SÀFILO S.p.A.

Annual Report Year 2006

April 30th, 2007

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FORWARD-LOOKING STATEMENTS

This Annual Report includes forward-looking statements. All statements other than statements of historical fact included in this Annual Report regarding our business, financial condition, results of operations and certain of our plans, objectives, assumptions, projections, expectations or beliefs with respect to these items and statements regarding other future events or prospects, are forward-looking statements. These statements include, without limitation, those concerning: our strategy and our ability to achieve it; expectations regarding sales, profitability and growth; plans for the launch of new products; our possible or assumed future results of operations; research and development, capital expenditure and investment plans; adequacy of capital; and financing plans. The words "aim", "may", "will", "expect", "anticipate", "believe", "future", "continue", "help", "estimate", "plan", "intend", "should", "shall" or the negative or other variations thereof as well as other statements regarding matters that are not historical fact, are or may constitute forward-looking statements. In addition, this Annual Report includes forward-looking statements relating to our potential exposure to various types of market risks, such as foreign exchange rate risk, interest rate risks and other risks related to financial assets and liabilities. We have based these forward-looking statements on our management's current view with respect to future events and financial performance. These views reflect the best judgment of our management but involve a number of risks and uncertainties which could cause actual results to differ materially from those predicted in our forward-looking statements and from past results, performance or achievements. Although we believe that the estimates reflected in the forward-looking statements are reasonable, such estimates may prove to be incorrect. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results and developments to differ materially from these expressed or implied by these forward-looking statements.

These factors include, among other things:

- factors affecting our ability to negotiate, maintain and renew license arrangements on satisfactory terms with leading designers;
- uncertainties associated with changing consumer preferences;
- the impact of currency exchange rate and interest rate fluctuations;
- risks relating to our manufacturing and distribution operations and our arrangements with third party manufacturers;
- risks relating to international sales and exposure to changing local conditions;
- factors affecting our ability to compete effectively in the eyewear market, including new products and distribution strategies of our competitors;
- risks associated with our significant debt and our ability to meet our financial obligations;
- human resource factors, including our ability to retain our senior management and other key personnel and employee costs;
- factors affecting our ability to design, develop and introduce successful new products;
- factors affecting our ability to obtain or maintain intellectual property protection for our products;
- uncertainties associated with general economic conditions;
- governmental factors, including the costs of compliance with regulations and the impact of regulatory changes; and
- other risks, uncertainties and factors inherent in our business.

These risks are not exhaustive. For further discussion of these factors and other risks, see “Risk Factors”, “Business Overview” and “Operating and financial review and prospects”.

We do not intend to update or revise any forward-looking statements whether as a result of new information, future events or otherwise. All subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained throughout this Annual Report. As a result of these risks, uncertainties and assumptions, you should not place undue reliance on these forward-looking statements as a prediction of actual results or otherwise.

PRESENTATION OF FINANCIAL AND OTHER INFORMATION

This Annual Report contains the historical financial information derived from the audited consolidated financial statements as of and for the years ended December 31, 2004, 2005 and 2006 that were prepared in accordance with International Financial Reporting Standards as adopted by the European Commission for use in the European Union ("IFRS").

Pursuant to European Community Regulation EC 1606/2002 and to the subsequent Legislative Decree n. 38 approved by the Italian government on February 25, 2005, companies listed on Italian stock exchange have been required to prepare their consolidated financial statements using IFRS instead of the current Italian GAAP for the financial year ending December 31, 2005.

Sàfilo S.p.A. is owned by Sàfilo Group S.p.A., which is listed on the Italian stock exchange. According to the above mentioned Legislative Decree n. 38, subsidiaries of companies listed on the Italian stock exchange can prepare their consolidated and their own stand alone financial statements according to IFRS for the financial year ending December 31, 2005.

Sàfilo S.p.A. has decided to apply IFRS for its consolidated and its own stand alone financial statements for the financial year ending December 31, 2005. The transition date was as of January 1, 2004.

The financial information included in this Annual Report is not intended to comply with SEC reporting requirements. Compliance with such requirements would require the presentation of U.S. GAAP financial information and the modification or exclusion of certain financial measures and the presentation of certain other information not included herein or the exclusion of certain information presented herein.

Certain defined terms

Unless otherwise indicated, references in this Annual Report to "Euro" or "€" are to the single currency introduced at the start of the third stage of the European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended; references to "dollar", "dollars", "U.S. dollars", "US$", "USD" or "$" are to the lawful currency of the United States of America; references to "GBP" are to the lawful currency of the United Kingdom; references to "billions" are to thousands of millions.

In this Annual Report, and unless the context indicates otherwise, the terms "we", "us", "our", "the Group" and "our Group" mean Sàfilo S.p.A. and our consolidated subsidiaries.

Except where indicated, references to "IFRS" in this Annual Report are to IFRS as adopted by the European Commission for use by companies on markets in the European Union.

Rounding Adjustments

Certain figures in this Annual Report, including percentage amounts, have been subject to rounding adjustments. Accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

EXCHANGE RATE INFORMATION

The following chart sets for the periods indicated, certain information regarding the Noon Buying Rate for Euros expressed in Dollars per Euro.

Year ended December 31, USD per Euro	2002	2003	2004	2005	2006
Exchange rate at end of period	1.0487	1.2630	1.3621	1.1797	1.3170
Average exchange rate during period(1)	0.9454	1.1313	1.2439	1.2441	1.2554
Highest exchange rate during period	1.0487	1.2630	1.3633	1.3507	1.3331
Lowest exchange rate during period	0.8578	1.0377	1.1802	1.1667	1.1826

Month, USD per Euro	At end of Period	Average rate(2) ($/Euro)	Highest exchange rate during the month	Lowest exchange rate during the month
October 2006	1.2696	1.2611	1.2737	1.2515
November 2006	1.3200	1.2881	1.3200	1.2702
December 2006	1.3170	1.3213	1.3331	1.3095
January 2007	1.2954	1.2999	1.3270	1.2893
February 2007	1.3211	1.3073	1.3230	1.2925
March 2007	1.3318	1.3104	1.3352	1.3083

(1) The annual average of the daily closing priced based upon European Central Bank data.
(2) The monthly average of the daily closing priced compiled upon European Central Bank data.

The noon buying rate on April 26, 2007 was US$ 1.3600 per Euro.

The above rates may differ from the actual rates used in the preparation of our consolidated financial statements and other financial information appearing in this Annual Report. Our inclusion of the exchange rates is not meant to suggest that the euro amounts actually represent such dollar amounts or that such amounts could have been converted into dollars at any particular rate, if at all.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

SELECTED HISTORICAL CONSOLIDATED FINANCIAL DATA

The selected consolidated financial data as of and for the years ended December 31, 2004, 2005 and 2006 have been derived from our audited consolidated financial statements prepared in accordance with IFRS.

The selected historical consolidated financial data in the tables below should be read in conjunction with the audited consolidated financial statements and relative notes in Item 18 and with "Operating and financial review and prospects" in Item 5 of this Annual Report.

As of and for the years ended December 31, 2004, 2005 and 2006

	Year ended December 31,		
(Euro in millions)	2004	2005	2006
Statement of Income Data			
Net sales	944.7	1,025.3	1,122.0
Cost of sales	(381.5)	(416.5)	(458.5)
Gross profit	563.2	608.8	663.5
Selling and marketing expenses	(344.1)	(379.4)	(415.3)
General and administrative expenses	(106.9)	(102.1)	(123.8)
Other expenses, net	(0.9)	1.0	1.4
Operating income	111.3	128.3	125.8
Share of income from associates	-	1.5	1.5
Interest expense and other financial charges, net	(66.1)	(104.8)	(56.2)
Income taxes	(20.5)	(11.4)	(30.1)
Net income/(loss)	24.7	13.6	41.0
Net income attributable to minority interests	3.1	3.2	3.3
Net income attributable to the Group	21.6	10.4	37.7

	Year ended December 31,		
(Euro in millions)	2004	2005	2006
Statement of Cash Flows Data			
Net cash provided by operating activities	50.3	28.4	20.8
Net cash (used in) investing activities	(28.6)	(37.3)	(36.9)
Net cash provided by (used in) financing activities	(22.0)	21.3	(13.6)

(Euro in millions)	As of December 31, 2004	2005	2006
Balance Sheet Data			
Cash in hand and at bank	33.8	151.0	35.6
Property, plants and equipment, net	195.8	193.6	202.0
Net working capital[1]	231.5	290.4	310.1
Total assets	1,171.6	1,392.0	1,383.2
Total debt[2]	787.9	652.2	575.3
Net debt[3]	754.1	501.2	539.6
Total shareholders' equity	68.6	385.8	391.9

(Euro in millions)	Year ended December 31, 2004	2005	2006
Other Data			
Capital expenditure	31.2	38.6	42.8
Depreciation and amortization[4]	35.6	35.2	36.8
EBITDA[5]	146.9	163.5	162.6

(Euro in millions)	Year ended December 31, 2004	2005	2006
Net income / (loss)	24.7	13.6	41.0
Income tax expenses	20.5	11.4	30.1
Interest expense and other financial charges, net	66.1	104.8	56.2
Share of income from associates	-	(1.5)	(1.5)
Amortization of intangibles	5.5	5.6	6.3
Property, plants and equipment depreciation	30.1	29.6	30.5
EBITDA[(5)]	146.9	163.5	162.6

[1] We define net working capital as total current assets (excluding cash in hand and at banks) less total current liabilities (excluding bank loans, short term debt, current portion of long-term borrowings and other borrowings).

[2] We define total debt as short-term borrowings plus long-term borrowings.

[3] We define net debt as total debt, net of cash in hand and at banks.

[4] Depreciation and amortization is included under cost of sales, selling and marketing expenses and general and administrative expenses in the consolidated financial statements of the Company.

[5] We have calculated EBITDA as net income before income tax expenses, net interest expenses and other financial charges, share of income from associates, amortization of intangibles and depreciation of property, plants and equipment. EBITDA is not a measurement of performance under IFRS, and you should not consider EBITDA as an alternative to (a) operating income or net income (as determined in accordance with generally accepted accounting principles), or as a measure of our operating performance, (b) cash flows from operating, investing or financing activities (as determined in accordance with generally accepted accounting principles), or as a measure of our ability to meet cash needs, or (c) any other measures of performance under generally accepted accounting principles. EBITDA may not be indicative of our historical operating results, nor is it meant to be predictive of our future results. We believe that EBITDA is a measure commonly reported and widely used by investors in comparing performance on a consistent basis without regard to depreciation and amortization, which can vary significantly depending upon accounting methods (particularly when acquisitions have occurred) or non-operating factors. Accordingly, EBITDA has been disclosed in this Annual Report to permit a more complete and comprehensive analysis of our operating performance relative to other companies and of our ability to service our debt. Because companies do not calculate EBITDA identically, our presentation of EBITDA may not be comparable to similarly titled measured used by other companies.

RISK FACTORS

Endogenous risks relating to Sàfilo

Our business depends on our ability to negotiate, maintain, comply with and renew license agreements on satisfactory terms with leading fashion brand owners.

We have entered into license agreements that enable us to manufacture and distribute prescription frames and sunglasses under brands owned by third parties. We believe that our ability to negotiate, maintain, comply with and renew license agreements on satisfactory terms with leading designers in the fashion and luxury goods industries is essential to managing a successful brand portfolio and, therefore, material to the success of our business. Accordingly, if we are unable to maintain and renew license arrangements on terms that are commercially acceptable to us with our current licensors or comparable replacements or if we are unable to negotiate new license agreements with other leading designers, our growth prospects and financial results could be materially and adversely affected.

The majority of our licenses, including certain of our key licenses, contain provisions that permit a licensor to terminate the license upon the occurrence of certain events including, by way of example, the following:

- change of control of our Group;
- outsourcing production without the consent of the licensor;
- selling models that are not approved by licensor;
- failure to reach certain revenue targets;
- selling products through distribution outlets that have not been approved by the licensor; and
- in the event that a competitor of the licensor acquires a controlling shareholding in our company.

Certain of the license agreements expressly define a change of control in our Group as Vittorio Tabacchi and his family directly or indirectly losing control of the Group or ceasing to be our majority shareholder.

Outside our top three licensed brands agreements, two license agreements grant the licensor the right to terminate the agreement in the event a competitor of the licensor acquires more than 10% of our share capital and is able to influence our company policies and strategies.

A few of our license agreements, including two of our top three licensed brands agreements allow the licensor to terminate the agreement if we replace our current key management. One of our top three licensed brand agreements provides for termination in the event that a competitor of that licensor becomes a member of our board of directors.

We may be unable to protect our proprietary rights, which would adversely affect our business and financial results.

We rely on trade secret, unfair competition, trade name, service mark, trademark, copyright and patent laws to protect our rights to certain aspects of our products, including product designs, proprietary manufacturing processes and technologies, product research and concepts and recognized trademarks, all of which we believe are important to the success of our products and our competitive position. However, pending patent and trademark applications may not generate registered patents and trademarks, and any patent or trademark registration that is granted may be ineffective in preventing competition and could be held invalid and/or revoked if subsequently challenged. In addition, the actions we take to protect our proprietary rights may be inadequate

to prevent imitation of our products. Our proprietary information could become known to competitors, and we may not be able to protect meaningfully our rights to proprietary information. Furthermore, other companies may independently develop substantially equivalent or better products that do not infringe on our intellectual property rights or could assert rights in, and ownership of, our proprietary rights. Moreover, the laws of certain countries do not protect proprietary rights to the same extent as the laws of the European Union and the United States.

If the level of potentially infringing activities by others were to increase substantially, we might have to increase significantly the resources we devote to protecting our rights. Additionally, an adverse determination in any dispute involving our proprietary rights could require us to grant licenses to, or obtain licenses from, third parties, or prevent us from manufacturing or selling our products or could subject us to substantial liability. Any of these possibilities could have a material adverse effect on our business, results of operations, financial condition and prospects.

Our results of operations could be adversely affected by a disruption of operations at our manufacturing facilities or our distribution centers or by problems with our third-party manufacturers.

We own and operate manufacturing facilities in Italy and Slovenia. Our primary distribution facility is located in Padua, Italy and our other key distribution facilities are in Parsippany, New Jersey (United States) and in Hong Kong (China). All of these facilities are subject to operational risks, including:

- equipment failure;
- failure to comply with applicable regulations and standards and to maintain necessary permits and approvals;
- material supply disruptions;
- labor force shortages or work stoppages;
- events impeding or increasing the cost of transporting our products;
- natural disasters; and
- terrorist attacks.

Any significant disruption in operations at our manufacturing facilities or our distribution facilities resulting from these or other events may, to the extent not covered by our business interruption insurance, adversely affect our results of operations.

In addition to our owned manufacturing facilities, we use third-party manufacturers and suppliers, mainly located in Asia but also in Italy and the United States, to produce certain of our products. The use of third-party manufacturers entails a number of additional risks, including the risk of termination and less control over the quality of manufactured products. Any delays or disruptions in the products furnished by third-party manufacturers, or disruption or termination of our present arrangements with third-party manufacturers without suitable alternative arrangements in place, could have an adverse effect on our business, results of operations and financial condition.

We rely on the continued availability of high quality raw materials and semi-finished products.

We manage the purchase of high quality raw materials and semi-finished goods used in our own production. Until now, we have been able to identify and purchase quality raw materials, semi-finished goods and finished goods to support our production volumes and sales requirements while preserving our high quality standards. If the availability of, our access to, or the cost of high quality raw materials, semi-finished or finished

goods is adversely affected (for example, due to a decrease in the number of suppliers or manufacturers of such materials or goods, or a reduction in the overall availability of such materials or goods, whether due to a lack of supply, the loss of a supply contract, or increased demand from our competitors), we may have to bear greater expenses for or be unable to acquire such materials or goods. Any such adverse change may require us to increase prices or stop producing certain products and could adversely affect our sales and results of operations.

We believe we are not dependent on any one supplier; however in the event of any material disruption in, or termination for any reason of, our relationship with our current suppliers, there could be negative effects on our operations and the process of selecting and evaluating qualified alternative suppliers may be onerous and time-consuming in light of the high quality standards that we require. We also can provide no assurance that in the event of such a disruption or termination that we would be able to find an alternative supplier able to supply the materials currently used in our products or that materials would be available at prices similar to those offered by our current suppliers.

The markets in which we compete are highly competitive, and a failure to maintain an extensive distribution network could harm our business.

The prescription frames and sunglasses markets in which we operate are highly competitive. We believe that, in addition to successfully introducing new products, responding to changes in the market and maintaining superior production capabilities, our ability to remain competitive is dependent on our maintaining an extensive distribution network. One of the key objectives of our business strategy is to strengthen our existing distribution network. This effort will require additional expenditures and may not be successful. If we are unable to strengthen and to maintain our distribution network, our business, results of operations and financial condition could be adversely affected.

We depend on the services of our senior management and other key personnel and, if we are not able to retain our senior personnel or retain suitable replacements, our business could be negatively impacted.

We are currently managed by a relatively small number of senior executive officers and employees, many of whom have numerous years of experience with us and in the eyewear industry, who would be difficult to replace. Our senior managers, including our Chairman, Vice Chairman, Chief Executive Officer, Co-Chief Executive Officer and Regional Managing Directors, and our senior product design, sales, marketing and production staff have extensive knowledge of our business, industry, licensors and customers. Any loss or interruption of the services of our key senior personnel, or our inability to recruit sufficient qualified replacement personnel, could adversely affect our ability to maintain the loyalty of key customers and licensors, to continue to develop important product improvements, to design, manufacture, distribute and market our products and to implement our strategy. This could adversely affect our business, results of operations and financial condition.

We believe that our continued growth and success largely depends on our ability to retain skilled, qualified and experienced managerial, design, research and development, sales, marketing and production personnel and to train our staff to produce and to sell successfully the broad range of products that we offer. Even if we are successful in attracting and retaining such personnel, competition for such employees may significantly increase our compensation costs and adversely affect our operating results.

We are subject to restrictive debt covenants, which limit our operating flexibility.

We have undertaken that, during the term of the new Senior Credit Agreement (as defined in Item 5), we will comply with certain covenants relating to our results of operations and financial condition such as interest cover and leverage, which must be calculated semi-annually at a consolidated level.

The Senior Credit Agreement and the indenture governing the Senior Notes contain covenants in line with market practice that impose some restrictions on the way our Group companies can operate, including restrictions on our ability to:

- incur additional indebtedness or guarantee indebtedness of others;

- make certain loans or investments;
- distribute dividends; or
- acquire or sell our own shares.

These covenants could limit our ability to finance our future operations and capital needs and our ability to pursue acquisitions and other business activities that may be in our interest.

Our ability to meet these covenants may be affected by events beyond our control and, as a result, we cannot assure you that we will be able to meet them in the future. In the event that we default under the Senior Credit Agreement, the lenders could terminate their commitments and accelerate the payment of the entire outstanding principal and interest due. Borrowings under other debt instruments that contain cross-acceleration or cross-default provisions may as a result also be accelerated and become due and payable. Any such failure or default could severely restrict our ability to fund our liquidity and capital expenditure needs and otherwise have a material adverse effect on our financial condition and results of operations.

Our high leverage and debt service obligations could adversely affect our business.

We are highly leveraged and have significant debt service obligations. As of December 31, 2006 we had €539.6 million of consolidated net debt.

For a description of our indebtedness, see Item 5 “Operating and financial review and prospects”. Should we be unable to generate income from ordinary operations sufficient to make payments due under the Senior Credit Agreement or the Senior Notes, this could result in a default on those financing obligations which could have a material adverse effect on our business, results of operations and financial condition.

We are controlled by our shareholders and their interests may conflict with your interests.

As of December 31, 2006, company controlled by Vittorio Tabacchi, funds advised by CSFB Private Equity and the market collectively own 100% of the capital shares of our parent company, Sàfilo Group S.p.A.. As a consequence, they have, directly or indirectly, the power, among other things, to affect our legal and capital structure and our day-to-day operations, as well as the ability to elect and change our management and to approve any other changes to our operations or strategic direction. The interests of these shareholders, in certain circumstances, may conflict with your interests as holders of the Notes. For example, our shareholders could vote to declare dividends or to cause us to incur indebtedness, in each case as permitted under the indenture, causing capital outflows or increasing our debt service obligations, all of which could hinder our ability to meet our obligations under the Notes.

Exogenous risks affecting Sàfilo

Our fashion eyewear business is sensitive to economic conditions and changing consumer preferences that are often guided by innovative products and trends.

The fashion eyewear industry is cyclical. Downturns in general economic conditions or uncertainties regarding future economic prospects, which affect consumer disposable income, have historically adversely affected consumer spending habits in our principal markets. Therefore, economic downturns or uncertainties could have an adverse effect on our business, results of operations and financial condition.

The fashion eyewear industry is also subject to rapidly changing consumer preferences. While eyewear has achieved a significant degree of acceptance as a fashion accessory, and the fashion eyewear industry has grown significantly in recent years, this growth may not continue and consumer preferences could change in a manner which will adversely affect the fashion eyewear industry as a whole and our business in particular. Changes in fashion preferences could also affect the popularity and, therefore, the commercial success of the licensed brand products. The prescription frames and sunglasses markets in which we compete could be affected by these changes in fashion trends and consumer preferences. Our future success will also depend on our continued ability to develop and introduce eyewear in accordance with consumers' shifting preferences. Any event or circumstance resulting in reduced market acceptance of one or more of these designers could reduce our sales and the value of our inventory of models based on that design. In addition, our success depends, in part, on our ability to anticipate and react to changing fashion trends in a timely manner. Any sustained failure to identify and respond to such trends would adversely affect our business, results of operations and financial condition.

The mid- and high-end prescription frames and sunglasses markets in which we compete are particularly vulnerable to changes in fashion trends and consumer preferences that are often guided by innovative products and trends. Our historical success is attributable, in part, to our introduction of innovative eyewear products which are perceived to represent an improvement over products otherwise available in the market. Our future success will depend on our continued ability to develop and introduce such innovative products.

Our business is subject to risks relating to international sales and exposure to changing local conditions.

We currently have operations in 34 countries and our products are sold in approximately 130 countries. We are therefore subject to various risks inherent in conducting business internationally including, by way of example, the following:

- exposure to local economic, political and civil conditions;
- export and import restrictions;
- currency exchange rate fluctuations and currency controls;
- changes in government regulations, including those relating to payments for prescription eyewear;
- withholding and other taxes on remittances and other payments by subsidiaries;
- investment restrictions or requirements; and
- local content laws requiring that certain products contain specified minimum percentage of components produced locally.

Our exposure to these and other risks and their potential impact on us varies from country to country and is unpredictable, but may have a significant effect on our business, results of operations, financial conditions and prospects.

Our business could be adversely affected by the availability of vision correction alternatives to prescription eyeglasses.

Our business could be adversely affected by the availability and acceptance of vision correction alternatives to prescription eyeglasses, such as refractive optical surgery. According to industry estimates, the use of refractive optical surgery has grown substantially since it was approved by the U.S. Food and Drug Administration in 1995.

Increased availability and use of vision correction alternatives could result in decreased use of our prescription eyewear products, which, in 2006, represented 37.4% of our consolidated revenues, and could have a material adverse effect on our business, results of operations, financial condition and prospects.

Because our assets, liabilities, sales and costs are denominated in multiple currencies, we are vulnerable to exchange rate fluctuations.

Our reporting currency is the Euro and we conduct and will continue to conduct transactions in currencies other than the Euro. As a result, we have been and will continue to be vulnerable to foreign exchange rate fluctuations because:

- we incur a significant portion of our manufacturing costs in Euro and generate a substantial portion of our revenues in other currencies, particularly U.S. Dollars, which represent approximately 55% of our consolidated revenues; therefore, a strengthening of the Euro relative to such other currencies in which we receive revenues could negatively impact our operating margins, which could adversely affect our business and results of operations; and

- a portion of our assets, liabilities, revenues and costs are denominated in various currencies other than Euro; as a result, our operating results, which are reported in Euro, are affected by currency exchange rate fluctuations.

Future movements of the exchange rate of the Euro against the U.S. dollar and other currencies may have a material adverse affect on our results of operations. Fluctuations could also significantly affect the comparability of performance between financial periods.

Our payment obligations are subject to fluctuations in interest rates.

We are subject to interest rate fluctuations as a result of our debt position, a portion of which is repayable at a floating interest rate, normally based on Euribor or Libor. As a result, we enter into interest rate swap contracts with the aim of hedging a portion of our interest rate risk. See Item 5 “Operating and financial review and prospects”. If significant fluctuations of floating interest rates occur, our interest obligations on the portion of interest that we have not hedged would become greater, which would adversely affect our results of operations.

Maintaining and achieving compliance with governmental regulations requires us to incur costs and may limit our operations or otherwise negatively affect our business.

Our operations are subject to various laws and regulations by governmental authorities in Europe, the United States and other jurisdictions in which we conduct business. Governmental regulations, whether in the European Union, the United States or other jurisdictions, have historically been subject to change. Violations of these laws and regulations, including those relating to the environment and other matters, could result in significant fines, or civil or criminal sanctions. We also could incur cleanup costs in the event that significant contamination is discovered at any of our facilities, or at any off-site location for which we may be responsible. In addition, new laws and regulations, or changes in how existing requirements are enforced, could require us to incur additional costs, subject us to unexpected liabilities, limit our operations or negatively affect our business.

Our operating results are subject to fluctuations in seasonality.

The market in which we operate is typically characterized by seasonal fluctuations, particularly with respect to sales of our sunglasses and the related invoicing, the majority of which is concentrated in the first two quarters of the year. As a result of these quarterly fluctuations, we believe that comparisons of our net sales and operating results between different quarters within a single fiscal year are not meaningful and such comparisons cannot be relied upon as an indication of our future net sales or operating results for the full year.

ITEM 4. INFORMATION ON THE COMPANY

HISTORY AND DEVELOPMENT OF THE COMPANY

Overview

We believe that we are the world's second largest wholesale eyewear producer in terms of net sales and that we are the worldwide leader in the high-end eyewear market segments, which comprise eyewear with retail prices above €100 in Europe and above USD100 in the United States. In 2004, our market share in the high-end eyewear market segments was approximately 40% (source: Bain & Company estimates). In 2003 we had a market share of 61% in the luxury segment of the high-end market (source: Bain & Company). Sales of our prescription frames and sunglasses positioned in the high-end market segments represented approximately 77% of our total net sales in 2006.

We design, manufacture and distribute high-quality eyewear products, including prescription frames, sunglasses frames and lenses, sport goggles and other sport accessories such as helmets and ski masks. We sell these products across a variety of geographic regions.

We believe that our prescription frames, sunglasses and brands are recognized worldwide for their high quality design and distinctiveness. We produce and distribute eyewear products under our owned brands as well as under license agreements for leading luxury and designer brands. Our license agreements typically are exclusive and have terms of five to eight years, and our relationships with some of our key licensors date back to the late 1980s. Our licensed brands include *Alexander McQueen*, *BOSS - Hugo Boss, Bottega Veneta, Boucheron, Diesel* and *55DSL, Dior, Emporio Armani, Giorgio Armani, Gucci, HUGO – Hugo Boss, Imatra, Marc Jacobs, Marc by Marc Jacobs, Max Mara, Max&Co., Oliver, Pierre Cardin, Stella McCartney, Valentino,* and *Yves Saint Laurent*. In addition, the following collections are exclusively for the American market: *A/X Armani Exchange, Banana Republic, Fossil*, *J.Lo by Jennifer Lopez, Juicy Couture, Kate Spade, Liz Claiborne, Nine West and Saks Fifth Avenue*. Our owned brands include *Sàfilo, Oxydo, Carrera, Smith* and *Blue Bay.*

We oversee the entire chain of production and distribution, which includes the following phases: technological research and innovation, product development and design, planning, purchase planning, production and quality control, marketing and sales, purchase management, distribution and logistics.

We currently operate five principal manufacturing plants, four located in Italy and one in Slovenia. We directly manage our internal production and closely monitor and supervise any third-party production. Third-party manufacturers are selected among primary manufacturers in Italy, the United States and the Asia Pacific region, in order to streamline costs, maintain flexibility during the production process and to manufacture products that are consistent with the design needs of our customers.

We operate three main distribution centers, one highly automated in Padua, one center in Parsippany (New Jersey) and one center in Hong Kong, as well as other smaller distribution centers. We distribute our products in approximately 130 countries, through a distribution network comprising 30 subsidiaries operating in 34 countries, and through approximately 170 independent distributors elsewhere. Each distribution subsidiary coordinates a network of local sales agents, most of whom sell our products on an exclusive basis, reaching over 130,000 retail points of sale, including optometrists, ophthalmologists, opticians, retail distribution chains, department store chains and specialty stores.

Our revenues are partially influenced by seasonality, as we experience our highest level of demand during the first semester due to sales of sunglasses leading up to the summer months, and we experience our lowest level of sales demand in the third quarter because, traditionally, the majority of shops are closed for some portion of the summer season.

Background

Sàfilo was founded in 1934 when Guglielmo Tabacchi (father of our current Chairman, Vittorio Tabacchi) assumed control of a lens and frame factory, Sàfilo ("*Società Azionaria Fabbrica Italiana Lavorazione Occhiali"*), which was established in 1878 in northeast Italy, a region where many leading companies in the eyewear industry are located. In 1964, we opened a second factory in Santa Maria di Sala (Venice), to which we have transferred all production of frames in acetate and cellulose. During the 1970s, we expanded our production facilities in Calalzo di Cadore, and we purchased and opened our offices in Padua in northeast Italy, the current location of our headquarters and our primary distribution facility (1975 - 1977).

Beginning in the 1980s, we began to create our first distribution subsidiaries in Belgium, Spain, Germany and France. In 1983 through 1986, we gained control of American Starline Optical Corp. (now known as Sàfilo USA Inc.), a large U.S. eyewear trading company that had been exclusively distributing our products in the United States since 1962.

The luxury eyewear market

In the 1980s our management team perceived potential for significant growth of the eyewear market and began promoting eyewear, especially sunglasses, as a luxury accessory as opposed to a device for correcting vision. We have since followed our strategy of cooperating with the leading luxury fashion houses, through license agreements for their trademarks, making priorities of innovation and superior product quality as well as being selective in our sales channels.

In line with our strategy, in 1984 we acquired Optifashion S.r.l., which had license agreements with *Ferrari* and *Ferré*. In 1988 we acquired American Optique du Monde Corp., a company that had a license agreement for the *Ralph Lauren* brand.

In the 1990s, we targeted the high-end eyewear market segments by entering into brand licensing agreements with well known fashion houses, including the following brands: *Gucci* (1990), *Pierre Cardin* (1991), *Diesel* (1994), *Dior* (related to the 1996 acquisition of certain assets of Carrera Optyl), *Max Mara* (1997), *Valentino* and *Oliver by Valentino* (1998), *Nine West* (1998), *Fossil* (2000), *Kate Spade* (2000), *Yves Saint Laurent* (2001), *Saks Fifth Avenue* (2001), *Bottega Veneta* (2002), *Stella McCartney* (2002), *Liz Claiborne* (2002), *Boucheron* (2002), *Alexander McQueen* (2002) *Giorgio Armani* (2003), *Emporio Armani* (2003), *J.Lo by Jennifer Lopez* (2003), *55DSL* (2003), *Marc Jacobs* (2004), *Imatra* (2005), *Juicy Couture* (2005), *BOSS* and *HUGO* (2005), *Banana Republic (2006), Marc by Marc Jacobs (2006), Max & Co. (2006), and Armani A/X (2006)*.

The sports goggles market

In 1996 we acquired certain assets of Carrera GmbH, a producer of specialized sports eyewear, including the Optyl know-how for plastic frames, and also acquired two manufacturing facilities in Traun, Austria, and Ormoz, Slovenia. With these acquisitions, we became one of the principal European producers and marketers of sports goggles and ski masks. In 1996, we also acquired the U.S. company Smith Sport Optics Inc. and added sports goggles targeted at the U.S. market to our product lines.

Industrial and commercial development and expansion

We began our industrial expansion plan in 1989, when we constructed a large new manufacturing facility in Longarone. The plant became operational in 1990 and was and continues to be among the most technologically advanced manufacturing eyewear plants in Europe. In 2001, we opened a centralized, highly automated warehouse at our headquarters in Padua.

During the past 15 years, we have followed a strategy aimed at strengthening and expanding our distribution network and opening distribution branches in the most promising markets in order to directly control distribution in the most important geographic areas. Implementation of our strategy has allowed us to create a closer relationship with our clients.

In 1994, we opened our Sàfilo Far East distribution branch in Hong Kong, to penetrate the Asian and Australian markets. In the late 1990s, we strengthened our presence in Europe by opening distribution branches in the UK, Greece, the Netherlands, Austria, Portugal and Switzerland, and in the rest of the world by opening distribution branches in Australia, South Africa, Japan, Brazil, India, Singapore, Hong Kong and Malaysia. In 2004, we opened our branch in Shenzhen, China, one of the markets we believe has significant growth potential.

Recent Developments

Production

During 2006, the production plant's rationalization leaded to the closure of production plant in Calalzo di Cadore (Belluno) and two minor production centers in Coseano and Ronchis (both in the province of Udine). The production carried out at the three facilities that had been closed has been moved to our other production plants, as described in "Business Strategy".

License agreements

On April 12, 2006, the Group announced the extension of the license agreement with Max Mara until the end of 2013, as well as a new agreement for the design, production and distribution of sunglasses branded *Max &Co.*. The first collection is to be launched during 2007.

On July 24, 2006, the Group presented the prestigious range of *Marc by Marc Jacobs* sunglasses for the first time on the market. The new collection strengthens Safilo's leadership further and consolidates the company's relation with the LVMH Group. The *Marc by Marc Jacobs* collection, which has started being distributed in the U.S. from October 2006 and then will be extended within one year to the rest of the world, will be subsequently completed with a range of prescription frames.

On November 9, 2006 the Group presented the first *Armani A/X* line, a young, fashion forward urban inspired collection that solidifies Safilo's relationship with the Armani Group. The line has been firstly distributed in the U.S. through the freestanding A/X Armani Exchange stores and, starting from January 2007, is distributed worldwide. A range of prescription eyewear is scheduled to follow.

On November 15, 2006 Banana Republic and Sàfilo announced a 5-year term (renewable for 3 more) license agreement for the design, development, production and distribution of both sunglasses and prescription frames under the brand *Banana Republic*. The first collection will be launched by the end of 2007 in the United States and in Canada.

Business development

On October 11, 2006 the Group announced the strengthening of its presence in the Far East, through the opening of a wholly-owned subsidiary. Sàfilo Korea Ltd, established in Seoul, started its operations in January 2007, with the target of becoming the national leader in the distribution of its products in the retail channel, through both opticians and department stores.

On November 9, 2006 the Group acquired Loop Vision, a Spanish retailer which accounted for 62 directly owned stores and 12 points of sales in franchising, further developing its presence in the retail segment of the market.

Starting from early 2007, the Group has direct access to the market in the Baltic Republics, thanks to the opening of local commercial branches.

Financial operations

On January 13, 2006, the subsidiary Sàfilo Capital International S.A. with headquarters in Luxembourg, repaid 35% of the bonds listed on the Luxembourg market (Senior notes 9 5/8%) for a total amount of Euro 105

million, making also a payment of approximately Euro 10 million for the applicable premium related to the advance repayment of the bond.

In March and April 2006, the main rating agencies (Moody's, Standard & Poor's and Fitch) upgraded the ratings on the Group and its rated loans, mainly thanks to the reduction of the leverage due to the IPO proceeds, the strong financial results and the positive outlook on the operations.

On June 26, 2006 Sàfilo Group S.p.A. announced the signing of a 400 million Euro credit facility replacing the 2002 Senior Credit Agreement. The new Senior Credit Agreement entails a significant reduction in the cost of debt, a slighter security package and less restrictive covenants.

