributor of Buena Vista International, a subsidiary of Walt Disney, distributing movies of Disney and Touchstone. In addition, Forum Film Poland distributes films from Spyglass and several other independent producers.

The main competitors of Cinema City are other multiplex chains of which Multikino is the largest with 8 multiplexes across Poland. Other major competitors are Silver-Screen, Helios, and Kinoplex.

Directors' report

Hungary

The Company is the second largest exhibitor in Hungary in number of screens (1), and has multiplexes mainly in the secondary cities, with an approximate 22%(2) share of the Hungarian exhibition market. The Company currently dominates the cinema market in larger cities outside Budapest. The Company recently signed a contract for opening a Megaplex and an IMAX® theatre in the Kerepesi shopping mall in Budapest which is planned to be one of the biggest shopping centers in Central-Eastern Europe. The project is currently slated for opening at the end of 2007. The main competitors in Hungary are Intercom Cinemas, Palace Cinemas and Budapest Film. In 2006, Palace Cinemas acquired Intercom and became the largest theatre operator in Hungary.

In 2005, the Company opened a new film distribution company in Hungary and received the rights to distribute films for Revolutionary, Spyglass and BVI. The first film was released in July 2005. In September 2006, the Company commenced operation of its DVD distribution company in Hungary. This distribution company is already the exclusive distributor of films and DVDs for two major US studios: Warner Bros and Sony (Columbia).

In October 2006, the Company established its advertisements company in Hungary. The operation begins in 2007.

(1) As of 30 June 2006.

(2) According to Dodona for 2005.

Czech Republic

Cinema City is one of the largest cinema operator in the Czech Republic with a strong presence in Prague. The cinema market in the Czech Republic outside Prague is relatively undeveloped. This offers opportunities for Cinema City to open multiplex theatres in other large cities. The Company's main competitors are Palace Cinemas, Cinestar and Village Roadshow.

Israel

The Company operates in Israel under the brand name of "Rav-Chen" and "Planet" (the brand name "Cinema City" was previously reserved in Israel by a competitor). The Israeli movie exhibition market is dominated by two cinema operators. As of the end of September 2006, the Company is the largest cinema operator in Israel based on number of screens with 23 theatres with 131 screens. Globus is the second largest operator with 24 theatres and 123 screens. In 2005, the Company had a 32% share in terms of admissions.

The Company is also a major film distributor through Forum Film, a 50% owned subsidiary of the Company. Forum Film is the exclusive film distributor of Disney and several other independent studios. The Company's main competitor is Globus that operates with 24 theatres with 123 screens, and that, through its distributions channel, acts as a distributor for Warner and UIP. Other players in the cinema market in Israel include Lev Cinemas, Cinema City (a brand registered by a competitor) and A.D. Mattalon. A.D. Mattalon is also a competitor in the Israeli film distribution business.

Directors' report

Business highlights during 2006

2006 was a successful year for the Company, with revenues, EBITDA (Earnings Before Interest, Taxation, Depreciation and Amortisation) and net income having increased materially in comparison to the prior year. The movie theatre operations recovered strongly from a relatively weak 2005, and the real estate activities continued to perform well. Consolidated Revenue increased from EUR 108.2 million during 2005 to EUR 143.8 million during 2006. Consolidated EBITDA increased from EUR 24.0 million in 2005 to EUR 31.2 million for 2006. Net income increased from EUR 7.9 million for 2005 to EUR 11.7 million for 2006.

Theatre operation activities

The Company's theatre operations performed strongly during 2006, supported by a relatively strong supply of movies. Geographically, Poland, which produced relatively the weakest results in 2005, performed very well, supported both by a string of well received international movies and a strong local supply. In 2005, the Polish market was particularly weak due to a combination of poorly received international movies, little local supply and the death of the Pope, which caused the Company to close all of its Polish cinemas for nearly two weeks in April. In addition, the new screens which the Company opened in Poland during the latter part of 2005 and which had their first full year of operations in 2006, helped to increase the positive results and contributed to record breaking results in Poland both in terms of number of admissions and EBITDA.

Theatre development

- In March 2006, the Company opened its 4th project in Prague, a small 5 screen multiplex.
- In May 2006, the Company opened a 15 screen multiplex (including an IMAX[®] theatre) in a new shopping centre in Łódz, Poland.
- In July 2006, the Company opened its first Cinema City in Sofia, Bulgaria, 13 screens including an IMAX[®] theatre. With this opening, the Company is now operating in five territories.
- In July 2006, the Company also opened its first new generation multiplex in Israel, the 15 screen YES Planet Multiplex in Ramat Gan, just north of Tel Aviv, and closed the old 4 screen multiplex in the same place. This new multiplex is the first project in Israel that is using the Company's new Israeli brand name "Planet". It is also being sponsored by the leading Israeli TV satellite company, "YES".

The Company's total screen count at the end of 2006 following these openings has grown to 466 (including 7 IMAX[®] theatres).

Most recently, in January 2007 the Company closed two multiplex theatres in Israel – in Ashdod and Karmiel. These closings are in line with the Company's ongoing plan to modernise and upgrade its Israeli chain through the closing of its smallest and oldest multiplexes while opening modern state-of-the-art larger multiplex theatres.

Directors' report

In January 2007, the Company acquired a modern recently developed 18 screen multiplex cinema in Poznań that previously had been operated by the Kinopolis Group. Under the agreement with Kinopolis, the Company acquired certain assets relating to Kinopolis' operation of the Poznań theatre and entered into a long-term lease of the 18 screen complex with Kinopolis, which continues to own the building. This multiplex has now become the Company's second theatre operation in Poznań.

In January 2007, the Company resolved a two year old dispute with the developer of two of the Company's planned multiplex sites in Poland – Wloclawek and Elblag. In early 2005, the developer sought to cancel existing lease agreements entered into with the Company for the development of multiplexes on those sites. Under the settlement, the Company has agreed not to seek to enforce the lease agreements and development of the sites in return for an agreed upon cash payment.

Real estate activities

The Company's real estate activities continued to contribute to the Company's results on the same level as in 2005. During 2006, the Company sold its remaining 25% interest in the Mall of Sofia, which was the main contributor to this strong result. The sale, which was to the same two European private equity companies that purchased the first 25% of the company holdings in the project a year earlier, was completed just prior to the Mall's opening in June. In July 2006, the Company signed an agreement to acquire, together with its original Mall of Sofia partner, 60% of a Bulgarian company whose main asset is a parcel of land in Plovdiv, Bulgaria. Plovdiv is one of the largest secondary cities in Bulgaria. Similar to the Mall of Sofia project (without an office complex), the Company plans to develop a modern shopping and entertainment centre on this parcel, which will include a multiplex theatre. The Company plans to sell the shopping mall while maintaining the lease of the multiplex theatre.

Other film-related activities - developments

In May 2006, the Israeli government anti-monopoly office approved the merger of the Company's video retail operations in Israel, which operate under the name Video Giant Ltd., with its main competitor, Blockbuster. Under the agreement signed between the parties, Video Giant Ltd. and Kafan Video Libraries Ltd. (operator of the Blockbuster video libraries in Israel) will form a 50/50 joint venture that will operate the combined video chain under the brand name Blockbuster. The Company will provide the MD (chief executive officer) for the new JV, while Kafan will provide the chairman of the board. As of 1 May 2006 the partnership began operating on a de facto basis, with the legal formalities expected to be finalised in the next 60 days. The JV will be jointly controlled between Kafan and the Company and the Company will consolidate the results of operations of this entity proportionally (50%).

In September 2006, the Company commenced the operation of its DVD distribution company in Hungary. This distribution company is already the exclusive distributor of films and DVDs for two major US studios: Warner Bros and Sony (Columbia).

In October 2006, the Company commenced operation of its screen advertising company in Hungary.

Directors' report

Initial public offering

In December 2006, the Company completed a successful initial public offering of its shares on the Warsaw Stock Exchange. The Company sold 10 million new shares and close to 8 million existing shares held by certain stockholders at an offering price of PLN 19.30 (EUR 5.05) per share. Following the IPO, the Company had a total market capitalisation of over EUR 256 million. CAIB served as the lead manager and ING Bank served as the co-manager in the offering. The Company's shares trade under the symbol "CCIINT".

The net proceeds from the newly issued shares will be used for the realization of the company's development plans as discussed on page 21 and for partial repayment of Bank Dept.

Directors' report**Overview of results**

The Company's net income for 2006 was EUR 11,738,000. An analysis of net income is shown below.

	For the year ended 31 December	
	2006	2005
	EUR	
	(thousands, except per share data)	
Revenues	143,791	108,181
Operating costs, excluding depreciation and amortisation	106,266	78,771
Gross result	37,525	29,410
General and administrative expenses	6,277	5,387
EBITDA *	31,248	24,023
Depreciation and amortisation	13,901	12,096
Operating profit	17,347	11,927
Financial income	795	2,198
Financial expenses	(5,465)	(4,951)
Loss on disposals and write-off of other investments	(34)	(151)
Net income before net result from associates	12,643	9,023
Net result from associates	-	(103)
Net income before taxation	12,643	8,920
Income taxes	1,377	1,198
Net income before minority interests	11,266	7,722
Minority interests	(472)	(188)
Net income attributable to equity holders of the parent company	11,738	7,910
Net earnings per ordinary share (basic and diluted of EUR 0.01 each)	0.28	0.19

* Earnings Before Interest, Taxation, Depreciation and Amortisation. Under this definition, gains and losses on disposals and write-off of other assets as well as currency exchange results are also not included in EBITDA.

Directors' report

Revenues

Total revenues increased by 32.9% from EUR 108.2 million during the year ended 31 December 2005 to EUR 143.8 million during the year ended 31 December 2006.

Theatre operating revenues increased by 34.6% from EUR 73.6 million during the year ended 31 December 2005 to EUR 99.1 million during the year ended 31 December, 2006. The increase in theatre revenues was a result of an increase in admission because of strong supply of movies especially in Poland compared to relatively weak supply of movies in same period last year, and a result of the contribution of new cinemas opened in 2005 and in the first half of 2006.

Distribution operating revenues increased by 45% from EUR 15.1 million during the year ended 31 December 2005 to EUR 21.9 million during the year ended 31 December 2006. The increase was mainly due to increase in the distribution activity in Poland because of strong supply of movies, due to the contribution of Forum Film Hungary, a new subsidiary of Group which is distributing films in Hungary and commenced its activities in the middle of 2005 and due to the first time contribution of Forum Home Entertainment Hungary a new subsidiary of the Group which is distributing DVDs in Hungary and commenced its activities only in September 2006.

Video operating revenues decreased by 16.3% from EUR 4.9 million during the year ended 31 December 2005 to EUR 4.1 million during the year ended 31 December 2006. The decrease was primarily a result of a decrease in DVD rentals during the first part of the year 2006. As of May, the Group has merged its video and DVD retail operations in Israel with Blockbuster, and is now only consolidating in its account 50% of the new merged group revenue.

Other revenue increased by 28.3% from EUR 14.5 million during the year ended 31 December 2005 to EUR 18.6 million during the year ended 31 December 2006. The increase in other revenue was primarily attributed to the increase in revenues from the real estate activities.

Operating costs

Operating costs excluding depreciation and amortisation increased by 34.9% from EUR 78.8 million during the year ended 31 December 2005 to EUR 106.3 million during the year ended 31 December 2006. This net increase resulted primarily from the total effects of:

- an increase in theatre operating expenses primarily explained by the increase in theatre revenues as described above. Theatre operating expenses, excluding depreciation and amortisation, as a percentage of total theatre revenue decreased to 73.3% for the year ended 31 December 2006, from 78.9% for the year ended 31 December 2005;
- an increase in distribution operating expenses as a result of the increase in revenues as described above. Distribution operating expenses, excluding depreciation and amortisation, as a percentage of total distribution revenue increased to 91.2% for the the year ended 31 December 2006, from 81.6% for the the year ended 31 December 2005. This increase is mainly due to the increasing weight of Central Europe in the Group's total distribution activities. The distribution activities in Israel are more diverse and enjoy higher profit margins than the relatively new distribution activities in Central Europe.

Directors' report

- a decrease in video operating expenses as a result of the increase in revenues as described above. Video operating expenses, excluding depreciation and amortisation, as a percentage of total video revenue during the year ended 31 December 2006 remained at a similar level as during the year ended 31 December 2005.

General and administrative expenses

General and administrative expenses increased by 16.7% from EUR 5.4 million for the year ended 31 December 2005 to EUR 6.3 million during the year ended 31 December 2006. General and administrative expenses as a percentage of total revenue decreased to 4.4% for the the year ended 31 December 2006, from 5.0% for the year ended 31 December 2005.

EBITDA

As a result of the factors described above, the earnings before interest tax depreciation and amortisation (EBITDA) increased by 30% from EUR 24.0 million for the year ended 31 December 2005 to EUR 31.2 million for the year ended 31 December 2006.

Depreciation and amortisation

Depreciation and amortisation expenses increased by 14.9% from EUR 12.1 million for the year ended 31 December 2005 to EUR 13.9 million for the year ended 31 December 2006. This is due to the operation of the Company's new multiplex screens opened during 2005 and 2006

Operating profit

As a result of the factors described above, the net sales result increased by 45.4% from EUR 11.9 million during the year ended 31 December 2005 to EUR 17.3 million during the year ended 31 December 2006.

Financial income/expenses

The balance of financial income and expenses resulted in a net expense of EUR 4.7 million during the year ended 31 December 2006 compared to a net expense of EUR 2.8 million during the year ended 31 December 2005. This net increase is mainly due to the net effect of (1) an increase in average borrowings in local currencies throughout 2005 and 2006 due to the financing of the development plans in Poland and in Israel, (2) a reduction in interest income on loans to non-consolidated subsidiaries explained by the sale of the investment in Sadyba Best Mall in May 2005 whereby the loan was fully redeemed, and (3) exchange rates differences.

Income tax

The income tax charge as a percentage of profit before income tax was 10.9% in the current year compared to 13.4% in the previous year.

Minority interests

Minority interests for the years ended 31 December 2006 and 31 December 2005 comprised the share of minority shareholders in losses from subsidiaries that are not 100% owned by the Company (EUR 0.5 million and EUR 0.2 million respectively).

Directors' report

Net income

As a result of the factors described above, the Company realised a net income of EUR 11.7 million during the year ended 31 December 2006 compared to net income of EUR 7.9 million during the year ended 31 December 2005.