Significant Corporate Events

In 1987, Sàfilo S.p.A. was listed on the Italian Stock Exchange. In July 2001, Sàfilo S.p.A.'s Chairman Vittorio Tabacchi acquired the majority of the share capital of that company and began a tender offer, through a special vehicle company called Programma 2002 S.p.A.. The original tender offer was launched at a price of €12.5 per share for an aggregate value of €161.3 million; the residual tender offer for the entirety of the share capital was launched at a price of €14.48 for an aggregate value of €9.4 million. After completion of the tender offer, Sàfilo S.p.A. was de-listed in December 2001.

In 2002, Sàfilo S.p.A. was merged into Programma 2002 S.p.A., which in turn was later merged into Programma 2001, another special vehicle company owned by Vittorio Tabacchi's family, which took the name of "Sàfilo S.p.A." and is the current Sàfilo S.p.A..

In December 2002 our holding company Sàfilo Holding S.p.A. (now Sàfilo Group S.p.A.) acquired, through a contribution in kind, 100% of Sàfilo S.p.A.'s outstanding share capital. In December 2002, two special vehicle companies, SunlightLuxco S.à.r.l. and SunlightLuxco II S.à.r.l., indirectly owned by CSFB Private Equity, became our holding's shareholders. Their shareholdings were later transferred to, respectively, SunlightLuxco A S.à.r.l. and SunlightLuxco III S.à.r.l., our holding's current shareholders.

On September 14, 2005, pursuant to a resolution of our extraordinary shareholders' meeting, our parent company changed its name from Sàfilo Holding S.p.A. to Sàfilo Group S.p.A.

On December 9, 2005 the shares of Sàfilo Group S.p.A., were admitted on the listing of the Italian Stock Exchange (Mercato Telematico Azionario) at an initial price of Euro 4.9 per share.

The Global Offer initially consisted in 140,000,000 shares, of which 64,300,000 shares offered for subscription, 3,947,252 shares offered to the beneficiaries of the 2003-2007 and 2004-2008 Stock Option Plans and 71,752,748 shares offered for sale by the shareholders SunlightLuxco A S.à.r.l. and SunlightLuxco III S.à.r.l..

Against the requests received and in virtue of the exercise, by the Coordinators of the Offer, of the loan option (so-called "Over allotment") totaling 16,800,000 shares, a total of 156,800,000 shares were allocated as follows:

- 37,873,800 shares to Italian retail investors in relation to the public offer;
- 118,926,200 shares, to Professional Investors in Italy and International Institutional Investors in relation to the Institutional Placement.

Following the exercise, in January 2006, of the so-called *Greenshoe* by the Co-ordinators of the Offer for a total amount of 7,667,515 shares, the selling shareholders SunlightLuxco A and SunlightLuxco III were returned the shares subject to the loan, equal to 9,132,485 shares.

The offer generated a total demand of over Euro 1.5 billion and the company commenced trading on the Stock Exchange with a capitalization of approximately Euro 1.4 billion, placing the Sàfilo Group amongst the largest Italian listed industrial companies.

The institutional placement related to the subscription of over 250 institutional investors which included the largest Italian and international investment funds. The shares reserved for the retail sector in Italy resulted in the subscription of over 43,000 private investors.

Sàfilo Group S.p.A. has used part of the proceeds received from the listing for a shareholders' contribution in Sàfilo S.p.A. for a total amount of Euro 294,713 thousand in order to give the subsidiary the opportunity to repay part of the Senior Credit Agreement and to redeem part of the Senior Notes (see "Liquidity and Capital resources" in Item 5 for further details).

BUSINESS OVERVIEW

Competitive Strengths

We believe that the following factors give us competitive advantages in the global eyewear industry:

- **a leadership position in the high-end eyewear market**. We have been in the market for over 70 years and we are one of the major operators in the sector of design manufacture and distribution of sunglasses and other eyewear products. We believe we are the global leader in the high-end market (comprising products with prices over €100 and USD100). We believe that we have obtained our global leadership in the high-end market segments through our focused strategy since the second half of the 1980s, and we intend to remain focused on these market segments.

- **a portfolio of prestigious licensed brands, focused primarily in the luxury and premium segments.** We manage a portfolio of selected brands by developing products that are consistent with our status of market leader with international prestige. We follow a marketing diversification strategy, have steadily won acceptance from the designers of the licensed brands and agreed to work with them for long periods (between five and eight years) under tailored licensing contracts, some of which have been renewed repeatedly.

- **superior product quality, design and innovation**. Our products are renowned for their quality and innovative features by both optical retailers and end customers. We believe that product quality is a key competitive factor that enables us to successfully position our products in the market. In addition, we believe that our emphasis on quality has been an important factor in establishing and retaining our leading portfolio of brands. We have traditionally placed value on product craftsmanship. All of our products are developed and designed internally by our design group of approximately 140 highly qualified employees, which we believe to be the largest design team in the eyewear industry. We have focused on providing innovative technical solutions for our end customer's optical needs.

- **worldwide distribution and sales network**. Our three main distribution centers supporting the sales network are the core of our distribution platform and are located in Padua, in Parsippany (New Jersey - USA) and in Hong Kong. Our worldwide distribution platform includes 30 commercial subsidiaries, enabling us to operate directly in 34 countries with a network of approximately 1,300 sales agents. Additionally, we are able to market our products in more than 100 countries through a network of some 170 independent distributors. Each member of our sales force is trained specifically to sell the product lines of a single licensed or owned brand. We maintain close contact with our distributors in order to monitor sales and to control the quality of the points of sale that display our products. We select our retail sales channels based on where our brands would be best placed. We believe that our careful selection of retailers is the key to our success, and has helped us to obtain and retain licenses.

- **superior client service**. We believe that we are a leader in providing service to our clients. We support our customers through our large and experienced sales force, modern call centers for telephone orders, strong advertising and promotional support at the point of sale and an extensive distribution network capable of rapid delivery. Our sales force of approximately 1,300 exclusive sales representatives is largely commissioned-based. This sales force is supported by approximately 700 persons who assist in meeting customer needs. We have created a structure inclusive of "key account managers", who assist our customer retail sales chains. For any customer assistance and re-orders, we have multi-language call centers in Europe and the United States, through which we seek to ensure that the reorder will be processed within 24 hours. The call centers use our proprietary customer relationship management software, which allows us to profile each customer and therefore process customers' requests more efficiently.

- **balanced sales mix**. We believe that we have been successful in balancing our net sales in terms of product mix, price per unit and geographic market, which allows us to hedge against market fluctuations and provides us with opportunities to expand into emerging markets. We generate a stable revenue stream (both in terms of seasonality fluctuations and as a component of our historical revenues over the past ten years) from sales of prescription frames, which have represented about half of our total net

sales and sales volume in recent years. Our prescription frame customer base primarily consists of an established network of independent optical industry professionals that purchase frames for prescription eyewear. In 2006, sales of prescription frames accounted for 37.4% of our net revenues and 29.6% of our sales in terms of number of units. We sell prescription frames to an independent client base of opticians and optometrists. On a geographic basis, our net sales by target market in the American region were 37.3% of total net sales in 2006 and our revenues in Italy and Europe were 46.4% in 2006. Within Europe, besides our home market of Italy, we have significant sales in the key markets of France, Spain, Germany and the United Kingdom. This geographic balance partly insulates us from a downturn in any particular region. Similarly, we believe that our diversified portfolio of brands mitigates against risks related to changes in fashion trends in any given market or market segment. In addition, we believe that the long-term nature of our license agreements provides stability to our sales. Finally, we believe our brands are positioned at distinct price points in the mid-range and high-end eyewear segments, and targeted at discrete groups of consumers.

- **sales growth.** In recent years, events such as the terrorist attacks on the World Trade Center, the SARS epidemic, the war in Iraq and a weakening of the U.S. dollar have had negative repercussions on the global economy. In the past ten years, however, our Group has been able to achieve constant growth in sales and revenues.

- **experienced management team**. We believe that our management team has a long track record in the eyewear industry and is well regarded in terms of industry knowledge and strategic outlook. Our management team is lead by our Chairman Vittorio Tabacchi, our Vice Chairman Giannino Lorenzon and by Claudio Gottardi and Massimiliano Tabacchi, respectively our Chief Executive Officer and our Co-Chief Executive Officer. A significant component of the compensation of our management team is based on the operating performance of our business. In addition, certain of our directors, senior management and other key employees have been granted options to subscribe for our shares under our stock option plans. See Item 6 “Directors, Senior Management and Employees”.

- **flexibility in production**. In the past few years, we have been streamlining our operations in order to achieve more efficient and flexible production. In accordance with our “lean manufacturing” plan, we have divided our production so that all our production involving metals, acetate or Optyl is each carried out in only one or two plants, so that each plant only manufactures products of only one material. Furthermore, we have increased our outsourced production, which has enabled us to optimize our production capacity at our own plants and allows us to meet peak periods of productivity without disruption and at lower costs. This strategy has also enabled our own plants to focus on production of products in the high-end market, which require more craftsmanship.

Competitive Position

The worldwide market for high quality prescription frames and sunglasses is highly competitive and fragmented. Our principal competitors on a worldwide basis are the Luxottica Group S.p.A., Oakley, Inc., Marchon Eyewear Inc., Silhouette International Schmied AG, Charmant Inc., Marcolin S.p.A. and De Rigo S.p.A. We also face competition from numerous national, regional and local companies in the markets in which we distribute our products.

We and a few other market operators, in the aggregate, represent approximately 27% of the wholesale eyewear market. In the high-end wholesale market, we had a market share of approximately 40% in 2004 (source: Bain & Company estimates). In the luxury segment of the high-end market, we held a market share of approximately 61% in 2003 (source: Bain & Company).

During the last years we believe we have steadily increased our market share in the high-end market in the principal countries where we operate. In 2004 our market share in North America was approximately 50%, in Europe it was 36%, and in Japan it was 30% (source: Bain & Company).

We believe that important competitive factors in the prescription frames and sunglasses markets include product quality and innovation, scope of product portfolio, brand name recognition, relationships with licensors, customer service and a strong distribution network. Some of our global competitors have acquired or established

their own significant retail distribution networks for their eyewear products. We instead have decided to continue to rely upon what we believe are our key competitive strengths. To showcase our luxury eyewear products, we have concentrated our retail efforts to open a small number of stores selling only luxury sunglasses in premium locations in few select metropolitan areas in the United States and Spain, thanks the acquisition of Loop Vision on November 9th, 2006.

Business strategy

We seek to strengthen our current position in the global eyewear market and enhance our financial profitability. As part of our strategy, we intend to:

- ***Improve the management of our portfolio of brands.*** We intend to continue to strengthen our portfolio of both owned and licensed brands. We believe that we are well-positioned to take advantage of the historically consistent revenues generated from sales of prescription frames to an established customer base while continuing to exploit the attractive sales growth opportunities available in the premium sunglasses market segments.

  Owned brands. We have identified the successful characteristics of each of our owned brands. We seek to ensure that each trademark reflects the consumers' wishes and to position each trademark with advertising campaigns aimed to the appropriate target audience. We aim to satisfy the needs of both our optician clients and those of the end customers. Significant efforts have been put in place in order to push sales from our owned brands, especially through dedicated marketing campaigns. The strong sales increase posted by this category of brands in 2006 proves the effectiveness of the strategies implemented during the year.

  Licensed brands. Jointly with the licensors of our global brands, we have prepared guidelines for expansion and promotion of our products to the appropriate target audience in order to achieve greater market penetration, both in terms of number of customers and of geographical areas. We carefully position our licensed brands in order to avoid duplicating brands that might appeal to the same type of consumer. Our policy is to diversify according to brand, geographical area and price, while maintaining our focus on market trends and demand.

- ***Improve our operating efficiency and effectiveness.*** We intend to improve continually the efficiency and effectiveness of our production and management processes. To achieve this goal, we are implementing the following projects:

  - *Lean Manufacturing:* This project aims to streamline our production structure and processes and concentrate, as a first step, manufacturing activities in three areas as follows:
    - Metal: at the plant in Longarone, which took over all the activities which were carried out at the Calalzo plant;
    - Plastics: at the plants in Santa Maria di Sala, Ormoz, Slovenia and Precenicco, which took over the activities carried out at the plant in Ronchis, and
    - Semi-finished products: at the plant in Martignacco which, in 2005, took over the activities carried out at the plant in Coseano.

    We believe this project will allow us to significantly increase efficiency, both in terms of making better use of available production capacity and in terms of rationalizing available production space and improve our inventory management.

  - *Time to Market:* This project is designed to help us better control the timing of our production, to avoid any backlog in order to reduce response times, limit our obsolete inventory, and avoid unnecessary work.

  - *Cost Efficiency*: This project aims to increase efficiency. We intend to improve our collections from customers and to limit our warehouse stock to improve cash flow. We

have established a compensation of our managers that is tied to performance and to increasing cost efficiency.

- ***Strengthen distribution and expand in new markets.*** We wish to continue our policy to strengthen our direct and indirect distribution network in the markets in which we operate, and to enter other markets with high-growth potential. We intend to select a specific market strategy for each market we approach, focusing on wholesale distribution. In more mature markets, we plan to improve our wholesale commercial structure, to become leaders in the wholesale channel. In growing markets where we are already present, we plan to increase our marketing activity, especially in high-growth markets such as China, India and Brazil. In other high-growth potential markets, such as Russia, we intend to continue to select local partners who have a tight control on distribution and a highly qualified sales network, aligned with our licensed portfolio. On January 1st, 2007 a new commercial subsidiary based in South Korea, which we believe to be a high-growing potential market, has become operational. Our target is to become market leader in the distribution of our products in the retail channel, through both opticians and department stores. Our "Selective Luxury Retail" project intends to strengthen our distribution network. We plan to increase the number of our U.S. Solstice stores, to increase the visibility of luxury eyewear specialty stores and enhance the prestige of our high-end licensed brands. As a consequence, during 2006, we have opened 31 new stores in the United States.

- ***Continue to focus on superior design, development and innovation***. In our 70 years of operations we have always emphasized technological research, design and innovation. These recent projects are examples of our commitment to technological innovation, which is linked to research and development machinery and products. Recently, we especially focused on the development of interchangeable 3-piece rimless frames, which can be used again after changing prescription frames (such as Giorgio Armani models no. 417 - 418 – 419 – 457). We provided our sport products with new features, as in the case of the Carrera XChange ski goggle (which has interchangeable lens), or with our sport helmets that allow for exclusive adjustable fitting system. Also, we are going on exploring the possibilities of nanotechnology, as it is more and more evident that it will determine great modifications on construction materials, production processes and product performances.

Products and brands

We design, manufacture and distribute high-quality eyewear in three product categories: prescription frames, sunglasses and sports goggles. Our product portfolio comprises both owned and licensed brands in the prescription frames and the sunglasses product categories, and owned brands (such as Carrera and Smith) in the sport products category.

Our prescription eyewear and sunglasses products are positioned mainly in the high-end eyewear market segments.

Our products are complementary, insofar as sunglasses are viewed by the market more as a fashion accessory and as related to fashion trends, while prescription frames are more linked to demographic trends.

We continually design and launch new models and update existing models to match consumers' preferences, fashion trends and technological innovations. Our products are generally launched concurrently with spring/summer and fall/winter fashion collections. Every quarter, generally in January, April, August and October, existing models are updated with new designs, colors and color combinations to meet uses and preferences in different geographic regions.

Every year we launch over 2,500 new prescription frames, sunglasses and sports goggles, making over 4,500 models of eyewear for sale each year.

Brand Portfolio

Our brand portfolio includes:

- our owned brands, for prescription frames, sunglasses, sports products; and
- licensed brands, for prescription frames and sunglasses.

To minimize the impact of volatility in consumer preferences, we aim to diversify our brand portfolio in terms of geographic area, gender, age, income and preference of the end user. Generally, we enter into worldwide agreements for our licensed brands, except where the trademark is one of principally local importance.

Our diversified portfolio includes brands of world-famous fashion designers, such as *Armani, Dior*, *Gucci* and *YSL*, fashion designers with a strong reputation in North America, such as *Liz Claiborne, Juicy Couture* and *Nine West,* specialized trademarks such as *Carrera, Imatra* and *Smith* and luxury sport trademarks, such as *Emporio Armani*. Our portfolio is diversified also in terms of age of the targeted consumer. For example, *Diesel* and *Kate Spade* appeal to younger customers, while *Valentino* and *Max Mara* appeal to consumers in a higher age range.

Owned Brands

Our owned brands are of strategic importance for our objectives in the mid-range and mid-to-high markets in the fashion, casual fashion, and sport segments. Our portfolio of owned brands includes *Sàfilo*, *Oxydo*, *Blue Bay*, *Carrera*, and *Smith*. Each of these brands is positioned to address a specific market segment.

Additionally, we have minor trademarks, such as *Adensco, Chesterfield, La Strada, Maurice Saint Michel, SunCloud and Denim*, which are used mainly in the U.S. market.

Sàfilo is our historic trademark, and since the 1930s has been the cornerstone of our international development of prescription frames. Today the *Sàfilo* brand is considered our "family master brand" and is positioned in the mid-range to high-end prescription eyewear segments. The *Sàfilo* brand has several sub-brands, each with specific collections and each targeted to consumers in a specific age range:

- *Sàfilo Junior*, for children from 4 to 14 years of age;
- *Sàfilo Design*, to meet the style, design and technological preferences of adult males;
- *Sàfilo Prestige*, this line is intended to meet the fashion and style preferences of a refined adult female clientele;
- *Sàfilo Diamond*, for women, and intended to connote great attention to details;
- *Sàfilo Library* and *Elasta*, designed mostly for a more senior clientele and to privilege functionality; and
- *Seventh Street*, for adolescents and young adults up to the age of 30, characterized by the use of vivid colors and innovative design.

We distribute the *Sàfilo* brand in most of the 130 countries we serve. In certain markets such as the United States, Japan and Germany, we develop specific collections to match the preferences or to fit the physical characteristics of local consumers.

The *Sàfilo* brand is our flagship brand, and during the next three years we plan to increase public awareness of this brand with advertising campaigns targeted to consumers and optical retail channels and to add innovations to the brand products to reinforce their image of specialist leader brand in prescription frames.

Oxydo was launched in the mid-1990s and is positioned in the casual sport segment. We plan to focus on the sunglasses sector, which is experiencing significant growth. The brand appeals to fashionable young adults

(18-35 years of age) of both sexes through its colorful and innovative design. Although the *Oxydo* brand is distributed primarily in the European markets, we intend to widen its distribution internationally, with specific advertising investments targeted to consumers and using testimonials from the music industry.

Blue Bay was launched in the early 1990s and is targeted to younger consumers (adolescents) who prefer not to wear designer eyewear but are still interested in good design and innovative colors. *Blue Bay* products are mainly sold in the European market, predominantly in Italy, Spain, France and Germany. We intend to test whether the Blue Bay brand has potential for a successful international distribution and to promote the brand's youth-oriented image with specific trade marketing activities.

Carrera is a specialized sports goggle and eyewear brand. We purchased the *Carrera* trademark in 1996 and it has been crucial in our development in the sports goggles and eyewear sectors, mainly in the European market and in emerging economies. The *Carrera* brand is targeted mostly to men who pursue outdoor and highly physical recreational activities. We support this *Carrera* brand image with advertising involving sports figures active in the fields of skiing, rugby, motorcycling and cycling. We wish to further strengthen the *Carrera* trademark in the main European countries and to test whether it could successfully be distributed in all our markets.

Smith is one of the most popular U.S. sports goggle and ski mask brands, and it is also sold in over 50 other countries. We acquired the *Smith* brand in 1996. Designed for active and competitive sports, such as free-style skiing, surfing and mountain biking, *Smith* sunglasses are targeted to young adults interested in technological innovation.

Licensed Brands

Our portfolio of licensed sunglasses and prescription frames, comprising brands from many of the leading luxury designers in the world, is one of the broadest and most diversified portfolios in the eyewear industry. Each of our licensed brands is designed, positioned and marketed to address a specific eyewear market segment. Our portfolio consists of both global brands, such as *Armani, Dior, Gucci,* and *YSL*, and brands positioned to address specific segments of the U.S. market, such as *Fossil, Kate Spade*, *Liz Claiborne*, *Nine West,* and *Saks Fifth Avenue*.

Our licensed brand eyewear products are positioned mainly in the high-end of the market, predominantly in the luxury segment.

The Group's brand portfolio as of the date of this Annual Report, comprising the most significant terms of the underlying agreements, is presented below:

Griffe	Term	Territory
ALEXANDER MCQUEEN	2002/2008	Worldwide
A|X ARMANI EXCHANGE	2006/2012	USA and Canada + Boutiques located worldwide
BANANA REPUBLIC	2006/2012	Worldwide Initial authorized markets: USA and Canada
BOTTEGA VENETA	2002/2008	Worldwide
BOUCHERON PARIS	2002/2008	Worldwide
DIESEL JEANS AND WORKWEAR	1996/2010	Worldwide
55DSL	2003/2010	Worldwide
Dior	1996/2010	Worldwide
EMPORIO ARMANI	2003/2012	Worldwide
FOSSIL	2000/2008	USA and Canada
GIORGIO ARMANI	2003/2012	Worldwide

GUCCI	1986/2010	Worldwide
BOSS HUGO BOSS / HUGO	2006/2013	Worldwide
IMATRA R.C., INC. by Safilo	2005/2008	UE, USA, Brasil, Japan, Australia, Malaysia, South Africa, China, Russia
JLO by JENNIFER LOPEZ	2002/2008 + 3 years under certain conditions	Worldwide, but in accordance with a roll-out plan: MAR 2006: Canada, Brasil & Mexico; OCT 2006: Italy, France & Spain; MAY 2007: Germany, UK & Japan
JUICY COUTURE	2005/2008	USA
kate spade	2000/2007	USA
liz claiborne	2002/2007	USA
MARC JACOBS	2004/2011	Worldwide
MARC BY MARC JACOBS	2007/2011	Worldwide

MAX&Co.	2006/2013 (1st collection October 2007)	Worldwide
MaxMara	1997/2013	Worldwide
NINE WEST	1999/2008	USA
OLIVER by VALENTINO	1998/2007	Worldwide
pierre cardin	1991/2010	Worldwide (USA excluded)
SAKS FIFTH AVENUE	2001/2011	USA
STELLA McCARTNEY	2002/2008	Worldwide
VALENTINO	1998/2011	Worldwide
YVES SAINT LAURENT	2001/2010	Worldwide

We pay a royalty for the use of the licensed brand name based on a percentage of the net sales of that brand. Under most of our licenses, we have to pay minimum annual guaranteed royalties to the licensors. Generally, minimum guaranteed royalty payments are payable quarterly and are calculated either as a predefined percentage (generally from 70% to 80%) of the previous year's royalty payments or, less often, are a predefined minimum amount.

Our licenses typically have a duration of five to eight years. In certain circumstances, for example if we have a change of control, outsource production without consent of the licensor, sell models that are not approved by the licensor, fail to reach minimum sales targets or sell products through distribution outlets that have not been approved by the licensor, a licensor may terminate a license agreement.

Pursuant to our license agreements, we incurred in royalty expenses of €98.5 million in 2006 and of €91.0 million in 2005.

The license agreements require us to invest a certain percentage of the previous year's sales for advertising and promotional campaigns for the licensed brand. Some licenses require us to contribute further amounts to the budget for the promotional activities carried out directly by the licensor.

Our portfolio of brands licensed from fashion designers is described below.

Alexander McQueen. The *Alexander McQueen* collection was launched in April 2004. Belonging to the Gucci group, *Alexander McQueen* is a design brand intended to convey creativeness and innovation. Collections for this brand use innovative materials, such as wood, lace and exclusive colors. The *Alexander McQueen* brand is intended to appeal predominantly to women from 25 to 45 years of age and is positioned in the luxury segment. The products are sold worldwide, mainly in Europe and the Asia Pacific region.

Armani A/X Exchange. The *Armani A/X Exchange* line is young, metropolitan and with strong stylish features. It conveys the accessibility and the spirit typical of the brand, which is originally interpreted and visible in all the models of the line. The collection is young, fashion forward, urban inspired and wide ranged, comprising models both in acetate and metal. The newly affordable priced sunglass line stays true to this spirit featuring a dynamic and comprehensive range of styles with the iconic A/X logo incorporated innovatively throughout.

Banana Republic. Banana Republic is a prestigious yet affordable modern luxury brand. The collection is targeted to the American market, especially to young men and women, among who the brand is most recognized and appreciated.

Bottega Veneta. We launched the first *Bottega Veneta* collection in March 2003. The *Bottega Veneta* brand is intended to convey exclusivity, elegance and craftsmanship, and therefore this brand's products are highly distinctive, with a trademark braided pattern, and bear no logo. *Bottega Veneta* appeals mainly to a female clientele, aged from 30 to 45 years of age, and is positioned in the luxury segment. The products are sold worldwide, mainly in Europe and the United States.

Boucheron. Boucheron is a brand of the Gucci group, and is the symbol of the French jewelry designer. The brand is positioned in the luxury segment. The products are created using materials inspired from the jewelry designed by the famous jewelry house since 1858. *Boucheron* are designed to appeal to customers who are sophisticated and elegant; the prescription frames are targeted to both men and women over 30 years of age, while sunglasses are targeted mostly to women over 40 years of age. The products are sold worldwide, mainly in Europe and the Asia Pacific region.

Diesel. The *Diesel* brand began as a jeans fashion brand, and *Diesel* eyewear is intended to convey aggressiveness, irony and to be in the forefront of fashion trends. *Diesel* products are targeted to young adults, aged from 15 to 35, of both sexes, and are positioned in the fashion segment of the market. The products are sold worldwide.

55DSL. A new innovative trademark of the *Diesel* group designed to appeal to young urban customers who enjoy vintage, 1970s-inspired products. *55DSL*'s products, with their angel-shaped logo, are targeted to young adults, aged from 15 to 24, of both sexes and are positioned in the fashion segment of the market.

Dior. *Dior* is a leading French luxury brand. *Dior* products are distinctive and exclusive both in shape and color. The collections are targeted primarily to women, but we have launched a collection, called *Dior Homme*, targeted to men, intended to convey technological innovation, modernity and elegance. *Dior*'s customers are generally aged from 16 to 40 and the brand is positioned in the premium and luxury segments of the market. The products are sold worldwide.

Emporio Armani. The *Emporio Armani* brand is intended to convey informality and extroversion, and uses various materials within the same product. The brand is targeted to young customers of both sexes and is positioned in the fashion segment of the market. The products are sold worldwide.

Fossil. The *Fossil* brand products are designed to complement the styling of *Fossil* brand watches. Fossil has a specific line for children's eyewear. The products are targeted to customers of both sexes, aged 18 to 55 and is positioned in the mid range of the market, in the casual-sport segment.

Giorgio Armani. *Giorgio Armani* brand products are intended to be elegant and simple, and to convey Italian style. The materials used are of the highest quality and exclusive to this brand, and each model has its own characteristics. We use advanced technologies to obtain a comfortable and functional product. The *Giorgio Armani* brand is intended to appeal to women and men, and is in the premium and luxury segments of the market. The products are sold worldwide.

Gucci. The *Gucci* brand is one of the most famous trademarks in the world and the eyewear products are well-recognized. The collections offer a wide range of models, mostly intended to convey sophistication and stylishness, and include the famous Gucci detail and style. The products are targeted to both men and women, aged 20 to 50, and are positioned in the premium and luxury segments of the market. The products are sold worldwide.

Hugo Boss. The *Hugo Boss* brand conveys class and elegance, care for the details and top quality materials. Hugo Boss' products are marked with the HUGO BOSS and BHB logos.

Imatra. Under the *Imatra* brand, we intend to convey the unity of the fashion world with the sports world. Motor GP winner Valentino Rossi promotes *Imatra*, which was developed to convey his image and was launched in April 2005. The *Imatra* brand is intended to appeal to men and women aged from 20 to 50 and is positioned in the casual-sport segment of the market. The products are sold predominantly in Europe.

Jennifer Lopez. The *J. Lo by Jennifer Lopez* brand was launched in 2001. The collections are intended to convey modernity, loudness, aggressiveness and self-assertiveness, and target young adults of both sexes from 15 to 30 years of age. The products are in the mass segment and are sold predominantly in the United States and, to a lesser extent, in Canada.

Juicy Couture. The *Juicy Couture* is a new brand, part of the Liz Claiborne Group. The brand is targeted to women aged 8 to 80 and is positioned in the fashion segment of the market. These products are sold exclusively in the United States.

Kate Spade. The *Kate Spade* brand is designed to embody clean classic lines, and the colors used are intended to convey sophistication. The collections are targeted to women 25 to 55 and are positioned in the fashion segment of the market. These products are sold exclusively in the United States.

Liz Claiborne. The *Liz Claiborne* brand, well known in the United States, is intended to convey femininity and classic style, with attention to color. The portfolio of this brand includes also the trademarks: *Villager, Lizwear*, *Crazy Horse, Axcess* and *First Issue*, which are lower priced lines targeted to a different market segment. The *Liz Claiborne* collections target women from 30 to 55 and men from 25 to 54 years of ages and are positioned to cover different market sectors. The *Liz Claiborne* trademark is in the casual segment. These products are sold predominantly in the United States.

Marc Jacobs. The brand is intended to embody two characteristics: fashion and quality. The collections are targeted to women from 25 to 45 years of age. The products are positioned in the luxury segment of the market. The products are sold worldwide.

Marc by Marc Jacobs. The *Marc by Marc Jacobs* collection, which is made up of a complete range of sunglass models produced in acetate and metal, is aimed at a young target that seeks fashion's most up-to-date tendencies. The styles capture vintage elements reinterpreting them in a modern and elegant style with the exclusive design details that are typical of the American stylist.

Max Mara. The *Max Mara* collection was launched in 1998, and is intended to convey distinctive elegance and refined identity reflecting the characteristics of the image projected in other *Max Mara* products and

accessories. We will continue to work closely with the licensor to harmonize the *Max Mara* eyewear collections with its other products and accessories, particularly the colors that characterize the *Max Mara* clothes line. The *Max Mara* collections are targeted to women aged 25 to 50 and are positioned in the fashion and premium segments of the market. The products are sold worldwide, predominantly in Europe and the Asia Pacific region.

Max & Co. The *Max & Co.* brand is predominantly targeted to young and stylish people. This brand perfectly suits the brand portfolio of the Group, widening the scope of customers which we address our products to. Eyewear products under the brand *Max & Co.* will be firstly presented to the market during 2007.

Nine West. The *Nine West* brand is a well known shoe and accessory trademark in the United States. The products are intended to be fashionable and trendy. The *Nine West* collections are targeted to women and men aged 18 to 30, and are positioned in the fashion segment of the high-end market. The products are sold in the United States.

Oliver. The *Oliver* brand was launched in 1998 along with *Valentino*. The *Oliver* collections are unisex in style and targeted to young customers aged 18 to 30. The products are positioned in the fashion segment of the market and are sold worldwide, predominantly in Europe.

Pierre Cardin. Under the *Pierre Cardin* brand, we produce "classic" prescription frames and sunglasses targeted for the mid-range market segment. The collection was launched in 1991, and has a very broad range, targeted to customers of both sexes aged 18 to 60. The products are positioned in the fashion segment and are sold in almost every country, but predominantly in Europe.

Saks Fifth Avenue. *Saks Fifth Avenue* collections are designed to embody simple elegance and understated designs and are targeted to women aged 25 to 55. The products are positioned in the fashion segment and are sold in the United States and Canada.

Stella McCartney. *Stella McCartney* is a new brand, inspired by vintage collections. We do not use any animal or vegetal products for these collections, respecting the desires of the designer. The collections are mainly targeted to women customers, aged 25 to 50, and are positioned in the fashion segment. The products are sold worldwide, predominantly in Europe.

Valentino. The *Valentino* brand is intended to convey Italian style, creativeness and elegance. Each model in these collections bears the distinctive "V" mark, in various colors. *Valentino* eyewear products are set apart by special details and innovative shapes. The collections are targeted to men and women aged 25 to 50, and are positioned in the luxury and premium segments of the market. The products are sold worldwide.

Yves Saint Laurent. The *Yves Saint Laurent* brand is intended to reflect French luxury and classic design, with sophisticated collections, and uses exclusive materials and a variety of shapes, bearing the "YSL" logo. The collections are targeted to men and women aged 25 to 50, and are positioned in the luxury and premium segments. The products are sold worldwide.

Our Business Model

Our business model covers the entire production and distribution process, from the research and development phase up through the distribution and logistics phase, seeking to assure a high quality product with a flexible and efficient production and distribution process. We strive to satisfy client demand and preferences based on the most recent trends and to achieve an efficient time-to-market of our products. Our production and distribution process starts with the development and design of the collections followed by production of the volumes determined jointly with the marketing department. Thereafter, our production is distributed to tens of thousands of opticians.

The graph below sets forth the time cycle of our production and distribution process for prescription frames and sunglasses, which lasts approximately nine months from design to finished product.

Our product development takes into account recommendations and other input provided by our internal designers and brand managers and by our licensors, as well as by our continued research and development efforts and technological innovations. Our planning process also considers data related to the sales of our products, client suggestions and market trends.

The manufacturing of our products is carried out internally in our five facilities and externally through selected third-party manufacturers. Quality control for both internal and external manufacturing is managed directly by our personnel.

The sales campaign is principally carried out by exclusive agents. Our distribution centers, the three principal of which are in Italy, the United States and Hong Kong, supply the products to retailers and wholesalers.

Planning, Programming and Purchases

The Planning, Programming and Purchases departments are under the direction of the operating division.

The Planning department uses information from internal sources (focused on commercial activities, promotional events, forecasts for sales by semester and past data) and from external sources (such as orders from clients and feedback from significant clients to indicate market trends) in order to make weekly production demands to be sent to the Programming department.

The Programming department analyses the production demands provided by the Planning department to develop a weekly production plan and to order supplies, taking into account the quantities available in our warehouses, the products under production and the limits on production capacity. The Programming department uses a system of analysis called Global Planning System (GPS). The GPS amends the weekly plan of production on a daily basis and further subdivides it for the two internal production divisions, one for plastics and one for metal, and for the outsourcing division. The outsourcing division purchases mid-range and lower-range finished products from third party manufacturers.

The Purchase department is responsible primarily for the purchase of raw materials (such as resins and catalysts for Optyl, steel, metals, lenses, cases and other packaging) and in exceptional circumstances also of other semi-finished goods such as temples and nosepieces. This department is managed primarily by the central office in Padua and partially by the Slovenian production subsidiary in Ormoz.

To guarantee the quality of raw materials and semi-finished goods, we use suppliers that we select and continuously assess on the basis of their delivery times and their ability to maintain certain standards of quality of materials and availability of production capacity.

We purchase raw materials and semi-finished goods primarily in the European market (78%) and to a lesser extent in other markets (approximately 21% in the Asia Pacific region and 1% in the United States). The acquisition of our subsidiary Lenti S.r.l. in 1996 has brought us the know-how for the production of lenses for sunglasses.

Production

We manufacture our products in our plants and through third-party manufacturers. In 2006, we produced nearly half of our prescription frames and sunglasses in our plants, with the remaining portion being manufactured by third-party manufacturers in Italy, the Asia Pacific region and the United States. In 2006, almost all *Carrera* ski masks were produced in our plants, and *Smith* ski masks were produced by third-party producers in the United States under the supervision of our design team.

Over the course of the past years, we have progressively increased the volume of production outsourced to third-party manufacturers, who are mostly located in the Asia Pacific region. This has allowed us to significantly reduce costs and has given us greater flexibility in production. We produce internally all our products that entail a very high degree of craftsmanship.

Direct Production

Our internal production is carried out at our four plants in Italy and at the Ormoz plant in Slovenia. Our Italian subsidiary, Lenti S.r.l., produces a part of the lenses for sunglasses we use in our products.

The following table sets forth the location and the production specialization of our plants as of the date of this Annual Report.

Product Division	Plant	Country	Production Specialization
Plastics	Santa Maria di Sala	Italy	Finished products
	Precenicco	Italy	Finishing, assembly and varnishing
	Ormoz	Slovenia	Semi-finished products, optyl, and injected plastics
Metals and semi-finished products	Longarone	Italy	Finished products
	Martignacco	Italy	Components and accessories

Aiming to streamline production coherently with our business plan, we have a system whereby each plant is specialized in working with specific materials and production technology and we have transferred the production from the plant in Traun (Austria) to our Italian plants. In 2006, 54.0% of the frames we produced (excluding ski masks) were metal, and 46.0% were of plastic materials.

The main plastic materials we use are described below:

- *Cellulose acetate*: this plastic is the most widely used in the production of eyewear frames, and is obtained from particles of cotton and wood and can be colored in a variety of ways. Acetate is worked by cold-cutting sheets of various sizes using precision machines. The advantages of working with acetate derive from the fact that it is easy to process and mould into the required shape, it is easy to insert lenses in acetate frames, and the shape of acetate frames does not change over time;

- *Injected plastics*: this material is injected in especially designed moulds at the liquid state. Use of this material guarantees characteristics of transparency and a high degree of flexibility in the choice of shape and size. Additionally, the material allows for high quality of colors and is very durable, it reflects light and it is highly resistant to sweat, cosmetic products and alcohol based detergents; and

- *Optyl*: this is a heat-hardening resin obtained through a specific and unique technique we developed internally. Moreover, it has a polished surface and more heat-resistance than other thermoplastic materials. Among its other advantages are that it is light and comfortable, adapts easily to the shape of the customer's face, does not deform at high temperatures, is resistant to sweat and cosmetic products, is non-allergenic and has unique color effects. easily to the shape of the customer's face, does not deform at high temperatures, is resistant to sweat and cosmetic products, is non-allergenic and has unique color effects.

The main metal materials we use are described below:

- *Titanium*: this material is used for luxury frames and does not contain any nickel. The advantages of titanium frames are their very light weight (titanium weighs 48% less than other metal alloys),

resistance against corrosion, resistance to high levels of acids, sweat and cosmetics, non-allergenic qualities and adaptability to the shape of a customer's face; and

- *Steel*: because steel can be cut very finely, weighs little, is resistant, allows for versatile designs, and is extremely flexible, it is one of the most useful materials for frames. Other advantages of steel are that it is guaranteed to resist corrosion, sweat and rain, is lightweight and adapts to the shape of a customer's face.

Phases of Production

The phases of production leading to the finished product can be grouped into three broad activities.

- *Structural manufacturing*: in this stage, the structure of the frame is made using moulds based on prototypes developed by the internal design team. For plastics, this stage of production uses milling, injection and sifting, while for metals it involves welding;

- *Treatment*: in this stage, the frames are varnished or treated with various coating methods. For plastics, the process involves coloring and varnishing; for metals, it is completed by galvanic treatment and varnishing the surfaces; and

- *Finishing*: in this phase, the products are assembled and completely accessorized. This is the most labor-intensive process. Lenses for sunglasses are cut at this stage. Both for plastics and for metals this production stage involves a process of assembly and finish.

We continually research, develop, design, and internally fine-tune precision instruments and moulds in order to improve the effectiveness, efficiency and quality of the production process. We believe that carrying out this activity internally will allow us to reduce time-to-market and consistently save on production costs.

Production by third parties

Our policy on outsourcing aims to optimize our productive capacity and to decrease costs. We avail ourselves of third-party manufacturers in Italy, the Asia Pacific region and the United States. Production of fewer units, or of models requiring complex handicraft work, is outsourced only to Italian manufacturers. Production of a greater number of units are outsourced to Asian manufacturers. This policy allows us to manage either peak production or low demand periods and to focus our own production on products targeted to the luxury market segment.

Quality control

Our quality control procedures aim to offer our clients products that meet not only the applicable safety regulations but also the best quality standards. We have a dedicated team, coordinated by a manager, in each of our production facilities and distribution centers.

We test incoming raw materials and semi-finished products, production and distribution processes and finished goods (or final products).

Quality control of incoming raw materials and semi-finished products

Our quality control system is the same for all types of incoming materials/products. We carry out laboratory analysis to verify that the quality of incoming materials/products is in line with our standards. Quality control on raw materials is carried out on the basis of strict criteria. Our quality control involves:

- identification of the technical and chemical characteristics of the products; and

- sample survey of incoming raw materials and sample testing prior to purchase

Quality control of the production and distribution processes

We monitor all phases of the production and distribution processes, and we sample test our products for defects and irregularities.

Quality control of finished goods (or final products)

We sample test our finished products by:

- mechanical resistance tests: the frames and their parts are tested for strength, movement and endurance; and
- physical chemical resistance tests: we simulate aging from sun exposure, using a powerful source of UV light. We test products by exposing them to aggressive chemical substances at higher than normal temperatures.

Finished goods manufactured by third parties are inspected, on a sample basis, prior to delivery to our distribution centers. We have two quality control teams, one located in Hong Kong and one located in the Italian production facilities and in the Padua distribution center. Most of our Asian manufacturers have obtained ISO certifications.

All our products bear the CE logo and are ISO 9001:2000 certified. After obtaining the ISO 9002:1994 quality certification in 1996, in 2003 we obtained by the ISO 9001:2000 quality certification Det Norske Veritas (DNV). We have also achieved the International Quality Rating System (IQRS). The ISO 9000 standards series is an international quality management standard sanctioned by the International Organization for Standardization based in Geneva, Switzerland.

The ISO 9002:1994 standards set out 20 provisions for developing, implementing and maintaining an effective quality management system.

Marketing and Communication

Our marketing strategy seeks:

- to ensure the correct image of the brands in our portfolio, positioning them in the high-end market—mostly in the luxury and premium segments, and
- to communicate to our customers the design and technology behind all products (prescription frames, sunglasses, sports goggles).

We develop our marketing strategy and advertising plan worldwide by a three-year marketing plan and by a one-year plan. We develop our plans considering market trends, customer needs, prices, type of products and advertising and promotional investments. We develop and implement a strategy for the marketing of each brand in our portfolio in order to achieve the optimal positioning of the individual brand and avoid products with overlapping images. We develop the strategy for each licensed brand working closely with the licensors. In 2006, our total investment in marketing and advertising activities was approximately €88.8 million, equal to 7.9% of the consolidated revenues.

Our marketing and communication activities comprise both activities dedicated to customers and trade marketing in our points of sale. Activities dedicated to customers constitute about two-thirds of our advertising and promotional investments. We mostly use the press (weekly and monthly magazines), posters, television (mainly for our owned brands), sponsorships (with particular reference to sports goggles branded *Carrera* and *Smith*), public relations with fashion journalists and product placement with fashion, sports and show business personalities. Trade marketing activities in our points of sale comprise approximately one-third of our advertising and promotional investments. These activities are important to foster customer confidence. We provide marketing materials to our points of sale, such as posters, banners, displays, specialized window displays as well as training courses and brochures of our brands and products.

We focus on the quality of advertising and promotional materials to ensure the appropriate positioning of our brands. Our marketing and promotion program with respect to each point of sale is divided into four promotional campaigns per year to support the launch of collections of new products, which generally occurs in January, April, August and October. We emphasize corporate communication both through our participation to the most important trade fairs worldwide, including the Mido in Milan, the Visionexpo in the United States and the Silmo in Paris, and through internet communication on our website.

We coordinate promotional materials and activities with the licensors. We benefit from the promotional and advertising activities directly carried out by the licensors. We take part in this activity by paying the licensors a predetermined percentage of our turnover related to the products with licensed brands. We allocate our investments on a geographical basis pursuant to medium- to long- term strategic purposes of growth identified in our three-year plans. Our promotional activity and our media strategy are coordinated with and adapted to the specific market needs to ensure efficiency in our marketing efforts.

On December 31, 2006, our marketing and promotion department comprised approximately 130 persons, who work in the central coordinating unit and marketing divisions, which are located in the various business units and in each commercial subsidiary.

Sales and Distribution

Our products are primarily sold to wholesale customers, and to a much lesser extent to retail customers, in approximately 130 countries and approximately 130,000 points of sale.

The table below shows our consolidated revenues for the financial years ended December 31, 2004, 2005 and 2006, broken down by target market and distribution channel.

	December 31,					
(Euro in millions)	**2004**	**%**	**2005**	**%**	**2006**	**%**
Italy	123.5	13.1	138.6	13.5	159.7	14.2
Europe (excluding Italy)	329.6	34.9	339.4	33.1	357.7	31.9
The Americas	332.3	35.2	353.7	34.5	379.8	33.8
Asia Pacific	99.8	10.6	119.8	11.7	129.2	11.5
Other	40.5	4.2	44.2	4.3	53.2	4.7
Wholesale total	925.7	98.0	995.7	97.1	1,079.6	96.2
Solstice [(1)]	19.0	2.0	29.6	2.9	38.8	3.5
Loop Vision [(2)]			-	-	3.6	0.3
Retail total	19.0	2.0	29.6	2.9	42.4	3.8
Total	**944.7**	**100.0**	**1,025.3**	**100.0**	**1,122.0**	**100.0**

(1) Specialized retail channel in the United States.
(2) Specialized retail channel in Spain.

Our clients are independent opticians, optometrists, chains of optics stores, department stores, specialty stores, our licensors' stores, duty free and sports gear stores.

We distribute our products directly in 34 of our largest markets (representing approximately 90% of our consolidated revenues in 2006) through our 30 commercial subsidiaries. In the remaining markets, where we do not have commercial subsidiaries, we distribute our products through some 170 independent distributors. Each

distribution subsidiary coordinates its own network of sales agents who are, in most cases, compensated on a commission basis. Our network of sales agents currently consists of about 1,300 sales agents and, depending on the country, approximately 30% are employees, while the rest are independent sales agents. Our agents sell our prescription frames and sunglasses exclusively, and undertake not to sell our competitors' products with regards to sports goggles and other sports products.

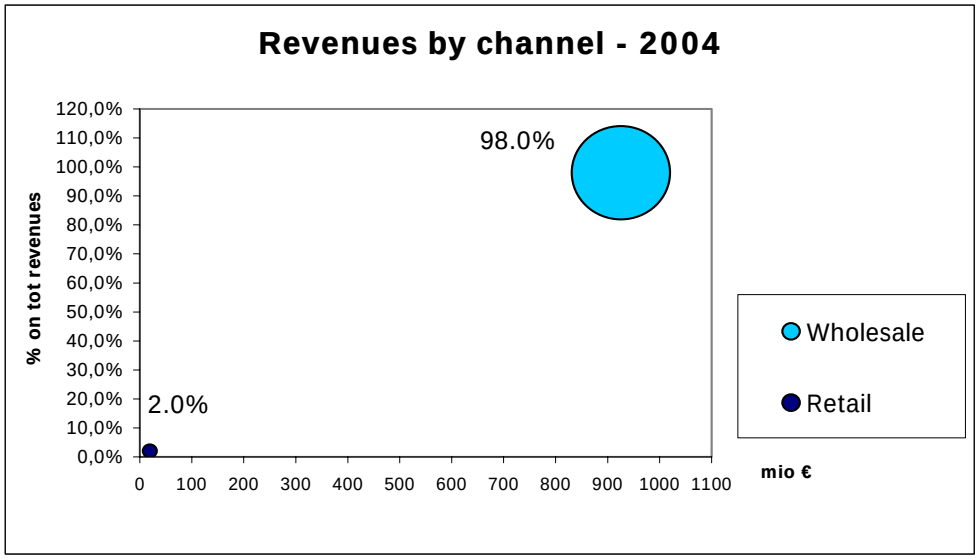
In our major markets, such as Europe and the United States, we have created dedicated sales teams led by Key Account Managers, which service the major chains selling eyewear in the territory.

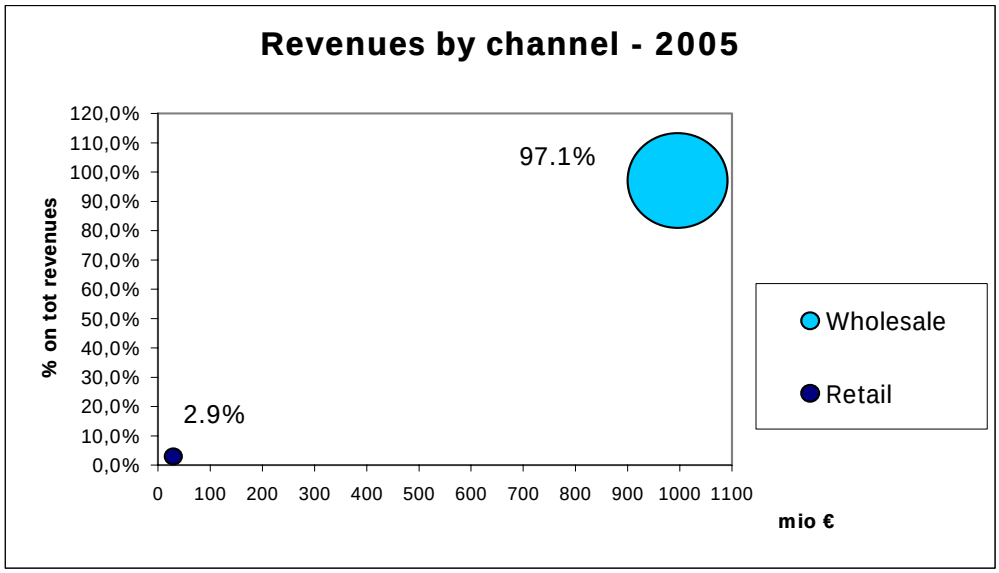
We maintain close contact with our distributors in order to monitor sales and to control the quality of the points of sale that display our products. We typically enter into distribution agreements with such distributors that establish minimum annual purchases and impose territorial limitations. In addition, to the extent permitted by law, we allow for distribution only through specifically authorized retail channels and qualified sales agents. We select our retail sales channels based on where our brands would be best placed.

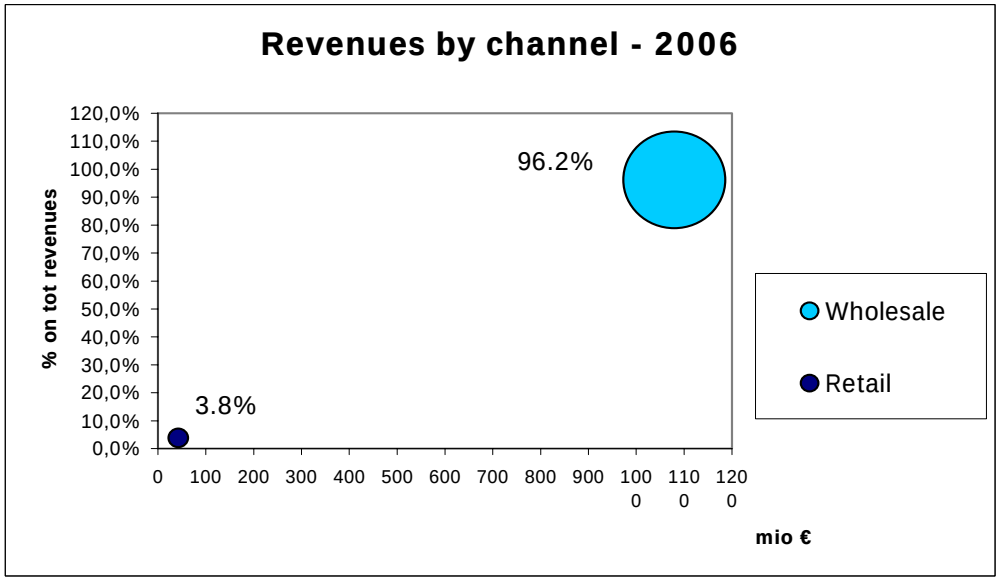
Additionally, we have a number of showrooms in prime locations to showcase our products in Milan, New York, London and Paris.

Our distribution network is divided geographically into three divisions called "business units" covering, respectively, the Americas (North and South America), Asia and Australia, and Europe and other parts of the world. Each business unit is managed by a top manager reporting directly to the chief executive officer who is responsible for the overall coordination of the three business units.

During 2006, we have further developed the retail channel of distribution by growing in the American market through the opening of 31 stores of the Solstice chain and through the acquisition of the high-end market Spanish chain Loop Vision. The graphs below highlight the increase both in absolute values and in percentage on sales of the retail channel in spite of the wholesale distribution, which nevertheless still accounts for most of the Group sales.




Revenues by channel - 2005
% on tot revenues
120,0%
110,0%
100,0%
90,0%
80,0%
70,0%
60,0%
50,0%
40,0%
30,0%
20,0%
10,0%
0,0%
97.1%
2.9%
0 100 200 300 400 500 600 700 800 900 1000 1100
mio €
Wholesale
Retail


Revenues by channel - 2006
% on tot revenues
120,0%
110,0%
100,0%
90,0%
80,0%
70,0%
60,0%
50,0%
40,0%
30,0%
20,0%
10,0%
0,0%
96.2%
3.8%
0 100 200 300 400 500 600 700 800 900 1000 1100 1200
mio €
Wholesale
Retail

The following table lists our branches, divided by business unit:

Business Unit 1 - Europe and the rest of the world	Business Unit 2 - Asia Pacific	Business Unit 3 – The Americas
Sàfilo S.p.A.	Sàfilo Far East Ltd. (Hong Kong)	Sàfilo U.S.A. Inc. (New Jersey, U.S.A.)
Sàfilo UK Ltd. (England)[(a)]	Sàfilo Hong Kong Ltd. (Hong Kong)	Sàfilo Canada Inc. (Canada)
Sàfilo Switzerland A.G. (Switzerland)	Sàfilo Singapore Pte Ltd. (Singapore)	Canam Sport Optics Inc. (Canada)
Sàfilo Benelux S.A. (Belgium)	Sàfilo Optical Sdn Bhd (Malaysia)	Smith Sport Optics Inc. (Idaho, U.S.A.)
Sàfilo Nederland B.V. (the Netherlands)	Sàfilo Trading Shenzen Co. Ltd. (China)	Solstice Marketing Concepts LLC (New Jersey, U.S.A.)
Sàfilo Nordic A.B. (Sweden) [(b)]	Sàfilo Japan Co. Ltd. (Japan)	Sàfilo Do Brasil Ltda (Brazil)
Sàfilo France S.à r.l. (France)	Sàfilo Australia Partnership (Australia)	
Sàfilo G.m.b.H. (Germany)	Sàfilo Korea LTD (South Korea)	
Sàfilo Austria G.m.b.H. (Austria)		
Carrera Optyl D.o.o. (Slovenia)		
Sàfilo Espana S.A. (Spain)		
Fashion Optic S.L. (Spain)		
Navoptik S.L. (Spain)		
Sàfilo Portugal Lda (Portugal)		
Sàfilo Hellas Ottica S.A. (Greece)		
Sàfilo India (Pty) Ltd. (India)		
Sàfilo South Africa (Pty) Ltd. (South Africa)		

(a) Territory includes U.K. and Ireland.
(b) Territory includes Sweden, Denmark, Finland, Norway and the Baltic Republics (Estonia, Lithuania, Latvia).

Set forth below is a description of each business unit:

Europe. Our European regional headquarters is located in Padua, Italy. Our European managing director and business unit head is also responsible for other parts of the world, including the Middle East, Africa and India.

Our European client base is highly fragmented: in Italy most of our clients are independent retailers, in Great Britain our principal clients are distribution chains and in Germany our major clients are purchasing groups and distribution chains.

We distribute our products directly in 22 European countries. Almost 60% of our approximately 700 European sales agents are independent contractors and work on a commission basis and the remaining part are employees who receive a base salary and commission.

Most of our sales agents are connected to our centralized distribution system via laptop computers in order to process orders quickly. We can monitor sales and marketing information on a daily basis. We also have a special sales division for sports products (ski goggles, helmets and sports goggles).

In addition, we have created a key account team, based in Padua, to serve the major European distribution chains from one central location. Where we have no distribution branch, we have established a long-term relationship with local distributors, most of which distribute our products exclusively.

Furthermore, starting from November 9, 2006 the Group entered the European retail market, thanks to the acquisition of Loop Vision. The Spanish chain, which targets the high-end and luxury segments of the market, accounted for 63 directly owned stores and 12 points of sales in franchising by the end of 2006.

Finally, starting from early 2007, the Group has direct access to the market in the Baltic Republics, thanks to the opening of local commercial branches.

The Asia Pacific region. Our Asia Pacific headquarters are located in Hong Kong, where the managing director and business unit head oversees the Asian region. The Asian region managing director is also responsible for Australia and our global duty free business through a dedicated key account manager.

We currently distribute our products in the Asia Pacific market through distribution subsidiaries in China, Australia, Hong Kong, Japan, Malaysia, Singapore and, starting from January 2007, South Korea and through exclusive third-party distributors in other key markets. Our customer market is highly fragmented, and we sell mainly to independent stores and department stores.

We believe that the Japanese market represents a high potential for growth in our sales of our principal licensed brands and, therefore, we have developed design prescription frames to meet the specific fitting requirements of our Asia Pacific consumers (Asian fitting).

America. The head of our American business unit is responsible for the markets in the United States, Canada, the larger countries in Central and South America and for sales through our Solstice retail chain. The center of the American business unit is in New Jersey, United States.

We organize marketing and distribution in the United States based on our three distribution channels: opticians, ophthalmologists and optometrists; the retail market consisting of department stores and specialty stores; and sports stores. We sell to opticians, ophthalmologists and optometrists that are organized in large retail chains as well as individual stores and practices.

We have more than 500 independent sales agents who cover the American business unit. Approximately 60 operate in Canada and Brazil. In the United States, out of the approximately 450 independent sales agents, we have over 300 independent sales agents that focus on opticians, ophthalmologists and optometrists, 40 agents that focus on retail outlets such as department stores and specialty stores and 97 sales agents that are exclusive for a product category, such as sports goggles. We have a showroom in New York City dedicated to showing our sunglasses collections to our customers.

The major distribution chains are served directly through a key account structure. All distributors in Central and South America are managed through our Miami, Florida office of Sàfilo USA.

Solstice Specialty Store Program. We acquired our chain of Solstice specialty stores in early 2002 from Moët Hennessy Louis Vuitton. As of December 31, 2006, we had 83 stores and we plan to continue to selectively increase the number of our stores. We believe that the Solstice program will raise the visibility of our licensed brands. The Solstice stores are located in metropolitan areas selected pursuant to the potential customer base. Our Solstice stores sell exclusively sunglasses in the high-end market.

Account Management

Collection and management of orders is carried out by the commercial network and by the Planning & Logistics Department, respectively.

We have offices for order management in Italy, in every European country where a commercial branch is located, in the United States where they serve both North America and South America, and in the Asia Pacific region where they serve the Asian and Australian market.

Orders are either:

- collected by sale agents; or
- made by a telephone call from the client to the relevant call center; or
- ordered by the client by website trough the e-commerce system, or through electronic request forms, or at our head offices.

The majority of our orders are collected through our sales agents, who use specifically designed software and laptop computers to transmit all orders in real time.

Our call centers process reorders of final products and spare parts and provide client services (status of orders and technical problems with products). Our call centers employ more than 200 highly qualified persons and use modern software systems, which creates a profile of each client. Our Customer Relationship Management software, or CRM, allows us to monitor the market.

To optimize the management process and improve the level of service, we have consolidated all call centers located in the European territory into Padua.

Another important element of our order processing function relates to the e-commerce system, which allows clients to use the internet for order transmissions, to view the collection and to download technical information.

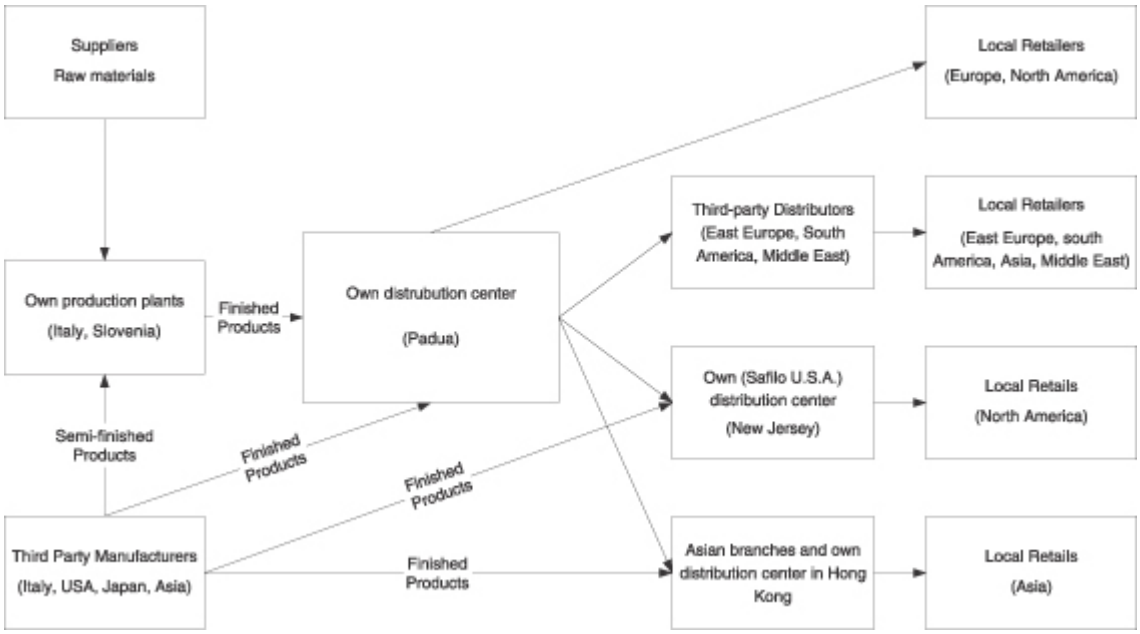
We process orders on the basis of the importance of credit risk of the client, the date of delivery and delivery logistics.

Subsequently, the order management system notifies the relevant warehouses and arranges for the delivery of the products. Our clients who order through our e-commerce website are notified by e-mail that their order has been shipped, and are billed monthly.

Logistics

We have one integrated logistics platform through which we are able to connect directly the distribution center in Padua with each single optician in Europe and with distributors in Asia and Australia. We are able to send products to opticians directly from our distribution center in Padua, without any intermediate steps, which helps us to provide superior customer service. Our platform also allows us to monitor effectively our stock of finished products.

The chart below illustrates the flow of our products in our distribution network.



As shown in the chart above, our distribution network is anchored by our highly automated distribution center in Padua. We also have distribution centers in Parsippany, New Jersey (United States), Hong Kong (China) and several minor distribution centers in Denver, Colorado (United States) and in Utah (United States), Japan, Australia, India, South Africa, Canada, Greece, Brazil, Singapore and China, each of which serves its assigned and specific geographic area. Thanks to our worldwide distribution centers, we are able to optimize client service in all markets we operate in.

In 2004, we completed the upgrading and reorganization of our distribution center in Padua. This has enabled us to service our customers better thanks to a higher level of automation of certain activities. Currently, our Padua distribution center has a distribution capacity of over 100,000 units per day.

To ensure minimum shipping times and maximum cost reduction, we select our shippers and couriers on the basis of efficiency and reliability.

We receive supplies from European countries mostly by road transport and from Asia mostly by ship. We receive finished products from Asia both by ship and air.

Upon completion of our production process, the finished products are sent to Padua to our distribution center. Shipping orders, costs and instructions for couriers are processed during the night. The processing system takes into account the area of delivery to minimize transportation costs and the number of trips to the same retailer. Transportation orders and schedules are generated, and the merchandise is picked up for distribution in the morning. Distribution to the retailers occurs generally within 24-48 hours throughout Italy and within 48-72 hours throughout Europe.

Information Technology

Our information technology department has two main data centers, one in Padua and one in Parsippany, New Jersey (United States). Certain distribution subsidiaries outside of Italy have smaller data centers. The information technology headquarters is in Padua and supports the information technology operations for the European subsidiaries and several Asian subsidiaries; the data center in Parsippany supports the information technology operations for the United States.

We develop and maintain a significant part of our management software, to promote continuous collection and timely update of the information necessary for the operative management of (i) production, (ii) tracking sales, (iii) logistics and credit management. Other applications allow clients and agents to have direct and quick access to the information.

The management software includes some standard software packets, bought from leading software producers and related mostly to administrative and accounting applications.

Our companies are interconnected by means of data transmission networks, which enable a continuous transmission and adjournment of information.

We use basic hardware and software for a safe and continuous functioning of the information systems. We have installed hardware and the relevant software supplied by leading producers, with whom we have maintenance contracts to ensure the integrity of our information system. We have created a disaster recovery program and have systems in place to prevent unauthorized access to our system, and minimize the risk of viruses attacking it.

As of December 31, 2006, our information technology department employs approximately 40 people in Europe and more than 20 in the United States. We outsource some services, such as personnel management to third-party information technology companies.

Regulatory matters

Our facilities and operations are subject to environmental and occupational health and safety laws and regulations in each of the jurisdictions we operate in. These laws govern, among other things, discharges of pollutants into the air, water and land, the use, storage and disposal of hazardous substances and wastes, and the clean-up of contaminated properties.

Violations of environmental laws and permits can result in significant fines or civil or criminal sanctions. In addition, the discovery of significant contamination at our facilities could require us to incur cleanup costs. Finally, environmental permits required for some of our operations may be reviewed, modified or revoked by the issuing authorities.

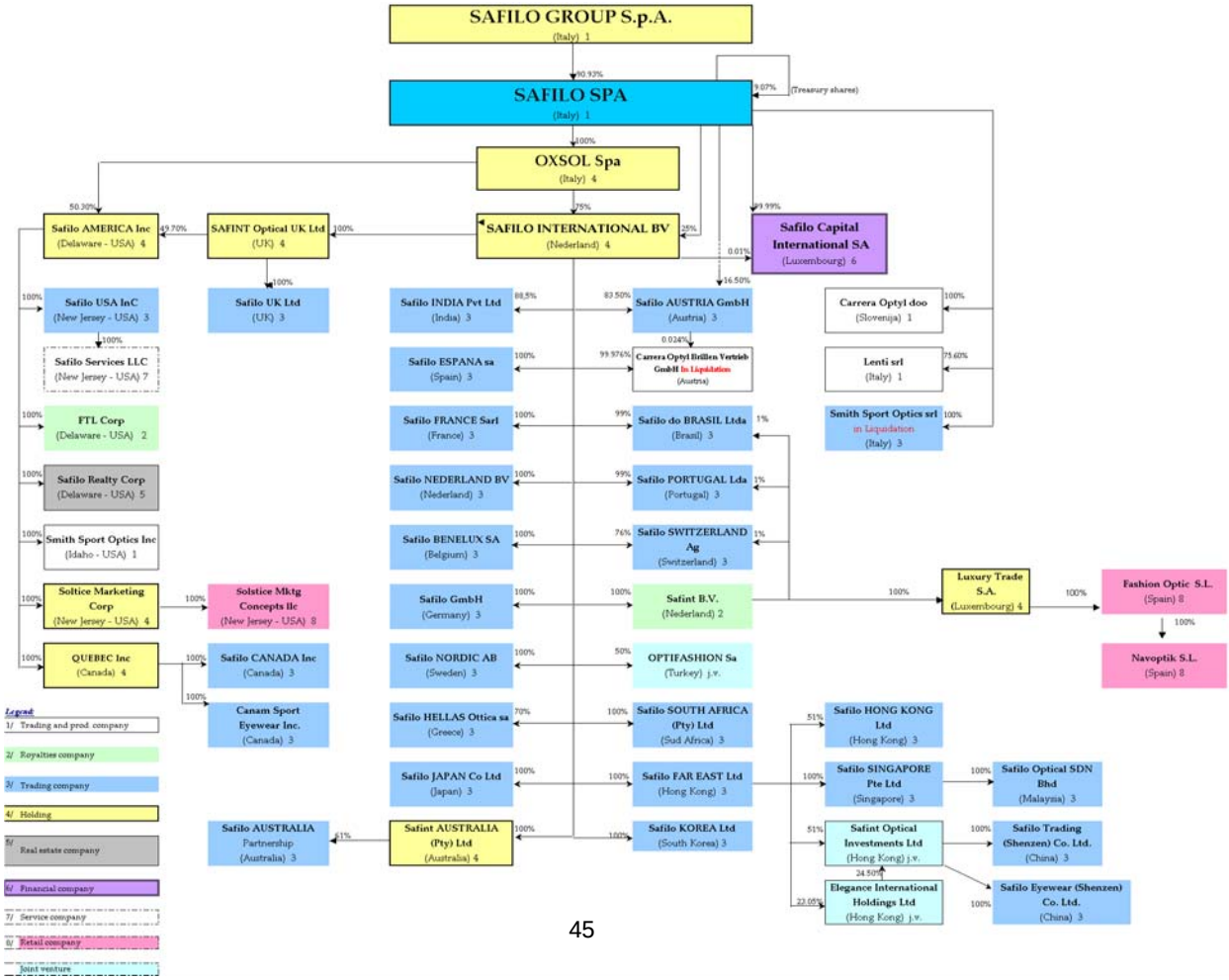
We believe that we are in material compliance with environmental laws and permits applicable to our business. However, from time to time we incur costs to maintain or achieve compliance with such requirements. Costs for these matters and our past environmental and safety costs have not significantly affected our operations, and future environmental costs are not expected to be material.

ORGANIZATIONAL STRUCTURE

Our commercial activities are carried out by the commercial companies of our Group in the 34 countries where we are present.

Additionally, our Group holds minority shareholdings in a limited number of companies, such as Elegance, which owns manufacturing plants in Hong Kong. We generally have the right to appoint the majority of the members of the Boards of Directors and other managing bodies of the companies in which we own the majority of the corporate capital.

The graph below illustrates the organizational structure of our Group as of December 31, 2006.



PROPERTY, PLANTS AND EQUIPMENT

Our major production facilities are partly owned and partly leased. In addition, we lease administrative and distribution office space in various locations we operate in.

The table below lists the address of the real estate property owned by Group companies as of December, 31 2006.

Owner	Location	Use	Surface Area (m2)
Italian companies			
Safilo S.p.A.	Via Malignani, 6 - Precenicco (UD)	Manufacturing plant and offices, land	13,000
	Via Spilimbergo, 154 - Martignacco (UD)	Manufacturing plant and offices, land	4,460
	Via Molinà, 1 - Calalzo di Cadore (BL)	Manufacturing plant and offices, land	14,516
	Zona Industriale Villanova di Faè - Longarone (BL)	Manufacturing plant and offices, land	55,200
	Settima Strada, 15 - Padua	Offices and distribution center, land	20,937
	Prima Strada, 45 - Padua	Warehouse and offices, parking lot	12,500
	Fagagna (UD)	Land	69,065
	Via Noalese, 206 - Santa Maria di Sala (VE)	Manufacturing plant and offices, land	47,020
Foreign companies			
Safilo Espana S.A.	Madrid (Spain) - c/ Julian Camarillo, 7 4A	Offices	600
Safilo Realty Corp	Ketchum (U.S.A.) - 280 Northwood Way	Offices and warehouse	2,330
Carrera Optyl D.o.o.	Ormoz (Slovenia) - Ljutomerska 38/a	Manufacturing plant and offices	20,314

The table below sets forth the real estate properties, which we lease or hold under a financial leasing agreement for which the annual lease is greater than €100,000 or equivalent amount in local currency.