Financial condition

Liquidity and capital resources

The Company funds its day-to-day operations principally from the cash flow provided by its operating activities. Such cash flow (not including changes in working capital) totalled EUR 23.5 million and EUR 19.7 million for the years ended 31 December 2006 and 2005, respectively. The difference between the Company's net income and its cash flow from operating activities (excluding the changes in working capital) is principally due to the Company's depreciation and amortisation expenses of EUR 14 million and EUR 12.1 million in 2006 and 2005, respectively, which are non-cash expenses. The periods between the receipt of cash from theatre operations and the use of that cash to pay the related expenses, together with the Company's collection of VAT, which is paid to the tax authorities between 15 and 45 days from the date of collection, allow the Company to operate in its day-to-day business from a negative working capital position.

Capital expenditure

The Company maintains a dynamic and flexible approach to developing its theatre projects whereby it will generally seek to lease theatres rather than to purchase them. The Company, however, will consider owning a multiplex if strategically desirable.

The Company's capital expenditures (including investment in subsidiary companies and net of proceeds from investments sold) aggregated EUR 26.7 million and EUR 13.5 million during 2006 and 2005, respectively. The Company has funded its capital expenditures principally from cash flow generated by its operating activities and bank borrowings. The Company's net cash flow provided by financing activities for the years ended 31 December 2006 and 2005 amounted to EUR 45.4 million and EUR 0.6 million negative, respectively. The large amount of cash flow provided by financing activities for the year ended 31 December 2006 is primarily explained by the net proceeds of the Company's initial public offering in December 2006 (EUR 46.5 million).

Asset and capital structure

The Company has historically financed the majority of its development to date through loans from Bank Leumi in Israel. The Company's local subsidiaries in Central Europe, mainly in Poland, have financed a growing part of their projects using financing provided by local banks, while providing securities such as mortgage of the assets of the financed projects, mortgage of the shares and assignments of the local subsidiaries revenues and insurance policies.

Debt and operational debt

As of 31 December 2006, the Company's total debt to banks amounted to EUR 91.4 million (2005: EUR 92.2 million). Taking into account the Company's liquid funds at 31 December 2006 amounting to EUR 53.2 million (31 December 2005: EUR 5.2 million), the net debt position of the Company amounted

Directors' report

to EUR 38.1 million at the end of 2006 (end of 2005: EUR 87 million). Out of this net debt, EUR 4.6 million was used to finance non-operational assets (construction in progress) and non-operational cinema equipment.

The Company's non-operational assets and cinema equipment consist mainly of investments in theatres under development (EUR 1 million), and investments in IMAX® and cinema equipment (EUR 3.6 million).

Equity and gearing

The Group's capital structure is as follows:

	31 December	
	2006	2005
	EUR (thousands)	
Cash and cash equivalents	53,194	5,167
Short-term bank deposits	-	-
Total liquid funds	53,194	5,167
Bank debt:		
Long-term borrowings, including current portion*	(76,290)	(83,865)
Short-term bank credit	(15,086)	(8,322)
Total debt	(91,376)	(92,187)
Net debt	(38,182)	(87,020)
Operational debt:		
Net debt	(38,182)	(87,020)
Construction in progress (see Note 5)	1,015	5,758
Cinema equipment not operated yet (see Note 5)	3,620	7,731
Loan to unconsolidated subsidiaries	-	-
Net debt financing operational and consolidated assets	(33,547)	(73,531)
Total equity	(132,176)	(73,117)
Total capital employed	(165,723)	(146,648)
Total balance sheet	257,460	202,021
EBITDA	31,248	24,023
Gearing (net debt/total equity)	28.9%	119%
Net debt/total capital employed	23%	59.3%
Total equity/total balance sheet	51.3%	36.2%
Net debt/EBITDA	1.22	3.62
Operational debt/EBITDA	1.07	3.06

* including line of credit from bank leumi Israel in the amount of EUR 32,122 thousands which was repaid in 2007. The repayment was funded by the proceeds from issuing of new shares.

Directors' report

The Company's debt profile is as follows:

	31 December	
	2006	2005
	EUR (thousands)	
Current:		
Short-term bank credit	15,086	8,322
Current portion of long - term loans	10,551	9,977
	25,637	18,299
Non-current:		
Long-term loans, net of current portion	65,739	73,888
	91,376	92,187

Employees

The average number of personnel employed by the Company and its subsidiaries – on a full – time equivalent basis - increased from 1,450 in 2005 to 1,509 in 2006. The increase is attributable to an increase of personnel in Central Europe largely as a result of expanded activities in that region, mainly in Bulgaria and Poland.

Outlook for the year 2007

In 2007, the Company plans to open approximately 100 additional screens throughout its territories. These include the following projects (in addition to the purchase of 18 screen multiplex cinema in Poznań that previously had been operated by the Kinopolis Group - see page 13):

- The Company has 4 new multiplexes scheduled to be opened in Poland in 2007, all related to projects currently under construction. These 4 multiplexes, with 32 screens in total, are located in Lublin, Sosnowicz, Rybnik and Gliwice. Currently, the Company expects to open at least 3 of these multiplexes by mid-year.
- The Company is developing a “megaplex” project in Budapest, Hungary, which will become the Company's largest theatre to date, with 24 screens and an IMAX® theatre. The project, scheduled to open in the second half of the year, is being built on leased space as part of a new shopping mall and entertainment centre that is now under construction.
- In Romania, the Company has recently signed lease agreements for three multiplexes in key cities, and currently plans to open at least two of these multiplexes by the end of the year 2007. These three multiplexes are in addition to the leases previously signed by the Company for three multiplex theatres in Bucharest, scheduled to open in 2008.
- The Company has one multiplex site under development in Israel scheduled to be opened during 2007.
- The Company has one multiplex site under development in the Czech Republic scheduled to be opened during 2007.

Directors' report

Considering the proceeds of the share issue and the group's liquidity and solvency position as at the end of 2006, the Company believes that the planned completion of the above mentioned developments is realistic.

Additional information to the report

Major shareholders

To the best of the Company's knowledge as of the date of publication of short report for the year ended 31 December 2006(28 February 2007), the following shareholders are entitled to exercise over 5% of voting rights at the General Meeting of Shareholders in the Company:

	As of 28 February 2007 Number of shares/ % of shares	Increase/ (decrease) Number of shares	As of 31 December 2006 Number of shares/ % of shares	Increase/ (decrease) Number of shares	As of 30 September 2006 Number of shares/ % of shares
I.T. International Theaters Ltd.,	32,709,996 / 64.49%	-	32,709,996 / 64.49%	(2,349,652)	35,059,648/ 86.09%
ING Nationale - Nederlanden Polska Otwarty Fundusz Emerytalny	2,616,914 / 5.2%	330,937	2,285,977 / 4.50%	2,285,977	-

Changes in ownership of shares and rights to shares by Management Board members in the fourth quarter of 2006 and until the date of publication of the report

Changes in ownership of shares and rights to shares by the Management Board members are specified below:

Shares

	As of 28 February 2007 Number of shares/ % of shares	Increase/ (decrease) Number of shares	As of 31 December 2006 Number of shares/ % of shares	Increase/ (decrease) Number of shares	As of 30 September 2006 Number of shares/ % of shares
Moshe Greidinger*	11,566,255 / 22.8%	-	11,566,255 / 22.8%	(2,577,431)	14,143,686 / 34.7%
Amos Weltsch	-	-	-	(600,000)	600,000 / 1.47%
Israel Greidinger*	11,566,255 / 22.8%	-	11,566,255 / 22.8%	(2,577,431)	14,143,686 / 34.7%

*The shares held by Messrs Moshe and Israel Greidinger are held indirectly through I.T. International Theaters Ltd.

Rights to shares

The members of the Management Board did not own or receive any rights to shares in the Company during the period 30 September 2006 until 28 February 2007.

Directors' report

Additional information to the report (cont'd)

Changes in ownership of shares and rights to shares by Supervisory Board members in the fourth quarter of 2006 and until the date of publication of the report

The members of the Supervisory Board did not own any shares and/or rights to shares in the Company during the period 30 September 2006 until 28 February 2007.

Changes in the composition of the Supervisory Board

During an Extraordinary General Meeting of Shareholders held in November 2006, Mr. Yair Shilhav was appointed member of the Supervisory Board of the Company. The appointment came into force with immediate effect.

Capital structure, restrictions regarding shareholder rights and issue of new shares in the Company

The share capital of the Company consists of ordinary shares only, whereby one share represents one vote. There are no restrictions in respect of exercising rights attached to the shares by any shareholder except for the restriction on a transfer of shares in the Company during specified period which has been agreed with certain shareholders as described on page 14. The Company can only issue shares pursuant to a resolution of the General Meeting of Shareholders for a fixed number of shares and for a fixed period not exceeding 5 years. Such decision can only be taken upon a proposal by the Management Board subject to approval by the Supervisory Board.

Risk factors

The risks that may affect the Company's business, financial condition, operating results and corporate structure can be summarized as follows:

A. Risks Related to the Company's Business and Industry

- A lack of motion picture production and poor performance of motion pictures would have a negative effect on film attendance
- The Company is subject to uncertainties relating to its future expansion plans, including its ability to identify suitable site locations
- The Company is subject to risks related to the development of real estate
- A prolonged economic downturn could have a material adverse effect on the Company's business and results of operations by reducing consumer spending in its industry
- A deterioration in relationships with film distributors could adversely affect the Company's ability to obtain commercially successful films
- An increase in the use of alternative film distribution channels, such as home theatre video and the Internet, and other competing forms of entertainment may drive down movie theatre attendance and limit ticket prices
- The Company is subject to uncertainties related to new technologies, including the potentially high costs of re-equipping theatres
- Changes in laws could adversely affect the Company
- The Company's results of operations may fluctuate on a seasonal basis and may be unpredictable

Directors' report

Additional information to the report (cont'd)

Risk factors (cont'd)

A. Risks Related to the Company's Business and Industry (cont'd)

- The loss of services of one or more members of the Company's senior management team could adversely affect the Company's business, results of operations and its ability to effectively pursue its business strategy
- The Company may not be able to sustain and grow ancillary revenue streams
- Covenants in debt agreements concluded by the Company may restrict its ability to borrow and invest, which could affect flexibility to operate and ability to expand
- The Company is subject to additional risks relating to its operations in Israel
- Political, economic and legal risks associated with countries in emerging markets, including Central and Eastern Europe, could adversely affect the Company's financial condition and results of operation
- Accession to the European Union in May 2004 by a number of Central European countries, including Hungary, the Czech Republic and Poland, may lead to uncertainty in the regulatory environment in which the Company operates
- The Company's operations may be subject to limitations imposed by antimonopoly regulations
- The Company faces competition that may adversely affect its business
- The Company could be negatively affected if certain copyright claims against it are successful
- Terms of leases and lease renewal
- The Company is subject to currency-related and interest rate risks
- Uninsured and underinsured losses

B. Risks Related to the Company's Corporate Structure

- The interests of the Company's controlling shareholder may conflict with those of minority shareholders
- Exercise of certain shareholders' rights and tax treatment for non-Dutch investors in a Dutch company may be more complex and costly

Directors' report

Additional information to the report (cont'd)

Representation concerning accounting policies

Management Board confirms that, to the best knowledge, consolidated financial statements together with comparative figures, has been prepared according to all applicable accounting standards and give a true and fair view of the state of affairs of the Group at the end of the year and of the profit or loss of the Group for the period then ended.

Management Discussion and Analysis in this annual report shows true view of the state of affairs of the Group, including evaluation of major risks and uncertainties.

Representation concerning election of the Company's auditor

The Company's auditor has been elected according to applicable rules and that the audit firm and its chartered accountants engaged in the audit of the financial statement of Cinema City International N.V. meet the objectives to present an objective and independent report.

Other

As of 31 December 2006, the Group has guarantees for loans that in total amount to EUR 12 million and Polish zloty 115.5 (EUR 29.9) million in connection with loans provided to subsidiaries.

As of 31 December 2006, the Group has no litigations for claims or liabilities that in total exceed 10% of the Group's equity.

The following net movements in the Group's provisions took place during the financial year 2006:

- an increase in the provision for deferred tax liabilities of EUR 272,000;
- a decrease in the provision for accrued employee retirement rights of EUR 866,000;
- a decrease in the provision related to onerous lease contracts of EUR 1,608,000.

The Management Board

Moshe J. (Mooky) Greidinger
President of the Board
General Director

Amos Weltsch
Management Board
Operational Director

Israel Greidinger
Management Board
Financial Director

Rotterdam, 18 April 2007



To: the Shareholders of Cinema City International N.V.

AUDITOR'S REPORT

Report on the financial statements

We have audited the accompanying financial statements for the year ended 2006 of Cinema City International N.V., Rotterdam. The financial statements consist of the consolidated financial statements and the company financial statements. The consolidated financial statements comprise the consolidated balance sheet as at 31 December 2006, the consolidated profit and loss account, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The company financial statements comprise the company balance sheet as at 31 December 2006, the company profit and loss account for the year then ended and the notes.

Management's responsibility

Management is responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code, and for the preparation of the directors' report in accordance with Part 9 of Book 2 of the Netherlands Civil Code. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of the financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on the financial statements based on our audit. We conducted our audit in accordance with Dutch law. This law requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

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

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

KPMG Accountants N.V. KPMG Accountants N.V., registered under number 33263683 with the Chamber of Commerce in Amsterdam, is a member of KPMG International, a Swiss cooperative.



Opinion with respect to the consolidated financial statements

In our opinion, the consolidated financial statements give a true and fair view of the financial position of Cinema City International N.V. as at 31 December 2006, and of its result and its cash flow for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Netherlands Civil Code.

Opinion with respect to the company financial statements

In our opinion, the company financial statements give a true and fair view of the financial position of Cinema City International N.V. as at 31 December 2006, and of its result for the year then ended in accordance with Part 9 of Book 2 of the Netherlands Civil Code.

Report on other legal and regulatory requirements

Pursuant to the legal requirement under 2:393 sub 5 part e of the Netherlands Civil Code, we report, to the extent of our competence, that the Directors' report is consistent with the financial statements as required by 2:391 sub 4 of the Netherlands Civil Code.

Amstelveen, 18 April 2007

KPMG ACCOUNTANTS N.V.

P. Mizrachy RA

KPMG Accountants N.V. KPMG Accountants N.V., registered under number 33263683 with the Chamber of Commerce in Amsterdam, is a member of KPMG International, a Swiss cooperative.