Parties to the Lease	Location	Use	Expiry of Lease	Annual Rent Amount (1)
Italian companies				
Bi-Otto S.r.l./Safilo	VII Strada 18 Padua	Warehouse and parking lot	September 30 2007	191,520
Sanpaolo Leasint S.p.a./Safilo	VII Strada 17/2 Padua	Prototyping facility	March 5, 2012	129,086
Sanpaolo Leasint S.p.a./Safilo	VII Strada 15 Padua	Warehouse	August 1, 2015	1,369,747
Safilo España SA	Xaudaró, 24 28034 Madrid	Offices	February 28, 2012	183,240
Fashion Optic S.L.	Xaudaró, 24 28034 Madrid	Offices and warehouse	February 28, 2012	140,760
Safilo France S.a.r.l.	142, Av. des Champs Elysées 75008 Paris	Showroom	January 31, 2011	206,778
Safilo Nordic AB	Svardvagen 19 182 33 Danderyd	Offices, parking lot, small storage room	December 31, 2011	SEK 2,242,600 (Euro 242,315)
Safilo UK Ltd	Suite E - 2nd Floor, Holborn Hall 193-197, High Holborn London	Offices and showroom	March 24, 2012	GBP 93,000 (Euro 136,424)
Safilo Far East Ltd	52/F The Center. 99 Queen's Road Central Hong Kong	Offices	August 31, 2007	HK$ 3,983,319 (Euro 408,361)
	52/F The Center. 99 Queen's Road Central Hong Kong	Sales offices	August 31, 2007	HK$ 1,025,579 (Euro 105,140)
Safilo Japan Co. Ltd	Nihonbashi Kato Bldg, 5/F2-1-14 Nihonbashi Chuo-ku Tokio 103-0027	Offices	May 19, 2007	JPY 40,776,000 (Euro 279,258)
Safilo Canada Inc	4800, Molson Street Montréal (Quebec) H1Y 3N1	Offices and warehouse	August, 31 2013	CAD 150,935 (Euro 106,016)
Safilo do Brasil Ltda	Rua Dr. Virgilio de Carvalho Pinto, 519 - 521 CEP 05415-030 Pinheiros - Sao Paulo SP	Offices, warehouse, showroom	September 20, 2009	REAIS 348,000 (Euro 127,328)
Safilo USA Inc	801, Jefferson Road Parsippany,NJ, 07054 USA	Offices and warehouse	December 31, 2009	US$ 1,446,268 (Euro 1,152,038)
	SunSights 404 Fifth Avenue New York, NY	Showroom	June 30, 2008	US$ 439,774 (Euro 350,306)
	Outlook Eyewear 12360 East 46th Ave, Suite 300 Denver, CO 80239	Warehouse	December 31, 2014	US$ 712,519 (Euro 567,563)
Smith Sport Optics Inc	Safilo Realty Corp, 280 Northwood Way Ketchum, ID 83340	Offices	December 31, 2007	US$ 480,000 (Euro 382,348)
Solstice Marketing Concepts LLC#1001	The Florida Mall Sp 132, 8001 S. Orange Blossom Trail Orlando, FL 32809	Retail store	January 31, 2010	US$ 154,560 (Euro 123,116)
Solstice Marketing Concepts LLC#1003	Garden State Plaza, 1 Garden State Plaza T19C Paramus, NJ, 07652	Retail store	January 31, 2011	US$ 143,996 (Euro 114,701)
Solstice Marketing Concepts LLC#1004	Valley Fair Mall, Ste. 2561 2855 Stevens Creek Blvd Santa Clara, CA 95050	Retail store	January 31, 2012	US$ 136,350 (Euro 108,611)
Solstice Marketing Concepts LLC#1009	500 Fifth Avenue New York, NY, 10110	Retail store	December 31, 2017	US$ 169,400 (Euro 134,937)
Solstice Marketing Concepts LLC#1011	The Mall at Short Hills, Route 24 & JFK Parkway Short Hills, NJ 07078	Retail store	January 31, 2013	US$ 150,000 (Euro 119,484)
Solstice Marketing Concepts LLC#1012	805 Lincoln Road Miami, FL 33139	Retail store	June 30, 2012	US$ 136,596 (Euro 108,807)
Solstice Marketing Concepts LLC#1013	27 West 34th Street New York, NY, 10001	Retail store	December 30, 2009	US$ 262,254 (Euro 208,901)
Solstice Marketing Concepts LLC#1031	Beverly Center, 8522 Beverly Boulevard Suite 786 Los Angeles, CA, 90048	Retail store	January 31, 2013	US$ 140,000 (Euro 111,518)
Solstice Marketing Concepts LLC#1032	Houston Galleria, 5135 West Alabama Suite 7220 Houston, TX 77056	Retail store	January 31, 2014	US$ 124,320 (Euro 99,028)
Solstice Marketing Concepts LLC#1035	Columbus Circle #10, Space 306, Shops at Col Circle New York, NY, 10023	Retail store	January 31, 2015	US$ 139,305 (Euro 110,965)
Solstice Marketing Concepts LLC#3001	Ralph Lauren Optical Store, 811 Madison Avenue New York, NY, 10021	Retail store	November 30, 2015	US$ 567,750 (Euro 452,246)

(1) Local currency exchanged to Euro at the average rate for 2006.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following is a discussion of our results of operations and financial conditions as of and for the years ended December 31, 2004, 2005 and 2006. You should read this discussion in conjunction with the sections entitled "Presentation of Financial and Other Information", "Selected Financial Data" and our consolidated financial statements and accompanying notes included elsewhere.

We have prepared our consolidated financial statements as of and for the years ended December 31, 2004, 2005 and 2006 in accordance with IFRS, which differ from Italian GAAP and U.S. GAAP in certain respects. The Safilo Group adopted IFRS on January 1, 2005. The information required by IFRS 1 – First time adoption of International Financial Reporting Standards on the effects of transition to IFRS was included in the Appendix to the Consolidated Financial Statements at December 31, 2005, to which reference should be made.

The following discussion and analysis contains statements reflecting our views about our future performance and are considered "forward-looking statements". These views may involve risks and uncertainties that are difficult to predict and may cause our actual results to differ materially from the results discussed in such forward-looking statements. You should consider that various factors including changes in general economic conditions, nature of competition, developments in distribution, industry trends, influence of currency fluctuations and inflation, and other factors discussed below, may affect our projected performance.

OPERATING RESULTS

Overview

We are the parent company of the Group Sàfilo S.p.A., a leader in the production and sale of prescription frames, sunglasses and sports eyewear. Our products are sold in approximately 130 countries through a distribution network comprising 30 distribution subsidiaries operating in 34 countries and through approximately 170 independent distributors elsewhere. Our net sales of prescription frames, sunglasses and sports products accounted for 37.4%, 55.0% and 5.9%, respectively, of our net sales in 2006. We also sell a limited line of complementary accessories, which accounted for 1.7% of our net sales in 2006. We produce and distribute eyewear products under license agreements that are typically long-term, as well as under our owned brands. Our principal geographic target markets are the Americas (principally the United States), which accounted for 37.3%; Italy, which accounted for 14.2%; Europe (excluding Italy), which accounted for 32.2%; and the Asia Pacific region, which accounted for 11.5% of our net sales in 2006.

Principal Factors Affecting our Results of Operations

Strengthening of Distribution Network

One of our key strategic objectives is to continue strengthening our distribution network through selective expansion into attractive geographic markets and through increasing our control over product distribution. We operate three main distribution centers: our Padua distribution center, a center in Parsippany (New Jersey) and a center in Hong Kong. During 2002, we began our Solstice specialty store business in the United States by acquiring six stores; at December 31, 2006 we manage 83 Solstice stores. Thanks to the acquisition of Loop Vision, the Group also directly manages 63 stores in Spain. We expect to continue to establish distribution subsidiaries in geographic markets where we currently use third-party distributors at such time as we determine that the size of the market (based on the number of units sold on a "per-annum" basis) would allow us to increase our net sales and profitability through direct control. According to this, during 2006 we have further strengthened our direct presence in the Far East through the opening of a commercial subsidiary based in South Korea, which started its operations in January 2007. With the same rationale, starting from early 2007, we established 3 branches in the Baltic Republics, directly accessing those markets. The strengthening of our distribution network through geographic expansion and increased control has affected, and is expected to continue to affect in future periods, our results of operations. The establishment of distribution subsidiary usually permits an increase in margins and the units sold resulting from our enhanced control and understanding of the brands placement.

Luxury Brands

Sales of licensed luxury brands have represented, and are expected to continue to represent, the most important component of our business. One of our strategic objectives is to renew existing agreements with top luxury fashion houses and designers and to enter into new agreements on favorable terms for new internationally known brands or established brands in attractive regional and national markets. Despite the payment of royalties from sales of licensed luxury brands (which account for the majority of our overall luxury brand sales), luxury brands have been profitable due to their high margins.

Working Capital Requirements

Net working capital, which we define as total current assets (excluding cash in hand and at banks) less total current liabilities (excluding the current portion of medium-and long-term loans), largely depends upon customer requirements for prompt delivery of our products and the prevailing payment terms in the eyewear business. Therefore, our working capital requirements, including inventory and trade receivables, are significant.

Outsourcing of Production

Another strategic objective is to maintain production flexibility by efficiently allocating our own production resources, utilizing subcontractors for certain phases of production and purchasing finished products from third-party manufacturers. We have reduced the use of sub-contractors and have optimized the use of our own production facilities, while increasingly purchasing finished products from third-party manufacturers in order to maintain maximum flexibility and cost-effectiveness without threatening intellectual property protection or product quality. Our goal is also to reduce excess capacity and to realize economies of scale through the efficient allocation of processes and products at our own production facilities. We aim to outsource the production of models that have lower prices to manufacturers that can produce at a lower cost per unit than we would internally, and we retain in our own facilities the production of those models that require a more intensive or technical production process, whether from a design or engineering standpoint. We have a high degree of control over third-party production and have set the same quality standards as for the units we produce ourselves.

Seasonality and Cash Flows

Our revenues are somewhat seasonal as we experience our highest level of net sales during the first half of the year (55% in 2005 and 54% in 2006), primarily due to the higher sales of sunglasses leading up to the summer, and our lower level of net sales in the third quarter of the year. Also, due to this seasonality in net sales, our profitability fluctuates on a quarterly basis, with our EBITDA being better in the first half of the year both in terms of absolute amount and as a percentage of net sales. Our cash levels tend to be lower in the first half of each year because we have higher working capital requirements, as a result of increased receivables deriving from stronger sales.

Business combinations

On November 9, 2006 the Group took over the Loop Vision chain, with 62 stores throughout Spain. The overall cost for the purchase by the Group company Safint B.V. is Euro 2,721 thousand (including accessory costs) for the acquisition of 100% of the shares of the Luxembourg company Luxury Trade S.A., which holds the entire capital of the Spanish trading company Fashion Optic S.A. which, in turn, holds 100% of the shares in the trading company Navoptik S.A..

The transaction was posted using the acquisition method, and the difference between the purchase price and the fair value of the purchased net assets was entirely allocated to goodwill. In accordance with the provisions of IFRS n. 3, paragraph 62, the initial value for the enterprise group was determined temporarily, determining just the fair value to assign to the assets, liabilities and potential liabilities in the acquired companies. The adjustments of these provisional values, in accordance with paragraph 62 above, will be determined within twelve months from the date of acquisition.

The assets and liabilities acquired on November 9, 2006 are as follows:

Acquired assets and liabilities	Fair value
Cash in hand and at banks	400
Trade receivables, net	431
Inventory	4,173
Other current assets	466
Property, plant and equipment	3,474
Net intangible fixed assets	184
Other non-current assets	1,215
Trade payables	(10,735)
Other current liabilities	(3,414)
Long-term loans	(20,170)
Provisions for risks	(142)
Total net assets	**(24,118)**
Goodwill	26,839
Price paid	**2,721**

Goodwill is entirely attributable to the excess income that is expected from distributing Group products through the retail chains and from the synergies that will result from the grouping. The goodwill was submitted to impairment test on both the date of purchase and at the end of the financial year and, further to the test, no needs emerged to account for any reduction in value.

Despite the fact the transaction took place near the end of the period, it was considered best to consolidate the costs and income of the companies for the period between the purchase date of the subsidiaries and the end of the 2006 financial year. Since the purchase date, there has been net sales of Euro 3.642 thousand and a loss of Euro 565 thousand. If the acquisition had been made on January 1, 2006 the Group net sales would have been higher by Euro 21,923 thousand, and the net income for the year lower by Euro 4,502 thousand.

No acquisitions were made in 2004 and 2005.

Critical Accounting Estimates

The preparation of this consolidated financial information requires management to apply accounting methods and policies that are based on difficult or subjective judgments, estimates based on past experience and assumptions determined to be reasonable and realistic based on the related circumstances. The application of these estimates and assumptions affects the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of income and expenses during the reporting period. Actual results may differ from these estimates given the uncertainty surrounding the assumptions and conditions upon which the estimates are based. We have summarized below our accounting estimates that require the more subjective judgment of our management in making assumptions or estimates regarding the effects of matters that are inherently uncertain and for which changes in conditions may significantly affect the results reported in the combined and consolidated financial statements.

Goodwill

The Group tests at least annually whether goodwill is subject to impairment. The recoverable amounts of the cash-generating units are determined based on fair value calculations. Should the fair values result in a lower value than the book value of the asset, an impairment is recorded. The allocation of goodwill amongst the cash-generating units and the valuation under fair value requires management to make estimates that depend on many factors that can change through time. Changing the assumptions selected by management to determine the level, if any, of impairment, including the discount rates or the growth rate assumptions in the cash flow projections, could materially affect the net present value used in the impairment test and, as a result, affect the Group's financial condition and results of operations.

Impairment of long-lived assets

Assets that are subject to depreciation and amortization are reviewed to determine whether there is any indication that the carrying value of these assets may not be recoverable and have suffered an impairment loss. If any such indication exists, the recoverable amount is the higher of an asset's fair value less costs to sell and value in use. Such impairment loss is recognized in the consolidated income statement.

Management judgment is required in the area of asset impairment, particularly in assessing: (i) whether an event has occurred that may affect asset values; (ii) whether the carrying value of an asset can be supported by the net present value of future cash flows which are estimated based upon the continued use of the asset in the business; and (iii) the appropriate key assumptions to be applied in preparing cash flow projections including whether these cash flow projections are discounted using an appropriate rate. Changing the assumptions selected by management to determine the level, if any, of impairment, including the discount rates or the growth rate assumptions in the cash flow projections, could materially affect the net present value used in the impairment test and, as a result, affect the Group's financial condition and results of operations.

Deferred tax assets

Deferred income tax assets are recognized to the extent that is probable that future taxable income will be available against which the temporary differences can be utilized. The valuation of future taxable income depends on assumptions that can change through time with the possibility of causing significant differences on the final valuation of deferred income tax accounted for by management. Judgment is required to determine the key assumptions adopted in the assessment and changes to these key assumptions can significantly affect the outcome of the assessment.

Derivative financial instruments

The fair value of the financial instruments traded in an active market is based on the listed price at the balance sheet date.

The fair value of the financial instruments not traded in an active market is calculated in accordance with valuation techniques. The techniques used are varied and the assumptions used are based on the market conditions at the balance sheet date. More specifically:

- the fair value of the interest rate swaps is calculated on the basis of the current value of the future cash flows;
- the fair value of the forward currency hedging contracts is determined on the basis of the current value of the differences between the contracted forward exchange rate and the spot market rate at the balance sheet date;
- the fair value of the advanced repayment option included in the bond issued by the subsidiary Capital International S.A. is valued using models applied by primary financial institutions;
- the fair value of the stock option is calculated using the *Black & Scholes* model.

Segment Information

The following information is provided with reference to the geographical areas where the Group operates. The geographical area has been identified as the primary segment. The criteria used in identifying the primary segment have been based on the modality of which management operates the Group and the way it attributes managerial responsibilities. In particular, such criteria are based on the grouping by geographical areas which are defined by the location of the registered office of each Group Company. Therefore, the sales identified in accordance with this segmentation are determined by origin of invoicing and not by target market.

At the date of the present report no secondary segments were identified. In particular, the secondary segments could be related, also in consideration of market practices, to the "distribution" system. In the circumstances, however, the distribution of the products is almost exclusively wholesale; in fact the distribution activity through points of sales directly controlled by the Group (retail sales) is marginal.

December 31, 2006 *(Euro/000)*	**Italy (1)**	**Europe (2)**	**America (3)**	**Asia (4)**	***Corporate* (5)**	**Eliminat.**	**Total**
Net sales							
-to other segments	342,674	48,238	1,925	45	-	(392,881)	-
-to third parties	268,625	312,462	411,721	129,175	-	-	1,121,983
Total Net Sales	**611,299**	**360,700**	**413,646**	**129,220**	**-**	**(392,881)**	**1,121,983**
Gross Profit	**245,065**	**144,541**	**214,131**	**61,932**	**-**	**(2,200)**	**663,470**
Operating income	**44,237**	**26,799**	**37,196**	**18,899**	**(32)**	**(1,301)**	**125,797**
Interest expense							(71,196)
Interest income							14,996
Share losses of inv. - equity method	-	(1)	-	-	(104)		(105)
Share income/(loss) of associates	-	-	146	1,046	426		1,618
Income taxes							(30,122)
Net income							**40,988**
Gross profit margin	*40%*	*40%*	*52%*	*48%*			*59%*
Operating income margin	*7%*	*7%*	*9%*	*15%*			*11%*
Other information							
Segment assets	492,405	305,832	331,613	184,797	1,907		1,316,553
Investment in equity method assoc.	-	-	939	11,393	202		12,535
Unallocated corporate assets							54,084
Consolidated total assets							**1,383,172**
Segment liabilities	233,628	45,057	49,891	16,750	1,046		346,370
Unallocated corporate liabilities							639,476
Consolidated total liabilities							**985,846**
Capital expenditure	20,385	6,633	14,372	1,369	27		42,786
Depreciation & amortization	25,584	5,526	4,664	1,068	21		36,861
Non-cash expenses other than depreciation	8,835	5,681	1,723	834	-		17,073

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

December 31, 2005 *(Euro/000)*	Italy (1)	Europe (2)	America (3)	Asia (4)	*Corporate* (5)	Eliminat.	Total
Net sales							
-to other segments	280,865	37,540	1,833	977	-	(321,215)	-
-to third parties	240,196	288,389	376,899	119,786	4		1,025,274
Total Net Sales	**521,061**	**325,929**	**378,732**	**120,763**	**4**	**(321,215)**	**1,025,274**
Gross Profit	**207,167**	**143,100**	**199,029**	**60,930**	**4**	**(1,461)**	**608,769**
Operating income	**32,128**	**51,341**	**40,996**	**20,960**	**727**	**(17,870)**	**128,282**
Interest expense							(116,164)
Interest income							14,755
Share losses of inv. - equity method	(3,370)						(3,370)
Share income/(loss) of associates			123	1,398	11		1,532
Income taxes							(11,373)
Net income							**13,662**
Gross profit margin	*40%*	*44%*	*53%*	*50%*			*59%*
Operating income margin	*6%*	*16%*	*11%*	*17%*			*13%*
Other information							
Segment assets	560,156	255,475	284,324	183,560	4,265		1,287,780
Investment in equity method assoc.			893	12,293	306		13,492
Unallocated corporate assets							89,478
Consolidated total assets							**1,390,750**
Segment liabilities	214,585	34,783	39,947	16,699	1,798		307,812
Unallocated corporate liabilities							697,182
Consolidated total liabilities							**1,004,994**
Capital expenditure	26,406	5,688	5,544	1,027	-		38,665
Depreciation & Amortization	24,999	5,615	3,601	961	21		35,197
Non-cash expenses other than depreciation	5,666	2,793	457	887	-		9,803

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

December 31, 2004 *(Euro/000)*	**Italy (1)**	**Europe (2)**	**America (3)**	**Asia (4)**	***Corporate* (5)**	**Eliminat.**	**Total**
Net sales							
-to other segments	275,951	44,587	1,088	348	30	(322,004)	-
-to third parties	221,801	280,398	342,699	99,815	27		944,740
Total Net Sales	**497,752**	**324,985**	**343,787**	**100,163**	**57**	**(322,004)**	**944,740**
Gross Profit	**192,258**	**137,793**	**181,174**	**54,454**	**58**	**(2,526)**	**563,211**
Operating income	**33,577**	**32,426**	**32,708**	**22,539**	**659**	**(10,510)**	**111,399**
Interest expense							(84,619)
Interest income							18,469
Share income/(loss) of associates	2			(111)	67		(42)
Income taxes							(20,474)
Net income							**24,733**
Gross profit margin	*39%*	*42%*	*53%*	*54%*			*60%*
Operating profit margin	*7%*	*10%*	*10%*	*23%*			*12%*
Other information							
Segment assets	405,944	254,780	265,193	175,743	1,343		1,103,003
Investment in equity method associates				9,871	296		10,167
Unallocated corporate assets							58,439
Consolidated total assets							**1,171,609**
Segment liabilities	178,045	37,769	42,433	16,747	5,466		280,460
Unallocated corporate liabilities							822,590
Consolidated total liabilities							**1,103,050**
Capital expenditure	21,949	5,921	2,210	972	169		31,221
Depreciation & Amortization	23,989	6,893	3,848	762	13		35,505
Non-cash expenses other than depreciation	4,522	3,852	4,261	1,202	-		13,837

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

Results of Operations for the Years Ended December 31, 2004, 2005 and 2006

Year Ended December 31, 2006, compared with Year Ended December 31, 2005 and 2004

Consolidated Statement of Operations *(Euro in millions)*	2004	% of net sales	2005	% of net sales	2006	% of net sales	Change % '05 vs. '04	Change % '06 vs. '05
Net sales	944.7	100.0	1,025.3	100.0	1,122.0	100.0	8.5	9.4
Cost of sales	(381.5)	(40.4)	(416.5)	(40.6)	(458.5)	(40.9)	9.2	10.1
Gross profit	**563.2**	**59.6**	**608.8**	**59.4**	**663.5**	**59.1**	**8.1**	**9.0**
Selling and marketing expenses	(344.1)	(36.4)	(379.4)	(37.0)	(415.3)	(37.0)	10.3	9.5
General and administrative expenses	(106.9)	(11.3)	(102.1)	(10.0)	(123.8)	(11.0)	(4.5)	21.3
Other operating income and expenses, net	(0.9)	(0.1)	1.0	0.1	1.4	0.1	(211.1)	40.0
Operating income	**111.3**	**11.8**	**128.3**	**12.5**	**125.8**	**11.2**	**15.3**	**(1.9)**
Share of income/ (loss) of associates	-	-	1.5	0.1	1.5	0.1	n.s.	0.0
Interest expense and other financial charges, net	(66.1)	(7.0)	(104.8)	(10.2)	(56.2)	(5.0)	58.5	(46.4)
Income before taxation	**45.2**	**4.8**	**25.0**	**2.4**	**71.1**	**6.3**	**(44.7)**	**n.s.**
Income tax expense	(20.5)	(2.2)	(11.4)	(1.1)	(30.1)	(2.7)	(44.4)	n.s.
Net income	**24.7**	**2.6**	**13.6**	**1.3**	**41.0**	**3.7**	**(44.9)**	**n.s.**
Net income attributable to minority interests	3.1	0.3	3.2	0.3	3.3	0.3	3.2	3.1
Net income attributable to the Group	**21.6**	**2.3**	**10.4**	**1.0**	**37.7**	**3.4**	**(51.9)**	**n.s.**
EBITDA	**146.9**	**15.5**	**163.5**	**15.9**	**162.6**	**14.5**	**11.3**	**(0.6)**

Net sales

Financial year 2006

Consolidated turnover reached Euro 1,122.0 million, with an increase of 9.4% compared to 2005 (+9.8% at constant exchange rates), with strong performances in all the key international markets.

Significant improvements were obtained in Europe, with a remarkable performance in the domestic market and clear progress in the other countries.

The Group recorded brilliant growth in the American market thanks to the strength of the brands portfolio and despite the non-renewal of the *Polo Ralph Lauren* license.

Finally, Far East achieved noteworthy results, particularly in the emerging markets (such as China and India) despite the loss of sales due to the decision to not distribute products in Korea prior to the opening of the local commercial subsidiary (January 2007).

The Group's owned brands performed remarkably (+12.4%), especially *Carrera* enjoyed significant growth (+19.4%).

On the other hand, licensed brands posted a +8.3% growth compared to 2005, with a double-digit growth rate for the top-performing brands in terms of turnover (*Armani*, *Dior* and *Gucci*).

Financial year 2005

Group sales, at current exchange rates, reached to Euro 1,025.3 million up to 8.5% compared to Euro 944.7 million recorded in 2004. The slight fluctuation in the average Euro/US dollar exchange rate did not result in any significant changes.

The improved results were achieved due to the increase in the sales of licensed products (+12.2%) and to the strong increase in sales in all of the markets in which the Group operates, with the Asian market having a noteworthy impact(+20.0%).

The year also confirmed the important growth in the sunglasses segment (+18.5%), together with substantially stable sales for optical frames.

The opening of new outlets continued at a sustained rate, in particular for the outlet chain Solstice. We also launched new brands such as *Marc Jacobs* and *Imatra*, the latter advertised by the Grand Prix motorbike world champion- Valentino Rossi.

The tables below set forth our net sales by geographic region and product category for the years ended December 31, 2004, 2005 and 2006.

Net sales by geographical region	December 31,						Change %	
(Euro in millions)	2004	%	2005	%	2006	%	'05 vs. '04	'06 vs. '05
Italy	123.5	13.1	138.6	13.5	159.7	14.2	12.2	15.2
Europe (excluding Italy)	329.6	34.9	339.4	33.1	361.3	32.2	3.0	6.5
The Americas	351.3	37.2	383.3	37.4	418.6	37.3	9.1	9.2
Asia Pacific	99.8	10.6	119.8	11.7	129.2	11.5	20.0	7.8
Other	40.5	4.2	44.2	4.3	53.2	4.8	9.1	20.4
Total	**944.7**	**100.0**	**1,025.3**	**100.0**	**1,122.0**	**100.0**	**8.5**	**9.4**

Net sales by product	December 31,						Change %	
(Euro in millions)	2004	%	2005	%	2006	%	'05 vs. '04	'06 vs. '05
Prescription frames	425.0	45.0	422.1	41.2	419.5	37.4	(0.7)	(0.6)
Sunglasses	445.5	47.2	527.7	51.5	617.1	55.0	18.5	16.9
Sports products	57.5	6.1	61.2	6.0	66.1	5.9	6.4	8.0
Other	16.7	1.7	14.3	1.3	19.3	1.7	(14.4)	35.0
Total	**944.7**	**100.0**	**1,025.3**	**100.0**	**1,122.0**	**100.0**	**8.5**	**9.4**

Net sales by distribution channel	December 31,						Change %	
(Euro in millions)	2004	%	2005	%	2006	%	'05 vs. '04	'06 vs. '05
Wholesale	925.7	98.0	995.7	97.1	1,079.6	96.2	7.6	8.4
Retail	19.0	2.0	29.6	2.9	42.4	3.8	55.8	43.4
Total	**944.7**	**100.0**	**1,025.3**	**100.0**	**1,122.0**	**100.0**	**8.5**	**9.4**

Italy

Financial year 2006

Revenues in the domestic market posted an increase of +15.2% to Euro 159.7 million, thanks to the excellent results achieved in both prescription frames (+18.6%) and sunglasses (+13.1%). Growth in the Italian market is confirmed to be strong in terms of volumes and involves the majority of the brands in the Group's portfolio.

As far as the licensed brands are concerned, *Diesel* and all the other key brands enjoyed remarkable growth. As regards the house brands, instead, noteworthy is the re-launch of the brands *Sàfilo* and *Carrera* and the general positive performance in the sport sector (+21.7%).

Financial year 2005

The sales in the domestic market increased by 12.2% compared to 2004. The Italian eyewear market due to the Group collections has permitted the Group to reach strong results, both in the sales of sunglasses (+13.9%) and optical frames (+9.1%). The growth recorded in this latter sector represents a significant

achievement within the Group's strategy to increase the presence in the optical frame market. Sporting articles, helmets and goggles also recorded strong results with an increase of approximately 50%. The major brands which contributed to this strong performance were *Armani*, *Dior*, *Gucci* and *Valentino*, *Oxydo* and *Sàfilo*.

Europe (excluding Italy)

Financial year 2006

The European market enjoyed a +6.5% growth to Euro 361.3 million, with a noteworthy performance in all the Northern region (Germany, Norway, UK, Sweden, etc.) where a double-digit growth rate was achieved compared to 2005.

As far as the brands are concerned, *Sàfilo* and *Blue Bay* recorded a strong increase, as well as *Armani* and *Dior*.

Financial year 2005

The European market recorded a growth of 3.0% with a positive performance in the sunglasses category (+9.4%) and substantially stable sales in the optical eyewear frames category (-1.3%). In relation to geographical information, Spain and Germany offered the greatest contribution to the good performance in sales. In terms of growth by brand *Armani*, *Dior*, *Gucci* and *Valentino* were the best performers.

The Americas

Financial year 2006

The American market achieved revenues of Euro 418.6 million, with a 9.2% increase compared to last year.

The negative impact due to the *Ralph Lauren* license expiration has been overwhelmed by the impressive overall performance achieved by the majority of the other brands, both world-wide known (such as *Armani, Gucci, Dior and Yves Saint Laurent*) and regional (*Juicy Couture, Liz Claiborne, Nine West*, etc.).

The sport sector posted a good performance, with remarkable growth of the sales of products under the brand *Smith* (+20.0%).

As regards the performance by country, sales in the Canadian market registered a strong increase (+20.0%).

Financial year 2005

The sales in the American markets continued the growth as in the previous quarters of 2005 with an increase of 9.1% compared to the previous year (at constant exchange rates: +9.9%). Canada and Brazil continue to be markets in strong growth increasing by 19.1% and by 52.2%, respectively. The Group has successfully focused its marketing strategies on the independent opticians and department stores sectors, becoming absolute leader in both sales channels. In relation to the brands, strong results were obtained in all of the most important collections, in particular *Armani, Dior* and *Gucci*, together with the traditional American brands such as *Kate Spade, Liz Claiborne* and *J.Lo*. The strong performance in the sporting sector was also as a result of the important growth in the sale of goggles and sunglasses of the brand Smith.

Strong results were also recorded in the sales division Outlook (+19.1%) and in the retail chain Solstice (+56.2%), which now is represented by 83 outlets.

Asia Pacific

Financial year 2006

2006 turnover in the area was Euro 129.2 million, with a +7.8% increase compared to 2005.

The double-digit growth recorded in China (+33.3%), Singapore (+18.1%) and Thailand (+24.7%) more than compensated the lack of sales in the Korean market due to the suspension of the distribution of the Group's products, in anticipation of the kick-off of the local commercial subsidiary in January 2007.

As regards the analysis by brand, outstanding performances have been posted by *Armani* (+26.2%), *Gucci* (+15.8%), *Dior* (+9.3%) and *Valentino* (+37.7%).

Financial year 2005

The Asian market throughout the year confirmed the strong growth rates reported in the previous quarters. Revenues increased in the year by 20.0%. All the merchandise categories continued to provide strong results, both in terms of volumes and turnover. The optical frames reached the same growth rates as the sunglasses with an increase of 20% compared to 2004. This success is due to the continued strategy of the Group regarding the Asian market. In 2004 compared to 2003, the revenues in the Asian market had already increased by approximately 30%. Furthermore in Asia, as in America, almost all the major brands contributed to the strong growth in the year with particularly good results in Australia (+8.4%), Japan (+10.9%), Korea (+72.6%), Philippines (+97.3%) and China (+110%).

Cost of sales

(Euro in millions)	2004	2005	2006	Change % '05 vs. '04	Change % '06 vs. '05
Purchase of raw materials and finished goods	263.1	282.9	368.5	7.5	30.3
Change in inventories	(36.7)	(7.8)	(68.4)	(78.7)	n.s.
Payroll and social security contributions	95.8	91.3	100.5	(4.7)	10.1
Capitalization of costs for increase in property, plant and equipment	(7.5)	(9.9)	(10.0)	32.0	1.5
Subcontracting costs	33.5	23.3	37.3	(30.4)	60.3
Depreciation	24.8	25.4	20.1	2.4	(20.6)
Rental and operating leases	1.0	0.8	0.8	(20.0)	3.0
Other industrial costs	7.5	10.5	9.7	40.0	(8.4)
Total	**381.5**	**416.5**	**458.5**	**9.2**	**10.1**

Financial year 2006

Cost of sales increased by 10.1% to €458.5 million compared to €416.5 million in 2005, mainly due to higher purchase cost of raw materials and finished goods and to non recurring costs relating to the provision for the likely obsolescence of the *Polo Ralph Lauren* finished goods inventories, due to the termination of the license agreement on December 31, 2006.

Financial year 2005

Cost of sales increased by 9.2% from €381.5 million in 2004 to €416.5 million in 2005, remaining substantially stable when considered as a percentage of net sales (40.6% in 2005 and 40.4% in 2004).

Selling and marketing expenses

Financial year 2006

As a percentage on sales, selling and marketing expenses remained stable at 37.0% even if new promotional campaigns sustaining the housebrands and the new licensed brands had been implemented during the year. The 9.5% increase versus last year is mainly the consequence of the fact that this category of costs is heavily impacted by the sales trend.

Financial year 2005

Selling and marketing expenses increased by 10.3% from €344.1 million in 2004 to €379.4 million in 2005 mainly as a consequence of increased sales to which those costs are directly related. As a percentage of net sales, our selling and marketing expenses increased from 36.4% in 2004 to 37.0% in 2005. Part of this growth is due to our royalty expenses, which increased 13.8% from €80.0 million in 2004 to €91.0 million in 2005 due mainly to a shift in revenues generated from our owned brands to licensed brands.

General and administrative expenses

Financial year 2006

General and administrative costs increased by 21.3% to €123.8 million compared to €102.1 million in 2005. The main driver for this trend is to be found in higher personnel costs, both due to the increase in number of employees, especially in Padua headquarters, and in the regular wages and salaries dynamic.

Financial year 2005

General and administrative expenses decreased from €106.9 million in 2004 to €102.1 million in 2005; also as a percentage of net sales our general and administrative expenses decreased from 11.3% in 2004 to 10.0% in 2005 as a result of cost containment activities taken by the Group during 2005 financial year.

Interest expense and other financial charges, net

Financial year 2006

The renegotiation of the 2002 Senior Loan and the proceeds deriving from the IPO helped in improving the Company's net financial position leading to much lower interest expenses. The reduced amount of non recurring financial expenses, mainly relating to the costs sustained for the anticipated repayment of the 2002 Senior Loan led to a further reduction of the impact of financial charges on the bottom line. As a consequence, financial charges dropped by 46.4% to €56.2 million, compared to € 104.8 million in 2005.

Financial year 2005

Interest expense and other financial charges, increased by 58.5% from €66.1 million in 2004 to €104.8 million in 2005.

This increase was mainly due to exchange losses related to the American Dollar revaluation impacting foreign currency loans and resulting in a charge to the income statement for a total amount of €15.0 million due to both the exchange losses recorded on the repayments made during the year and unrealized exchange losses deriving from the valuation of loans in U.S. Dollars at the exchange rate at the balance sheet date.

Furthermore, the advance repayment of a portion of the Senior loan and of one third of the High Yield bond through the use of proceeds received from Sàfilo Group S.p.A. had the following effect on the income statement:

- higher financial costs due to the accelerated amortization of charges related to the above borrowings, in accordance with the IFRS;
- a penalty to be paid to High Yield bond holders.

Income tax expense

Financial year 2006

Increased income tax expenses, up from €11.4 million in 2005 to €30.1 million in 2006, are the consequence of higher profit before taxes, the effective tax rate dropped from 45.4% in 2005 to 42.4% in 2006, mainly as a consequence of the reduced impact of the IRAP tax and of other non-deductable costs.

Financial year 2005

Income tax expense decreased from €20.5 million in 2004 to €11.4 million in 2005; however, as a percentage of the income before taxation, our income taxes remained stable (45.4% in 2005 and 45.4% in 2004).

Net income attributable to Group

Financial year 2006

As a result of the events described in the preceding paragraphs, our net income attributable to the Group increased from €10.4 million in 2005 to €37.7 million in 2006, with a 3.4% percentage on sales when compared to 1.0% in 2005.

Financial year 2005

For the reasons stated above, our net income attributable to the Group decreased from €21.6 million in 2004 to €10.4 million in 2005.

LIQUIDITY AND CAPITAL RESOURCES

Cash Flow

The following table summarizes our cash flow activity during the years ended December 31, 2004, 2005 and 2006.

(Euro in millions)	Year ended December 31, 2004	2005	2006
Net cash flow:			
Provided by operating activities	50.3	28.4	20.8
Used in investing activities	(28.6)	(37.3)	(36.9)
Provided by / (used in) financing activities	(22.1)	21.3	(13.6)
Cash and cash equivalents at the end of the period	18.2	25.9	(0.8)

Net Cash Flow provided by Operating Activities

Financial year 2006

Cash flow from operating activities decreased from €28.4 million in 2005 to €20.8 million in 2006. This decrease was mainly due to the combined effect of (i) a higher net income compared to previous year, mainly due to lower financial expenses and reduced non recurring expenses, both operating and financial; (ii) lower interest charges as a result of the reduced financial position; (iii) a remarkable increase in inventories stock, in order to maximize productivity levels and improve the quality of client service.

Financial year 2005

Net cash flows provided by operating activities consist of net income adjusted for changes in working capital and non-cash items such as depreciation and amortization.

Cash flow from operating activities decreased from €55.7 million in 2004 to €30.0 million in 2005. This decrease was mainly due to the combined effect of (i) a lower net income compared to the previous period due primarily to higher financial costs and non-recurring financial charges, (ii) an increase in trade receivables and other current receivables as a result of the growth in sales in the fourth quarter of 2005 compared to the previous year, and (iii) a lower increase in our inventory comparing 2005 to 2004 as a consequence of an improved inventory control policy.

Cash Flow used in Investment Activities

Financial year 2006

The cash flow absorbed by investing activities is in line with last year, and mainly relates to industrial investments, opening new shops in the Solstice chain and the Loop acquisition.

Financial year 2005

Net cash used in investment activities consists of additions to property, plant and equipment, net of disposals, increases in intangible assets and acquisitions of equity investments.

Cash used in investment activities increased in 2005 when compared to 2004 as a result of higher investments mainly related to Italian factories for the renewal of plants and equipments relating to production of new models. In Europe investments in property, plant and equipment mainly refers to the factory in Slovenia whilst in the United States capital expenditures mainly relate to the development of the Solstice outlet chain.

Investments in intangible assets mainly relate to software and the management of the brands in our portfolio.

Cash Flow provided by Financing Activities

Financial year 2006

The cash flow absorbed by the financing activity mainly relates to the repayment of part of the Senior Loan.

Financial year 2005

Net cash flows provided by financing activities include repayment of loans, additional proceeds form loans, movements in share capital and dividend payments to shareholders. Cash flow from financing activities increased by €43.3 million from an outflow of €22.0 million in 2004 to a cash generation of €21.3 million in 2005. This effect was mainly due to new borrowings from the capex facility of the Senior Credit Agreement.

Capital Resources

Intra-Group Funding

We operate a central treasury function that controls all significant decisions and commitments regarding cash management, arrangement of borrowing facilities and banking relationships.

The Group's cash management account structure and management of accounts is decentralized. Local current accounts are established with domestic banks for collection and disbursement purposes. All account receivables and account payables functions are handled locally as well.

The temporary liquidity needs of each Group company are principally met by managing intra-Group payment obligations arising from intra-Group trading.

We usually manage debt service requirements arising from the Senior Notes issued by Sàfilo Capital International S.A., through payments under the loan agreement with Sàfilo International BV.

The Group's main U.S. operating subsidiary, Sàfilo USA, is a borrower under the senior credit facilities. To date, Sàfilo USA has met, and we expect that it will continue to meet, its debt service obligations under the senior credit facilities through internally generated funds. We also expect that Sàfilo USA will continue to fund the capital requirements of the Solstice specialty store program.

External Sources of Liquidity

Our external sources of liquidity consist mainly of our Senior Credit Facilities, the Senior Notes, factoring agreements and equity contributions. We also have un-drawn credit lines and overdraft facilities and have entered into finance leases. The following is a description of our primary external sources of liquidity:

Senior Credit Facilities

Structure

On June 26, 2006 the Group completed an important refinancing operation through the replacement of the Senior Credit Agreement negotiated in 2002, with a new loan. After completion of primary syndication, the banks of the re-financing operation were Intesa San Paolo, HVB, Banca di Roma, Natexis, BBVA, Fortis.

The Group repaid the previous Senior Loan with a total payment equal to Euro 300,340 thousands. The settlement of the previous loan resulted in non-recurring financial charges booked in the income statement for a total amount of Euro 8,959 thousands, related to the accelerated amortization of the transaction costs incurred on the repaid loan.

The new Senior Credit Agreement provides for better conditions compared to the previous loan, like the slighter guarantees package, the longer maturity and the lower margin applied to the reference parameters (EURIBOR or LIBOR), equal to a spread of 0.60%. The previous spread, depending on the different tranches, was in the range of 2.25% to 3.25%.

The table below summarizes the various facilities of the Senior Credit Agreement and their terms.

December 31, 2006 *(Euro in millions)*	Currency	Interest rate	Internal interest rate	Fair Value	Repayment date
Facility A1	*EURO*	Euribor + 0.60%	4.8704%	79.1	31/12/11
Facility A2	*USD*	Libor + 0.60%	6.6615%	47.5	31/12/11
Facility A3	*USD*	Libor + 0.60%	6.4706%	54.6	31/12/11
Revolving facility	*EURO*	Euribor + 0.60%	4.4094%	110.0	31/12/11
High Yield	*EURO*	9.625%	10.6887%	215.4	15/05/13

The fair value of the borrowings is represented by the nominal outstanding value as of December 31, 2006 but for the High Yield, whose fair value is represented by the market value as at the same date.

Commissions and fees paid on the Senior Credit Agreement are calculated as follows: (i) commitment fee equal to 25% of the margin on un-drawn portions of the Revolving Facility, payable quarterly; (ii) agency fee of €50,000 per year.

Covenants

The Senior Credit Agreement contains customary operating and financial covenants, subject to certain agreed exemptions, which impose some restrictions on the way our Group companies can operate, including restrictions on our ability to:

- incur additional indebtedness or guarantee indebtedness of others;
- make certain loans.

The Senior Credit Agreement requires us to maintain specified customary ratios (interest cover, starting from June 2007 and leverage) to be calculated at the Sàfilo Group S.p.A. consolidated level. As of December 31, 2006, the leverage test has been met.

Mandatory Prepayments

All obligations under the Senior Credit Agreements must be prepaid in full in case of a change of control and must be prepaid in part in case of sale proceeds of our assets exceeding a certain amount.

Maturity and Amortization

The facilities A1, A2 and A3 are repayable in semiannual installments, beginning December 31, 2006, and continuing through December 31, 2011. The Revolving Facility will cease to be available for drawing on December 31, 2011. The termination date of the Revolving Facility could be extended until December 31, 2012, by the end of June 2007.

As of December 31, 2006, the total outstanding amount of the Senior Credit Facilities was approximately €291,186 thousands, with a short-term portion equal to Euro 110,000 thousands and a medium/long-term portion equal to Euro 181,186 thousands.

In relation to the High Yield bond, the short-term portion at December 31, 2005 was repaid on January 13, 2006 by the Luxembourg subsidiary Sàfilo Capital International S.A. for an amount equal to 35% of the nominal value of Euro 300 million. The remaining part of the bond equal to a nominal value of Euro 195 million is included in the account "Long-term borrowings". The payable for the advanced High Yield payment in the financial statements at December 31, 2005 refers to the additional charges paid to the bondholders following the above-mentioned advance repayment.

The above loans, valued under the amortized cost method, are principally guaranteed by pledges on the shares of Sàfilo S.p.A. and by personal guarantees provided by the companies directly financed.

The breakdown of our long-term borrowings as per repayment year is as follows:

(Euro in millions)	December 31, 2005	December 31, 2006
Within 2 years	30.5	38.7
Within 3 years	33.6	39.7
Within 4 years	20.5	39.8
Within 5 years	131.1	163.7
Beyond 5 Years	252.7	193.7
	468.2	**475.6**

Borrowings by currency are as follows:

(Euro in millions)	December 31, 2005	December 31, 2006
Short-term		
Euro	162.6	84.9
U.S. Dollar	19.2	11.2
BRL	-	2.3
HKD	2.2	1.4
Total	**184.0**	**99.7**
Medium/long-term		
Euro	403.0	383.4
U.S. Dollar	65.3	90.9
YEN	-	1.3
Total	**468.2**	**475.6**
Total borrowings	**652.2**	**575.3**

The following table shows credit lines granted to the Group, their utilization and the credit lines available at the balance sheet date:

(Euro in millions)	Granted credit lines	Utilization	Available credit lines
Credit lines on short-term borrowings	149.5	34.2	115.4
Credit lines on long-term borrowings	391.7	301.7	90.0
Total	**541.2**	**335.9**	**205.4**

Factoring Agreement

In 2004 we entered into a without-recourse factoring agreement with Centro Factoring S.p.A. We transfer some of our Italian trade receivables on a revolving basis and receive an up-front payment of 90% of the face value of the approved receivables we sell. The difference between cash received and trade receivables sold will be collected at its maturity date. We have a servicing obligation to act as a collection agent on behalf of Centro Factoring S.p.A.

As of December 31, 2006 the amount due under the factoring agreement described above was €38.1 million.

Financial Indebtedness

The Group net debt position as of December 31 2006 compared with the same as of December 31, 2005 is the following:

Net debt position *(Euro in millions)*	**December 31, 2005**	**2006**	**Change**
Current portion of long-term borrowings	(135.6)	(23.6)	111.9
Bank overdrafts and short-t. bank borrowings	(10.0)	(36.4)	(26.4)
Other short-term borrowings	(38.4)	(39.6)	(1.2)
Cash and cash equivalents	151.0	35.6	(115.4)
Short-term net debt position	**(33.0)**	**(64.0)**	**(31.0)**
Long-term borrowings	(468.2)	(475.6)	(7.3)
Long-term net debt position	**(468.2)**	**(475.6)**	**(7.3)**
Net debt position	**(501.2)**	**(539.6)**	**(38.4)**

Inflation

We do not believe that inflation has had a material impact on our operations in the past, although there can be no assurance that this will be the case in the future.

RESEARCH AND DEVELOPMENT, PATENT AND LICENSES, ETC.

Research and Development

Our research and development activities are divided into two principal segments:

- development of new materials, new production processes and technologies and, instruments and machinery; and
- product design.

Our research and development of new materials, new production processes, instruments and machinery is carried out by an internal division known as the Research and Technological Innovation Division. Development of product designs is carried by our three Design Centers (in Italy, the United States and Hong Kong), each focusing on the design needs of a specific geographic area.

New raw materials, new production processes and instruments and machinery

Through the Research and Technological Innovation Division, which is principally responsible for testing the use of new materials, we seek to improve our products' technical specifications as well as innovate our production process to obtain higher efficiency and a better product quality.

During the course of 2006, the Research and Technical Innovation Division focused on:

- increasing our products' resistance and durability;
- developing innovative features for sports goggles;
- improving lenses, both in terms of aesthetics and as protective gear for sports eyewear;
- improving our products in terms of weight and fit; and
- designing and building new machinery to improve efficiency and quality of product.

During the past several years, our research and development efforts resulted in the filing of numerous patents for, among other things, flexible hinges, lenses bases, nose pieces, three-piece mount rimless frames and ski mask internal and external protection. For further information on our patents see the following paragraph "Intellectual Property and Licenses - Patents".

Our instruments and machinery research and development aims to provide us with designs and precision instruments and moulds that we may use to increase the capacity, efficiency and quality of our production process. We believe that carrying out this type of activity internally allows for a shorter time-to-market of our products as well as a continued reduction in our production costs.

The Research and Technological Innovation Division was composed of 27 members as of December 31, 2006, with the research part of the group based in the Santa Maria di Sala production site center, who works closely with our production process, while the technical innovation part based in Padua, working closely with our design center.

Product design

Over a decade ago, we identified product design as a strategic objective of our Group, especially in connection with high-end products. Our design research and development activity consists of developing shapes and color and material schemes for the creation of new eyewear models. Our design group is divided into three centers, collectively referred to as our Design Center, and is made up of designers engaged in the development of our product prototypes. Our principal Design Center is located in Italy with the remaining two centers located in the United States, specializing in the development of designs for the American exclusive brands, and in Hong

Kong. As of December 31, 2006, our worldwide design team consisted of approximately 140 people, including designers and staff in charge of the creation of prototypes.

Our design center in Padua is subdivided into six units, each dedicated to the development of a range of brands, and is coordinated by a senior designer. Each brand design team meets the licensor to discuss ideas and concepts for the brand during the development phase of our new collections. The marketing department, together with the brand manager, provides our designers with market demand and consumer preference data. With this information, we create style guidelines for our collections in order to achieve an appropriate positioning of our products.

Once new models are defined and the technical feasibility is confirmed by the department of Research and Technological Innovation, the stage of prototyping is commenced. The prototypes are formed using design and industrial computer programs called "computed aided design" (CAD) and "computer aided manufacturing" (CAM). The CAD and CAM technology allows the visualizing of the frames with two-dimensional and three-dimensional images and allows the modifying of the design directly on the computer. The integration of the CAD and CAM design technology with the production process strongly simplifies the consequent industrialization and production of the prototype.

For the licensed brands, the development unit makes use of the designs of the new collections on the basis of the indications of the licensors in relation to colors, shapes and materials and once the prototypes are ordered, the collections are approved by the licensors.

Of the 4,500 current models, 2,500 were new models designed by our design center in 2006. There is a complete regeneration of the collections every two years, with the exception of a few models (called "evergreen models"), which remain in the collection for a longer period.

Intellectual Property and Licenses

Patents

We hold patents for inventions, models and designs. Patents for inventions relate to parts of our products, such as flexible hinges, nose hinges, lenses bases, nose pieces and internal and external protection for ski masks. Patents for models and designs cover our most characteristic and cutting-edge models of sunglasses and sports goggles. As at December 31, 2006, we had more than 60 patents registered or pending in the United States and many European countries. Each year, we apply for approximately eight to ten new patents, generally for hinges and other structural parts of the product. In particular, our formerly patented (expired) and currently trademarked *Elasta* (self-adjusting hinges) is an important eyewear feature for many of our end customers. *Elasta* has more than 20 variations, many of which have been registered. We also have the know-how for Optyl, the result of a unique process of a special combination of resins we developed. Optyl hard-plastic products are lightweight, non-allergenic, have attractive, sophisticated chromatic effects and are resilient even in extreme temperatures, thus retaining the shape of the frame under harsh conditions such as inside a hot vehicle. The molecular structure of this material also ensures strength and permanent elasticity with improved fit.

In 2005, we developed the "Klap" model, which we currently use in our Oxydo products. The Klap model uses technical characteristics normally used only on ski goggles and masks to sunglasses. The Klap has an innovative lens, which does not fog and offers a high degree of protection from UVA and UVB rays. As at the date of this Annual Report, our patent for the Klap system is pending.

Licenses

Revenues

We have license agreements with several companies pursuant to which we manufacture and distribute prescription frames and sunglasses. Our performance is strongly affected by these licenses. In terms of revenues, our top three license agreements are those with *Armani, Dior, Gucci*.

Royalties

We pay a royalty for use of the licensed brand name based on a percentage of net sales of that brand, which may be offset by guaranteed minimum royalty payments. Our licenses typically have a duration of five to eight years. In certain circumstances, a license agreement may be terminated by the licensor such as if there is a change in our control, we outsource production without consent of the licensor, we sell models that are not approved by the licensor, we fail to reach minimum sales targets or we sell products through distribution outlets that have not been approved by the licensor. Many of these conditions apply to our key licenses.

We incurred in royalty expenses of €98.5 million in 2006 and of 91.0 million in 2005.

In many of our agreements there are minimum annual guaranteed royalty payments to the licensor. Often the guarantee is 80% of the prior year's royalty payment or a certain amount is specified. We will be required to pay the minimum guaranteed royalties under these provisions of the license agreements even if sales decrease significantly or did not meet expectations.

The license agreements also provide for a mandatory payment for the advertising and promotion of the brand linked to the prior year's sales. In some cases, the licensor requires payments to assist the licensor in its own advertising and promotional activities. Certain of our licenses require minimum guaranteed payments for promotional and advertising expenses.

TREND INFORMATION

During 2006, we renewed each of our license agreements with *Yves Saint Laurent* for three additional years, up to 2010, with *Max Mara* for seven additional years, up to 2013, as well as our USA licensed brand *Saks Fifth Avenue*, renewed for further five years, up to 2011. As already communicated, the license relationship with *Polo Ralph Lauren* expired on December 31, 2006 but Sàfilo is allowed to distribute, on a no-exclusive basis, the remaining products until June 2007, in accordance with the sell-off period stated under the agreement.

With reference to the license agreement executed with Hugo Boss on November 2005, the first collection bearing the trademark *BOSS – Hugo Boss* had been launched on October 2006.

On April 10th, 2006 we entered into a new seven-year license agreement with *Max & Co.* for the worldwide design, production, distribution and sale of sunglasses and prescription frames bearing the relevant trademark. We will begin distributing the first collection of *Max & Co.* on October 2007.

Moreover, on November 2006 we entered into an exclusive license agreement with Banana Republic Group, effective until January 2013 with possible renewal of further 3 years, for the worldwide manufacturing, sourcing, promotion, sale and distribution of sunglasses and optical frames bearing such trademark. In particular, the distribution of such products is authorized, for the moment, only for the USA and Canada markets, starting from September 2007.

On November 9th, 2006 the Group presented the first *Armani A/X* line, a young, fashion forward urban inspired collection that solidifies Safilo's relationship with the Armani Group. The line has been firstly distributed in the U.S. through the freestanding A/X Armani Exchange stores and, starting from January 2007, is distributed worldwide. A range of prescription eyewear is scheduled to follow.

During December 2006 and January 2007 Sàfilo started the distribution of the new collection *Marc by Marc Jacobs*, in accordance with the timing agreed with the licensor under the license agreement signed on 2003 and concerning both the trademarks, *Marc Jacobs* and *Marc by Marc Jacobs*.

OFF-BALANCE SHEET ARRANGEMENTS

The table below sets forth our off-balance sheet commitments as of December 31, 2004, 2005 and 2006:

(Euro/000)	As at december 31, 2004	2005	2006
Unsecured guarantees given to third parties	**2,845**	**2,697**	**2,584**
Secured guarantees given to third parties:			
- Mortgage and lien on property, plant and equipment of Group companies	125,751	163,432	-
- Lien on trade receivables of Safilo S.p.A.	169,333	185,827	-
Total secured guarantees	**295,084**	**349,259**	**-**
Total	**297,929**	**351,956**	**2,584**

The Senior Credit Agreement is granted by pledges on Sàfilo S.p.A. shares and by guarantees of those companies of the Group which are directly financed by it.

CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

We have numerous contractual obligations providing for payments pursuant to, among other things, royalty agreements with licensors, leases for plant, warehouse and office facilities, as well as certain equipment leases.

The following table sets forth the scheduled minimum lease commitments and minimum royalty arrangements as of December 31, 2006:

(Euro/000)	Payments due by period				
Contractual Obligations and Commercial Commitments as of December 31, 2006	**Total**	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Long-term debt obligations (including current portion)	557,800	91,925	76,286	201,349	188,240
Finance lease obligations (including current portion)	10,829	1,121	2,063	2,211	5,433
Operating Lease Obligations	93,143	18,094	30,365	20,852	23,833
Minimum Royalty Arrangements	219,891	88,652	60,575	46,765	23,899
Total	**881,663**	**199,791**	**169,289**	**271,178**	**241,404**

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

DIRECTORS AND SENIOR MANAGEMENT

Board of Directors

As of the date of this Annual Report, our board of directors (the "Board of Directors") is composed of 7 members.

The following table sets forth the names and dates of birth of the members of our Board of Directors.

Board of Directors	Name	Date of Birth	Domicile for the Office	Date of appointment
Chairman	Vittorio Tabacchi	October 26, 1939	Sàfilo S.p.A., Settima Strada, 15 Z.I. Padova	April, 27 2006
Vice-Chairman	Giannino Lorenzon	September 26, 1939	Sàfilo S.p.A., Settima Strada, 15 Z.I. Padova	April, 27 2006
Chief Executive Officer	Claudio Gottardi	June 24, 1956	Sàfilo S.p.A., Settima Strada, 15 Z.I. Padova	August, 03 2006 confirmed October, 24 2006
Co-Chief Executive Officer	Massimiliano Tabacchi	October 10, 1970	Sàfilo S.p.A., Settima Strada, 15 Z.I. Padova	August, 03 2006
Directors	Carlo Gilardi	November 17, 1942	Via Massimi, 119, Roma	April, 27 2006
	Ennio Doris	September 3, 1940	Mediolanum S.p.A., Via F. Sforza, Palazzo Meucci, Milano 3, Basiglio (MI)	April, 27 2006
	Riccardo Ruggiero	August 26, 1960	Telecom Italia S.p.A., Piazza Einaudi 8, Milano	April, 27 2006

Vittorio Tabacchi, our Chairman since 1993, is the second son of our founder, Guglielmo Tabacchi. Mr. Vittorio Tabacchi joined our Group in 1970 as Production Manager, and later served as Vice Chairman and as Managing Director. In June 2004, he received an honorary degree in engineering from the University of Padua.

Giannino Lorenzon has been our Vice Chairman since 2005. He joined the Group in 1973 as Director of the Finance, Administration and Control department. From 1986 to 2004, Mr. Lorenzon was Chief Executive Officer of Sàfilo S.p.A., overseeing the Finance, Administration and Control, Human Resources, Information Technology, Legal, Organization and Quality departments. He has been a registered accountant since 1975 and an auditor since 1995.

Claudio Gottardi joined Sàfilo S.p.A. in 1985 as Area Manager for Central Europe and, after gaining experience at Sàfilo USA, became Director of Marketing in 1993. In 1996, he became Managing Director for our Business Unit 3 (the Americas), and he is the CEO of Sàfilo USA, Smith Sport Optics, Solstice Marketing Corp., Solstice Marketing Concepts LLC, Sàfilo Canada Inc., and Canam Sport Optics. On August, 3rd 2006 he has been appointed CEO of Sàfilo Group. Prior to joining our Group, he headed the Marketing department of the Italian subsidiary of W.L. Gore, in Munich, Germany.

Massimiliano Tabacchi, had been our Chief Operating Officer from January 1, 2005 until the recent appointment as Co-Chief Executive Officer of the Group; he is the son of our Chairman. He began working with our Group in Sàfilo USA, then at our manufacturing facility in Santa Maria di Sala, Italy, and became our Director of Operations in 2002. Prior to joining our Group, Mr. Massimiliano Tabacchi was contract project manager at OTIS.

Carlo Gilardi has been our Director since 2004. From 2001 to 2003, he was the Managing Director of Cofiri S.p.A. and from 1995 until 2001 he was the Managing Director of Benetton Group S.p.A.. Prior to 1995, Mr. Gilardi was a finance manager for Banca di Roma.

Ennio Doris is our Director starting from March 2006. He is also the Chairman of Banca Mediolanum S.p.A. and is Director of Mediobanca S.p.A. and of Banca Esperia S.p.A.. Prior to joining Banca Mediolanum S.p.A., Mr. Doris was a financial consultant for Fideuram and the RAS Group. He has founded Programma Italia, a securities brokerage company, of which he has been Managing Director.

Riccardo Ruggiero is our Director starting from March 2006. As of December 31 2006, he is also the Managing Director of Telecom Italia S.p.A. Prior to joining Telecom Italia S.p.A.. in July 2001, Mr. Ruggiero was Sales Director at Fininvest, as well as Sales and Marketing Director of AT&T Italy. He has also worked in the Olivetti Group in various roles, and in 1996 was appointed Managing Director of Infostrada.

Management

The table below sets forth the names, dates of birth and seniority of the senior managers of our Sàfilo S.p.A.

Position	Name	Year of Birth	Seniority
Director of Legal Department	Katia Buja	January 20, 1966	2 years
Director of Finance	Christian De Felice	August 20, 1970	5 years
Director of Operations	Augusto Lippi	July 7, 1969	1 year
Director of Business Development	Massimo Lisot	November 2, 1969	8 years
Managing Director Business Unit 1	Giovanni Materassi	June 23, 1959	13 years
Managing Director Business Unit 2 (Manager of Sàfilo Far East Ltd.)	Mario Pietribiasi	February 4, 1957	13 years
Director of Corporate Communication and Identity	Samantha Tabacchi	May 11, 1974	6 years
Director of Administration and Control	Francesco Tagliapietra	March 18, 1967	6 years
Director of Human Resources	Alessandro Visconti	May 2, 1953	18 years
Director of Marketing and Licensing	Alberto Zotta	October 2, 1971	10 years

Katia Buja has been Head of our Legal Department since January 1, 2005. Prior to joining our legal department in 1995, Ms. Buja worked for several years as a trainee and then an attorney in several law firms, specializing in corporate, probate and bankruptcy law.

Christian De Felice has been our Director of Finance since 2002. From 1999 to 2002, he was Head of Structured Finance and Treasury at e.Biscom and Fastweb. Prior to 1999, Mr. De Felice was Treasurer of Omnitel (now Vodafone) and a trader with Banca di Roma, London Branch, in the Capital Markets Division. Mr. De Felice has been registered in Italy as an actuary since 1995.

Augusto Lippi has been our Director of Operations since 2006. From 2001 to 2005, he was a consultant with McKinsey & Company. Prior to 2001, Mr. Lippi worked for General Electric Oil & Gas (Nuovo Pignone) from 1997 to 1999 and with Ferrari Auto between 1996 and 1997.

Massimo Lisot has been our Director of Business Development since 2001, and has also been Manager of Licensing. Prior to joining our Group, Mr. Lisot worked for three years at Morgan Stanley International Limited, in the corporate finance sector of the Private Wealth Management Group.

Giovanni Materassi joined our Group in 1988 as Sales Manager for Italy, and in 1992 became Sales Manager for other European sales areas. He has been Manager of our Business Unit 1 (Europe, Middle East, India and South Africa) since 1997. Prior to joining our Group, Mr. Materassi had been a Sales Area Manager for Stefanel and for Superga.

Mario Pietribiasi joined us in 1987 as Area Manager, and in 1993 became Sales Director of other European sales areas. In 1997, he became Managing Director and manager for our Business Unit 2 (Asia). Prior to joining our Group, he was Area Manager for Cartiera Rossi and for Simod.

Samantha Tabacchi our Director of Corporate Communication and Identity, is the daughter of our Chairman. She joined the Group in October 2000, and is in charge of all the sponsoring activities and the public relations. Before joining our company, she worked in the sales and communication departments of the Gucci Group.

Francesco Tagliapietra joined us in 1997 as Senior Controller and has been our Director of Administration and Control since 2001. He oversees the department responsible for budgeting, reporting and administration. Prior to joining us, Mr. Tagliapietra was a consultant with two consultancy firms and a controller for Alfa Laval Artec S.p.A.

Alessandro Visconti has been Manager of our Human Resources department since 1997. Prior to joining our Group, Mr. Visconti had been Manager of Human Resources at Ricordati S.p.A., Glaxo S.p.A. and Jolly Hotel S.p.A.

Alberto Zotta joined us in 1996 and had been working abroad (Spain, France, Belgium) in the Logistics, Auditing and Sales departments. He was Sales Manager in Safilo France between 1997 and 1998, then became Managing Director (1998-2000). Between 2001 and 2006 he was responsible for the Western Europe. Since 2006, Mr. Zotta is Director of Marketing and Licensing.

Board of Statutory Auditors and Independent Auditors

Pursuant to Italian law, we also maintain a Board of Statutory Auditors, composed of three individuals who are required to have no other affiliation with us and who must satisfy certain professional criteria and other standards. The Board of Statutory Auditors is required to verify that: (i) we comply with the applicable law and bylaws; (ii) we comply with the principles of fair management; (iii) our organizational, administrative and accounting structure is adequate and in operation. Although members of the Board of Statutory Auditors are required to attend the meetings of the Board of Directors and Shareholders, they do not vote at such meetings.

The Board of Statutory Auditors is required to meet at least once a quarter and is also obliged to report specific matters to the Shareholders and to the Board of Directors. Any member of the Board of Statutory Auditors may request information directly from the Board of Directors; and the Board of Statutory Auditors or any two of its members may, subject to prior notification to the Chairman of the Board of Directors, call meetings of the Shareholders, the Board of Directors and the Executive Committee, if any. The Statutory Auditors may also request information from the Directors regarding our management, carry out inspections at the Company and exchange information with our external auditors.

The following table sets forth the current members of the Board of Statutory Auditors and their dates of birth. The current Board of Statutory Auditors was appointed by the ordinary Shareholders' meeting on April 29, 2005. The Board of Statutory Auditors was nominated for a three-year period and its mandate is due to expire upon approval of the financial statements as at and for the year ending December 31, 2007. Pursuant to our By-laws, the members to the Board of Statutory Auditors are elected for a maximum of three-year terms and may be re-elected.

Office	Name	Date of Birth
Chairman	Franco Corgnati	July 10, 1942
Regular Auditor	Paolo Mazzi	October 10, 1946
Regular Auditor	Lorenzo Lago	February 1, 1966
Alternate Auditor	Giampietro Sala	February 17, 1938
Alternate Auditor	Ornella Rossi	January 20, 1946

Independent Auditors

Italian law requires companies whose shares are listed on an Italian regulated market and its subsidiaries to appoint a firm of independent accountants to verify that the financial statements of the company fairly present the financial position of the company and its results of operations in compliance with Italian regulations governing financial statements and IFRS. The independent accountants express their opinion on the financial statements in a report that may be consulted by shareholders prior to the relevant shareholders' meeting.

During the Shareholders' meeting held on March 7, 2006, we appointed PricewaterhouseCoopers S.p.A. for the auditing of the yearly financial statements for the financial years 2005 to 2010. The Unified Financial Act, article 159 provides that listed companies may not appoint the same independent accountants for more than nine financial years, which may not be renewed within the first three years from the end of the previous engagement.

COMPENSATION

Board of Directors' and Board of Statutory Auditors compensation

According to Company by-laws, the Board of Directors and the Board of Statutory Auditors receive reasonable compensation plus reimbursement for out of pocket expenses that they incur in connection with their service as members of the Board of Directors and Board of Statutory Auditors, respectively. The overall amount of the compensation paid to the members of our Board of Directors (directors' fees, any salary, bonuses and benefits) and compensation paid to the Board of Statutory Auditors (auditors' fees) for the year ended December 31, 2006 was respectively €12.1 millions and €0.1 millions.

Name and surname	Office	Period of office	Expiry of office
Directors			
Vittorio Tabacchi	Chairman	all 2006	Approval of financial statements as at 31/12/2008
Giannino Lorenzon	Vice Chairman	all 2006	Approval of financial statements as at 31/12/2008
Claudio Gottardi	Chief Executive Officer	from 3/8 to 31/12/2006	Approval of financial statements as at 31/12/2008
Massimiliano Tabacchi	Co-Chief Executive Officer	from 3/8 to 31/12/2006	Approval of financial statements as at 31/12/2008
Roberto Vedovotto	Chief Executive Officer	from 1/1 to 31/7/2006	
Ennio Doris	Director	all 2006	Approval of financial statements as at 31/12/2008
Carlo Gilardi	Director	all 2006	Approval of financial statements as at 31/12/2008
Riccardo Ruggiero	Director	all 2006	Approval of financial statements as at 31/12/2008
Charles Paul Pieper	Director	from 1/1 to 15/2/2006	
Julian Masters	Director	from 1/1 to 15/2/2006	
Colin Taylor	Director	from 1/1 to 15/2/2006	
Thompson Dean	Director	from 1/1 to 15/2/2006	
Board of Statutory Auditors			
Franco Corgnati	Chairman	all 2006	Approval of financial statements as at 31/12/2008
Lorenzo Lago	Regular Auditor	all 2006	Approval of financial statements as at 31/12/2008
Paolo Mazzi	Regular Auditor	all 2006	Approval of financial statements as at 31/12/2008

Management Compensation

Members of our management team are compensated on the basis of a fixed salary plus a bonus based on economic and qualitative performance objectives. The aggregate compensation, including bonuses, paid by the Company during 2006 to the senior executives amounted to €2.5 million.

Stock Option Plans

On March 25, 2003, the extraordinary Shareholders' meeting of Sàfilo Holding S.p.A. (now Sàfilo Group S.p.A.) approved the "Piano Stock Option Sàfilo Group S.p.A. e Sàfilo S.p.a. 2003-2007" (the so-called "2003 Plan"), which provides for the free grant of rights for the subscription of new shares issued to some employees and consultants of the companies of the Group.

On November 24, 2004 the extraordinary Shareholders' meetings of Sàfilo Group S.p.A. approved a new plan, the "Piano Stock Option Sàfilo Group S.p.A. e Sàfilo S.p.A. 2004-2008" (the so-called "2004 Plan"), which provides for the free grant of rights for the subscription of new shares issued to some employees and consultants of the companies of the Group.

In compliance with the powers delegated by the Shareholders' meeting of October 24, 2005, the Board of Directors of Sàfilo Group S.p.A. on May 31, 2006 approved a share capital increase of the Company up to a maximum nominal value of Euro 2,125,296.25 through the issue of a maximum of 8,501,185 ordinary shares with a value of Euro 0.25 each and a share premium of Euro 4.16. The shares had been and will be offered in accordance with the regulations of the new "Piano Stock Option 2006-2010 Sàfilo Group S.p.A." (the so-called "2006 Plan") approved by the Board. This plan will have a duration of four financial years (2006-2010). The beneficiaries of the plan will be (in a similar manner to previous plans) some directors, executives and collaborators of companies of the Sàfilo Group. The plan provides for the grant of option rights that will vest yearly, based on ¼ tranche for each year of the Plan. The criteria for the vesting of the options are based on the reaching, by the Sàfilo Group S.p.A., of prefixed consolidated EBITDA levels set by the Board of Directors.

The fair value of the options, in accordance with the requirements of IFRS, is recorded under personnel costs with a corresponding increase in a specific equity reserve over the duration of the vesting period, as the stock option plans are "equity-settled". In compliance with the requirements of IFRS 2, irrespective of which company is obliged to issue the new shares, the stock option cost is recorded in the company in which the employees carry out their employment. The amount received when the options are exercised, net of the costs directly attributable to the transaction, will be credited to the share capital (nominal value) and the share premium reserve.

With reference to the first stock option plan mentioned above ("2003 Plan"), the Group has decided to apply the exemption for share based payments. In substance, IFRS 2 is applied from January 1, 2004 for all the options issued after November 7, 2002 but not matured ("vested") before January 1, 2005. The application of this exemption results in the recording of only the third tranche of the 2003-2007 Stock Option Plan as a cost in the income statement of the Group.

It should be noted that in December 2005 the holders of the options related to 2003 Plan and 2004 Plan, in consideration of the quotation of the company Sàfilo Group S.p.A. on the Italian Stock Market, exercised 50% of the rights in their possession. The holders will be able to exercise the remaining rights in their possession respectively within June 20, 2007 and September 20, 2008.