Consolidated Balance Sheet

	Note	31 December	
		2006	2005
		EUR (thousands)	
ASSETS			
FIXED ASSETS			
Intangible fixed assets	4	719	198
Property and equipment, net	5	170,554	166,610
Deferred tax asset	25	796	1,057
Investment in associates	6	-	2,283
Total fixed assets		172,069	170,148
CURRENT ASSETS			
Inventories	7	3,919	2,998
Receivables			
Trade accounts receivable	8	11,642	7,083
Receivable from related parties	26	1,846	1,702
Income taxes receivable		423	105
Other accounts receivable and prepaid expenses	9	10,642	14,763
Total receivables		24,553	23,653
Securities			
Marketable securities		56	55
Non-marketable securities held for sale	10	3,669	-
Total securities		3,725	55
Liquid funds			
Cash and cash equivalents	11	53,194	5,167
Total liquid funds		53,194	5,167
Total current assets		85,391	31,873
TOTAL ASSETS		257,460	202,021

See accompanying notes to the Consolidated Financial Statements.

Consolidated Balance Sheet

	Note	31 December	
		2006	2005
		EUR (thousands)	
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY			
	12		
Share capital		507	407
Share premium reserve		89,945	43,553
Accumulated currency translation adjustment		4,967	4,158
Retained earnings		36,757	24,999
Total equity attributable to equity holders of the Company		132,176	73,117
Minority interests	14	(895)	(411)
Total equity		131,281	72,706
LONG-TERM LIABILITIES			
Long-term loans, net of current portion	17	65,739	73,888
Accrued employee retirement rights, net	15	41	907
Deferred tax liabilities	25	2,190	1,918
Provision related to onerous lease contracts	16	5,173	6,781
Other long-term payables	20(1)h	2,358	2,767
Income received in advance		91	182
Total long-term liabilities		75,592	86,443
CURRENT LIABILITIES			
Short-term bank credit	18	25,637	18,299
Trade accounts payable		10,740	9,923
Payable to related parties	26	455	437
Employee and payroll accruals		1,303	1,312
Other accounts payable	19	12,452	12,901
Total current liabilities		50,587	42,872
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		257,460	202,021

See accompanying notes to the Consolidated Financial Statements.

Consolidated Income Statement

	Note	For the year ended 31 December	
		2006	2005
		EUR	
(thousands, except per share data and number of shares)			
Revenues	21	143,791	108,181
Operating costs	22	120,167	90,867
Gross margin		23,624	17,314
General and administrative expenses		6,277	5,387
Operating profit		17,347	11,927
Financial income	23	795	2,198
Financial expenses	23	(5,465)	(4,951)
Loss on disposals and write-off of other investments	24	(34)	(151)
Income before result from associates		12,643	9,023
Result from associates		-	(103)
Operating income before taxation		12,643	8,920
Income taxes	25	(1,377)	(1,198)
Net income before minority interests		11,266	7,722
Attributable to:			
Equity holders of the Company		11,738	7,910
Minority interests	14	(472)	(188)
Net income before minority interests		11,266	7,722
Number of average equivalent shares (basic)	13	41,436,329	40,724,000
Net earnings per ordinary share (basic and diluted) of EUR 0.01 each	13	0.28	0.19

See accompanying notes to the Consolidated Financial Statements.

Statement of Changes in Shareholders' Equity

	Share capital	Share premium	Translation reserve	Retained earnings	Total	Minority interest	Total Equity
EUR (thousands) except number of shares							
Balance as of 31 December 2004	407	43,553	(975)	17,089	60,074	(174)	59,900
Net income for the year 2005	-	-		7,910	7,910	(188)	7,722
Foreign currency translation adjustment	-	-	5,133		5,133	(49)	5,084
Balance as of 31 December 2005	407	43,553	4,158	24,999	73,117	(411)	72,706
New shares issued	100	46,392*	-	-	46,492		46,492
Share based payments under the stock option plan	-	-		20	20		20
Net income for the year 2006	-	-		11,738	11,738	(472)	11,266
Foreign currency translation adjustment	-	-	809		809	(12)	797
Balance as of 31 December 2006	507	89,945	4,967	36,757	132,176	(895)	131,281

* After deducting an amount of EUR 4,125 thousands representing the total costs directly attributed to the initial public offering. Those costs represent mainly underwriters' fees, legal, tax and accounting fees, road show, related public relations and marketing costs.

See accompanying notes to the Consolidated Financial Statements.

Consolidated Statement of Recognised Income and Expense

	For the year ended 31 December	
	2006	2005
	EUR (thousands)	
Foreign currency translation adjustment	797	5,084
Net income recognised directly in equity	797	5,084
Profit for the year	11,266	7,722
Total recognised income and expense for the year	12,063	12,806
Attributable to:		
Equity holders of the Parent Company	12,547	13,043
Minority interests	(484)	(237)
Total recognised income and expense for the year	12,063	12,806

See accompanying notes to the Consolidated Financial Statements.

Consolidated Statement of Cash Flows

	For the year ended 31 December	
	2006	2005
	EUR (thousands)	
Cash flows from operating activities		
Net sales result	17,347	11,927
<i>Adjustments to reconcile net income to net cash provided by operating activities:</i>		
Depreciation and amortisation	14,016	12,096
Decrease in value of other assets (including write-offs)	431	367
Decrease in provision related to onerous lease contracts	(1,608)	(1,608)
(Decrease)/increase in accrued employee rights upon retirement, net	(847)	50
Effect of foreign currency exchange and others	1	1
Interest received	781	670
Interest paid	(5,568)	(3,492)
Income taxes paid	(1,050)	(306)
Operating income before working capital	23,503	19,705
Increase in inventories	(1,112)	(309)
Increase in accounts receivable	(3,349)	(1,012)
(Decrease)/increase in prepaid expenses	6,283	(2,004)
Increase in governmental institutions	(2,187)	(693)
Increase in long-term film distribution costs and deferred expenses	(909)	(683)
(Decrease)/increase in accounts payable	7,357	(204)
(Decrease)/increase in employee and payroll accruals	7	(47)
(Decrease) / increase of amount due from related parties	(121)	(133)
Decrease in income received in advance	(88)	(4)
Net cash from operating activities	29,384	14,616
Cash flows from investing activities		
Purchase of property and equipment and other assets ^{*)}	(26,936)	(33,614)
Investment in intangible fixed assets	(1,031)	(198)
Investment in subsidiaries	(71)	164
Acquisition of other investments –held for sale	(3,669)	-
Proceeds from disposition of property and equipment	2,829	6,542
Increase in long-term receivables	-	(2,054)
Short-term bank deposits	-	678
Loans to unconsolidated subsidiaries	-	14,599
Loans to third party	(294)	164
Proceeds from disposition of marketable securities	(2)	132
Proceeds from sale of subsidiaries	2,283	-
Proceeds from disposition of other assets	164	117
Net cash used in investing activities	(26,727)	(13,470)

See accompanying notes to the Consolidated Financial Statements.

^{*)} taking into account movements in investment creditors

Consolidated Statement of Cash Flows (cont'd)

	For the year ended 31 December	
	2006	2005
	EUR (thousands)	
Cash flows from financing activities		
Proceeds from new shares issued	50,637	-
Costs directly attributed to the new shares issued	(4,125)	-
Proceeds from long-term loans	22,967	36,623
Repayment of long-term loans	(30,640)	(40,927)
Increase in long-term payables	(414)	(265)
Short-term bank credit, net increase	6,940	3,945
Net cash provided by/(used in) financing activities	45,365	(624)
Net cash effect due to exclusion of a subsidiary from consolidation	-	(69)
Foreign currency exchange differences on cash	5	177
Increase/(decrease) in cash and cash equivalents	48,027	630
Cash and cash equivalents at beginning of year	5,167	4,537
Cash and cash equivalents at end of year	53,194	5,167

See accompanying notes to the Consolidated Financial Statements.

Notes to the Consolidated Financial Statements

Note 1 - General and principal activities

Cinema City International N.V. (“the Company”) is incorporated in Amsterdam, the Netherlands. The address of the Company is Weena 210-212, 3012 NJ Rotterdam, the Netherlands. The accompanying Consolidated Financial Statements present the financial position, results of operations, changes in shareholders’ equity, and cash flows of the Company and its subsidiaries (together referred to as “the Group”) and the Group’s interest in associates.

The shares of the Company are traded on the Warsaw stock exchange. As at 31 December 2006, 64.5% of the outstanding shares are held by I.T. International Theatres Ltd. (“ITIT”), incorporated in Israel. (31 December 2005 86.09 %).

The Group is principally engaged in the operation of entertainment activities in various countries including Poland, Hungary, the Czech Republic, Bulgaria and Israel. The Company is also engaged in managing and establishing its own entertainment real estate projects for rental purposes, in which the Company operates motion picture theatres. In addition, the Company is involved in short-term and long-term real estate trading in Central Europe. The Company’s business is dependent both upon the availability of suitable motion pictures from third parties for exhibition in its theatres, and the performance of such films in the Company’s markets.

Note 2 – Summary of significant accounting policies

A. Statement of compliance

The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as adopted by the EU as well as in accordance with article 362.9 of the Netherlands Civil Code. The Company has adopted the standards and interpretations with an effective date before 31 December 2006.

The Company’s separate financial statements (the ‘Company Financial Statements’) are prepared in accordance with Part 9 of Book 2 of the Netherlands Civil Code and are taken up on pages 82 through 90.

The financial statements were authorised for issue by the directors on **18 April 2007**.

Notes to the Consolidated Financial Statements

Note 2 - Summary of Significant Accounting Policies (cont'd)

B. Basis of presentation

(1) Measurement basis

The financial statements are presented in euros, rounded to the nearest thousand. They are prepared on the historical cost basis adjusted for the change in the measurement currency. Unless otherwise stated, monetary assets and liabilities are presented at nominal value. Marketable securities are presented at fair value.

(2) Functional and presentation currency

The functional currencies of the operations in Central Europe are the relevant local currencies: the Bulgarian leva, the Czech crown, the Hungarian forint and the Polish zloty. The functional currency of the operations in Israel is the New Israeli shekel (NIS).

The financial statements of the above mentioned foreign operations are translated from the functional currency into euros (presentation currency) for both 2005 and 2006 as follows:

Assets and liabilities, both monetary and non-monetary are translated at the closing exchange rate. Income statement items were translated at the average exchange rate for the year. Foreign exchange differences arising on translation have been recognised directly in equity.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)

C. Exchange rates

Information relating to the relevant euro exchange rates (at year-end and averages for the year):

As of 31 December	Exchange rate of euro				
	Czech crowns (CZK)	Hungarian forints (HUF)	Polish zloty (PLN)	US dollar (USD)	Israeli shekel (NIS)
2006	27.53	252.90	3.86	1.32	5.56
2005	29.00	252.62	3.86	1.18	5.45
Change during the year	%	%	%	%	%
2006	(5.07)	0.11	0.00	11.86	2.02
2005	(4.95)	2.61	(5.62)	(13.24)	(7.30)
Average for year	Exchange rate of euro				
	Czech crowns (CZK)	Hungarian forints (HUF)	Polish zloty (PLN)	US dollar (USD)	Israeli shekel (NIS)
2006	28.37	264.91	3.91	1.26	5.59
2005	29.80	248.54	4.03	1.25	5.58
Change year over year	%	%	%	%	%
2006	(4.80)	6.59	(2.98)	0.80	0.18
2005	(6.73)	(1.42)	(11.03)	0.81	0.00

D. Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions. These judgements, estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)**D. Principles of consolidation**

The Consolidated Financial Statements include the accounts of the Company, its subsidiaries, and jointly controlled entities.

Subsidiaries are those enterprises which are controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the Consolidated Financial Statements from the date that control effectively commences until the date that control effectively ceases.

Jointly controlled entities are those enterprises over whose activities the Company has joint control, established by contractual agreements. The Consolidated Financial Statements include the Company's proportionate share of the enterprises' assets, liabilities, revenues and expenses with items of similar nature on a line-by-line basis, from the date that joint control commences until the date that joint control ceases.

All inter-company accounts and transactions are eliminated when preparing the Consolidated Financial Statements. Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Group's interest in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

A list of the companies whose financial statements are included in the Consolidated Financial Statements and the extent of ownership and control appears in page 80 to these financial statements.

E. Investment in associates

Investment in associates comprise minority interests held by the Group and is accounted for using the equity method.

F. Share capital

Incremental costs directly attributable to the issue or buying back of ordinary shares and to the issue of share options are recognised as a deduction, net of any tax effects, from equity through the share premium reserve.

G. Intangible fixed assets

Intangible fixed assets that are acquired by the Group are stated at cost less accumulated amortisation, calculated over the estimated useful life of the assets, and after impairment losses, if any. The carrying amount of the intangible fixed assets is reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount is estimated as the higher of net selling price and value in use.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)

H. Property and equipment

- (1) Property and equipment are stated at cost less accumulated depreciation and impairment losses. Expenditures for maintenance and repairs are charged to expenses as incurred, while renewals and improvements of a permanent nature are capitalised.
- (2) Depreciation is calculated by means of the straight-line method over the estimated useful lives of the assets.

Annual rates of depreciation are as follows:

	%
Buildings	2 - 3
Cinema equipment	Mainly 10
Leasehold improvements	Mainly 5
Computers, furniture and office equipment	6 - 33
Vehicles	15 - 20
Video movie cassettes and DVDs	50
Video machines	20

- (3) Leasehold improvements are depreciated over the estimated useful lives of the assets, or over the period of the lease, including certain renewal periods, if shorter.
- (4) Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Property and equipment acquired by way of finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation.
- (5) The carrying amount of assets mentioned above is reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the recoverable amount is estimated as the higher of net selling price and value in use.
- (6) Financing expenses relating to short-term and long-term loans, which were taken for the purpose of purchasing or constructing property and equipment, as well as other costs which refer to the purchasing or constructing of property and equipment, are capitalised to property and equipment, in accordance with IAS 23.

I. Impairment of non-financial assets

Assets that have an indefinite useful life, for example land, are not subject to amortisation or depreciation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds the recoverable amount. The recoverable amount is the higher of net selling price and value in use. Non-financial assets that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)**J. Inventories**

Inventories are valued at the lower of cost or net realisable value, and include concession products, spare parts, music cassettes, CDs and video cassettes. Cost is determined by means of the “first in, first out” method. Cost of music cassettes is determined on the basis of the average purchase price. Net realisable value is the estimated selling price during the normal course of business, less the estimated costs of completion and variable selling expenses.

K. Allowance for doubtful accounts

The allowance for doubtful accounts is determined based upon management’s evaluation of receivables doubtful for collection on a case-by-case basis.