The total costs recorded for the financial years 2005 and 2006 are summarized as follows:

(Euro/000)	December 31, 2005	December 31, 2006
2003 Plan	79	-
2004 Plan	1,635	389
2006 Plan		138
	1,714	**527**

The table below sets forth the relevant information relating to the stock option plan (SOP) for the year 2006 compared to 2005:

SOP I (2003-2007)	2006			2005		
	Strike	N. of shares	N. of rights	Strike	N. of shares	N. of rights
As of January, 1	2.5325	909,400	227,350	2.5325	3,932,540	983,135
Issued	-	-	-	-	-	-
Granted	-	-	-	-	-	-
Not Assigned	-	-	-	-	-	-
Forfeited	-	-	-	-	-	-
Exercised	-	-	-	2.5325	(3,023,140)	(755,785)
As of December, 31	2.5325	909,400	227,350	2.5325	909,400	227,350
- of which exercisable	*2.5325*	*909,400*	*227,350*	*2.5325*	*909,400*	*227,350*
- Avg expiring date (years)			*0.5*			

SOP II (2004-2008)	2006			2005		
	Strike	N. of shares	N. of rights	Strike	N. of shares	N. of rights
As of January, 1	3.5438	3,037,832	759,458	3.5438	4,016,316	1,004,079
Issued	-	-	-	-	-	-
Granted	-	-	-	-	-	-
Not Assigned	-	-	-	-	-	-
Forfeited	-	-	-	3.5438	(54,372)	(13,593)
Exercised	-	-	-	3.5438	(924,112)	(231,028)
As of December, 31	3.5438	3,037,832	759,458	3.5438	3,037,832	759,458
- of which exercisable	*3.5438*	*3,037,832*	*759,458*	*3.5438*	*3,037,832*	*759,458*
- Avg expiring date (years)			*1.7*			

SOP III (2006-2010)	2006			2005		
	Strike	N. of shares	N. of rights	Strike	N. of shares	N. of rights
As of January, 1	-	-	-	-	-	-
Issued	4.4100	8,501,185	8,501,185	-	-	-
Granted	4.4100	3,548,817	3,548,817	-	-	-
Not Assigned	-	-	-	-	-	-
Forfeited	4.4100	(34,014)	(34,014)	-	-	-
Exercised	-	-	-	-	-	-
As of December, 31	4.4100	3,514,803	3,514,803	-	-	-
- of which exercisable	-	-	-	-	-	-
- Avg expiring date (years)			*4.0*			

TOTAL	2006			2005		
	Strike	N. of shares	N. of rights	Strike	N. of shares	N. of rights
As of January, 1	3.3108	3,947,232	986,808	3.0435	7,948,856	1,987,214
Issued	4.4100	8,501,185	8,501,185	-	-	-
Granted	4.4100	3,548,817	3,548,817	-	-	-
Not Assigned	-	-	-	-	-	-
Forfeited	4.4100	(34,014)	(34,014)	3.5438	(54,372)	(13,593)
Exercised	-	-	-	2.7693	(3,947,252)	(986,813)
As of December, 31	4.1690	7,462,035	4,501,611	3.3108	3,947,232	986,808
- of which exercisable	*3.3108*	*3,947,232*	*986,808*		*3,947,232*	*986,808*
- Strike range (min)	*2.5325*					
- Strike range (max)	*4.4100*					
- Avg. Expiring dates (years)			*3.4*			

BOARD PRACTICES

Sàfilo S.p.A. Directors are appointed at the general Shareholders' meeting to serve a maximum 3 years term. The terms of all current directors will expire upon approval of the financial statements as at and for the year ending December 31, 2008.

The Board must consist of a minimum of 3 members and a maximum of 11 members, and the Directors may be re-elected. They may be removed at any time by the voting at a Shareholders' general meeting, and they may resign at any time by written notice to the Board of Directors and to the Chairman of the Company's Board of Statutory Auditors. If a vacancy occurs, the remaining Directors may choose an interim Director to fill the vacancy and serve until the next Shareholders' meeting when the latter will be asked to vote to ratify the nomination of the interim Director.

EMPLOYEES

Overview

As of December 31, 2006, we had 7,355 employees worldwide, comprising 4,632 factory employees, 2,647 clerical employees and 76 executive-level employees.

We believe that the majority of our European employees are represented by trade unions. We consider our relationship with the unions to be good and are committed to maintaining those relationships. We have not experienced any material labor strike or disruption.

The following tables set forth the number of our employees as of December 31, 2004, 2005 and 2006, broken down by job function and by job location.

	December 31,		
	2004	2005	2006
Headquarter (Padua - Italy)	707	765	845
Factory personnel	4,561	4,192	4,573
Subsidiaries	1,024	1,053	1,083
Retail chains	221	374	854
Total	**6,513**	**6,384**	**7,355**

	December 31, 2004			December 31, 2005			December 31, 2006		
	Italy	Other Countries	Total	Italy	Other Countries	Total	Italy	Other Countries	Total
Managers	30	49	79	30	45	75	30	46	76
Clerical	749	1,088	1,837	805	1,282	2,087	855	1,792	2,647
Factory	2,976	1,621	4,597	2,824	1,398	4,222	3,013	1,619	4,632
Total	**3,755**	**2,758**	**6,513**	**3,659**	**2,725**	**6,384**	**3,898**	**3,457**	**7,355**

Public Fund for Employees' Salaries

On July 21, 2005, we signed an agreement with the trade unions before the Ministry of Labor in relation to our plan to close our industrial plant in Calalzo di Cadore and our two production facilities in Coseano and Ronchis. The agreement allows us to seek access to the special Italian public fund *Cassa Integrazione Guadagni Straordinaria* ("CIGS"), which is funded by contributions from both employers and employees. As of the date of this Annual Report, we obtained the authorization to access CIGS for 41 employees of the Calalzo industrial plant.

Use of CIGS entails suspension from work of each employee involved for a maximum period of 24 months. During their CIGS suspension period, the affected employees will attend training and/or retraining

courses to improve their skills for re-entry in the labor force. At the expiry of the 24-month CIGS period, any employee who has not been relocated will be made redundant.

SHARE OWNERSHIP

We have one Shareholder, Sàfilo Group S.p.A., which owns 90,9% of our ordinary shares. The remaining share are owned by Sàfilo S.p.A. itself as treasury shares.

None of the members of the Board of Directors, the Board of Statutory Auditors or senior managers hold shares of Sàfilo S.p.A. or its subsidiaries.

The Chairman and some members of the Board of Directors hold shares in companies having an indirect controlling interest in Sàfilo S.p.A..

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

MAJOR SHAREHOLDERS

Sàfilo's capital stock as of December 31, 2006 consisted of 35,000,000 ordinary shares with full voting rights, of which 31,824,000 are owned by Sàfilo Group S.p.A. and 3,176,000 are held by Sàfilo S.p.A. as treasury shares.

As of December 31, 2006 Sàfilo Group S.p.A., whose shares are publicly traded on the Italian Stock Exchange, was owned by a company controlled collectively by Vittorio Tabacchi's family, funds advised by CSFB Private Equity and the market.

RELATED PARTY TRANSACTIONS

The nature of the related party transactions is given in the following table:

Related parties *(Euro/000)*	Relationship	December 31, 2006	December 31, 2005	December 31, 2004
Receivables				
Elegance International Holdings Ltd	(a)	-	750	525
Optifashion As	(b)	4	-	-
Safilens S.r.l. (*)	(a)	-	207	-
Total		**4**	**957**	**525**
Payables				
Elegance International Holdings Ltd	(a)	10,360	8,533	10,715
Safilens S.r.l. (*)	(a)	-	22	-
Total		**10,360**	**8,555**	**10,715**

Related parties	Relationship			
(Euro/000)		2006	2005	2004
Revenues				
Elegance International Holdings Ltd	(a)	611	578	4
Optifashion As	(b)	221	179	268
Safilens S.r.l. (*)	(a)	-	2	-
Total		**832**	**759**	**272**
Costs				
Elegance International Holdings Ltd	(a)	27,192	20,673	21,654
Safilens S.r.l. (*)	(a)	-	81	387
TBR Inc.	(a)	1,152	1,107	1,054
Total		**28,344**	**21,861**	**23,095**

(a) Associated companies;
(b) unconsolidated subsidiaries;
(*) investment transferred during 2006.

These transactions relate to commercial relationships on the basis of prices defined at normal market conditions, similar to transactions with third parties.

Safilo USA rents its headquarters and distribution centre in the USA (New Jersey), based on a rental contract with TBR Inc., a company one third owned by Vittorio Tabacchi, Chairman of the Board of Directors and shareholder of Safilo Group S.p.A., one third by a subsidiary of the Safilo Group S.p.A. and one third by a third party. Safilo Group S.p.A. indirectly acquired the holding in TBR Inc. in 2002 for Euro 629 thousand. In 2006 the Group paid rent of Euro 1,152 thousand to TBR Inc. The price and other conditions of the rental contract are in line with market conditions for similar contracts.

Safilo Far East Limited, a subsidiary of Safilo Group S.p.A., holds 23.05% of Elegance International Holdings Limited ("Elegance"), a company listed on the Hong Kong Stock Exchange. Elegance is a producer of eyewear products in Asia, to which the Group assigns part of its production. The price and other conditions of the production contract between Safilo Far East Limited and Elegance are in line with those applied by Elegance to its other clients. Massimiliano Tabacchi, director of Safilo Group S.p.A., and Mario Pietribiasi, executive of the Group, are non-executive directors of Elegance. In addition, Mario Pietribiasi is also a shareholder of the company with a holding of less than 0.5%.

ITEM 8. FINANCIAL INFORMATION

CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION

See ITEM 18 "Financial Statements."

Legal proceedings

We are currently party to various claims and legal actions that arise in the ordinary course of business. We believe such claims and legal actions, individually and in the aggregate, will not have a material adverse effect on our business, financial condition or results of operations.

In June 2005, a claim was filed with the Court of Milan against Sàfilo S.p.A. and other defendants for approximately €7 million in legal fees allegedly owed to an Italian law firm for legal services provided to the defendants from 1999 to 2001. We believe the claim is unsupported and that no money is to be owed to the plaintiff, and consequently we have not reserved any provision in connection with this matter. The next hearing regarding this legal proceeding has been set for September 25, 2007.

In June 2003, a claim alleging unfair business practices was filed with the Court of Rome against Sàfilo S.p.A. by one of our clients, who later filed bankruptcy. The claim has been taken over by the plaintiff's receiver, who seeks approximately €2 million in damages. We have denied all allegations concerning this claim. A hearing was held on November 23, 2005 to hear witness statements and the next hearing is scheduled for December 2007. Our legal counsel has advised us that the claim is unsupported, therefore we have not reserved any provision in connection with this matter.

In February 2005, two companies (having the same owner) that are clients of the Group filed two claims against Sàfilo S.p.A. with the Court of Vicenza, seeking €3.7 million in damages for breach of contract. We filed a response reaction challenging the jurisdiction of the Court of Vicenza. No decision has been rendered on either the jurisdiction matter or the merits of the case. The two companies are currently challenging this order. Next hearing on the matter is scheduled for July 12, 2007.

Dividend Policy

Payment of an annual dividend is subject to the approval of our Shareholders at an ordinary Shareholders' meeting, which must be convened within 120 days, or, in certain exceptional circumstances, 180 days, after the end of the financial year to which it relates. It is the practice in Italy that the Shareholders vote on a proposal made by a company's Board of Directors as to the amount of a dividend.

As provided by Italian law, before dividends may be paid with respect to any financial year, we must allocate at least 5% of our net income for such year as legal reserve until such reserve, including amounts set aside during prior years, is equal to at least 20% of the aggregate nominal value of our issued share capital. Net income allocated to dividends is divided in accordance with the resolutions approved by a Shareholders' meeting. Dividends are payable on the date specified by the Shareholders' meeting. Dividends not claimed within five years from the date upon which they become payable will be forfeited to us.

Sàfilo S.p.A. did not pay any dividends to its Shareholders for the financial years ended December 31, 2004 and December 31, 2005.

The Shareholders' meeting held on November 13th, 2006 deliberated, for the year ended December 31, 2006, a dividend distribution in favor of its parent company Sàfilo Group S.p.A. for a total amount of €16 million.

SUBSEQUENT EVENTS

In the period subsequent to the closing of the financial year, there were no events that could be considered to significantly affect the data contained in the present report.

ITEM 9. THE OFFER AND LISTING

Offer and listing details

The Company has 9.625% Senior Notes due May 2013, issued through its subsidiary Sàfilo Capital International S.A. (the "Notes"), listed on the Luxembourg Stock Exchange. The table below sets forth the annual high and low closing sales prices of the Notes, as reported by Bloomberg L.P., for the four most recent financial years; 2003 data refer to May-December since the Notes began trading on the Luxembourg Stock Exchange in May 2003:

	High	Low
2003	105.09%	86.04%
2004	102.37%	76.74%
2005	113.15%	100.60%
2006	114.41%	110.40%

The table below sets forth, by fiscal quarter, the high and low closing sales prices of the Notes, as reported by Bloomberg L.P., for the two most recent full financial years:

	High	Low
2005		
First quarter	107.78%	101.54%
Second quarter	108.41%	100.60%
Third quarter	112.87%	107.88%
Fourth quarter	113.15%	111.94%
2006		
First quarter	114.41%	112.06%
Second quarter	113.19%	111.55%
Third quarter	111.78%	110.43%
Fourth quarter	110.57%	110.40%

The table below sets forth the high and low closing sale prices of the Notes, as reported by Bloomberg L.P., for the most recent six months:

	High	Low
2006		
October	110.56%	110.44%
November	110.57%	110.44%
December	110.52%	110.40%
2007		
January	110.50%	110.21%
February	110.52%	110.34%
March	110.34%	109.86%

ITEM 10. ADDITIONAL INFORMATION

MEMORANDUM AND ARTICLES OF ASSOCIATION

Registration

As set forth in Article 4 of the Articles of Association, the Company's corporate purposes are:

a) carrying out, directly or indirectly, through subsidiaries or affiliates, in Italy or abroad, activities in the field of the manufacturing and marketing of eyeglasses frames, sunglasses, sport glasses, lenses, machinery and equipment for the production of eyewear and other accessories for optics, sport and leisure-time gadgets;

b) the acquisition, negotiation and management of shareholdings in companies operating in the sectors of optics and precision mechanics; implementation of financial transactions; financing of subsidiaries or affiliates and execution of financial agreements for the technical and financial co-ordination of their activities, except that any activity deemed "financial" under the law will not be carried out in relation to the public at large but exclusively within the Group;

c) advising on the economic, administrative, structural and commercial planning of some sectors of the market or of single enterprises; their restructuring; feasibility studies on acquisitions of companies; management of development programs for relationships with foreign countries; management of industrial and commercial enterprises operating in the field of optics and precision mechanics. The company may carry out all commercial and industrial transactions, on movable or immovable property, which the Board deems necessary or instrumental to achieve the corporate purpose; it may receive loans from its Shareholders, and grant or receive intra-group loans; it may give guarantees and endorsements, and any other security, provided not in relation with the public; it may represent national or foreign enterprises, and directly or indirectly, purchase shares in other companies, consortia, partnerships and enterprises which have an identical, similar, related corporate purpose.

Directors' Voting Powers

Under Italian law, attendance of a majority of the Board of Directors at a Board meeting is required in order to establish a quorum.

Any Director also may participate in any meeting of the Board in person, by telephone conference call, video conference or by any other similar means allowing all directors participating in the meeting to hear one another.

There is no age limit for Directors and there are no requirements that a Director must own a minimum number of shares in order to qualify to act as a Director.

According to Italian law, in the case of a conflict of interest of a Director, the Director must inform the Board of Directors and the Board of Auditors of the conflict and should abstain from voting on any issue in which he is materially interested.

Shareholders vote on Director's compensation at the Shareholders' general meeting which appoints the Board. The Board of Directors may determine specific compensation for those Directors appointed in the Board of Directors with the specific offices of Chairman, Vice Chairman and Chief Executive Officer.

Share Rights, Preferences and Restrictions

The authorized and issued share capital is EUR 35,000,000.00, divided into 35,000,000 ordinary shares, each with a nominal value of EUR 1.00.

The Shareholders' meeting may, in the circumstances provided for by law, reduce the share capital by assigning to the single Shareholders certain assets of the company ("attività sociali") or shares/quotas of other companies which it owns.

Pre-emption Rights

New issue of ordinary shares or other classes of capital stock may be authorized by a Shareholder's resolution passed at an extraordinary Shareholders' meeting. The articles of association may also authorize the Board of directors to increase the share capital up to a pre-defined amount within a five-year period. Pursuant to Italian law, Shareholders are entitled to subscribe for new issues of: (i) shares; (ii) debt instruments convertible into ordinary shares; and (iii) any other instruments such as warrants, rights or options entitling the holder to acquire shares, in each case in proportion to their respective shareholdings. Subject to certain conditions and special voting majorities principally designed to prevent dilution of the rights of Shareholders these pre-emption rights may be waived or limited in whole or in part for all such Shareholders for any particular issue of such securities, but only by way of a resolution adopted at an extraordinary meeting with the affirmative vote of Shareholders representing more than 50% of the outstanding shares, even if such vote is taken at a Shareholders' meeting held on a second or third call and provided that our interest so requires. In any event such pre-emption rights will not apply where the increase in share capital is to be subscribed by way of a contribution in kind.

Pre-emption rights can also be limited when the newly issued shares are offered for subscription to our employees or employees of our subsidiaries or of the controlling company. Pursuant to Italian law, resolutions that exclude pre-emption rights for less than one quarter of the newly issued shares must be adopted at an extraordinary meeting with the required majorities. When the exclusion of pre-emption rights relates to more than one quarter of the newly issued shares when these are offered for subscription to our employees or employees of our subsidiaries or of the controlling company then the relevant resolution must be adopted with the affirmative vote of Shareholders representing more than 50% of the outstanding shares, even if such vote is taken at a Shareholders' meeting held on the second call.

Different Classes of Shares

In accordance with Italian law, we are permitted to issue different classes of shares, defining the rights to which such shares will be entitled, within the limits of the applicable law. We could issue shares that may not have the right to vote in any Shareholders' meeting or only in certain Shareholders' meetings or regarding certain matters or under certain conditions, to be defined in the by-laws. We could issue shares that may have preferential rights with respect to the payment of dividends and to the repayment of capital in the event of liquidation.

Shareholders' Meetings

Under Italian law, Shareholders' meetings may be either ordinary or extraordinary.

The ordinary Shareholders' meeting must be convened at least once a year, within 120 days from the end of the financial year, or within 180 days in case certain conditions are met.

The Board of Directors may also call a meeting whenever it deems it appropriate and it is required by Italian law to promptly call a Shareholders' meeting upon the request of shareholders representing at least 10% of the issued and outstanding share capital, or a lower percentage if the By-laws so provide. Additionally, the Board of Statutory Auditors, or the president of the Court that has jurisdiction over the company has the duty to call Shareholders' meetings in certain circumstances under Italian law, by giving Notice.

According to the By-Laws, meetings are called by the Board of Directors by giving a written notice that states the date, time, place and agenda for the meeting (the "Notice"). According to the By-Laws, Shareholders are informed of all shareholders' meetings to be held by publication of the Notice in the *Gazzetta Ufficiale*, or, alternatively, by transmission of the Notice through means which guarantee its receipt by the addressee at least 8 days before the meeting in the first call. The notice may specify a date for a second call in the event that the quorum required by the law for the validity of the Shareholders' meeting and its resolutions is not met in the first call.

The provisions of the Italian Civil Code will apply to determine the valid constitution of Shareholders' meetings and the validity of their resolutions. Meetings may be held by video or telephone conference if some conditions aimed at ensuring full participation by all Shareholders are met.

Shareholders who hold ordinary shares are entitled to attend and vote both at ordinary and extraordinary Shareholders' meetings. Each holder will be entitled to cast one vote for each Share held. Votes may be cast personally or by proxy. However, the voting rights of shares held in breach of applicable law may in some cases not be exercised.

Resolutions adopted at a Shareholders' meeting are binding on all Shareholders, including dissenting or absent Shareholders. However, pursuant to Italian law, any Shareholders who do not vote in favor of a resolution passed at a Shareholders' meeting or who do not attend such meeting or abstain from voting, representing a shareholding equal to or higher than 5% of the share capital of a company (as well as all Directors and Statutory Auditors) are entitled to challenge the resolution on the basis that it was taken in violation of the applicable laws or By-laws. Such challenges must be made within 90 days from the date of the resolution or, if the resolution is subject to required registration in the companies' register, within 90 days of registration.

There are no restrictions arising under Italian law or the By-laws on the rights of non-resident or foreign persons to hold or vote the shares other than those limitations that apply generally to all Shareholders.

Change in Control

The transfer of Company's shares is no longer subject to the pre-emption right in favor of the other Shareholders, due to the resolution of the Shareholders' extraordinary meeting which amended the articles of association of the Company.

Liquidation Rights

Under Italian law, and subject to satisfaction of the claims of all other creditors, Shareholders are entitled to a distribution of the remaining liquidated assets in proportion to the nominal value of the shares they hold in the capital stock. Thereafter, if there were surplus assets, Shareholders of ordinary shares would rank equally in their claims to the distribution of such surplus assets, unless the share capital of the company includes classes of shares that have preferential rights with respect to distribution of the company assets in case of liquidation.

Purchase by us of our own shares

We may purchase our own shares, subject to certain conditions and limitations imposed by applicable law and provided that the shares are fully paid. These purchases must be authorized by the ordinary Shareholders' meeting and only paid out of retained earnings or distributable reserves remaining from the last approved unconsolidated financial statements. Further, we may only repurchase fully paid shares. The nominal value of shares to be repurchased, together with any shares previously repurchased by us or any of our subsidiaries, may not (except in limited circumstances) exceed in the aggregate 10% of the company's share capital then issued and outstanding.

We are not entitled to vote or to receive dividends on the shares we own. Neither we nor any of our subsidiaries can subscribe for new shares in the case of capital increases, except the case where Shareholders, within the limits described above, may authorize the exercise of our pre-emption right on our own shares. Ordinary shares owned by us and our subsidiaries count at Shareholders' meetings for quorum purposes.

In 2002 Sàfilo S.p.A. repurchased 3,176,000 ordinary shares or 9.1% of Share Capital for an aggregate cost of €80,988 thousands.

Company and Shareholders' actions against our board of directors

Under Italian law, actions against members of a board of directors may be brought by a company pursuant to a resolution adopted by the ordinary Shareholders' meeting. In addition, under Italian law, a single Shareholder may bring an action against the members of a board of directors in respect of any damage directly suffered for negligence or wilful misconduct within five years from the occurrence of the event that prejudiced Shareholders.

Shareholders' Agreements

There are no Shareholders' agreements concerning the company.

MATERIAL CONTRACTS

Senior Credit Facilities and Senior Notes

On June 26, 2006 the Group completed an important refinancing operation through the replacement of the Senior Loan received in 2002.

In 2003, our affiliate Sàfilo Capital International S.A. issued €300,000,000 9 5/8% Senior Notes. The Senior Notes are guaranteed on a senior subordinated basis by Sàfilo S.p.A. and certain of its subsidiaries and are governed by an indenture dated May 15, 2003 between Sàfilo S.p.A., Sàfilo Capital International S.A., Sàfilo Group S.p.A. and certain subsidiaries and The Bank of New York as Trustee. On January 13, 2006, the Group has refunded in advance 35% of the Senior Notes.

For details, see section entitled "Liquidity and Capital Resources" included in Item 5.

Intercreditor agreement

As part of our refinancing in 2006, we amended the previous inter-creditor agreement to confirm the relative rights of certain creditors, between Sàfilo Capital International S.A., Sàfilo S.p.A., its parent Sàfilo Group S.p.A., the subsidiary guarantors of the Notes, the lenders under the senior credit agreement and The Bank of New York as the trustee under the indenture for the Notes.

In the event of insolvency, the intercreditor agreement provides that all obligations in respect of the Notes, the guarantees and the issuer loan agreement are subordinated to the prior payment in full of all obligations under the senior credit agreement.

Factoring agreement

In 2004 we entered into a without-recourse factoring agreement with Centro Factoring S.p.A. We transfer some of our Italian trade receivables on a revolving basis and receive an up-front payment of 90% of the face value of the receivables we sell. The difference between cash received and trade receivables sold will be collected at its maturity date. We have a servicing obligation to act as a collection agent on behalf of Centro Factoring S.p.A.

As of December 31, 2006 the amount due to the factor was €38.1 million.

ITALIAN EXCHANGE CONTROLS

The following is a summary of the relevant Italian laws in force as of the date of this Annual Report but does not purport to be a comprehensive description of all exchange control considerations that may be relevant.

There are no exchange controls as such in Italy restricting rights deriving from the ownership of the Notes. Residents of Italy may hold foreign currency and foreign securities of any kind, within and outside Italy. Non-residents may invest in Italian securities without restriction and may transfer to and from Italy cash, instruments of credit and securities, in both foreign currency and Euro, representing interest, dividends, other asset distributions and the proceeds of dispositions.

Certain procedural requirements, however, are imposed by Italian legislation that implements an EU directive regarding the free movement of capital. Such legislation requires that transfers into or out of Italy of cash or securities in excess of €12,500 be reported in writing to the *Ufficio Italiano dei Cambi* (the Italian Exchange Office) by residents or non-residents that effect such transfers directly, or by credit institutions or other intermediaries that effect such transactions on their behalf. In addition, credit institutions and other intermediaries effecting such transactions on behalf of residents or non-residents of Italy are required to maintain records of such transactions for five years, which may be inspected at any time by Italian tax and judicial authorities. Non-compliance with these reporting and record-keeping requirements may result in administrative fines or, in the case of false reporting and in certain cases of incomplete reporting, criminal penalties. The *Ufficio Italiano dei Cambi* is required to maintain reports for a period of ten years and may use them, directly or through other government offices, to police money laundering, tax evasion and any other crime or violation.

Individuals and non-profit entities that are residents of Italy must disclose on their annual tax declarations all investments and financial assets held outside Italy, as well as the total amount of transfers to, from, within and between countries other than Italy relating to such foreign investments or financial assets, even if at the end of the taxable period such persons no longer owned such foreign investments or financial assets. Such disclosure requirement does not apply if the total value of the investments and assets at the end of the taxable period or the total amount of the transfers carried out during the year is not greater than €10,300. Corporations and partnerships resident in Italy are exempt from such disclosure requirements with respect to their annual tax declarations because this information is required to be disclosed in their financial statements.

There can be no assurance that the present regulatory environment in or outside Italy will continue or that particular policies presently in effect will be maintained, although Italy is required to maintain certain regulations and policies by virtue of its membership of the EU and other international organizations and its adherence to various bilateral and multilateral international agreements.

TAXATION

Taxation related to Notes

U.S. Federal Income Tax Considerations

The following discussion is a summary of certain material U.S. federal income tax consequences of the purchase, ownership and disposition of the Notes by U.S. Holders (as defined below). The summary is not a complete analysis or description of all potential tax consequences to U.S. Holders and does not address all tax considerations that may be relevant to all categories of holders (such as dealers or traders in securities, commodities, or currencies, tax-exempt investors, investors whose "functional currency" is not the U.S. dollar, investors who own 10 percent or more of our voting stock, financial institutions, thrifts, regulated investment companies, insurance companies, grantor trusts, individual retirement accounts or other tax-deferred accounts, partnerships and other pass-through entities and persons who hold the Notes through such partnerships or other pass-through entities, investors that hold the notes as part of a "hedging", "integrated", "conversion" or constructive sale transaction, as part of a “synthetic security” or a "straddle", persons who have ceased to be U.S. citizens or to be taxed as resident aliens, or investors liable for the alternative minimum tax).

This summary is based on the Internal Revenue Code of 1986, as amended (the "Code"), judicial decisions, administrative pronouncements, and existing and proposed U.S. Treasury Regulations, changes to any of which after the date of this annual report could apply on a retroactive basis and affect the tax consequences described herein.

You are a U.S. Holder, for U.S. Federal income tax purposes, if you are:

- a citizen or resident of the United States;
- a corporation, or other entity treated as a corporation, created or organized in or under the laws of the United States or any State;
- an estate, the income of which is subject to U.S. federal income taxation regardless of its source; or
- a trust:
  - (a) the administration of which is subject to the primary supervision of a court within the United States and for which one or more U.S. persons have the authority to control all substantial decisions; or
  - (b) that has a valid election in effect under applicable U.S. Treasury Regulations to be treated as a U.S. person.

If a partnership holds the Notes, the U.S. federal income tax treatment of a partner generally will depend upon the status of the partner and the activities of the partnership. Partners of partnerships holding the Notes should consult their own tax advisors concerning the associated tax consequences.

Holders of the Notes should consult their own tax advisors concerning the U.S. Federal, state and local tax consequences of the purchase, ownership and disposition of the Notes.

Payments of Interest

Payments of interest on a note will be includible in the gross income of a U.S. Holder as ordinary income from foreign sources at the time it is received or accrued, in accordance with the U.S. Holder's method of accounting for U.S. federal income tax purposes, under the rules set forth below.

In the case of a U.S. Holder that is not required to accrue interest income prior to the receipt thereof (for example, an individual U.S. Holder who uses the cash method of accounting), the amount of interest income in respect of any interest payment will be determined by translating such payment into U.S. dollars at the spot exchange rate in effect on the date such interest payment is received. No exchange gain or loss will be realized with respect to the receipt of such interest payment, other than exchange gain or loss that is attributable to the actual disposition of the euros received.

In the case of a U.S. Holder that is required to accrue interest income prior to receipt thereof (for example, a U.S. Holder that uses the accrual method of accounting), the amount of any interest income accrued during any accrual period will generally be determined by translating the accruals into U.S. dollars at the average spot exchange rate applicable to the accrual period, or, with respect to an accrual period that spans two taxable years, the part of the period within the taxable year. A U.S. Holder will additionally realize exchange gain or loss with respect to any interest income accrued on the date such interest income is received (or on the date the note is disposed of) in an amount equal to the difference between (x) the amount determined by converting the amount of the payment received into U.S. dollars at the spot exchange rate in effect on the date such payment is received (or on the date the note is disposed of) and (y) the amount of interest income accrued in respect of such payment according to the rule set forth in the preceding sentence. Notwithstanding the preceding two sentences, a U.S. Holder that is required to accrue interest income prior to receipt thereof may alternatively make an election to apply a "spot accrual convention," as set forth in Section 1.988-2(b)(2)(iii)(B) of the U.S. Treasury

Regulations. A U.S. Holder who makes this election translates accrued interest into U.S. dollars at a single spot exchange rate, which is generally the rate in effect on the last day of the accrual period or, in the case of an accrual period that spans two taxable years, the exchange rate in effect on the last day of the part of the accrual period within the taxable year. If the last day of the accrual period is within five business days of the date the interest payment is actually received, an electing accrual basis U.S. Holder may instead translate that interest payment at the exchange rate in effect on the day of actual receipt. This election must be applied consistently to all debt instruments from year to year and cannot be changed without consent from the Internal Revenue Service. Exchange gain or loss is treated as ordinary income or loss from sources within the United States for U.S. federal income purposes.

Interest payments on a note received by a U.S. Holder will be treated as foreign source income for purposes of computing the U.S. Holder's foreign tax credit allowable under U.S. federal income tax law. The rules relating to foreign tax credits and the timing thereof are complex and U.S. Holders should consult their own tax advisors regarding the availability of a foreign tax credit and the application of foreign tax credit limitations to their particular situation.

Sale, Exchange, Retirement and Other Disposition of the Notes

Upon the sale, exchange, retirement or other disposition of a note, a U.S. Holder will generally recognize taxable gain or loss equal to the difference between the amount realized (not including any amounts received that are attributable to accrued and unpaid interest, which will be taxable as interest income, and exchange gain or loss on such accrued, unpaid interest, as set out above) and the U.S. Holder's tax basis in the note. A U.S. Holder's tax basis in a note generally will be its U.S. dollar cost calculated at the exchange rate in effect on the date of purchase. The amount realized on the sale, exchange or retirement of a note for an amount of foreign currency will be the U.S. dollar value of that amount on (i) the date the payment is received in the case of a cash basis U.S. holder, (ii) the date of disposition in the case of an accrual basis U.S. holder, or (iii) in the case of a note traded on an established securities market (as defined in the applicable U.S. Treasury Regulations), that is sold by a cash basis U.S. holder (or an accrual basis U.S. holder that so elects), on the settlement date for the sale.

Gain or loss on the sale, exchange or retirement of a note that is attributable to changes in currency exchange rates will be ordinary income or loss and will be characterized as principal exchange gain or loss. Principal exchange gain or loss will generally equal the difference between the U.S. dollar value of the issue price of the note in foreign currency determined using the spot exchange rate on the date of the sale, exchange or retirement, and the U.S. dollar value of the issue price of the note in foreign currency determined using the spot exchange rate on the date the U.S. Holder acquired the note. Such gain or loss will be recognized only to the extent of the total gain or loss realized by the U.S. Holder on the sale, exchange or retirement of the note, and will generally be treated as ordinary income or loss from sources within the United States for U.S. federal income tax purposes.

Gain or loss in excess of principal exchange gain or loss will be capital gain or loss, and will be long-term capital gain or loss if the note was held for more than one year at the time of the disposition. Certain U.S. Holders (including individuals) are eligible for preferential rates of U.S. federal income tax in respect of long-term capital gain. The deduction of long-term capital losses is subject to significant limitations. Gain or loss recognized by a U.S. Holder generally will be treated as U.S. source income or loss.

Non-US Holders

As used herein, a non-US Holder is a person who is not a US Holder. Subject to the discussion concerning information reporting and backup withholding below, generally, a non-US Holder will not be subject to US federal income tax on payments of interest on, or gain on the sale of a note, unless such non-US Holder held the note in connection with a US trade or business carried on by such non-US Holder, or in the case of the sale of a note to a non-US Holder who is an individual, such individual was present in the US for 183 days or more during the tax year in which such gain is realized and certain other conditions are met.

Backup Withholding and Information Reporting

The paying agent or the financial intermediary through whom you hold the Notes may be required to file information returns with the US Internal Revenue Service in connection with payments made in respect of a note to certain US persons. If you are a US Holder, you generally will not be subject to a US backup withholding tax on such payments if you provide your taxpayer identification number and certain other information in the required manner to such paying agent or financial intermediary. You may also be subject to information reporting and backup withholding tax requirements with respect to the proceeds from a sale or other disposition of the Notes. If you are a non-US Holder, you may have to comply with certification procedures to establish that you are not a US person in order to avoid information reporting and backup withholding tax requirements. Backup withholding is not an additional tax. Amounts withheld as backup withholding may be credited against a holder's US federal income tax liability.

Italian Tax Considerations

The statements herein regarding taxation are based on the laws in force in Italy as of the date of this Annual Report and are subject to any change in law occurring after such date, which changes could be made on a retroactive basis. The following summary does not purport to be a comprehensive description of all the tax considerations which may be relevant to non-individual holders or to individual holders that hold notes in a business.

Interest on the Notes

Interest, premium and other proceeds paid on Notes by the non-resident Issuer to a beneficial owner who is not resident in Italy for tax purposes, without a permanent establishment in Italy to which the Notes are effectively connected, should not be subject to any Italian taxation.

If you are a resident of Italy for Italian tax purposes, and you are a private individual holding Notes not in connection with entrepreneurial activity, payments of interest, premium and other proceeds in respect on the Notes will be subject to final *imposta sostitutiva* (substitute tax) at a rate of 12.5%. The 12.5% final *imposta sostitutiva* will be applied by the Italian resident qualified financial intermediaries that will intervene, in any way, in the collection of interest, premium and other proceeds on the Notes or in the transfer of the Notes. Where interest, premium and other proceeds, on the Notes are not collected through the intervention of an Italian resident qualified financial intermediary and as such no *imposta sostitutiva* is applied, the Italian resident beneficial owners will be required to declare interest, premium and other proceeds, in their yearly income tax return and subject them to final substitute tax at a rate of 12.5%, unless option for a different regime is allowed and made.