L. Marketable securities

The investments in securities held by the Group are classified as trading securities. Trading securities are bought and held principally for the purpose of selling them in the short term and are recorded at fair value. The fair value of investments held for trading is their quoted bid price as of the balance sheet date. Unrealised gains and losses on these securities are included in the income statement. Dividends and interest income are recognised when earned.

M. Non-marketable securities held for sale

Non-marketable securities held for sale comprising investments that are held principally for the purpose of selling them in the short term and are thus classified as held for sale under current assets. These investments are valued at cost less impairment losses, if any. The carrying amount of the non-marketable securities is reviewed at each balance sheet date to determine whether there is any indication of impairment.

N. Cash and cash equivalents

Cash and cash equivalents comprise cash balances and short-term highly liquid investments, that are readily convertible to known amounts of cash, and which are subject to insignificant risks of changes in value.

O. Employee benefits - defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in the income statement as incurred.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)**P. Employee benefits – severance pay**

In certain countries in which the Group operates, employees are entitled to severance pay at the end of their employment. The Group's liability for these severance payments is calculated pursuant to local applicable severance pay laws and employee agreements based on the most recent salary of the employees. The Group's liability for all of its employees is partly provided by monthly deposits with insurance policies and by accruals. The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfilment of the obligation pursuant to local severance pay law or labour agreements. The value of the deposited funds is based on the cash value of these policies, and includes immaterial profits. The unfunded portion of the Group's liability is taken up in the balance sheet as a provision under the heading "Accrued employee retirement rights, net". The provision is stated at present value. During 2006, the company changed the severance pay calculation method from the nominal value to the actuarial method using a discounted cash flow approach. Implementation of the method did not have a material effect on the company's financial statements.

Q. Employee benefits – share options granted

The Group operates a share-based incentive plan. The fair value of share options granted to management and other employees as at the grant date is recognised as an employee expense, with a corresponding increase in equity recognised in Retained earnings, over the period during which the employees become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the actual number of share options that vest.

R. Provision related to onerous lease contracts

During July 2002, the Group acquired a cinema chain in Poland at a discount, which was allocated to the lease agreements of the cinemas acquired. In the financial statements of the Company the discount is presented as a provision related to onerous lease contracts and is released to the income statement over the term of the lease (see also Note 16).

S. Long-term loans

All long-term loans and borrowings are initially recognised at fair value, being the amount of the consideration received net of issue costs associated with the borrowing.

After initial recognition, interest-bearing loans are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognised in profit or loss when the liabilities are derecognised or impaired, as well as through the amortisation process.

For information regarding the fair value of long-term liabilities reference is made to Note 27.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)**T. Revenue recognition**

- (1) Revenues from admission (ticket sales) and concession sales (snack-bars operated by the Company) are recognised when services are provided.
- (2) Revenues from distribution of cinema films are recognised on an accrual basis by a percentage of admissions from the related films.
- (3) Revenues from distribution of films to cable television companies and television stations are recognised over the agreed period for the screening of the film.
- (4) Revenues from sales of video cassettes and DVDs are recognised upon delivery to the customer.
- (5) Revenues from video cassettes and DVD rentals are recognised as the rental services are provided.
- (6) Revenues from “on screen” advertising contracts are included in theatre revenues and are recognised when the related advertisement or commercial is screened, or, in some cases, over the period of the contract.
- (7) Revenues from rental contracts are included in other revenues and are recognised on an accrual basis.
- (8) Revenues from the sale of real estate are included in other revenues and are recognised when the significant risks and benefits of the ownership have been transferred, when the buyer is committed to the purchase, and when the sales price is considered collectible.

U. Cost of revenues

- (1) Cost of theatre sales include direct concession product and joint theatre facility costs such as employee costs, theatre rental and utilities, which are common to both ticket sales and concession operations.
- (2) Cost of films distributed are capitalised until the time the films are distributed for screening. Once the films have been distributed and screening has begun, the costs are amortised at a rate equal to the ratio of revenues in the period to total estimated revenues for the films.
- (3) General advertising expenses are expensed as incurred. Film advertising expenses are expensed when the film is distributed or is shown to the public.

V. Net financing cost

Net financing costs comprise interest payable on borrowings calculated using the effective interest rate method, and interest receivable on funds invested. Foreign exchange gains and losses, and gains and losses that are recognised on hedging instruments are recognised in the income statement. Interest income is recognised in the income statement as it accrues, taking into account the effective yield on the asset.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)**W. Derivative financial instruments**

The Group uses derivative financial instruments to hedge its exposure to foreign exchange rate risks arising from operational and financing activities.

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are stated at fair value with changes being accounted for in the profit and loss account. The fair value of foreign contracts is based on the relevant current exchange rates at balance sheet date.

Where a derivative financial instrument is used to economically hedge the foreign exchange exposure of a recognised monetary asset or liability, no hedge accounting is applied and any gain or loss due to the change in the fair value of the hedging instrument is recognised in the income statement.

X. Income taxes

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year calculated at the applicable local tax rates.

Deferred income tax is provided using the balance sheet liability method on all temporary differences at the balance sheet date between the carrying amounts of assets and liabilities for financial reporting purposes and the tax bases of assets and liabilities. The amount of deferred tax provided is based on the expected timing of the reversal of the temporary differences, using tax rates enacted or substantially enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the unused tax losses and credits can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

Y. Earnings per share

Earnings per share are computed according to IAS 33. The computation of the basic earnings per share is determined on the basis of the weighted average par value of the issued and paid-in share capital outstanding during the year. The Diluted earnings per share is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

Z. Segment reporting

A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

Notes to the Consolidated Financial Statements

Note 2 - Summary of significant accounting policies (cont'd)

AA. New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2006, and have not been applied in preparing these consolidated financial statements:

IFRS 7 -Financial Instruments: Disclosures and the Amendment to IAS 1 Presentation of Financial Statements: Capital Disclosures require extensive disclosures about the significance of financial instruments for an entity's financial position and performance, and qualitative and quantitative disclosures on the nature and extent of risks. IFRS 7 and amended IAS 1, which become mandatory for the Group's 2007 financial statements, will require additional disclosures with respect to Group's financial instruments and share capital.

IFRIC 7 -Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies addresses the application of IAS 29 when an economy first becomes hyperinflationary and in particular the accounting for deferred tax. IFRIC 7, which becomes mandatory for the Group's 2007 financial statements, is not expected to have material impact on the consolidated financial statements.

IFRIC 8 -Scope of IFRS 2 Share-based Payment addresses the accounting for share-based payment transactions in which some or all of goods or services received cannot be specifically identified. IFRIC 8 will become mandatory for the Group's 2007 financial statements, with retrospective application required. The Group has not yet determined the potential effect of the interpretation.

IFRIC 9 -Reassessment of Embedded Derivatives requires that a reassessment of whether embedded derivative should be separated from the underlying host contract should be made only when there are changes to the contract. IFRIC 9, which becomes mandatory for the Group's 2007 financial statements, is not expected to have material impact on the consolidated financial statements.

IFRIC 10 -Interim Financial Reporting and Impairment prohibits the reversal of an impairment loss recognised in a previous interim period in respect of goodwill, an investment in an equity instrument or a financial asset carried at cost. IFRIC 10 will become mandatory for the Group's 2007 financial statements, and will apply to goodwill, investments in equity instruments, and financial assets carried at cost prospectively from the date that the Group first applied the measurement criteria of IAS 36 and IAS 39 respectively. IFRIC 10, which becomes mandatory for the Group's 2007 financial statements, is not expected to have material impact on the consolidated financial statements.

Notes to the Consolidated Financial Statements

Note 3 - Changes in consolidated entities**(I) Changes in consolidated and associated entities during 2006:**

- (a) In May 2006, the Israeli government anti-monopoly office approved the merger of the Company's video retail operations in Israel, which operate under the brand name Video Giant, with its main competitor, Blockbuster. Under the agreement signed between the parties, Video Giant and Kafan Video Libraries Ltd. (operator of the Blockbuster video libraries in Israel) formed a 50/50 joint venture to operate the combined video chain under the brand name Blockbuster. The Company will provide the MD (chief executive officer) for the new JV, while Kafan will provide the chairman of the board. The JV will be jointly controlled between Kafan and the Company and the Company has consolidated the results of operations of this entity proportionally.
- (b) During the first half of 2006, the Company sold its remaining 25% interest in MO Sofia EAD. The Company has received EUR 13.1 million.
- (c) Forum Film Home Entertainment KFT 100% shares - new subsidiary incorporated in Hungary. The company commenced its operation in September 2006 and specialises in video and DVD distribution in Hungary. This distribution company is expected to be the exclusive distributor of the Film DVD activity of 2 major US studios: Warner Bros and Sony (Columbia).
- (d) New age Cinema KFT 100% shares - new subsidiary, incorporated in Hungary. The Company commenced operation in October 2006 and specializes in screen advertising.

(II) Changes in consolidated entities during 2005:

- (a) Forum Hungary Film Distribution KFT - 100% Shares. New subsidiary, incorporated in Hungary. This company commenced operation in February 2005 and specialises in distribution of films in Hungary.
- (b) Per 30 June 2005, the Company, through a subsidiary sold 25% of the shares in MO Sofia EAD after which the Company still holds a further 25% interest in this company.
The Company has provided the buyers with a cost overrun guarantee, to cover its part in any costs of completion of the project exceeding the budget, and has retained the responsibility of the completion.
The remaining 25% interest in MO Sofia EAD is included in the consolidated balance sheet per 31 December 2005 as "Investments in associate" under "Financial fixed assets". In prior years, the 50% interest was proportionally consolidated in the Company's financial statements.
- (c) All Job Poland Sp.z o.o. - 100% shares. New subsidiary, incorporated in Poland. This company commenced operation in November 2005 and specialises in recruitment and employment of the company staff in Poland.

Notes to the Consolidated Financial Statements

Note 4 - Intangible fixed assets

The intangible fixed assets comprise mainly investments in the development of Cinema Megaplex in Israel and are stated at cost less accumulated amortisation and impairment losses, if any.

Composition:

	Financial year 2006			Balance at end of year
	Balance at beginning of the year	Additions during the year	Foreign currency translation adjustments	
	EUR (thousands)			
Cost	966	1,031	(4)	1,993
Accumulated amortisation	768	516	(10)	1,274
Carrying value	198	515	6	719

	Financial year 2005			Balance at end of year
	Balance at beginning of the year	Additions during the year	Foreign currency translation adjustments	
	EUR (thousands)			
Cost	708	198	60	966
Accumulated amortisation	539	181	48	768
Carrying value	169	17	12	198

Notes to the Consolidated Financial Statements

Note 5 - Property and equipment, net

	Financial year 2006				Balance at end of year
	Balance at beginning of the year	Additions during the year	Foreign currency translation adjustments	Sales and disposals during the year	
	EUR (thousands)				
Cost					
Land and buildings (1)	67,666	-	772	(3,367)	65,071
Cinema equipment (1)	68,450	4,696	105	(397)	72,854
Leasehold improvements	77,494	13,573	(119)	(962)	89,986
Computers, furniture and office equipment	10,029	1,055	(176)	(1,319)	9,589
Vehicles	1,187	320	(14)	(257)	1,236
Video movies	9,520	870	(189)	(7,020)	3,181
Video machines	1,138	93	(29)	(1,143)	59
	<u>235,484</u>	<u>20,607</u>	<u>350</u>	<u>(14,465)</u>	<u>241,976</u>
Accumulated depreciation					
Land and buildings	9,674	3,191	132	(705)	12,292
Cinema equipment	30,684	5,660	(71)	(1,044)	35,229
Leasehold improvements	12,478	2,709	(75)	(770)	14,342
Computers, furniture and office equipment	7,129	714	(127)	(998)	6,718
Vehicles	579	154	(8)	(160)	565
Video movies	7,263	906	(178)	(5,736)	2,255
Video machines	1,067	51	(28)	(1,069)	21
	<u>68,874</u>	<u>13,385</u>	<u>(355)</u>	<u>(10,482)</u>	<u>71,422</u>
Carrying value	<u>166,610</u>	<u>7,222</u>	<u>705</u>	<u>(3,983)</u>	<u>170,554</u>

- (1) The balance as of 31 December 2006 includes EUR 1,015,000 construction in progress for entertainment purposes and cinema equipment to an amount of EUR 3,620,000 not operational yet (see also Note 20 (1) b. and c.).

Notes to the Consolidated Financial Statements

Note 5 - Property and equipment, net (cont'd)

	Financial year 2005				Balance at end of year
	Balance at beginning of the year	Additions during the year	Foreign currency translation adjustments	Sales and disposals during the year	
EUR (thousands)					
Cost					
Land and buildings (1)	68,064	8,456	3,320	(12,174)	67,666
Cinema equipment (1)	58,466	8,102	2,682	(800)	68,450
Leasehold improvements	57,184	16,639	3,854	(183)	77,494
Computers, furniture and office equipment	9,173	494	654	(292)	10,029
Vehicles	1,033	179	68	(93)	1,187
Video movies	7,733	1,189	598	-	9,520
Video machines	1,046	9	83	-	1,138
	<u>202,699</u>	<u>35,068</u>	<u>11,259</u>	<u>(13,542)</u>	<u>235,484</u>
Accumulated depreciation					
Land and buildings	6,516	2,711	447	-	9,674
Cinema equipment	24,157	5,208	1,321	(2)	30,684
Leasehold improvements	10,082	1,875	626	(105)	12,478
Computers, furniture and office equipment	6,431	446	463	(211)	7,129
Vehicles	451	147	29	(48)	579
Video movies	5,457	1,341	465	-	7,263
Video machines	811	187	69	-	1,067
	<u>53,905</u>	<u>11,915</u>	<u>3,420</u>	<u>(366)</u>	<u>68,874</u>
Carrying value	<u>148,794</u>	<u>23,153</u>	<u>7,839</u>	<u>(13,176)</u>	<u>166,610</u>

- (1) The balance as of 31 December 2005 includes EUR 5,758,000 construction in progress for entertainment purposes and cinema equipment to an amount of EUR 7,731,000 not operational yet (see also Note 20 (1) b. and c.).

Notes to the Consolidated Financial Statements

Note 6 - Investment in associates

As at 31 December 2005, the Group held a 25% interest in MO Sofia EAD, a company that is involved in the development of a shopping mall in Sofia, Bulgaria. During the first half of 2006, the Group reached an agreement to sell the 25% interest in MO Sofia EAD, for which the Group has received EUR 13.1 million.

As at 31 December 2004, the Group held a 50% interest in this company and therefore the investment was treated as a joint venture and as such was proportionally included in the Group's consolidated financial statements. Towards the end of June 2005, the Group reached an agreement to sell half of its interest in MO Sofia EAD. The joint venture results up to the date of sale (June 2005) of half of the Group's interest in MO Sofia EAD are included in the Group's consolidated income statement. In the consolidated balance sheet as at 31 December 2005, the remaining 25% interest in MO Sofia EAD was no longer proportionally consolidated, and presented under "Investment in associates" in accordance with the net equity method (until the date of the disposition in 2006).

MO Sofia EAD is a private entity that is not listed on any public exchange and therefore there is no quotation price for the fair value of this investment. The reporting date and reporting year of MO Sofia EAD is identical to reporting date and year of the Group.

The following table illustrates summarised information of the investment in MO Sofia EAD and represents the Company's interests in the assets and liabilities of MO Sofia EAD as at 31 December 2005:

	<u>EUR</u> <u>(thousands)</u>
Current assets	683
Non-current assets	9,983
Current liabilities	(2,888)
Non-current liabilities	<u>(5,495)</u>
Net assets	<u><u>2,283</u></u>

Notes to the Consolidated Financial Statements**Note 7 - Inventories**

Composition:

	31 December	
	2006	2005
	EUR (thousands)	
Concession products	970	758
Video cassettes and DVDs	1,127	459
IMAX films inventories	1,592	1,512
Video machines	22	94
Spare parts	208	175
	<u>3,919</u>	<u>2,998</u>

Valuation:

	31 December	
	2006	2005
	EUR (thousands)	
At cost	3,919	2,998
Provision for net realisable value	-	-
	<u>3,919</u>	<u>2,998</u>

All inventories included above are valued at cost.

Note 8 - Trade accounts receivable

Composition:

	31 December	
	2006	2005
	EUR (thousands)	
Trade accounts receivable	11,685	7,111
Allowance for doubtful accounts	(43)	(28)
	<u>11,642</u>	<u>7,083</u>

Notes to the Consolidated Financial Statements

Note 9 - Other accounts receivable and prepaid expenses

Composition:

	31 December	
	2006	2005
	EUR (thousands)	
Government institutions	1,239	3,426
Advances to suppliers	406	568
Prepaid expenses	4,956	5,432
Prepaid cinema film and video film distribution costs (1)	3,050	2,141
Other	991	3,196
	10,642	14,763

- (1) Stated at cost, in respect of video and cinema films which have not yet been distributed, after being reviewed for recoverability - see also Note 20 (1) d.

Note 10 - Non-marketable securities held for sale

In July 2006, the Company signed an agreement to acquire, together with its original Mall of Sofia partner, 60% of a Bulgarian company whose main asset is a parcel of land in Plovdiv, Bulgaria. Plovdiv is one of the largest secondary cities in Bulgaria. The investment is measured at the lower of their carrying amount and fair value less cost to sell, since the investment is acquired and held exclusively with a view to its subsequent disposal. The Company plans to sell the shopping centre while maintaining the lease of the multiplex theatre. Above acquisition is similar to the Mall of Sofia project (without an office complex), until the sale is completed the Company plans to develop a modern shopping and entertainment centre on this parcel, which will include a multiplex theatre.

This item includes a loan in the amount of EUR 333 thousands to the mentioned Bulgarian company. The loan is denominated in Euro and bear annual interest at the rate of 5%. The loan is due to be repaid upon the sale of the project in Plovdiv.

Note 11 - Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and in hand and short-term deposits freely available for the Group. The short-term deposits have an original maturity varying from one day to three months.

Composition:

	31 December	
	2006	2005
	EUR (thousands)	
Cash at bank and in hand	2,885	2,915
Short-term deposits	50,309	2,252
	53,194	5,167

Cash at bank and in hand earns interest at floating rates based on daily bank deposit rates. Short-term deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates. The fair value of the cash and cash equivalents is EUR 53,194,000 (2005: EUR 5,167,000).

Notes to the Consolidated Financial Statements

Note 12 - Shareholders' equity

a. Share capital

The authorised share capital of the Company consists of 175,000,000 shares of EUR 0.01 par value each.

The number of issued and outstanding ordinary shares as at 1 January 2005 was 40,724,000 and has remained unchanged during the financial year ended 31 December 2005. At 5 December 2006, as part of the Initial Public Offering of the Company's shares, the Company issued 10,000,000 ordinary shares. As a result of the share issue in 2006, the total number of shares issued and outstanding at 31 December 2006 totalled 50,724,000.

All shares issued and outstanding at 31 December 2006 have been fully paid up. Ordinary shares entitle one vote per share and participation in payments of dividends.

b. Share premium reserve

	Financial year	
	2006	2005
	EUR (thousands)	
Balance at beginning of the year	43,553	43,553
Net proceeds of new shares issued in excess of par value*	<u>46,392</u>	<u>-</u>
Balance at end of the year	<u><u>89,945</u></u>	<u><u>43,553</u></u>

* After deducting an amount of EUR 4,125 thousands representing the total costs directly attributed to the initial public offering. Those costs represent mainly underwriters' fees, legal, tax and accounting fees, road show and related public relations and marketing costs.

Notes to the Consolidated Financial Statements

Note 12 - Shareholders' equity (cont'd)

c. Share options

In December 2006 and as part of the successful initial public offering, a new long-term incentive plan (the "Plan") was implemented. The persons eligible for participation in the Plan are the employees of the Group, including the members of the Management Board. Under the Plan, share options are granted to members of the Management Board and selected employees. The exercise price of the granted options determined by the Supervisory Board on the date of granting the share options and shall not be less than the fair market value at the time of the grant of the options. Options are conditional on the employee being employed or Board member being in office at the time the Options are exercisable (vesting period). Options granted shall vest over three years after the date of the grant: one third vesting after one year, one third vesting after two years and one third vesting after three year. The options have a contractual option term of ten years.

On 6 December a total number of 477,000 options with an exercise price of EUR 5.05 each, vesting in 3 years and having an option term of 4 years, were granted to certain employees of the Group. Members of the Management Board did not receive any options during 2006. The vesting dates of the options are as follows:

	Number of options
6 December 2007	159,000
6 December 2008	159,000
6 December 2009	159,000
	<u>477,000</u>

The weighted average fair value of options granted in 2006 using the Black-Scholes valuation model was approximately EUR 1 per option. The significant inputs into the model were a weighted average share price of EUR 5.05 at the grant date, the exercise price mentioned above, volatility of 20%, dividend yield of 0%, an option life of 4 years and an annual risk free rate of 4%.

The impact of the share-based payment on the financial statements of the Company was an expense of EUR 20,000 recognised in the income statement with a corresponding increase in equity.

During 2006 no options were forfeited or exercised.

Notes to the Consolidated Financial Statements

Note 13 - Net earnings per share

The calculation of basic and diluted net earnings per share at 31 December 2006 was based on the profit attributable to ordinary shareholders of EUR 11,738,000 (2005: EUR 7,910,000) and a weighted average number of ordinary shares outstanding as presented below:

Weighted average number of ordinary shares (basic):

	Financial year	
	2006	2005
	number of shares	
Balance at beginning of the year	40,724,000	40,724,000
Effect of shares issued in December 2006	712,329	-
Balance at end of the year	<u>41,436,329</u>	<u>40,724,000</u>

Weighted average number of shares (diluted):

	Financial year	
	2006	2005
	number of shares	
Weighted average number of ordinary shares (basic)	41,436,329	40,724,000
Effect of shares options on issue	30,831	-
Balance at end of the year	<u>41,467,160</u>	<u>40,724,000</u>

Note 14 - Minority interests

	Financial year	
	2006	2005
	EUR (thousands)	
Balance at beginning of the year	(411)	(174)
Minority interests in (losses)/earnings of		
Consolidated subsidiaries	(472)	(188)
Translation adjustments	(12)	(49)
Balance at end of the year	<u>(895)</u>	<u>(411)</u>

The minority Shareholders are committed to cover any deficits and losses realised by the relevant subsidiaries to the extent of their interest in these subsidiaries.

Notes to the Consolidated Financial Statements

Note 15 - Accrued employee retirement rights

- a. According to the relevant laws, the Company's subsidiaries in Europe are required to deposit amounts, on a monthly basis, to retirement and pension funds on behalf of their employees, and therefore have no such liabilities towards them.
- b. Local applicable labour laws and agreements require group companies to pay severance pay to dismissed or retiring employees (including those leaving their employment under certain other circumstances). The calculation of the severance pay liability was made in accordance with labour agreements in force and based on salary components that, in Management's opinion, create entitlement to severance pay. Group companies' severance pay liabilities to their employees are funded partially by regular deposits with recognised pension and severance pay funds in the employees' names and by purchase of insurance policies and are accounted for as if they were a defined contribution plan. The amounts funded as above are netted against the related liabilities and are not reflected in the balance sheets since they are not under the control and management of the companies.
- c. The amounts of the liability for severance pay presented in the balance sheets (see (d) below) reflect that part of the liability not covered by the funds and the insurance policies mentioned in (b) above, as well as the liability that is funded by deposits with recognised central severance pay funds held under the name of the Company's subsidiaries.
- d. The cost of severance provision is determined according to the actuarial method, the projected unit credit method. It has been calculated using a discounted cash flow approach. The calculations are based on the following financial assumptions:

Discount at 31 December	3.66%
Expected return on plan assets at 1 January	3%

- e. The provision for accrued employee rights upon retirement, net, comprises:

	31 December	
	2006	2005
	EUR (thousands)	
Present value of unfunded obligation	978	1,896
Less: fair value of plan assets	(937)	(989)
	<u>41</u>	<u>907</u>

Notes to the Consolidated Financial Statements

Note 15 - Accrued employee retirement rights (cont'd)

- f. The movements in the provision for accrued employee rights upon retirement during the financial year is as follows:

	Financial year 2006		
	Gross amount	Amount deposited	Net amount
	EUR (thousands)		
Balance at beginning of the year	1,896	(989)	907
Translation difference	(40)	21	(19)
Monthly payments to deposit	-	31	31
Net movement in provision			
Charged to net profit	(878)	-	(878)
Balance at end of the year	<u>978</u>	<u>(937)</u>	<u>41</u>

	Financial year 2005		
	Gross amount	Amount deposited	Net amount
	EUR (thousands)		
Balance at beginning of the year	1,662	(868)	794
Payments made upon retirement	132	(69)	63
Monthly payments to deposit	-	(52)	(52)
Net movement in provision			
Charged to net profit	102	-	102
Balance at end of the year	<u>1,896</u>	<u>(989)</u>	<u>907</u>

Notes to the Consolidated Financial Statements

Note 16 - Provision related to onerous lease contracts

In July 2002, the Group purchased four multiplex cinemas in Poland from Ster Century Europe Limited. The multiplexes comprised a total of 46 screens and approximately 10,000 seats. As part of the transaction, the Group acquired all of the shares of Ster Century Europe's Polish subsidiaries, and purchased shareholder loans provided to these subsidiaries, for a total consideration of approximately EUR 19 million (USD 20 million). The acquisition also involved the assumption of certain long-term lease contracts with onerous terms, expiring in 2009 to 2010. A provision of EUR 12,731,000 (USD 13,369,000), relating to these onerous lease contracts, which the acquired subsidiaries were party to prior to the acquisition, has been recorded as part of the acquisition.

The provision is amortised over the non-cancellable periods of the lease contracts. Amortisation in 2006 amounted to EUR 1,608,000 (2005: EUR 1,608,000) and was credited to the lease expenses under operating expenses.

Movements:

	Financial year	
	2006	2005
	EUR (thousands)	
Balance at beginning of the year	6,781	8,389
Amortisation during the year	(1,608)	(1,608)
Balance at end of the year	<u>5,173</u>	<u>6,781</u>

Notes to the Consolidated Financial Statements

Note 17 - Long-term loans

A. Composition:

	Interest rates	31 December	
		2006	2005
		EUR (thousands)	
	%		
In CZK	(1)	4,980	8,452
In EUR	(2)	47,052	55,563
In USD	(3)	-	29
In NIS	(4)	133	402
In PLN	(5)	24,087	19,377
Loan from minority interest holder	(6)	38	42
		76,290	83,865
Less - current portion		10,551	9,977
		65,739	73,888

- (1) PRIBOR + 2%
(2) EURIBOR + 1.5% - 2%
(3) LIBOR + 1% - 1.75%
(4) 5.7%, linked to the Israeli CPI
(5) 7.1%.
(6) In USD, bearing no interest.

The interest rates shown concern the rates per the end of the appropriate financial years.

B. The loans mature as follows:

	31 December	
	2006	2005
	EUR (thousands)	
First year - current maturities	10,551	9,977
Second year	12,349	9,986
Third year	9,682	11,834
Fourth year	9,750	9,286
Fifth year	9,823	9,536
Sixth year and thereafter	13,367	24,607
Undefined	10,768	8,639
	76,290	83,865

C. Liens - see Note 20 (2).

Notes to the Consolidated Financial Statements

Note 18 - Short-term bank credit

Composition:

	Interest rates	31 December	
		2006	2005
	%	EUR (thousands)	
Current maturities	See Note 17	10,551	9,977
<i>Short-term bank credit:</i>			
Unlinked (NIS)	(1) 5.9%	15,086	8,322
		<u>25,637</u>	<u>18,299</u>

(1) Variable

The interest rate shown concerns the rate per 31 December 2006.

Note 19 - Other accounts payable

Composition:

	31 December	
	2006	2005
	EUR (thousands)	
Investment creditors	279	7,411
Accrued expenses	5,294	2,986
Government institutions	895	323
Advances and income received in advance (1)	1,712	2,075
Other	4,272	106
	<u>12,452</u>	<u>12,901</u>

(1) Consist mainly of advances received from several customers, for feature video rentals and film distribution.

Notes to the Consolidated Financial Statements

Note 20 - Commitments, contingent liabilities and liens

(1) Commitments

- a. The Company and its subsidiaries conduct most of their cinema, video library stores and corporate operations in leased premises. These leases, which have non-cancellable clauses, expire at various dates after 31 December 2006. Many leases have renewal options. Most of the leases provide for contingent rentals based on the revenues of the underlying cinema or video library stores, while certain leases contain escalating minimum rental provisions. Most of the leases require the tenant to pay city taxes, insurance, and other costs applicable to the leased premises.