The same regime upon described is also applicable to Italian resident beneficial owners who are partnerships, other than public and private entities, not carrying out commercial activities.

Payments of interest, premium and other proceeds in respect on the Notes, to Italian resident corporations or permanent establishments in the Republic of Italy of non resident corporations, will not be subject to the *imposta sostitutiva* at the rate of 12.5%. In fact, interest, premium and other proceeds on the Notes accrued to these subjects will be included in the taxable business income for corporate income tax purposes (and, in certain cases, depending on the *status* of the Notes holders, may also be included in their taxable net value of production for purposes of regional tax on productive activities – IRAP) of such beneficial owners, subject to tax in Italy in accordance with ordinary tax rules. A tax credit for withholding taxes applied outside Italy, if any, should be generally available.

Capital gains

If you are not a resident of Italy for income tax purposes, gains realized on the sale or other disposition of the Notes will not be subject to Italian tax, even if the Notes, listed on a regulated market, are held in Italy.

If capital gain, realised upon the sale for consideration or redemption of the Notes, derives by Noteholders who are Italian resident corporations, permanent establishments in Italy of foreign corporations to which the Notes are effectively connected or Italian resident individuals carrying out a commercial activity, would be treated as part of the taxable business income (and, in certain cases, may also be included in taxable net value of production for IRAP purpose), subject to tax in Italy according to the relevant tax provisions.

Any capital gain realised by Italian resident individuals holding the Notes not in connection with entrepreneurial activity, upon sale for consideration or redemption of the Notes would be subject to an *imposta sostitutiva* at the current rate of 12.5%.

Inheritance and gift taxes

According to the Bill of Law No. 262 of 2006 and the successive Law no. 286 of 2006, Italian inheritance and gift tax, previously abolished by Law 383 of 18 October 2001, has been restored. For any issue not explicitly regulated by the above mentioned Law and Bill of Law, the regulation to refer to is the Legislative Decree no. 346 of 1990.

The inheritance and gift taxes will apply to all inheritances and gifts successive to October 3rd, 2006. All inheritances and gifts occurred between October 25th 2001 and October 2nd 2006 are not taxable according to Law 383 of 18 October 2001.

Any transfer of goods due to "mortis causa" will be taxable, for either donees or legatees and devisees, each one of them separately. The tax rate to be applied varies as follows:

- 4% on the net amount transferred to spouses or direct descendants or ancestors, exceeding 1 million Euro per each beneficiary.
- 6% on the net amount transferred to brothers and sisters, exceeding 100,000 Euro each.
- 6% on the net amount transferred to other relatives up to the 4th degree, to the in-laws in straight line and collateral line up to the 3rd degree.
- 8% for all other beneficiaries.

All payees, regardless of the parental bound to the "de cuius", suffering from severe handicaps (as per Law no. 104 of February 5th 1992) can enjoy a 1,500,000 Euro franchise on the net amount received.

The taxable amount is to be computed as the net between the value of the goods transferred and:

- any debt subscribed by the deceased, the medical expenses sustained in the last 6 months as well as the funeral expenses;
- any legacy or burden on the inheritance.

Everything subjected to the transfer, including credits, shares of investment funds and money, constitute the taxable amount. According to Legislative decree no. 346 of 1990 are subject to taxation:

- money, furniture and jewels, to the extent of 10% of the overall taxable amount;
- all kind of securities whose income was part of the taxable income as per the last income tax return presented by the deceased;
- all movables and all kind of bearer securities owned by the departed or held by third parties under his name;
- investments in any kind of companies.

According to articles 14-19 of the Legislative Decree no. 346 of 1990, the value of the stocks or other securities traded on the stock exchange market (the Notes) is the average of the last 3 months before the inheritance opening, increased by all the accrued interests afterwards.

The value of the stocks or other securities not traded is the share of the shareholder's equity as per the last approved financial statements, including any successive event (net of goodwill) that may have modified it.

The value of shares in investment funds is to be deducted from the related statements.

The value of the bonds or securities not falling under the categories above is to be determined by benchmarking comparable securities which are traded on the market or by estimating their fair value under determined indicators.

Other taxes

No Italian transfer, stamp turnover or other similar taxes will be payable upon the issue, purchase or sale of the Botes.

Changes in The European Union "Savings Directive"

On June 3, 2003, the Council of the European Union adopted a directive regarding the taxation of savings income (the "Directive"). The Italian government adopted the above Directive through the approval of the Legislative Decree n. 84 del 2005 and, as a consequence, companies resident in Italy are required as from July 1, 2005 to provide to the tax authorities of another Member State details of payments of interest within the meaning of the Directive (including interest, premiums, discounts or other debt income) made by a paying agent within the jurisdiction to an individual resident in that other Member State (the "Disclosure of Information Method"). The term "paying agent" is defined in the Directive as any economic operator who pays, or secures the payment of interest for the immediate benefit of individuals, who are the beneficial owners of the interest. However, throughout the transitional period, paying agents established in certain Member States (the Grand Duchy of Luxembourg, Belgium and Austria) will withhold an amount on interest payments instead of using the Disclosure of Information Method used by other Member States. The rate of such withholding tax would equal 15% for the first three years after the date of implementation of the Directive, this rate being increased to 20% (three years after the date of implementation of the Directive) and 35% (six years after the date of implementation of the Directive). Such transitional period will end if and when the European Union enters into agreements on exchange of information upon request with several jurisdictions (Switzerland, Liechtenstein, San Marino, Monaco and Andorra) and when the Council of the European Union agrees that the United States is committed to use the Disclosure of Information Method.

DOCUMENTS ON DISPLAY

You may inspected the documents concerning us referred to this Annual Report at Sàfilo S.p.A. headquarters at Settima Strada, 15 – Padua – Italy.

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the ordinary course of our business, we are exposed to a variety of market risks arising from fluctuations in interest rates, commodity prices and exchange rates. We monitor and manage these risks as an integral part of our overall risk management program, which recognizes the unpredictability of financial markets and seeks to reduce their potentially adverse effects on our results.

We operate a central treasury function that controls all significant decisions and commitments regarding cash management, arrangement of borrowing facilities, banking relationships and foreign currency commitments. Our treasury operations are conducted within the framework that has been authorized by our Board of Directors. Weekly reports from subsidiaries have been established to ensure that treasury related activities are appropriately managed.

To reduce our currency translation and interest rate risks, we selectively use a number of financial instruments.

Interest Rate Risk Management

Our income and operating cash flows are substantially independent of changes in market interest rates. Our cash flow interest rate risk arises from long-term borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. We manage our cash flow interest rate risk by using floating-to-fixed interest rate swaps. Such swaps have the economic effect of converting borrowings from floating rates to fixed rates. We raise long-term borrowings at floating rates and then swap part of them with fixed rates instruments. Under the interest rate swaps, we agree with other parties to exchange, at specified intervals (mainly quarterly), the difference between fixed contract rates and floating market rates interest amounts calculated with reference to the agreed notional principal amounts.

As of December 31, 2006, we were hedged by 5 years' average swap maturity on approximately 75% of our exposure in euro and by 3 months' average swap maturity on approximately 45% of our exposure in U.S. dollars.

Foreign Exchange Risk Management

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the U.S. Dollar. Some Group companies use derivative instruments, under the control of the Group's finance department, to manage their foreign exchange risk arising from future commercial transactions. Nevertheless, unfavorable fluctuations in currency exchange rates could adversely affect our results of operations.

With respect to the U.S. Dollar, Sàfilo S.p.A. manages cash inflows related to the portion of our net sales derived from operations outside of Europe, primarily in North America and Asia, and cash outflows related to the purchases from third-party suppliers, and to the payment of interest and principal installments of the U.S. Dollar denominated tranches of the Senior Credit Agreement. The net exposure resulting after offsetting such streams of cash flows is regularly assessed and hedged to safeguard our activities on a continuous basis, by using appropriate hedging instruments for periods consistent with our foreign exchange exposure. We do not enter hedging arrangements for trading or speculative purposes.

In our financial statements prepared according to IFRS, these derivative instruments are valuated at their fair value.

Commodity Price Risk Management

Due to the limited quantities purchased, we believe that we do not face significant risks in procuring raw materials or risks associated with price variations of such raw materials. The management of commodity risk is carried out by monitoring both market supply and prices and by our procurement policies. In case of increased price volatility, and consequently, an increase in our financial exposure to such procurement risks, we are confident that we will be able to implement appropriate policies, including the use of derivative instruments to manage such risks.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

ITEM 14. MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

None.

ITEM 15. CONTROLS AND PROCEDURES

Not applicable.

ITEM 16. [Reserved]

PART III

ITEM 17. FINANCIAL STATEMENTS

Not applicable.

ITEM 18. FINANCIAL STATEMENTS

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ITEM 19. EXHIBITS

Not applicable.

AUDITOR REPORT IN ACCORDANCE WITH ARTICLE 156 AND WITH ARTICLE 165 OF LAW DECREE N° 58 DATED 24 FEBRUARY 1998

To the Shareholder of
Safilo - Società Azionaria Fabbrica Italiana Lavorazione Occhiali S.p.A.

1 We have audited the consolidated financial statements, which comprise the balance sheet, statement of operations, statement of recognized income and expense, cash flow statement and the related notes of Safilo - Società Azionaria Fabbrica Italiana Lavorazione Occhiali S.p.A. and its subsidiaries ("Safilo Group") as of 31 December 2006. These consolidated financial statements are the responsibility of Safilo - Società Azionaria Fabbrica Italiana Lavorazione Occhiali S.p.A.'s directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

2 We conducted our audit in accordance with the auditing standards and criteria recommended by CONSOB. In accordance with those standards and criteria, the audit has been planned and performed to obtain the necessary assurance about whether the consolidated financial statements are free of material misstatement and, taken as a whole, are reliable. An audit includes examining, on a sample basis, evidence supporting the amounts and disclosures in the financial statements, as well as assessing the appropriateness of the accounting principles used and the reasonableness of the estimates made by the Directors. We believe that our audit provides a reasonable basis for our opinion.

The consolidated financial statements present for comparative purposes the corresponding data for the prior year. For the opinion on the prior year's consolidated financial statements, reference should be made to our report dated 12 April 2006.

3 In our opinion, the consolidated financial statements of Safilo - Società Azionaria Fabbrica Italiana Lavorazione Occhiali S.p.A. as of 31 December 2006 comply with the International Financial Reporting Standards as adopted by the European Union, and with the resolutions issued in conformity with the article 9 of the Legislative Decree n. 38/2005; accordingly, they give a true and fair view of the financial position, the results of operations, the statement of recognized income and expense and the cash flows of Safilo Group for the year then ended.

Padova, 6 April 2007

(This report has been translated from the original which was issued in accordance with Italian legislation. References in this report to the Financial Statements refer to the Financial Statements in original Italian and not to their translation)

PricewaterhouseCoopers SpA
signed by

Antonio Taverna
(Partner)

Consolidated Financial Statements as of and for the years ended December 31, 2006 and December 31, 2005

Consolidated Balance Sheet

(Euro/000)	*Note*	31/12/2006	31/12/2005
ASSETS			
Current assets			
Cash in hand and at banks	*4.1*	35,643	151,018
Trade receivables, net	*4.2*	319,517	307,558
Inventory, net	*4.3*	271,573	208,802
Assets held for sale	*4.4*	-	2,984
Derivative financial instruments [1]	*4.5*	1,597	-
Other current assets [1]	*4.6*	57,027	44,433
Total current assets		**685,357**	**714,795**
Non-current assets			
Property, plant and equipment, net	*4.7*	201,951	193,603
Intangible assets	*4.8*	22,274	25,580
Goodwill	*4.9*	382,759	365,121
Investments in associates	*4.10*	12,535	13,492
Financial assets available-for-sale	*4.11*	3,472	6,009
Deferred tax assets	*4.12*	51,172	49,279
Derivative financial instruments [1]	*4.5*	1,921	2,506
Other non-current assets [1]	*4.13*	21,731	21,603
Total non-current assets		**697,815**	**677,193**
Total assets		**1,383,172**	**1,391,988**

[1] *The amounts relating to financial derivative instruments are exposed in a dedicated line item. The financial statements as at December 31, 2005 presented for comparison purposes has been reclassified accordingly. The financial derivative instruments in the financial statements as at December 31, 2005 were included among the "other current assets" and "other non-current assets".*

(Euro/000)	Note	31/12/2006	31/12/2005
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities			
Short-term borrowings	4.14	99,677	184,006
Trade payables	4.15	228,346	182,633
Tax payables	4.16	20,676	20,870
Derivative financial instruments [2]	4.5	-	878
Other current liabilities [2]	4.17	89,788	79,423
Provision for risks and charges	4.18	828	128
Total current liabilities		**439,315**	**467,938**
Non-current liabilities			
Long-term borrowings	4.14	475,583	468,242
Employee benefits liability	4.19	40,880	39,365
Provision for risks and charges	4.18	10,478	8,644
Deferred tax liabilities	4.12	13,082	10,969
Derivative financial instruments [2]	4.5	1,336	4,509
Other non-current liabilities [2]	4.20	5,172	6,565
Total non-current liabilities		**546,531**	**538,294**
Total liabilities		**985,846**	**1,006,232**
Shareholders' equity			
Share capital	4.21	35,000	35,000
Share premium reserve	4.22	53,350	53,350
Retained earnings and other reserves	4.23	264,086	285,326
Fair value and cash flow reserves	4.24	1,859	(3,899)
Income attributable to the Group		37,642	10,442
Total shareholders' equity attributable to the Group		**391,937**	**380,219**
Shareholders' equity attributable to minority shareholders		**5,389**	**5,537**
Total shareholders' equity		**397,326**	**385,756**
Total liabilities and shareholders' equity		**1,383,172**	**1,391,988**

[2] The amounts relating to financial derivative instruments are exposed in a dedicated line item. The financial statements as at December 31, 2005 presented for comparison purposes has been reclassified accordingly. The financial derivative instruments in the financial statements as at December 31, 2005 were included among the "other current liabilities" and "other non-current liabilities".

Consolidated Statement of Operations

(Euro/000)	*Note*	2006	2005	2004
Net sales	*5.1*	1,121,983	1,025,274	944,740
Cost of sales	*5.2*	(458,513)	(416,505)	(381,529)
Gross profit		**663,470**	**608,769**	**563,211**
Selling and marketing expenses	*5.3*	(415,258)	(379,419)	(344,067)
General and administrative expenses	*5.4*	(117,799)	(102,122)	(106,879)
Other op. income/(expenses), net	*5.5*	1,384	1,054	(866)
Non recurring operating costs	*5.6*	(6,000)	-	-
Operating income		**125,797**	**128,282**	**111,399**
Share of income/(loss) of associates	*5.7*	1,513	1,532	(42)
Interest expense and other financial charges, net	*5.8*	(47,241)	(85,272)	(66,150)
Non recurring financial charges	*5.9*	(8,959)	(19,507)	-
Income before taxation		**71,110**	**25,035**	**45,207**
Income taxes	*5.10*	(30,122)	(11,373)	(20,474)
Net income		**40,988**	**13,662**	**24,733**
Net income attributable to minority interests		3,346	3,220	3,123
Net income attributable to the Group		**37,642**	**10,442**	**21,610**

Consolidated statement of recognised income and expense

(Euro/000)	***Note***	**2006**	**2005**	**2004**
Profit (loss) attributable to the cash flow reserve	*4.24*	2,533	(2,780)	(3,637)
Profit (loss) attributable to the fair value reserve	*4.24*	1,016	(452)	(398)
Actuarial gains/(losses)	*4.23*	2,014	(3,207)	-
Profit (loss) attributable to the conversion fund	*4.23*	(17,577)	10,153	4,843
Profit (loss) attributable to shareholders' equity	*4.23*	(551)	701	-
Total		**(12,565)**	**4,415**	**808**
Net income for the year		40,988	13,662	24,733
Total recognized income for the year		**28,423**	**18,077**	**25,541**
Attributable to:				
Group		25,509	14,650	22,313
Minority shareholders		2,914	3,427	3,228
Total recognized income for the year		**28,423**	**18,077**	**25,541**

Consolidated statement of cash flows

(Euro/000)	2006	2005 (*)	2004(*)
A - Opening net cash and cash equivalents (net financial indebtedness - short term)	**25,866**	**18,151**	**23,234**
Cash flows from (for) operating activities			
Net income (including minority interests)	40,988	13,662	24,733
Stock option	527	1,714	658
Depreciation and Amortization	36,839	35,197	35,504
Share (income) / loss on equity investments	(1,491)	(726)	770
Net movements in the employee benefits liability	4,608	1,546	6,079
Net movements in other provisions	2,443	2,232	(4,474)
Interest expenses	49,654	84,597	64,309
Income tax expense	30,122	11,373	20,474
Income from operating activities prior to movements in working capital	**163,690**	**149,595**	**148,053**
Changes in operating Assets and Liabilities			
(Increase) Decrease in trade receivables and other current receivables	(38,220)	(39,672)	1,290
(Increase) Decrease in inventory, net	(68,548)	(2,314)	(37,153)
Increase (Decrease) in trade payables and other current payables	30,300	25,562	25,922
Interest expenses paid	(35,900)	(71,085)	(59,947)
Income taxes paid	(30,559)	(33,675)	(27,837)
Total (B)	**20,763**	**28,411**	**50,328**
C - Cash Flows from (for) investing activities			
Purchase of property, plant and equipment (net of disposals)	(35,137)	(27,737)	(26,643)
Acquisition of subsidiaries (net of cash acquired)	(2,321)	-	-
Disposal of investments in associates and financial assets	3,553	-	514
Purchase of intangible assets	(2,969)	(9,602)	(2,491)
Total (C)	**(36,874)**	**(37,339)**	**(28,620)**
D - Cash Flows from (for) financing activities			
Proceeds from borrowings	320,390	24,967	4,863
Repayment of borrowings	(330,961)	(190,382)	(48,770)
Bank deposit for High Yield repayment	-	(105,000)	-
Net increase in share capital	-	294,713	25,000
Dividends paid	(3,063)	(3,025)	(3,149)
Total (D)	**(13,634)**	**21,273**	**(22,056)**
E - Cash flow for the year (B+C+D)	**(29,745)**	**12,345**	**(348)**
Translation exchange differences	3,078	(4,630)	(4,735)
G - Closing net cash and cash equivalents (net financial indebtedness - short term)	**(801)**	**25,866**	**18,151**

(*) Some items relating to financial years 2004 and 2005 have been reclassified according to 2006 cash flow structure.

Statement of changes in Shareholders' Equity

(Euro/000)	Share capital	Share premium	Shareholders' stock account payment	Treasury shares	Translation difference	Fair value and cash flow reserve	Change in consolidation scope	Retained earnings	Net profit	Total equity
Group Shareholders' equity at January 1, 2004	**34,350**	**29,000**	**4,810**	**(80,988)**	**-**	**(826)**	**-**	**40,547**	**-**	**26,893**
Changes in other reserves	650	24,350	-	-	(4,738)	(5,516)	-	237	-	14,983
2004 net profit	-	-	-	-	-	-	-	-	21,610	21,610
Group Shareholders' equity at December 31, 2004	**35,000**	**53,350**	**4,810**	**(80,988)**	**(4,738)**	**(6,342)**	**-**	**40,784**	**21,610**	**63,486**
Minority interests at January 1, 2004	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**5,876**	**-**	**5,876**
Retained earnings	-	-	-	-	(105)	-	-	(672)	-	(777)
Dividends distribution	-	-	-	-	-	-	-	(3,149)	-	(3,149)
2004 net profit	-	-	-	-	-	-	-	-	3,123	3,123
Minority interests at December 31, 2004	**-**	**-**	**-**	**-**	**(105)**	**-**	**-**	**2,055**	**3,123**	**5,073**
Consolidated net equity at Dec. 31, 2004	**35,000**	**53,350**	**4,810**	**(80,988)**	**(4,843)**	**(6,342)**	**-**	**42,839**	**24,733**	**68,559**

(Euro/000)	Share capital	Share premium	Shareholders' stock account payment	Treasury shares	Translation difference	Fair value and cash flow reserve	Change in consolidation scope	Retained earnings	Net profit	Total equity
Group Shareholders' equity at January 1, 2005	**35,000**	**53,350**	**4,810**	**(80,988)**	**(4,738)**	**(6,342)**	**-**	**40,784**	**21,610**	**63,486**
Previous year's profit allocation	-	-	-	-	-	-	-	21,610	(21,610)	-
Share capital increase	-	-	294,713	-	-	-	-	-	-	294,713
Changes in other reserves	-	-	-	-	9,946	2,443	-	(811)	-	11,578
2005 net profit	-	-	-	-	-	-	-	-	10,442	10,442
Group Shareholders' equity at December 31, 2005	**35,000**	**53,350**	**299,523**	**(80,988)**	**5,208**	**(3,899)**	**-**	**61,583**	**10,442**	**380,219**
Minority interests at January 1, 2005	**-**	**-**	**-**	**-**	**(105)**	**-**	**-**	**2,055**	**3,123**	**5,073**
Previous year's profit allocation	-	-	-	-	-	-	-	3,123	(3,123)	-
Retained earnings	-	-	-	-	207	-	-	62	-	269
Dividends distribution	-	-	-	-	-	-	-	(3,025)	-	(3,025)
2005 net profit	-	-	-	-	-	-	-	-	3,220	3,220
Minority interests at December 31, 2005	**-**	**-**	**-**	**-**	**102**	**-**	**-**	**2,215**	**3,220**	**5,537**
Consolidated net equity at Dec. 31, 2005	**35,000**	**53,350**	**299,523**	**(80,988)**	**5,310**	**(3,899)**	**-**	**63,798**	**13,662**	**385,756**

(Euro/000)	Share capital	Share premium	Shareholders' stock account payment	Treasury shares	Translation difference	Fair value and cash flow reserve	Change in consolidation scope	Retained earnings	Net profit	Total equity
Group Shareholders' equity at January 1, 2006	**35,000**	**53,350**	**299,523**	**(80,988)**	**5,208**	**(3,899)**	**-**	**61,583**	**10,442**	**380,219**
Previous year's profit allocation	-	-	-	-	-	-	-	10,442	(10,442)	-
Share capital increase	-	-	-	-	-	-	-	-	-	-
Changes in other reserves	-	-	-	-	(17,473)	5,758	294	(14,503)	-	(25,924)
2006 net profit	-	-	-	-	-	-	-	-	37,642	37,642
Group Shareholders' equity at December 31, 2006	**35,000**	**53,350**	**299,523**	**(80,988)**	**(12,265)**	**1,859**	**294**	**57,522**	**37,642**	**391,937**
Minority interests at January 1, 2006	**-**	**-**	**-**	**-**	**102**	**-**	**-**	**2,215**	**3,220**	**5,537**
Previous year's profit allocation	-	-	-	-	-	-	-	3,220	(3,220)	-
Retained earnings	-	-	-	-	(104)	-	(294)	(33)	-	(431)
Dividends distribution	-	-	-	-	-	-	-	(3,063)	-	(3,063)
2006 net profit	-	-	-	-	-	-	-	-	3,346	3,346
Minority interests at December 31, 2006	**-**	**-**	**-**	**-**	**(2)**	**-**	**(294)**	**2,339**	**3,346**	**5,389**
Consolidated net equity at Dec. 31, 2006	**35,000**	**53,350**	**299,523**	**(80,988)**	**(12,267)**	**1,859**	**-**	**59,861**	**40,988**	**397,326**

1. General information

1.1 General information

Safilo S.p.A., holding company, is a joint stock company established in Italy and registered with the Belluno Companies' Register. The company's head office is in Pieve di Cadore (BL) – Piazza Tiziano no. 8 and has a secondary branch in Padua – Zona Industriale VII Strada no. 15.

These consolidated financial statements are presented in thousands of Euro, covering the financial period from January 1, 2006 to December 31, 2006, with comparative figures for the period from January 1, 2005 to December 31, 2005 and January 1, 2004 to December 31, 2004, only for the Consolidated Statement of Operations.

These financial statements were approved by the Board of Directors on March 23, 2007.

Companies included in the consolidation area are reported in paragraph 2.3 "Consolidation method and area".

2. Summary of significant accounting policies

2.1 General information

Accounting policies adopted for the preparation of these consolidated financial statements are those here below; they have been applied in a comparative manner for both financial years presented.

Consolidated financial information reported for financial years ended December 31, 2006 and December 31, 2005 was prepared in accordance with the IFRS issued by the International Accounting Standards Board (IASB) and approved by the European Commission as at December 31, 2006. The application of the accounting principles or interpretations issued by IFRIC to the financial statement at December 31, 2006 has not had any significant impact.

Some new IFRS principles, some amendments and IFRIC interpretations have already been issued by IASB and will be effective after the approval of these consolidated financial statements, even it they can be used in advance. In particular they refer to:

- The new *IFRS 7* accounting principle – *financial instruments: additional information* valid from January 1, 2007;

- The new *IFRS 8* accounting principle – *Operational sectors:* valid from January 1, 2009;

- Complementary amendment to *IAS 1 – Presentation of financial statements: additional information about share capital;*

The Group has decided not to apply the new accounting principles and IAS 1 amendment in advance and is currently assessing the impact that these changes could have.

The remaining accounting principles, amendments and interpretations that are applicable after the date of the financial statement are either not applicable or will not have a significant impact.

The consolidated financial statements are presented in Euro. The Euro is the functional currency as it is the currency in which the Group principally operates.

The consolidated financial statement was prepared in accordance with the cost criteria, except for the available for sale financial assets and some financial assets and liabilities including derivative instruments.

The preparation of the consolidated financial statements in accordance with IFRS accounting principles, requires the management to make estimates and assumptions that impact on the amounts reported in the schedules in the financial statements and the relative notes. Actual results could differ from those estimates. The financial statements areas most impacted by the above estimates and assumptions are reported in section 2.21 “Use of estimates”.

2.2 Format of financial statements

The Safilo Group presents the income statement by function (so-called “cost of sales”), which is considered the most representative with respect to presentation by expense, as it greater conforms to the internal reporting methods and business management and is in line with international practice in the eyewear field.

For the balance sheet, a distinction is made in the assets and liabilities between current and non-current, as described in paragraph 51 and following of IAS no. 1. For the statement of cash flows, the indirect method has been used.

2.3 Consolidation method and area

The direct and indirect holdings, included in the consolidation area under the line-by-line method, in addition to the parent company Safilo S.p.A., are the following:

	Currency	Share capital	Share held %
ITALIAN COMPANIES			
Oxsol S.p.A. - Pieve di Cadore (BL)	EURO	121,000	100.0
Lenti S.r.l. – Bergamo	EURO	500,000	75.6
Smith Sport Optics S.r.l. (in liquidation) – Padua	EURO	102,775	100.0
FOREIGN COMPANIES			
Safilo International B.V. - Rotterdam (NL)	EURO	24,165,700	100.0
Safint B.V. - Rotterdam (NL)	EURO	18,200	100.0
Safilo Capital Int. S.A. – Luxembourg (L)	EURO	31,000	100.0
Luxury Trade S.A – Luxembourg (L)	EURO	1,650,000	100.0
Safilo Benelux S.A. - Zaventem (B)	EURO	560,000	100.0
Safilo Espana S.A. - Madrid (E)	EURO	390,650	100.0
Fashion Optic S.L. - Madrid (E)	EURO	1,126,845	100.0
Navoptik S.L. - Madrid (E)	EURO	664,118	100.0
Safilo France S.a.r.l. – Paris (F)	EURO	960,000	100.0
Safilo Gmbh – Cologne (D)	EURO	511,300	100.0
Safilo Nordic AB - Taby (S)	SEK	500,000	100.0
Safilo Far East Ltd. - Hong Kong (RC)	HKD	49,700,000	100.0
Safint Optical Investment Ltd - Hong Kong (RC)	HKD	10,000	51.0
Safilo Hong-Kong Ltd – Hong Kong (RC)	HKD	100,000	51.0
Safilo Singapore Pte Ltd - Singapore (SGP)	SGD	400,000	100.0
Safilo Optical Sdn Bhd – Kuala Lumpur (MAL)	MYR	100,000	100.0
Safilo Trading Co. Inc. - Shenzhen (RC)	CNY	2,481,000	51.0
Safilo Eyewear (Shenzhen) Company Limited	USD	700,000	51.0
Safilo Korea Ltd – Seoul (K)	KRW	300,000,000	100.0
Safilo Hellas Ottica S.a. – Athens (GR)	EURO	489,990	70.0
Safilo Nederland B.V. - Bilthoven (NL)	EURO	18,200	100.0
Safilo South Africa (Pty) Ltd. – Bryanston (ZA)	ZAR	3,383	100.0
Safilo Austria Gmbh -Traun (A)	EURO	217,582	100.0
Carrera Optyl Gmbh (in liquidation) – Traun (A)	EURO	7,630,648	100.0
Carrera Optyl D.o.o. - Ormoz (SLO)	SIT	135,101,000	100.0
Safilo Japan Co Ltd - Tokyo (J)	JPY	100.000.000	100.0
Safilo Do Brasil Ltda – San Paolo (BR)	BRL	8,077,500	100.0
Safilo Portugal Lda – Lisbon (P)	EURO	500,000	100.0
Safilo Switzerland AG – Liestal (CH)	CHF	1,000,000	77.0
Safilo India Ltd - Bombay (IND)	INR	42,000,000	88.5
Safint Australia Pty Ltd.- Sydney (AUS)	AUD	3,000,000	100.0
Safilo Australia Partnership – Sydney (AUS)	AUD	204,081	61.0
Safint Optical UK Ltd. – London (GB)	GBP	21,139,001	100.0
Safilo UK Ltd. - North Yorkshire (GB)	GBP	250	100.0
Safilo America Inc. - Delaware (USA)	USD	8,430	100.0
Safilo USA Inc. - New Jersey (USA)	USD	23,289	100.0
FTL Corp. - Delaware (USA)	USD	10	100.0
Safilo Realty Corp. - Delaware (USA)	USD	10,000	100.0
Safilo Services LLC - New Jersey (USA)	USD	-	100.0
Smith Sport Optics Inc. - Idaho (USA)	USD	12,162	100.0
Solstice Marketing Corp. – Delaware (USA)	USD	1,000	100.0
Solstice Marketing Concepts LLC – Delaware (USA)	USD	-	100.0
2844-2580 Quebec Inc. – Montreal (CAN)	CAD	100,000	100.0
Safilo Canada Inc. - Montreal (CAN)	CAD	2,470,425	100.0
Canam Sport Eyewear Inc. - Montreal (CAN)	CAD	300,011	100.0

Investments in subsidiaries

The companies in which the Group exercises control (subsidiary companies), either due to direct shareholdings or indirect holding of the majority of the voting rights, having the power to determine the financial and operating choices of the company and thus obtaining the relative benefits even regardless the relationships deriving from the share ownership, are consolidated using the line-by-line method. The existence of potential exercisable voting rights at the balance sheet date are considered in order to determine control. The subsidiary companies are consolidated from the date on which control is assumed and are deconsolidated from the date when control ceases.

The business combinations, in which the control of a company/entity is acquired, are recorded applying the purchase method, where the assets and liabilities acquired are initially measured at their current value at the acquisition date. The difference between the purchase cost and the current value of the assets and liabilities acquired, if positive, is allocated to goodwill, if negative is recorded in the income statement. The acquisition cost is based on the fair value, at the purchase date, of assets sold, of liabilities incurred and of capital instruments issued, and any other accessory charges.

On consolidation, the amounts resulting from intra-group operations between consolidated companies are eliminated, in particular in relation to receivables and payables at the balance sheet date, costs and revenues as well as financial income and charges. Also excluded are the gains and losses realised between companies that are fully consolidated.

The accounting principles used by the subsidiaries have been amended where necessary to adjust them to those adopted by the parent company.

Investments in associates

The holdings in companies/entities in which a significant influence is exercised ("associated companies"), is presumed to exist when the percentage held is between 20% and 50%, and are valued under the equity method. Due to the application of the equity method, the value of the investment is aligned to the net equity adjusted, where necessary, to reflect the application of the IFRS approved by the European Commission, and includes the recording of any goodwill identified at the moment of acquisition. The share of gains/losses realised by the associated companies after the acquisition is recorded in the income statement, while the quota of movements of the reserves after the acquisition is recorded in the equity reserves. When the share of losses of the Group in an associated company is equal to or exceeds its holding in the associated company, taking into account all receivables not guaranteed, the value of the investment is fully written down and the Group does not record further losses above its share, except where the Group has the obligation to cover these losses. The gains and losses not realised generated on operations with associated companies are eliminated for the part pertaining to the Group.

2.4 Segment information

The segment information is provided with reference to the geographic areas in which the Group operates. The geographic areas were identified as the primary segments of activity. The criteria applied for the identification of the primary segments of activity were inspired, among others, by the manner in which management directs the Group and attributes managerial responsibility. In particular, this criteria is based on the regrouping by geographical area of the headquarters of the companies belonging to the Group; therefore, the sales identified in accordance with this segmentation are determined by origin of invoicing and not by target market.

Finally, it is noted that at the date of the present report no secondary segments were identified. In particular, the secondary segments could be related, also in consideration of market practices, to the "distribution" system. In the circumstances, however, the distribution of the products is almost exclusively wholesale; in fact the distribution activity through points of sales directly controlled by the Group (retail sales) is marginal.

2.5 Translation of financial statements in currencies other than Euro

The rules for the translation of financial statements of companies in currencies other than the functional currency of the Euro are the following:

- The assets and liabilities were translated using the exchange rate at the balance sheet date;
- The costs, revenues, income and charges were translated using the average exchange rate for the year;
- The "conversion reserve" includes foreign exchange differences generated from the translation of the opening shareholders' equity and the movements during the year at a rate different that that at the balance sheet date;
- The goodwill and fair value adjustments related to the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the exchange rate at the balance sheet date.

The exchange rates applied in the conversion of financial statements of companies prepared in currency other than Euro at December 31, 2006 and December 31, 2005 were as follows:

	Year end December 31, 2006	Year end December 31, 2005	Average 2006	Average 2005	Average 2004
USD	1.3170	1.1797	1.2554	1.2441	1.2439
HKD	10.2409	9.1474	9.7544	9.6768	9.6881
CHF	1.6069	1.5551	1.5729	1.5483	1.5438
CAD	1.5281	1.3725	1.4237	1.5079	1.6167
JPY	156.9300	138.9000	146.0153	136.8492	134.4446
GBP	0.6715	0.6853	0.6817	0.6836	0.6787
SEK	9.0404	9.3885	9.2549	9.2822	9.1244
AUD	1.6691	1.6109	1.6668	1.6327	1.6905
ZAR	9.2124	7.4642	8.5402	7.9191	8.0092
SIT	239.6400	239.5000	239.5961	239.5681	239.0874
BRL	2.8133	2.7432	2.7331	3.0346	3.6329
IND	58.2975	53.1679	56.9098	54.8365	56.3422
SGD	2.0202	1.9628	1.9938	2.0702	2.1016
MYR	4.6490	4.4584	4.6040	4.7567	4.7262
CNY	10.2793	9.5204	10.0096	10.1983	10.2975
KRW	1,224.8100	1,195.1831	1,214.6900	1,273.4000	1,422.5546

Foreign currency transactions are converted into the functional currency using the exchange rate at the transaction date. The foreign exchange gains and losses resulting fro the settlement of transactions and from the translation at the balance sheet date of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

2.6 Property, plant and equipment

Tangible fixed assets are measured at purchase or production cost, net of accumulated depreciation and of possible loss in value. The cost includes all charges directly incurred in bringing assets to their current location and condition. Costs incurred after the purchase are recorded only if they increase the future economic benefits of the asset they refer to. Interest charges relating to the construction of tangible fixed assets are charged directly to the income statement.