Future minimum lease payments under non-cancellable operating leases from third parties for the years after 31 December 2006 are as follows:

	EUR
	(thousands)*
2007	12,359
2008	16,312
2009	15,699
2010	14,994
2011	14,826
After 2011	46,013
	120,203

- * Does not include contingent rental, which is subject to the Company's decision to exercise the option to extend the operating lease period.

Future minimum lease payments under non-cancellable operating leases from third parties for the years after 31 December 2005 are as follows:

	EUR
	(thousands)*
2006	14,269
2007	15,025
2008	15,783
2009	15,051
2010	14,624
After 2010	52,538
	127,290

- * Does not include contingent rental, which is subject to the Company's decision to exercise the option to extend the operating lease period.

Notes to the Consolidated Financial Statements

Note 20 - Commitments, contingent liabilities and liens (cont'd)

- a. Rental expenses for theatres are summarised as follows:

	31 December	
	2006	2005
	EUR (thousands)	
Minimum rental	15,038	12,514
Contingent rental	-	31
	<u>15,038</u>	<u>12,545</u>

- b. The Group is party to a master agreement with a developer, Control Centres Ltd. ("Control Centres"), for the construction of theatre sites in shopping malls and other commercial centres throughout Hungary, Poland and the Czech Republic. Under this agreement, the Company has opened 18 multiplexes that are already operating in shopping malls in Central Europe.
- c. As at 31 December 2006, the Group has unpaid commitments to invest in the development of properties of approximately EUR 10 million and further commitments to acquire equipment of approximately EUR 21.5 million in connection with the development of new systems and movie theatres. In addition, the Group is committed to pay a percentage of its revenues from movie systems, subject to a minimum monthly cost per system.
- d. In consideration for its rights to be the exclusive distributor of their films in Israel, Poland and Hungary, subsidiary companies are committed to pay fees to certain producers based on a percentage of its revenues (or in some cases, specific profits) from the films. In some cases, a minimum fee has been determined.
- e. Ya'af Network, a subsidiary company, and later as part of Kafan Et Anak partnership (see note 3.I) has agreements for the rental of video library stores, and for the rental of space for video mats, which it uses in its operations. The rental terms pursuant to these agreements (including renewal options) granted for periods of one to ten years. The rental expenses relating to these agreements are calculated as a lump-sum linked either to the Israeli CPI or to the US dollar, or as a percentage of the turnover. Annual rent expenses for 2006 amounted to EUR 700,000.
- f. Subsidiary companies signed agreements with third parties in Israel, Poland and Hungary. According to these agreements, the subsidiary companies grant the third parties exclusive broadcasting rights on Israeli, Polish and Hungarian television for specific movies. These rights are for various periods and will end during the years 2007 - 2008.
- g. Movie films are typically licensed from film distributors representing film production companies. Film exhibition licences typically specify rental fees based upon a gross receipts formula, which is negotiated on a movie-by-movie basis in advance of distribution. The fees are generally related to the anticipated performance of the movie based on the distributor's experience in other markets, if possible. Under such a formula, the distributor receives a specified percentage of box office receipts, with the percentage declining over the term of the run.

Notes to the Consolidated Financial Statements

- h. Lease contracts of certain cinema equipment of IMAX® systems are classified as finance lease and as such the equipment is included in Property and equipment under Cinema equipment. The total of the lease obligation at 31 December 2006 amounted to EUR 2,358,000 (31 December 2005: EUR 2,767,000), and is classified as Other long-term payables. The capital lease is bearing 7% annual interest. The lease term expires on 31 December 2020, after which the ownership will be transferred to the Company.

(2) Liens

- a. As part of a restructuring of activities in 2003, the Company has assumed the majority of the Group's bank debt, provided originally via ITIT. Based on the agreement between the Company and ITIT of December 2003, the bank will provide the Company with loans, which will be used to pay back ITIT's loans to the bank. In order to secure the Company's liabilities for such bank credits and loans in the amount of approximately EUR 43 million, the Company has provided the bank the following: (i) a registered first degree fixed lien on IT-2004's (the Israeli subsidiary) outstanding share capital and goodwill; (ii) a first degree floating lien on IT-2004's assets, including insurance benefits in respect of the assets and rights of any kind which ITIT has or will have in the future; (iii) that the assets of IT-2004 will not be pledged and the lien cannot be transferred without the agreement of the bank; (iv) ITIT has agreed to guarantee the debt of the Company (v) that certain financial covenants will be fulfilled and maintained.
- b. The local subsidiaries in Poland and the Czech Republic have obtained financing from banks for some of the cinema complex projects. The securities given include: mortgage on the assets of the financed projects, pledge on the shares of the subsidiaries, and an assignment of all revenues and insurance policies of the projects. As 31 December 2006, the Company had issued a guarantee for EUR 12 million to a Polish bank in connection with a loan provided to a subsidiary. In addition, the Company has issued a guarantee for a total amount of PLN 115.5 million to a Polish bank in order to secure several loan agreements with this bank.
- c. In order to secure an outstanding loan from a Hungarian bank of approximately EUR 3.6 million, a subsidiary company has provided to the bank the following: (i) a registered first degree fixed lien on its outstanding share capital and goodwill; (ii) a first degree floating lien on its assets, including insurance benefits in respect of the assets and rights of any kind which the subsidiary has or will have in the future; (iii) that the assets of the subsidiary will not be pledged and the lien cannot be transferred without the agreement of the bank.
- d. In order to secure an outstanding loan from a Bulgarian bank of approximately EUR 3.8 million a subsidiary company has provided to the bank with several commitments such as going concern pledge agreement, trade mark pledge agreement, sponsor support agreement and receivables pledge agreement.

Notes to the Consolidated Financial Statements

Note 20 - Commitments, contingent liabilities and liens (cont'd)

(3) Contingent Liabilities

From time to time, the Group is involved in routine litigation and proceedings during the normal course of business. As of balance sheet date, the Group is not involved in any litigations or proceedings except for the following:

Cinema City Poland Sp.z o.o. a 100% owned by the company, is the defendant in a claim brought by Związek Autorów i Kompozytorów ("Zaiks"), a Polish collection society representing screenplay authors and authors of other literary and musical works used in audiovisual works that are exhibited in Poland. The Company understands that Zaiks has also brought similar claims against every other major cinema exhibitor and cable TV operators in Poland. The claimant seeks royalties in the amount of approximately EUR 2.0 million plus interest for the use of works by certain of its members in movies exhibited in Poland. Based on legal advice, the Management Board does not expect the outcome of the action to have a material effect on the Group's financial position.

Toward the end of February 2007, the Company learned that one of its main Polish competitors lost a similar case before the "second instance" court in Poland. Based on the advice of the Company's lawyers, the Management Board maintains the position that the complaint has no merit and the plaintiff has no standing. The Company will continue to defend the case vigorously.

The Company has accrued for future legal expenses in connection with the case in the balance sheet per 31 December 2006.

Notes to the Consolidated Financial Statements

Note 21 - Revenues

	Financial year	
	2006	2005
	EUR (thousands)	
Theatre sales	99,133	73,641
Distribution	21,905	15,138
Video	4,120	4,877
Other	18,633	14,525
	143,791	108,181

Note 22 – Operating costs

	Financial year	
	2006	2005
	EUR (thousands)	
Cost of theatre sales	72,686	58,077
Distribution operations	19,981	12,349
Video operations	2,920	3,454
Other	10,679	4,891
Depreciation and amortisation	13,901	12,096
	120,167	90,867

Notes to the Consolidated Financial Statements

Note 23 - Financial income/expenses

A. Financial income

	Financial year	
	2006	2005
	EUR (thousands)	
Interest income	406	769
Currency exchange gains	389	1,429
Total financial income	<u>795</u>	<u>2,198</u>

B. Financial expenses

	Financial year	
	2006	2005
	EUR (thousands)	
Interest expenses incurred	(5,246)	(4,472)
Interest cost capitalised (1)	318	999
Other currency exchange losses	(537)	(1,478)
Total financial expenses	<u>(5,465)</u>	<u>(4,951)</u>

- (1) The Company has capitalised interest expenses to the cost of buildings in progress as well as to other fixed assets components before being taken into operation.

Note 24 - Loss on disposals and write-off on other investments

This item comprises a net capital loss on the disposal of property, equipment and other assets (2005: a net capital loss).

Notes to the Consolidated Financial Statements

Note 25 - Income taxes

I. Tax laws applicable to the Group

1. Results of operations for tax purposes of the Company and its Dutch subsidiaries are computed in accordance with Dutch tax legislation.
2. Tax rates applicable to the Company and its subsidiaries are as follows:

<u>The subsidiary</u>	<u>Tax rate</u>
Netherlands	29.6% - (2005-31.5%)
Hungary	16% - (2005-16%)
Czech Republic	24% - (2005- 26%)
Poland	19% - (2005-19%)
Israel	31%- (2005-34%)
Bulgaria	15 %-(2005-15%)

In several countries in which the Group is operating, tax rates will change as of 1 January 2007 as follows:

- Netherlands to 25.5%
- Israel to 29%

3. Tax ruling in Israel

The Group has received a special ruling from the Israeli tax authorities to allow for the transfer of the Israeli activities to IT-2004, and to transfer the shares of all the operating Israeli subsidiaries to the Dutch company. Under the ruling, ITIT has committed not to sell its shares in the Company for a period of four years, and the Company has committed to pay tax in Israel on any future gains on the sale of Israeli subsidiaries.

II. **Deferred income taxes**

1. Deferred income taxes are primarily provided for all temporary differences between the tax and the accounting basis of assets and liabilities based on the tax rate that is expected to be in effect at the time the deferred income taxes will be realised.

Realisation of the deferred income tax assets is dependent upon generating sufficient taxable income in the period that deferred income tax assets are realised. Based on all available information, management believes that all of the deferred income tax assets are realisable and therefore has not provided for valuation allowance.

Notes to the Consolidated Financial Statements

Note 25 - Income taxes (cont'd)

2. Changes in deferred income taxes in relation to tax assets are in respect of the following items:

	31 December	
	2006	2005
	EUR (thousands)	
Accrued employee rights	(148)	(79)
Fixed assets	(108)	(282)
Operating tax loss carry – forwards	(617)	(2,146)
Long-term liabilities	-	1,353
Other	389	574
	<u>(484)</u>	<u>(580)</u>

3. Deferred income taxes in relation to tax liabilities are in respect of the following items:
Deferred income tax included in assets:

	31 December	
	2006	2005
	EUR (thousands)	
Accrued employee rights	19	66
Fixed assets	(49)	17
Operating tax loss carry - forwards	784	667
Other	42	307
	<u>796</u>	<u>1,057</u>

Deferred income tax included in liabilities:

	31 December	
	2006	2005
	EUR (thousands)	
Fixed assets	2,993	2,890
Other	(803)	(972)
	<u>2,190</u>	<u>1,918</u>

III. Income taxes in the income statement comprise:

	Financial year	
	2006	2005
	EUR (thousands)	
Current taxes	653	648
Deferred income taxes	392	550
In respect of previous years	318	-
Effect of reduction in tax rate	14	-
	<u>1,377</u>	<u>1,198</u>

Notes to the Consolidated Financial Statements

Note 25 - Income taxes (cont'd)

IV. Tax reconciliation

The difference between the amount of tax calculated on income before taxes at the regular tax rate and the tax expenses included in the financial statements is explained as follows:

	Financial year	
	2006	2005
	EUR (thousands)	
Tax calculated at the regular rate (2006: 29.6%; 2005: 31.5%)	3,742	2,842
Adjustment for reduced tax rate in foreign subsidiaries	(530)	(221)
Non-deductible expenses	119	115
Effect of tax losses utilised	(704)	360
Income exempt from taxes	(2,388)	(2,608)
Taxes in respect of previous years	318	-
Other differences	820	710
Actual tax charged	<u>1,377</u>	<u>1,198</u>

Note 26 - Related party transactions

Related parties

Parties are considered to be related if one party has the ability to control or exercise significant influence over the other party in making financial and reporting decisions.

Such relationships include:

1. Parent-subsidiary relationships.
2. Entities under common control.
3. Individuals who, through ownership, have significant influence over the enterprise and close members of their families.
4. Key management personnel.

The Group is controlled by I.T. International Theatres Ltd, incorporated in Israel, which owns 64.5% of the outstanding shares (2005- 86.09%) . The remaining 35.5% are held by the public and listed at Warsaw stock exchange. The ultimate parent of the Group is Israel Theatres Ltd, incorporated in Israel. The ultimate controlling parties are Mr Moshe Greidinger and Mr Israel Greidinger, both managing directors of the Company.

Notes to the Consolidated Financial Statements

Note 26 - Related party transactions (cont'd)

Transactions with related parties:

a. Income (expenses):

	Financial year	
	2006	2005
	EUR (thousands)	
Financing	31	-
Rental fees	(495)	(610)
Management services	303	392

- b. In December 2003, employment agreements with Mr Moshe Greidinger, Mr Israel Greidinger, and Mr. Amos Weltsch ("Managing Directors"), signed originally with ITIT in 1998, were assigned to the Company. The fulfilment of the Company's obligation under the agreements will be performed by the Company, or by its Israeli subsidiaries.

In accordance with the said agreement, the aggregate gross monthly remuneration for the Managing Directors amounts to EUR 27,000 (USD 37,000) per month (not linked), which, together with related employee benefits, will amount to EUR 32,000 (USD 44,000) per month.

In addition, the Managing Directors are entitled to an annual bonus aggregating to 7% of the Company's consolidated profits before tax for any fiscal year. The above mentioned Managing Directors undertook to be employed by the Company for an indefinite period, with 6 month notice of termination, and to refrain from competing with the Company's business for a period of 12 months following termination of their employment with the Company.

On 24 November 2006, the General Meeting of Shareholders of the Company approved a new remuneration policy which confirmed the entitlement of the members of the Management Board to receive a monthly base salary and annual participation in a cash bonus pool designated for the members of the Management Board equal to 7% of the Company's pre-tax profit before the bonus. In addition, under the same remuneration policy, each member of the Management Board is entitled to a car, contribution to a severance fund as well as to statutory provident fund, a travel allowance and reimbursement of reasonable business expenses.

Also on 26 November 2006, the General Meeting of Shareholders of the Company approved a new long-term incentive plan (the "Plan"). The persons eligible for participation in the Plan are the employees of the Group, including the members of the Management Board.

Under the Plan, both option rights to acquire shares in the Company and cash bonuses may be granted to the participants. During the financial year 2006, no share options have been granted to members of the Management Board.

The Managing Directors of the Company received remuneration totalling EUR 1,588,000 (2005: EUR 1,178,000). The members of the Supervisory Board received fees totalling EUR 52,500 (2005: EUR 51,500). The total remuneration is included in general and administrative expenses. The members of the Management and Supervisory Board did not receive any option rights to acquire shares in the Company during the financial year 2006.

Notes to the Consolidated Financial Statements

Note 26 - Related party transactions (cont'd)

The remuneration for the managing directors is divided between the managing directors as follow:

	Financial year	
	2006	2005
	EUR (thousands)	
General director	712	520
Operational director	452	332
Financial director	424	326
Total	<u>1,588</u>	<u>1,178</u>

The remuneration for the supervisory board members is principally divided equally.

Forum Film Ltd., a 50% subsidiary, will participate in the aforementioned remunerations to Mr. Moshe Greidinger and Mr. Israel Greidinger at the rate of 33% thereof and will fully cover the portion of the above mentioned bonuses that relate to its own revenues.

- c. The Greidinger family has indirect control of the Company's majority shareholder, ITIT, through its majority shareholding in Israel Theatres Limited. More than 75% of the shares in Israel Theatres Limited are held by Mr Israel Greidinger, Mr Moshe Greidinger and their relatives.

The 50% of Norma Film not owned by the Company is held by M.I. Greidinger Investment Limited, in which both Mr Moshe Greidinger and Mr Israel Greidinger each hold a 50% interest.

- d. In June 1998, Israel Theatres Ltd. (the parent company of ITIT) leased to ITIT the real estate properties on which four of the Company's theatres are located, until 30 November 2007, subject to the Company's right to terminate any lease prior to its original termination date. The annual lease payments for the above properties aggregate to EUR 278,000 (USD 392,000). These leases were assigned to IT-2004, a 100% subsidiary of the Company, as part of the reorganisation.
- e. In May 1998, ITIT entered into a management services agreement with Israel Theatres pursuant to which the Company will provide Israel Theatres for an indefinite period, but not less than three years, with certain management services. Management services include office and accounting services through providing Israel Theatres with senior personnel and administration of Israel Theatres' business. The management services agreement is for a fixed annual sum of EUR 299,000 (USD 377,000). In December 2003, this agreement was assigned to IT-2004, the 100% Israeli subsidiary of the Company.
- f. Forum Film Ltd. and Giant Video have been leasing offices and storage space from Israel Theatres since February 1994, for consideration of EUR 10,000 (USD 13,000) per month, linked to the changes in the CPI. Israel Theatres leased offices in Herzlia and in Haifa to IT-2004 until 30 November 2007, in consideration of EUR 49,000 (NIS 286,000) per annum. The rental fees are linked to the Israeli CPI.

Notes to the Consolidated Financial Statements

Note 26 - Related party transactions (cont'd)

- g. The minority interests mainly represent a 50% indirect share in the equity of Forum Film Ltd. By M.I. Greidinger Investment Limited (see note 26.c above) . Pursuant to Forum Film Ltd's Articles of Association, the Company has the right to appoint three of Forum Film Ltd's five directors, and accordingly, maintains control over all major company decisions.
- h. The Company has entered into an indemnification agreement with each executive officer and director. These agreements endeavour to fully indemnify and limit the personal liability of the officers and directors, in certain circumstances, both to the Company and to its shareholders, for acts or omissions by them in their official capacity. The Company had obtained officers' and directors' liability insurance.
- i. Israel Theatres, ITIT and its directors and principal officers undertook not to compete, whether directly or indirectly, with the Company's business in the film exhibition, distribution and video rental fields. The length of this undertaking is for as long as they are directors or officers in either of the companies, or beneficially own a controlling interest in the Company. The agreement specifically states that Israel Theatres and ITIT may not engage in the development, sale or lease of property for theatrical or video rental use without the prior written consent of the Company, unless it is to be used by the Company.
- j. As part of the completion of the initial public offering on the Warsaw stock exchange in December 2006, the Company incurred costs related both to the primary shares and the secondary shares. The Company charged the proportionate part of the mentioned expense (EUR 1,368,000) to the selling shareholders.
The receivables as per 31 December 2006 amount to EUR 1,258,000.

Notes to the Consolidated Financial Statements

Note 27 - Financial instruments

The Group's principal financial instruments, other than derivatives, comprise bank loans, loans from the shareholder, operating leases and short-term bank credits. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various other financial instruments such as trade debtors and trade creditors, which arise directly from its operations.

The Group also enters into derivative transactions, principally forward currency contracts. The purpose is to manage the currency risks arising from the Group's operations and its sources of finance. It is, and has been throughout the financial year 2006 and 2005, the Group's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and credit risk. The Board reviews and agrees policies for managing each of these risks and they are summarised below. The Group also monitors the market price risk arising from all financial instruments.

The Group's accounting policies in relation to derivatives are set out in Note 2.

Credit risk

Financial instruments that potentially subject the Group to concentrations of credit risk consist principally of cash and cash equivalents, short-term investments and receivables. The Group places its cash and cash equivalents and short-term investments in financial institutions with high credit ratings. Management does not expect any counterparty to fail to meet its obligations. Concentrations of credit risk with respect to trade receivables are limited due to the large number of customers comprising the Group's customer base.

Interest rate risk

The Group adopts a policy of a mixture of flat and floating interest rates (see Notes 17 and 18). At 31 December 2006, the Group has no borrowings at fixed rates of interest.

Notes to the Consolidated Financial Statements

Note 27 - Financial instruments (cont'd)**Foreign currency risk**

The Group incurs foreign currency risk on sales, purchases and borrowings that are denominated in a currency other than the euro. The currencies giving rise to this risk are primarily USD, PLN, NIS, HUF, BGN and CZK.

In order to minimise exposure to foreign currency risk, among other things, the Group has entered for a major part into long-term loan agreements denominated in euros.

During the financial year 2006, the Company has entered into forward foreign exchange contracts comprising a commitment to buy EUR 350,000 at the beginning of each month during 2007 and until December 2008 at fixed prices denominated in Polish Zloty, and forward foreign exchange contracts comprising a commitment to buy USD 195,000 at the beginning of each month during 2007 at fixed prices denominated in Hungarian forint. These forward foreign exchange contracts have been valued in the consolidated balance sheet at 31 December 2006 at their fair value.

Fair values

The following are details of the fair values of all of the Group's financial instruments that are carried in the financial statements at other than fair values and for which it is practicable to estimate such value:

- a. Cash and cash equivalents, short-term bank deposit and short-term bank credit.
The carrying amounts approximate their fair value because of the short maturity of these instruments.
- b. Marketable securities.
The carrying amounts approximate their fair value.
- c. Trade accounts receivable, other accounts receivable, accounts payable and accrued liabilities.
The carrying amounts approximate their fair value because of the short-term nature of these instruments.
- d. Debt - as of 31 December 2006, the aggregate fair value of the Company's long-term debt obligations is similar to its carrying value of EUR 76 million. As of 31 December 2005, the aggregate fair value of the Company's long-term debt obligation was approximately EUR 86 million compared to the carrying value of EUR 86 million. The above fair values have been based on terms for debts with conditions and maturities similar to those of the Company's debts as prevailing in the market at balance sheet date.

Notes to the Consolidated Financial Statements

Note 28 - Linkage terms of monetary items

	31 December 2006			Total
	In or linked to EUR	In or linked to USD	In or linked to foreign currencies	
	EUR (thousands)			
Assets				
Cash and cash equivalents	46,303	267	6,624	53,194
Trade accounts receivable	86	-	11,556	11,642
Other accounts receivable	424	-	10,218	10,642
Related parties receivable	1,510	-	336	1,846
Marketable securities	-	-	56	56
	<u>48,323</u>	<u>267</u>	<u>28,790</u>	<u>77,380</u>
Liabilities				
Short-term bank credit	-	-	15,086	15,086
Trade accounts payable	952	790	8,998	10,740
Employee and payroll accruals	2	-	1,301	1,303
Other accounts payable	3,791	41	8,620	12,452
Due to related parties	5	-	450	455
Long-term loans (including current - Portion)	47,052	38	29,200	76,290
Accrued employee rights upon retirement	-	-	41	41
	<u>51,802</u>	<u>869</u>	<u>63,696</u>	<u>116,367</u>

Notes to the Consolidated Financial Statements

Note 28 - Linkage terms of monetary items (cont'd)

	31 December 2005			Total
	In or linked to Euro	In or linked to USD	In or linked to foreign currencies	
	EUR (thousands)			
Assets				
Cash and cash equivalents	1,568	197	3,402	5,167
Trade account receivable	-	-	7,083	7,083
Other accounts receivable	2,958	-	11,805	14,763
Related parties receivable	1,445	54	203	1,702
Marketable securities	-	-	55	55
	<u>5,971</u>	<u>251</u>	<u>22,548</u>	<u>28,770</u>
Liabilities				
Short-term bank credit	-	-	8,322	8,322
Trade accounts payable	54	806	9,063	9,923
Employee and payroll accruals	-	-	1,312	1,312
Other accounts payable	1,648	-	11,253	12,901
Due to related parties	5	-	432	437
Long-term loans (including current - Portion)	55,562	71	28,232	83,865
Accrued employee rights upon retirement	-	-	907	907
	<u>57,269</u>	<u>877</u>	<u>59,521</u>	<u>117,667</u>

Note 29 - Segment reporting

Segment information is presented in respect of the Group's business and geographical segments. The primary format, business segments, is based on the Group's management and internal reporting structure.

The Group's operations in Israel and Central Europe are organised under the following major business segments:

- Theatre operations;
- Distribution - Distribution of movies;
- Video + DVD – Rental and sale of video cassettes and DVD;
- Other, this includes the Company's real estate business.

Notes to the Consolidated Financial Statements

Note 29 - Segment reporting (cont'd)

Business segments:

	Financial year 2006					Consolidated
	EUR (thousands)					
	Theatre Operations	Distribution	Video & DVD	Other	Eliminations	
Revenues						
External sales	99,134	21,904	4,120	18,633	-	143,791
Inter-segment sales	-	5,996	312	-	(6,308)	-
Total revenues	<u>99,134</u>	<u>27,900</u>	<u>4,432</u>	<u>18,633</u>	<u>(6,308)</u>	<u>143,791</u>
Results						
Segment results before depreciation, amortisation and impairment write – downs	23,212	658	636	6,742	-	31,248
Depreciation, amortisation and impairment write – downs	12,281	143	1,129	348	-	13,901
Segment results	<u>10,931</u>	<u>515</u>	<u>(493)</u>	<u>6,394</u>	<u>-</u>	<u>17,347</u>
Net financial expense						(4,670)
Gain and loss on disposals						(34)
Income taxes						(1,377)
Minority interests						472
Net income						<u>11,738</u>
	31 December 2006					
	EUR (thousands)					
	Theatre operations	Distribution	Video & DVD	Other	Unallocated	Consolidated
Assets						
Segment assets	<u>181,480</u>	<u>11,899</u>	<u>2,689</u>	<u>14,838</u>	<u>46,554*</u>	<u>257,460</u>
Liabilities						
Segment liabilities	<u>19,833</u>	<u>5,723</u>	<u>1,304</u>	<u>4,858</u>	<u>93,566</u>	<u>125,284</u>
Other information						
Capital expenditure	<u>19,423</u>	<u>221</u>	<u>1,456</u>	<u>538</u>	<u>-</u>	<u>21,638</u>

*includes the proceeds from the public offering held in cash as per 31 December 2006.

Notes to the Consolidated Financial Statements

Note 29 - Segment reporting (cont'd)

	Financial year 2005 (*)					Consolidated
	EUR (thousands)					
	Theatre Operations	Distribution	Video & DVD	Other	Eliminations	
Revenues						
External sales	73,641	15,138	4,877	14,525	-	108,181
Inter-segment sales	-	3,778	325	-	(4,103)	-
Total revenues	<u>73,641</u>	<u>18,916</u>	<u>5,202</u>	<u>14,525</u>	<u>(4,103)</u>	<u>108,181</u>
Results						
Segment results before depreciation, amortisation and impairment write-downs	12,867	2,048	1,012	8,096	-	24,023
Depreciation, amortisation and impairment write-downs	9,787	137	1,720	452	-	12,096
	<u>3,080</u>	<u>1,911</u>	<u>(708)</u>	<u>7,644</u>	<u>-</u>	<u>11,927</u>
Segment results						(2,753)
Net financial expense						(151)
Gain and loss on disposals						-
Income taxes						(103)
Minority interests						(1,198)
Net income						<u>188</u>
						<u>7,910</u>
31 December 2005						
EUR (thousands)						
	Theatre operations	Distribution	Video & DVD	Other	Unallocated	Consolidated
Assets						
Segment assets	<u>172,923</u>	<u>7,280</u>	<u>3,016</u>	<u>17,745</u>	<u>1,057</u>	<u>202,021</u>
Liabilities						
Segment liabilities	<u>28,867</u>	<u>2,584</u>	<u>1,851</u>	<u>1,497</u>	<u>94,105</u>	<u>128,904</u>
Other information						
Capital expenditure	<u>29,795</u>	<u>1,011</u>	<u>1,292</u>	<u>3,168</u>	<u>-</u>	<u>35,266</u>

Notes to the Consolidated Financial Statements**Note 29 - Segment reporting (cont'd)**

In addition to the information on business segments based on the structure of the Group, the figures below present information for geographical segments. Determination of geographical segments is based on location of assets and is identical to customer location.

	31 December 2006			
	EUR (thousands)			
	Central Europe	Israel	Unallocated	Consolidated
Revenues				
External sales	111,054	32,737	-	143,791
Assets				
Segment assets	174,163	36,743	46,554	257,460
Capital expenditure	13,469	8,169	-	21,638

	31 December 2005			
	EUR (thousands)			
	Central Europe	Israel	Unallocated	Consolidated
Revenues				
External sales	77,116	31,065	-	108,181
Assets				
Segment assets	175,075	25,889	1,057	202,021
Capital expenditure	31,289	3,977	-	35,266

Notes to the Consolidated Financial Statements

Note 30 - Personnel

Personnel costs are specified as follows:

	31 December	
	2006	2005
	EUR (thousands)	
Salaries and wages	13,201	12,703
Pension costs	394	349
Other social charges	2,101	1,780
Equity settled share-based payment transactions (see Note 12 (c))	20	-
Total personnel costs	15,716	14,832

For 2006 and 2005, the pension costs comprise defined contribution expenses only.

The average number of personnel, in full-time equivalents, employed by the Company and its subsidiaries during the year 2006 were 1,509 (financial year 2005: 1,450). A geographical allocation of the average number of personnel is as follows:

	31 December	
	2006	2005
Israel	489	546
Central Europe	1,019	903
Netherlands	1	1
Total average number of personnel	1,509	1,450

Notes to the Consolidated Financial Statements

Note 31 - Details of corporations in the Group

31 December 2006				
	Direct/indirect voting right of the Company	The Company's equity share in subsidiary	Consolidation	Country
	%	%	%	
I.T. International Theatres 2004 Ltd.	100%	100%	Full	(6)
I.T. Magyar Cinemas Kft	100%	100%	Full	(2)
Kino 2005 a.s.	100%	100%	Full	(3)
I.T. Sadyba B.V.	100%	100%	Full	(1)
Cinema City Poland Sp.z o.o.	100%	100%	Full	(4)
IT Development 2003	100%	100%	Full	(4)
I.T. Czech Cinemas S.R.O.	100%	100%	Full	(3)
I.T. Sofia B.V.	100%	100%	Full	(1)
New Age Media Sp.z o.o.	100%	100%	Full	(4)
Forum Film Poland Sp.z o.o.	100%	100%	Full	(4)
All Job Poland Sp.z o.o.	100%	100%	Full	(4)
Norma Film Ltd.	60%	50%	Full	(6)
Forum Film Ltd.	60%	50%	Full	(6)
Ya'af - Giant Video Library Network Ltd.	60%	30%	Full	(6)
Ya'af – Automatic Video Machines Ltd.	60%	50%	Full	(6)
Kafan et Anak limited partnership	25%	15%	Proportionate	(6)
Mabat Ltd.	100%	100%	Full	(6)
Teleticket Ltd.	100%	100%	Full	(6)
Cinema Plus Ltd.	100%	100%	Full	(6)
Cinema City Bulgaria EOOD	100%	100%	Full	(5)
Forum Film Home Entertainment KFT	100%	100%	Full	(2)
New Age Cinema KFT	100%	100%	Full	(2)
Forum Hungary Film Distribution KFT	100%	100%	Full	(2)
Mall of Plovdiv EOOD	30%	30%	Not consolidated-held for sale	(5)

(1) A holding company in the Netherlands.

(2) Hungarian corporation.

(3) Czech corporation.

(4) Polish corporation.

(5) Bulgarian corporation.

(6) Israeli corporation.

The details of corporation during 2005 were similar to the details of corporation in 2006 as shown above, except for the changes in consolidation disclosed in Note 3.

Associate companies valued using the equity method:

- MO Sofia EAD, Bulgaria in which the Company held a 25% interest from 30 June 2005 through early January 2006 (before 30 June 2005: a 50% interest which was proportionally consolidated).

Notes to the Consolidated Financial Statements

Note 32 - Information about agreed-upon engagements of the Group's auditor

Information about the agreements and the values from those agreements is disclosed below:

	31 December	
	2006	2005
	EUR (thousands)	
Remuneration for audit (1)	336	254
Remuneration for IPO services (2)	252	-
Remuneration for other services	2	22
	590	276

- (1) Remuneration for audit includes the amounts paid and due to KPMG worldwide for professional services related to audit and review of unconsolidated and consolidated financial statements of the Company for the relevant year.
- (2) Remuneration for related services includes other amounts paid and due to KPMG. These services relate to services provided in connecting with the initial public offering in December 2006.
- (3) Remuneration includes other services rendered by the auditor in 2006 and 2005.

Company Balance Sheet
(before appropriation of the result)

	Note	31 December	
		2006	2005
		EUR (thousands)	
ASSETS			
FIXED ASSETS			
Property and equipment	3	30	1,755
Financial fixed assets			
Investment in subsidiaries	4	125,903	62,685
Loans to subsidiaries	5	-	2,944
Total fixed assets		125,933	67,384
CURRENT ASSETS			
Receivables			
Receivable from subsidiaries		1,675	7,863
Income taxes receivable		46	56
Other accounts receivable and prepaid items		1,692	445
Liquid funds			
Cash and cash equivalents		45,758	1,436
Total current assets		49,171	9,800
TOTAL ASSETS		175,104	77,184

See accompanying notes to the Company Financial Statements.

Company Balance Sheet
(before appropriation of the result)

	Note	31 December	
		2006	2005
		EUR (thousands)	
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY			
	6		
Share capital		507	407
Share Premium reserve		89,945	43,553
Accumulated currency translation adjustments		4,967	4,158
Net profit for the year		11,738	7,910
Retained earnings		25,019	17,089
Total shareholders' equity		132,176	73,117
CURRENT LIABILITIES			
Trade accounts payable		213	77
Payable to subsidiaries		40,829	3,990
Other accounts payable		1,886	-
Total current liabilities		42,928	4,067
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		175,104	77,184

See accompanying notes to the Company Financial Statements.

Company Income Statement

	Note	31 December	
		2006	2005
		EUR (thousands)	
Revenue		887	834
General and administrative expenses		(406)	(431)
Net operating result		481	403
Financial income	7	113	482
Financial expenses	8	(153)	(2,025)
Currency exchange gain		-	773
Operating result before taxation		441	(367)
Income taxes	9	-	-
Net result after taxation		441	(367)
Result from subsidiaries after taxation	4	11,297	8,277
Net income		11,738	7,910

See accompanying notes to the Company Financial Statements.

Notes to the Company Financial Statements

Note 1 - General

Cinema City International N.V. (“the Company”) was incorporated on 12 April 1994, and has its statutory seat in Amsterdam, the Netherlands, and its corporate office in Rotterdam, the Netherlands.

The shares in the Company are traded on the Warsaw stock exchange. As at 31 December 2006, 64.5% of the outstanding shares are held by I.T. International Theatres Ltd. (“ITIT”), incorporated in Israel. The Company is a subsidiary of I.T. International Theatres Ltd. (“ITIT”), incorporated in Israel.

The Company holds and owns various companies in Europe and Israel that are active in the entertainment business in various countries, including Poland, the Czech Republic, Hungary, Bulgaria and Israel. The Company is also engaged in managing and establishing its own entertainment real estate projects for rental purposes, in which the Company operates motion picture theatres. In addition, the Company is involved in short-term and long-term real estate trading in Central Europe.

Note 2 - Accounting principles

The accounting principles and measurement basis of the Company’s statutory accounts are similar to those applied with respect to the Consolidated Financial Statements (see Note 2 to the Consolidated Financial Statements). The Company Financial Statements have been prepared in conformity with generally accepted accounting principles in the Netherlands (“Dutch GAAP”), whereas the Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as adopted by the EU and Dutch GAAP as described in Note 2 to the Consolidated Financial Statements.

Notes to the Company Financial Statements

Note 3 - Property and equipment

Composition:

	For the year ended 31 December 2006			Balance at year-end
	Balance at beginning of the year	Additions during the year	Sales and disposals during the year	
	EUR (thousands)			
Cost				
Cinema equipment (1)	1,737	-	(1,725)	12
Computers, furniture and office equipment	18	-	-	18
Carrying value	<u>1,755</u>	<u>-</u>	<u>(1,725)</u>	<u>30</u>

	For the year ended 31 December 2005			Balance at year end
	Balance at beginning of the year	Additions during the year	Sales and disposals during the year	
	EUR (thousands)			
Cost				
Cinema equipment (1)	5,083	547	(3,893)	1,737
Computers, furniture and office equipment	15	3	-	18
Carrying value	<u>5,098</u>	<u>550</u>	<u>(3,893)</u>	<u>1,755</u>

- (1) Consists of prepayments on account of IMAX® systems not operated yet. Therefore, no depreciation has been incurred.

Notes to the Company Financial Statements

Note 4 - Investment in subsidiaries

The subsidiaries of the Company are valued at their net equity value.

The movements in subsidiaries are as follows:

	Financial year	
	2006	2005
	EUR (thousands)	
Balance at beginning of the year	62,685	39,153
Currency translation adjustment	669	5,315
Investments in subsidiaries	51,252	9,940
Net result subsidiaries during the year	11,297	8,277
Balance at the end of the year	<u>125,903</u>	<u>62,685</u>

Note 5 - Loans to subsidiaries

	Financial year	
	2006	2005
	EUR (thousands)	
Balance at beginning of the year	2,944	69,815
Loans added	-	-
Loans redeemed	(2,944)	-
Loan assigned to subsidiary company*	-	(66,871)
Balance at the end of the year	<u>-</u>	<u>2,944</u>

* As of 1 January 2005 all loans to subsidiaries were assigned by the Company to a fully-owned subsidiary company.

Notes to the Company Financial Statements**Note 6 - Shareholders' equity**

	Share capital	Share Premium reserve	Retained Earnings	Net profit for the year	Accumulated currency translation adjustments	Total
	EUR (thousands)					
Balance as of 1 January 2005	407	43,553	11,749	5,340	(975)	60,074
Profit appropriation prior year	-	-	5,340	(5,340)	-	-
Net profit for the year 2005	-	-	-	7,910	-	7,910
Currency translation	-	-	-	-	5,133	5,133
Balance as of 31 December 2005	407	43,553	17,089	7,910	4,158	73,117
Profit appropriation prior year	-	-	7,910	(7,910)	-	-
New shares issued	100	46,392	-	-	-	46,492
Share based payments	-	-	20	-	-	20
Net profit for the year 2006	-	-	-	11,738	-	11,738
Currency translation	-	-	-	-	809	809
Balance as of 31 December 2006	507	89,945	25,019	11,738	4,967	132,176

As of 31 December 2006 and as of 31 December 2005, the authorised share capital of the Company consisted of 175,000,000 ordinary shares with a par value of EUR 0.01 each. For details on shares issued during 2006, reference is made to Note 12 of the Consolidated Financial Statements.

Note 7 - Financial income

Financial income for the years 2006 and 2005 mainly consisted of interest income on inter-company loans and receivables.

Note 8 – Financial expenses

The financial expenses for the year 2005 relates mainly to expenses to externals and to group companies

Note 9 - Income taxes

No Dutch income taxes have been recorded primarily because of available tax losses carried forward from prior years. Realisation of this deferred income tax asset is dependent upon generating sufficient taxable income in the period that the deferred income tax asset is realised. Based on all available information, it is not probable that the deferred income tax asset is realisable and therefore the deferred tax asset is valued at nil.

The accumulated tax losses carried forward as per 31 December 2005 are estimated to be EUR 2,140,766. These losses are caused mainly by exchange rate differences.

Notes to the Company Financial Statements

Note 10 - Personnel

The Company employed one employee during the year (2005: two employees).

Note 11 - Directors' remuneration

The Board of Managing Directors of the Company consists of 3 members; the board members are entitled to a total remuneration of EUR 1,588,000 during the year 2006. The amount of remuneration also includes fees, salaries and bonuses paid and have been paid through the Company's subsidiaries.

The Supervisory Board of the Company consists of 5 members; the supervisory directors are entitled to an annual fee of EUR 8,500 plus an amount of EUR 1,500 per board meeting (EUR 750 if attendance is by telephone). The total amount due in respect of supervisory board fees during 2006 is EUR 52,500.

Note 12 - Information about agreed upon-engagements of the Company's auditor

Information about the agreements and the values from those agreements is disclosed below:

	31 December	
	2006	2005
	EUR (thousands)	
Remuneration for audit (1)	149	78
Remuneration for IPO services (2)	228	-
	<u>377</u>	<u>78</u>

- (1) Remuneration for audit includes the amounts paid and due to KPMG Accountants N.V. for professional services related to audit and review of unconsolidated and consolidated financial statements of the Company for the relevant year (engagement letters dated 19 February 2007, 12 July 2006 for the year 2006 and 21 July 2005, 1 February 2006 for the year 2005).
- (2) Remuneration for related services includes other amounts paid and due to KPMG. These services relate to services provided in connecting with the initial public offering in December 2006.

Notes to the Company Financial Statements

**Rotterdam,
18 April 2007**

The Management Board

Moshe Greidinger

Amos Weltsch

Israel Greidinger

Supervisory Board

Coleman Kenneth Greidinger

Carrie Twist

Frank Pierce

Scott Rosenblum

Peter Weishut

Yair Shilvav

Other information

Articles of Association rules regarding profit appropriation

In accordance with Article 32 of the Articles of Association,

- 1) the Board of Managing Directors, with prior approval of the Supervisory Board, shall determine which portion of the profits – the positive balance of the profit and loss account – shall be reserved. The profit remaining shall be at the disposal of the general meeting;
- 2) profit distributions may only be made to the extent the equity exceeds the paid and called up part of the capital increased with the reserves which must be maintained pursuant to the law;
- 3) dividends shall be paid after adoption of the annual accounts evidencing that payment of dividends is lawful;
- 4) the Board of Managing Directors, with prior approval of the Supervisory Board may resolve to pay an interim dividend provided the requirement of the second paragraph has been complied with as shown by interim accounts drawn up in accordance with the provision of the law;
- 5) the general meeting may, subject to due observance of the provision of paragraph 2 and upon a proposal by the managing directors, resolve to make distributions out of a reserve which need not to be maintained by virtue of the law;
- 6) cash payments in relation to bearer shares if and in as far as the distributions are payable outside the Netherlands, shall be made in the currency of the country where the shares are listed and in accordance with the applicable rules of the country in which the shares of the Company have been admitted to an official listing on a regulated stock exchange in accordance. if such currency is not the same as the legal tender in the Netherlands the amount shall be calculated against the exchange rate determined by The Netherlands Central Bank ("De Nederlandsche Bank") at the end of the day prior to the day on which the general meeting shall resolve to make the distributions in accordance with paragraph.1 above. If and in as far as the Company on the first day on which the distribution is payable, pursuant to governmental measures or other extraordinary circumstances beyond its control is not able to pay on the place outside the Netherlands or in the relevant foreign currency, the board of Managing Directors is authorised to determine to that extent that the payments shall be made in euros and on one or more places in the Netherlands. In such case the provisions of the first sentence of this paragraph shall not apply.
- 7) the general meeting may, upon a proposal by the managing directors which proposal was approved by the Supervisory Board , resolve to pay dividends, or make distributions out of a reserve which need not to be maintained by virtue of the law, wholly or partially in the form of shares in the capital of the Company;
- 8) a claim of a shareholder to receive a distribution expires after 5 years;
- 9) for the calculation of the amount of profit distribution, the shares held by the Company shall be excluded.

Other information

Proposed profit appropriation

For the year ended 31 December 2006, Management proposes to allocate the net profit for the year 2006 amounting to EUR 11,738,000 to retained earnings. This proposal has not been reflected in the Company balance sheet per 31 December 2006.