The charges incurred for the maintenance and repairs of an ordinary and/or cyclical nature are directly charged to the income statement in the year in which they are incurred. The capitalisation of costs relating to the expansion, modernisation or improvement of owned tangible fixed assets or of those held in leasing, is made only when they satisfy the requirements to be separately classified as an asset or part of an asset. The booking value is adjusted for depreciation on a systematic basis, over its useful life.

When circumstances indicate that there may be a permanent impairment in value, an estimate is made of the recoverable amount of the asset, recording any loss in the income statement. When the reasons for the write-down no longer exist, the book value of the asset is restated through the income statement, up to the value at which the asset would be recorded if no write-down had taken place and depreciation had been recorded.

The assets held through finance lease contracts, where the majority of the risks and benefits related to the ownership of an asset have been transferred to the Group, are recognised as assets of the Group at their fair value or, if lower, at the current value of the minimum lease payments. The corresponding liability due to the lessor is recorded in the financial statements under financial payables. The assets are depreciated applying the criteria and rates indicated below.

The leased assets where the lessor bears the majority of the risks and benefits related to an asset are recorded as operating leases. The costs relating to operating leases are recorded on a straight-line basis in the income statement over the duration of the lease contract.

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset, in accordance with the following depreciation rates:

Buildings	20 – 33 years
Plant, machinery and equipment	5 – 15 years
Furniture, EDP and vehicles	4 – 8 years

Land is not depreciated.

When the asset to be depreciated is composed of separately identifiable elements whose useful life differ significantly from the other parts of the asset, the depreciation is made separately for each part of the asset, with the application of the “component approach” principle.

The remaining value of the tangible fixed assets and their useful life are reviewed at the end of each financial year. The capital gains or losses from the sale of the assets are posted to the income statement.

2.7 Intangible fixed assets

An intangible asset is an identifiable non-monetary asset without any physical substance, and capable of generating future economic benefits. These elements are recorded at purchase and/or production cost, including the costs of bringing the asset to its current use, net of accumulated amortisation and any loss in value. The amortisation begins when the asset is available for use and is recorded on a systematic basis over its useful life.

When circumstances indicate that there may be a permanent impairment in value, an estimate is made of the recoverable amount of the asset, recording any loss in the income statement. When the reasons for write-down no longer exist, the book value of the asset is restated through the income statement, up to the value at which the asset would be recorded if no write-down had taken place and amortisation had been recorded.

Goodwill

Goodwill represents the excess of the purchase cost compared to the fair value of the share of equity in the subsidiary or associated company at the purchase date, or of the business unit acquired. The goodwill deriving from the purchase of subsidiaries is recorded under intangible assets, while that deriving from the purchase of associated companies is included in the investments in associated companies. Goodwill is not amortised, but is subject to an impairment test on an annual basis to ascertain if there is any loss in value.

Trademarks and licences

Trademarks and licences are recorded at cost. They have a finite useful life and are recorded at cost net of accumulated amortisation. The amortisation is calculated on a straight-line basis allocating the cost of trademarks and licences over the duration of the relative contracts and the relative useful life of the trademarks owned by the Group.

Software

The licences purchased and relating to software are capitalised on the basis of the costs incurred for their acquisition and in bringing them to their current condition. The amortisation is calculated on a straight-line basis over their estimated useful life (from 3 to 5 years).

The costs associated with the development and maintenance of software programs are posted to the income statement when incurred. The costs which are directly associated with the production of unique and identifiable software products controlled by the Group and which generate future economic benefits beyond one year are recorded as intangible fixed assets if the following conditions are respected: the costs can be reliably calculated; the Group has the technical and financial resources to complete these products and intends completing the same; the technical feasibility of the product is guaranteed and the use of the products will generate probable future economic benefits beyond one year.

The direct costs include the costs relating to employees developing the software as well as any appropriate share of general costs.

2.8 Assets held for sale

These include non-current assets (or groups of assets held for sale) whose book value is recoverable mainly through sale rather than continued use. The assets available for sale are measured at the lower between their purchase cost, net of accumulated depreciation, and the current value less costs to sell.

2.9 Impairment of non financial assets

Assets with an indefinite useful life are not subject to amortisation but undergo an impairment test at least on an annual basis to control where their book value has been reduced.

Assets subject to amortisation undergo impairment tests when events or circumstances arise that indicate that the book value cannot be recovered. In both cases the loss in value is posted for the book value that exceeds the recoverable value. This value is given by the greater between the fair value of the asset net of the costs for sale and its value for use. If the value for use of an asset cannot be established individually, the recoverable value must be established of the unit that generates cash flow (so-called "*cash generating units*" or CGU) that the asset is part of. The assets are regrouped at the lowest level that there are independent cash flows for and the Group will then calculate the current value of the estimated future cash flows for the CGU, gross of taxes, applying a before tax discount rate, that reflects the current market evaluations of the long term value of the cash and specific risks with the asset.

When a loss on an asset, other than goodwill, no longer exists or is reduced, the book value of the asset or cash-generating unit is increased to the new estimated recoverable value, which cannot exceed the value that would have been established if there had been no loss due to reduction in value.

A reversal of loss in value is recorded in the income statement as provided by the value calculation model of IAS no. 16.

2.10 Financial instruments

The classification of the financial instrument is dependent on the purpose for which the financial instrument was acquired. Management determines the classification of its financial instruments on the initial recognition in the financial statements. The purchases and sales of financial instruments are recognised at the transaction date or at the date when the Group commits to purchase or sell the asset. All financial instruments are initially recognised at fair value.

Financial assets

The financial assets are classified into the following categories:

- Financial assets measured at fair value with changes recognised in the income statement: this category includes the financial assets acquired principally for sale in the short-term or those designated as such by management, in addition to derivative instruments unless they are not designated as hedges (in relation to the treatment of derivatives, reference should be made to the following paragraph). The fair value of these instruments is determined with reference to the market value (offer price) at the balance sheet date; in case of non-quoted instruments they are determined through technical financial valuation methods commonly used. The fair value changes of the instruments belonging to this category are recognised in the income statement. The financial instruments in this category are classified as short-term if they are "held for trading" or if it is expected that they will be sold within 12 months from the balance sheet date. The only assets of this category held by the Group and recorded in the financial statement are the derivative financial instruments.

- Loans and receivables: they are non-derivative financial instruments, with fixed or determinable payments, not quoted in an active market. They are stated as current assets except for amounts due beyond 12 months from the balance sheet date. These latter are classified under non-current assets. These assets are measured at amortised cost on the basis of the effective interest rate. Any loss in value determined through an impairment test is recognised in the income statement. In particular, trade receivables are initially recognised in the financial statements at their current value and subsequently recorded under the amortised cost method less any write-downs for loss in value. An allowance for doubtful accounts is made when there is evidence that the Group will not be capable of receiving the original amount due. The provisions made are recorded in the income statement.

- Investments held to maturity: they are non-derivative financial instruments with fixed or determinable payments, with a fixed maturity date, that the Group has the full intention and capacity to maintain until maturity. The receivables and investments held to maturity are measured under the amortised cost method using the effective interest rate net of any write-downs for loss in value. The Group did not hold this type of investment in the period reported on.

- Financial assets available for sale: they are non-derivative financial instruments that are explicitly designated in this category or are not classified in any of the previous categories. They are measured at fair value, determined with reference to market prices at the balance sheet date or through financial measurement techniques or models, recording the changes in value in an equity reserve. This reserve is recognised in the income statement only when the financial asset is sold, or, in the case of negative cumulative changes, when it is considered that the reduction in value already recorded under equity cannot be recovered. The classification as a current or non-current asset depends on the intentions of management and of the real liquidity of the security; they are recorded under current assets when they are expected to be realised within 12 months.

The financial assets are removed from the balance sheet when the right to receive the cash flows from the instrument ceases and the Group has transferred all the risks and benefits relating to the instrument.

Loans

Loans are initially recognised at fair value less transaction costs. After initial recognition, they are measured at amortised cost; all differences between the amount financed (net of the transaction costs) and the nominal value are recognised in the income statement over the duration of the loan using the effective interest method. When there is a change in the expected cash flows and management is capable of estimating it reliably, the value of the loans is recalculated to reflect the expected change in the cash flows. The value of the loans is recalculated on the basis of the current value of the new expected cash flows and of the internal rate of return.

The loans are classified under current liabilities unless the company has an unconditional right to defer the payment for at least 12 months after the balance sheet date.

The loans are removed from the balance sheet when they expire and the Group has transferred all the risks and benefits relating to the instruments.

Derivative instruments

In accordance with IAS 39 as approved by the European Commission, the derivative financial instruments used by the Group with the intention of hedging in order to reduce the foreign currency and interest rate risk, can be recorded according to the "hedge accounting" methodology only when:

- At the beginning of the hedge, a formal designation and documentation relating to the hedge exists,
- It is presumed that the hedge is highly effective,
- The effectiveness can be reliably measured and the hedge is highly effective over the accounting periods for which it was designated.

All the derivative financial instruments are measured at fair value, as established in accordance with IAS 39. When the financial instruments have the characteristics to be recorded under hedge accounting, the following accounting treatment is applied:

- *Fair value hedge* – if a derivative financial instrument is designated as a hedge to the exposure of the changes in the current value of an asset or liability in the financial statements attributable to a specific risk, which can have effects on the income statement, the profit or loss after the initial valuation of the fair value of the hedge instrument is recognized in the income statement. The profit or loss on the hedged item, related to the hedged risk, changes the book value of that item and is recognized in the income statement. In the financial years dealt with in these financial statements there were no fair value hedges.

- *Cash flow hedge* – if a derivative financial instrument is designated as a hedge to the exposure of the changes in the cash flows of an asset or liability recorded in the financial statements or of an operation considered highly probable and which may have effects on the income statement, the effective portion of the profits or losses of the financial instrument is recognised in an equity reserve. The cumulative profits or losses are reversed from equity and recorded in the income statement in the same period as the operation that is hedged. The profits or losses associated to a hedge or to that part of the hedge which has become ineffective, are immediately recorded in the income statement. If a hedge instrument or a relation of a hedge is closed, but the hedged operation has not yet been realised, the cumulative profits and losses, up to that moment recorded in equity, are recognised in the income statement when the relative operation is realised. If the hedged operation is no longer considered probable, the profits or losses not yet realised recorded in equity are immediately recognised in the income statement.

If the *hedge accounting* can be applied, the profits or losses deriving from the fair value of the derivative financial instruments are immediately recognised in the income statement.

2.11 Inventory

Inventories are measured at the lower of purchase or production cost and the net realisable value. The cost of raw materials and purchased finished products is calculated using the weighed average cost method. The cost of semi-finished products and internally produced finished products includes raw material, direct labour costs and the indirect costs allocated based on normal production capacity.

The net realisable value is determined based on the estimated selling price in normal market conditions, net of direct sales costs.

Against the value of stock as determined above, provisions are made in order to take account of obsolete or slow moving stock.

2.12 Trade receivables

Trade receivables are classified in the financial statements at their current value and then recalculated using the amortised cost method net of any write-downs for loss in value. An allowance for doubtful accounts is made when there is evidence that the Group will not be capable of receiving the original amount due. The provisions made are recorded in the income statement.

The Group operates with transferring commercial credits to factoring companies. However as said credits, even when they are legally transferred, do not respect all the provisions of the IAS 39, paragraph 17 and following for removal from the balance sheet, they are kept in the financial statement posting a financial debt to the factoring company as a counterbalance. In particular, despite the fact the commercial credits are transferred to the factoring company, the benefits and risks are still maintained on them. The guarantee that is supplied to the concessionaire is represented by the excess clause in the contract whereby, up to preset amount, the factoring company does not recognise the insolvency that is claimed by the Group and, therefore, up to the said present amount, the risk of insolvency of the transferred debtor effectively lies with the Safilo Group.

2.13 Cash in hand and at banks

Cash and cash equivalents include cash, bank deposits on demand, other highly liquid short-term investments available at three months from purchase. The items included in the net cash and cash equivalents are measured at fair value and the relative changes are recorded in the income statement. Bank overdrafts are stated under current liabilities.

2.14 Employee benefits

Pension plans

The Group recognises different forms of defined benefit plans and contribution plans, in line with the local conditions and practices in the countries in which it carries out its activities.

The premiums paid for defined contribution plans are recorded in the income statement for the part matured in the year. The defined benefit plans are based on the working life of the employees and on the remuneration received by the employee during a predetermined period of employment.

The obligation of the company to finance the defined benefit plans and the annual cost recognised in the income statement are determined by independent consultants using the projected unit credit method. The related costs are recorded in the income statement on the basis of the estimated employment period of employees. The company does not suspend actuarial gains or losses further to applying the projected unit credit method, but records them in an equity reserve in the period in which they arise.

Remuneration plans under the form of share capital participation

The Group recognises additional benefits to some employees and consultants through "equity settled" type stock options. In accordance with IFRS 2 – Share-based payments, the current value of the stock options determined at the vesting date applying the "Black & Scholes" method is recognised in the income statement under personnel costs in constant quotas over the period between the vesting date of the stock options and the maturity date, and directly to an equity reserve.

The effects of the vesting conditions not related to the market are not taken into consideration in the fair value of the vested options, but are important in the valuation of the number of options which are expected to be exercised.

At the balance sheet date the Group reviews its estimates on the number of options which are expected to be exercised. The impact of the revision of the original estimates is recognised in the income statement over the maturity period and directly in equity reserves.

On the exercise of the stock option, the amounts received from the employee, net of the costs directly attributable to the transaction, are credited to share capital for an amount equal to the nominal value of the shares issued and to the share premium reserve for the remaining part.

2.15 Provisions for risks and charges

The Group records provisions for risks and charges when it has an obligation, legal or implicit, to third parties, and it is probable that it will be necessary to use resources of the Group to settle the obligation, and a reliable estimate of the amount can be made. The changes in estimates are recorded in the income statement of the period in which the changes occur.

2.16 Revenue recognition

The revenues include the fair value of the sale of goods and services, less VAT, returns and discounts. In particular, the Group recognises the revenues from the sale of goods sold at the shipment date, when all the risks and rewards relating to the ownership of the goods have been transferred to the client, or on delivery to the client, in accordance with the sales terms agreed. If the sale includes the right for the client to return unsold goods (generally these clauses are only applied in the United States), the revenue is recognised on the shipment to the client date, net of a provision which represents the best estimate of the products to be returned by the client and which the Group will no longer be able to place on the market. This provision is based on specific historical data and on the specific knowledge of the clients; historically there have not been significant differences between the estimates made and the products actually returned.

2.17 Public contributions

The Group recognises public contributions when there is reasonable certainty that they will be received and that the conditions required for the contribution have been or will be respected.

The contributions received are recorded in the income statement for the time required to relate them to the relative costs and they are considered as deferred income.

2.18 Royalties

The Group recognises royalty income and expenses in accordance with the accruals principle and in compliance with the substance of the contracts agreed.

2.19 Dividends

They are recorded when the right of the Shareholders to receive the payment arises, which normally occurs at the Shareholders' meeting for the distribution of dividends. The distribution of dividends is therefore recorded as a liability in the financial statements in the period in which the distribution is approved by the Shareholders' meeting.

2.20 Income taxes

Income taxes include all the taxes calculated on the assessable income of the companies of the Group. The income taxes are recorded in the income statement, except those relating to accounts directly credited or debited to equity, in which case the fiscal effect is recognised directly to equity.

The deferred taxes are calculated on fiscal losses that can be carried forward and all the timing differences between the assessable income of an asset or liability and the relative book value, with the exception of those differences deriving from investments in subsidiaries for which a cancellation is not expected in the foreseeable future. The deferred tax assets are recognised only for those amounts for which it is probable there will be future assessable income to recover the amounts.

The current deferred tax assets and liabilities are compensated when the income tax is applied by the same fiscal authority and when there is a legal right of compensation. The deferred tax assets and liabilities are determined with the fiscal rates that are expected to be applied, in accordance with the regulations of the countries in which the Group operates, in the years in which the temporary differences will be realised or extinguished.

2.21 Use of estimates

The preparation of the consolidated financial statements require the Directors to apply accounting principles and methods that, in some circumstances, are based on difficulties and subjective valuations and estimates based on the historical experience and assumptions which are from time to time considered reasonable and realistic based on the relative circumstances. The application of these estimates and assumptions impact upon the amounts reported in the financial statements, such as the balance sheet, the income statement, the cash flow statement and on the disclosures in the explanatory notes. The final outcome of the accounts in the financial statements, which uses the above-mentioned estimates and assumptions, may differ from those reported in the financial statements due to the uncertainty which characterises the assumptions and the conditions upon which the estimates are based. Below are briefly described the accounting standards which require greater subjectivity by the directors in the preparation of the estimates and for which a change in the underlying conditions or the assumptions may have a significant impact on the consolidated financial statements of the Group.

- Goodwill: in accordance with the accounting standards adopted for the preparation of the financial statements, the company annually verifies the goodwill in order to ascertain the existence of any loss in value to be recorded in the income statement. In particular, the verification results in the determination of the fair value allocated to the financial cash-generating units. This value is determined according to their current value in use. The allocation of the goodwill to the cash-generating units and the determination of their value requires estimates which depend on factors that may change over time with consequent effects, which may be significant, compared to the valuations made by the Directors.

- Write-down of fixed assets: in accordance with the accounting standards applied by the Group, the fixed assets are verified to ascertain if there has been a loss in value which is recorded by means of a write-down, when it is considered there will be difficulties in the recovery of the relative net book value through use. The verification of the existence of the above-mentioned difficulties requires the Directors to make valuations based on the information available within the Group and from the market, as well as historical experience. In addition, when it is determined that there may be a potential loss in value, the Group determines this using the most appropriate technical valuation methods available. The correct identification of the indicators of the existence of a potential loss

in value as well as the estimates for the determination depends on factors which may vary over time, impacting upon the valuations and estimates made by the Directors.

- Deferred taxes: the accounting of the deferred tax assets is made on the basis of the expectations of future assessable income. The valuation of the expected assessable income in order to record the deferred taxes depends upon factors which may change over time and result in significant effects on the valuation of the deferred tax assets.

2.22 Estimates of the fair value

The fair value of the financial instruments traded in an active market is based on the listed price at the balance sheet date.

The fair value of the financial instruments not traded in an active market is calculated in accordance with valuation techniques. The techniques used are varied and the assumptions used are based on the market conditions at the balance sheet date. More specifically:

- The fair value of the interest rate swaps is calculated on the basis of the current value of the future cash flows;
- The fair value of the forward currency hedging contracts is determined on the basis of the current value of the differences between the contracted forward exchange rate and the spot market rate at the balance sheet date;
- The fair value of the advanced repayment option included in the bond issued by the subsidiary Capital International S.A. is valued using models applied by primary financial institutions;
- The fair value of the stock option is calculated using the *Black & Scholes* model.

3. Financial risks

The Group is exposed to various risks of a financial nature: market risks, credit risks and cash flow risks.

The financial risks are managed at a central level based on the Group hedging policies through the use of derivative instruments which minimise the effects deriving from foreign exchange rate fluctuations (especially in relation to the US dollar) and interest rate movements.

Market risks

The market risks can be divided into the following categories:

Exchange risks. The Group operates at international level and is therefore exposed to exchange rate risks, especially in relation to the US dollar as a large part of sales are made in the USA. The Group has constantly attempted to reduce the impact from the movements in the US dollar by procuring suppliers in areas where it is possible to buy in US dollars. For transactions not covered by purchases in US dollars, the Group uses hedging instruments such as forward foreign currency contracts on US dollars. The information on the fair value and accounts methods for the derivative financial instruments is given in the notes to the financial statements.

Changes in fair value risk. The Group holds some assets which may change in value over time, dependent on market movements.

Interest rate risk. The debt to the banking system exposes the Group to the risk of changes in interest rates. In particular, variable rate loans create a risk of changes in cash flow, while those at fixed rate create a potential variation in the fair value of the loans.

The Group assesses on a regular basis its risk to exposure to changes in interest rates and manages this risk through recourse to derivative financial instruments called interest rate swaps (IRS), which are used exclusively to hedge the cash flows. The counterparts are primary financial institutions and for the contracts in question, at the beginning of the hedge operation, there is the formal designation and documentation relative to the hedge. We should underline that the Group does not use financial instruments for speculative purposes.

Credit risk

The Group strives to reduce as far as possible the risk relating to the insolvency of its customers through rules that ensure the sales are made to customers who are reliable and solvent. These rules, based on information about the customers' solvency and historical data, are associated with exposure limits of individual clients, and permit a reduced concentration of the receivable and therefore minimises the retained risk. The credit risk is divided over a high number of counterparts and clients.

Cash flow risks

This risk could generate the inability to find the necessary financial resources at good terms to back up the operating activities in the right time. The cash flows, needs for finance and liquidity of the company are constantly monitored at central level by Group treasury, to guarantee effective and efficient management of the financial resources.

4. Notes to the Consolidated Balance Sheet

4.1 Cash in hand and at banks

The account represents the temporary liquidity held invested at market rates.

The important decrease compared to the previous year is due to the liquidity deriving from the Shareholders' stock account payment made by the parent company Safilo Group S.p.A. at the end of 2005 further to the IPO process, which had been used, during 2006, for the repayment of 35% of the bond (High Yield) for nominal Euro 105,000 thousand issued by the Luxembourg subsidiary Safilo Capital International S.A., and for the payment of the higher charges on advanced repayment for an amount of Euro 10,106 thousand.

The following table shows the reconciliation with the closing net cash reported in the cash flow statement:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Cash in hand and cash held at banks	35,643	151,018
Bank overdrafts	(36,444)	(10,046)
Current account for High Yield reimbursement	-	(115,106)
Totale	**(801)**	**25,866**

4.2. Trade receivables, net

The account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Gross value	342,485	328,928
Alllowance for doubtful accounts	(22,968)	(21,370)
Net value	**319,517**	**307,558**

At constant exchange rates, the net trade receivables increased by Euro 20,505 thousand due in particular to the increase in sales in the fourth quarter of 2006 (+12.0%) compared to the same period of the previous year.

The Group does not have a significant concentration of its credit risk as its receivables are related to a large number of customers.

The allowance for doubtful accounts includes the provision for products given to clients which, in accordance with specific contractual clauses, are expected to be returned as not placed to the final customers. This accrual is accounted for as a reduction of sales in the income statement.

The allowance for doubtful accounts also includes the accrual for insolvency accounted for in the income statement on the line "general and administrative expenses" (note 5.4).

The movements in the allowance for doubtful accounts are as follows:

(Euro/000)	Balance at January 1, 2005	Increase	Decrease	Transl. Diff.	Balance at December 31, 2005
Allowance for doubtful accounts	13,894	1,904	(3,750)	438	12,486
Sales return provision	6,481	7,660	(6,311)	1,054	8,884
Total	**20,375**	**9,564**	**(10,061)**	**1,492**	**21,370**

(Euro/000)	Balance at January 1, 2006	Increase	Decrease	Transl. Diff.	Balance at December 31, 2006
Allowance for doubtful accounts	12,486	4,356	(1,977)	(182)	14,683
Sales return provision	8,884	8,011	(7,663)	(947)	8,285
Total	**21,370**	**12,367**	**(9,640)**	**(1,129)**	**22,968**

4.3 Inventory

This account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Raw materials	50,491	43,784
Work-in-progress	7,868	8,123
Finished products	235,482	176,272
Gross	**293,841**	**228,179**
Obsolescence provision	(22,268)	(19,377)
Total	**271,573**	**208,802**

The growth in raw materials is directly related to the increased production levels in the Group factories and is aimed at supporting the forecast increase on internal production.

The increase in finished products compared to the previous year is further to sales policies aimed at improving the customer service levels. The development of the Solstice chain stores and the acquisition of the Spanish chain Loop have helped increase the value of finished product stock.

For obsolete and slow moving items a specific accrual, based on their possible future sale or use, has been accounted for. The accrual has impacted the income statement at the line “cost of sales” (note 5.2).

The movements in the obsolescence provision are as follows:

(Euro/000)	Balance at January 1, 2005	Increase	Transl. Diff.	Balance at December 31, 2005
Obsolescence provision	14,572	3,256	1,549	19,377
Total	**14,572**	**3,256**	**1,549**	**19,377**

(Euro/000)	Balance at January 1, 2006	Increase	Transl. Diff.	Balance at December 31, 2006
Obsolescence provision	19,377	4,321	(1,430)	22,268
Total	**19,377**	**4,321**	**(1,430)**	**22,268**

The high posting was due to the prudential valuation of the risk of obsolescence of finished "Polo Ralph Lauren" products, which may be sold, further to the licence contract in being, until June 30, 2007.

4.4 Assets held for sale

At December 31, 2005, the account included the net book value of the building of the Austrian subsidiary Carrera Brillen (Traun) which was classified under current assets, in view of the programmed sale of the assets over a short time period. The sale took place during the second quarter of 2006 with a capital gains of Euro 272 thousand.

4.5 Derivative financial instruments

The following table gives a summary of the derivative financial instruments in the balance sheet:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Current Assets		
- Foreign currency contracts	1,205	-
- Interest rate swaps - *cash flow hedge*	266	-
- Interest rate swaps - *at fair value through P&L*	126	-
Total	**1,597**	**-**
Non current Assets		
- Interest rate swaps - *cash flow hedge*	361	1,238
- Options	1,560	1,268
Total	**1,921**	**2,506**
Current liabilities		
- Foreign currency contracts	-	878
- Interest rate swaps - *at fair value through P&L*	-	-
Total	**-**	**878**
Non current liabilities		
- Interest rate swaps - *cash flow hedge*	-	4,509
- Interest rate swaps - *at fair value through P&L*	1,336	-
Total	**1,336**	**4,509**

Below is a summary of the features and fair values of the forward contracts in currency in being on December 31, 2006 and December 31, 2005:

Foreign currency contracts	December 31, 2006		December 31, 2005	
	Contractual value	*Fair value*	Contractual value	*Fair value*
	(USD/000)	*(Euro/000)*	*(USD/000)*	*(Euro/000)*
Expiry year 2006	-	-	$34,000	(878)
Expiry year 2007	$39,000	1,205	-	-
Total	**39,000**	**1,205**	**34,000**	**(878)**

The gains and losses directly posted to shareholders' equity at the end of a financial period are then posted to the income statement when the hedge contract is closed.

Below is a summary of the features and fair values of the interest rate swap contracts in being on December 31, 2006 and December 31, 2005:

Interest rate swaps (Euro/000)	December 31, 2006		December 31, 2005	
	Contractual value	*Fair value*	Contractual value	*Fair value*
Expiry year 2007	170,361	392	191,614	537
Expiry year 2010	25,000	(522)	25,000	(1,681)
Expiry year 2011	85,000	(453)	25,000	(2,127)
Total	**280,361**	**(583)**	**241,614**	**(3,271)**

The market value of the interest rate swaps contracts is calculated by specialised financial institutions on the basis of normal market conditions.

Further to the refinancing operation which was concluded on June 26, 2006 (see note 4.14 for more details), some of the interest rate swaps contracts, initially designated to hedge the cash flows derived from the previous Senior Loan, took on a different function.

In particular, some interest rate swaps contracts have been reallocated by the Group to hedge the cash flow from the new financing operation.

The derivative financial instruments which are no longer used for hedging have been reclassified from "interest rate swaps – cash flow hedge" to "interest rate swaps – fair value recorded in the income statement", with allocation of the variation in fair value between the financial income/charges instead of to the shareholders' equity.

The non-current assets include the fair value of the advance repayment option included in the bond issued by the subsidiary Safilo Capital International S.A.. The valuation was made using the models applied by primary financial institutions, recognising a fair value to the option of Euro 1,560 thousand.

4.6 Other current assets

The account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Receivables from the holding company Safilo Group S.p.A.	14,595	13,518
VAT receivable	5,306	4,453
Tax credits and payments on account	9,515	11,445
Prepayments and accrued income	7,505	5,281
Receivables from agents	4,483	4,943
Other current receivables	15,623	4,793
Total	**57,027**	**44,433**

The receivables from the holding company Safilo Group S.p.A. mainly refer to the loan granted by Safilo S.p.A. to its parent company for Euro 14,200 thousand at the 3-month Euribor rate plus a 0.10% spread on an annual basis, which will expire on December 31, 2007. The remaining part of the account includes the interests on the loan itself, for Euro 126 thousand and advances conceded to the holding company.

The tax credits and payments on account principally relate to the income tax payments on account and will be compensated against the relative taxes payable.

Prepayments and accrued income at December 31, 2006 amount to Euro 7,505 thousand against Euro 5,281 thousand at December 31, 2005 and include:

- prepaid advertising costs of Euro 2,268 thousand;
- prepaid insurance premiums of Euro 263 thousand;
- prepaid rent and operating leases of Euro 1,181 thousand;
- prepaid costs for the part of the financing operation called “Revolving Facility” for Euro 1,451 thousand;
- other prepaid costs, mainly of commercial nature, for Euro 2,342 thousand.

The receivables from agents mainly refer to receivables deriving from the sale of samples.

The other short-term receivables refer to:

- advance royalties payments relative to 2007 for Euro 11,779 thousand;
- insurance repayments and other receivables in the financial statements of some companies of the Group.

4.7 Property, plant and equipment

Below are the changes in the property, plant and equipment for the periods closed on December 31, 2005 and December 31, 2006:

(Euro/000)	Balance at January 1, 2005	Increase	Decrease	Reclass.	New acquisitions	Transl. Diff.	Balance at December 31, 2005
Gross value							
Land and buildings	109,527	4,510	(1,025)	(5,444)	-	535	108,103
Plant and machinery	151,195	6,989	(2,061)	-	-	413	156,536
Equipment and other assets	105,784	18,339	(2,038)	-	-	4,540	126,625
Assets under construction	3,542	1,493	-	(2,268)	-	64	2,831
Total	**370,048**	**31,331**	**(5,124)**	**(7,712)**	**-**	**5,552**	**394,095**
Accumulated depreciation							
Land and buildings	20,472	3,440	(249)	(2,460)	-	99	21,302
Plant and machinery	80,406	11,265	(1,651)	-	-	172	90,192
Equipment and other assets	73,402	14,913	(1,897)	-	-	2,580	88,998
Total	**174,280**	**29,618**	**(3,797)**	**(2,460)**	**-**	**2,851**	**200,492**
Net book value	**195,768**	**1,713**	**(1,327)**	**(5,252)**	**-**	**2,701**	**193,603**

(Euro/000)	Balance at January 1, 2006	Increase	Decrease	Reclass.	New acquisitions	Transl. Diff.	Balance at December 31, 2006
Gross value							
Land and buildings	108,103	2,555	(165)	(1,277)	-	(433)	108,783
Plant and machinery	156,536	8,256	(1,308)	319	-	(397)	163,406
Equipment and other assets	126,625	25,347	(4,547)	-	10,998	(4,561)	153,862
Assets under construction	2,831	4,441	-	(1,197)	-	(56)	6,019
Total	**394,095**	**40,599**	**(6,020)**	**(2,155)**	**10,998**	**(5,447)**	**432,070**
Accumulated depreciation							
Land and buildings	21,302	3,242	(38)	(1,277)	-	(117)	23,112
Plant and machinery	90,192	11,621	(1,085)	78	-	(183)	100,623
Equipment and other assets	88,998	15,673	(3,374)	-	7,524	(2,437)	106,384
Total	**200,492**	**30,536**	**(4,497)**	**(1,199)**	**7,524**	**(2,737)**	**230,119**
Net book value	**193,603**	**10,063**	**(1,523)**	**(956)**	**3,474**	**(2,710)**	**201,951**

Investments in tangible and intangible fixed assets are mainly concentrated in the holding company Safilo S.p.A., which the Italian factories report to. These investments in 2006 were addressed mainly to renewing the plant and equipment for the new models. Investments in intangible fixed assets mainly referred to software and managing the brand portfolio.

The foreign investments were mainly addressed to managing the factory of the Slovenian subsidiary, and in the United States for the development of the Solstice chain stores.

Some of the Group companies have tangible fixed assets in leasing. The following table shows the gross value and the related accumulated depreciation fund, while the information related to the leasing contracts is given in paragraph 4.14 "Payables to banks and loans".

(Euro/000)	December 31, 2006	December 31, 2005
Land and buildings	14,261	14,261
Accumulated depreciation (-)	(573)	(230)
Net book value	**13,688**	**14,031**
Plant and machinery	3,248	3,248
Accumulated depreciation (-)	(1,931)	(1,499)
Net book value	**1,317**	**1,749**
Equipment and other assets	635	555
Accumulated depreciation (-)	(286)	(285)
Net book value	**349**	**270**
Net book value	**15,354**	**16,050**

4.8 Intangible fixed assets

Below are the changes in the intangible fixed assets for the periods closed on December 31, 2005 and December 31, 2006:

(Euro/000)	Balance at January 1, 2005	Increase	Decrease and write-down	Other movements	Transl. Diff.	Balance at December 31, 2005
Gross value						
Software costs	6,972	1,709	(739)	-	197	8,139
Trademarks and licences	33,826	7,618	-	-	65	41,509
Other intangible assets	6,404	416	-	-	342	7,162
Intangible assets in progress	162	-	-	(141)	12	33
Total	**47,364**	**9,743**	**(739)**	**(141)**	**616**	**56,843**
Accumulated depreciation						
Software costs	5,257	1,304	(739)	-	120	5,942
Trademarks and licences	14,818	3,986	-	-	14	18,818
Other intangible assets	6,063	288	-	-	152	6,503
Total	**26,138**	**5,578**	**(739)**	**-**	**286**	**31,263**
Net book value	**21,226**	**4,165**	**-**	**(141)**	**330**	**25,580**

(Euro/000)	Balance at January 1, 2006	Increase	Decrease and write-down	New acquisitions	Transl. Diff.	Balance at December 31, 2006
Gross value						
Software costs	8,139	2,264	(19)	308	(170)	10,522
Trademarks and licences	41,509	367	-	33	(52)	41,857
Other intangible assets	7,162	753	(2,014)	686	(174)	6,413
Intangible assets in progress	33	-	(16)	-	(2)	15
Total	**56,843**	**3,384**	**(2,049)**	**1,027**	**(398)**	**58,807**
Accumulated depreciation						
Software costs	5,942	1,592	(19)	287	(108)	7,694
Trademarks and licences	18,818	4,268	-	19	(39)	23,066
Other intangible assets	6,503	442	(1,616)	537	(93)	5,773
Total	**31,263**	**6,302**	**(1,635)**	**843**	**(240)**	**36,533**
Net book value	**25,580**	**(2,918)**	**(414)**	**184**	**(158)**	**22,274**

Amortisation and depreciation costs related to property, plant and equipment and intangible fixed assets for the 2006 and 2005 financial years are divided in these income statement lines:

(Euro/000)	Note	2006	2005
Cost of sales	5.2	20,126	25,382
Sales and marketing costs	5.3	3,227	2,545
General and administrative costs	5.4	13,485	7,270
Total		**36,838**	**35,197**

4.9 Goodwill

(Euro/000)	Balance at January 1, 2005	Increase / (Decrease)	Transl. Diff.	Balance at December 31, 2005
Goodwill	363,161	-	1,960	365,121
Net book value	**363,161**	**-**	**1,960**	**365,121**

(Euro/000)	Balance at January 1, 2006	Increase / (Decrease)	Transl. Diff.	Balance at December 31, 2006
Goodwill	365,121	26,839	(9,201)	382,759
Net book value	**365,121**	**26,839**	**(9,201)**	**382,759**

The changes in goodwill with respect to the previous year refer to the purchase of the Loop Vision chain stores and the exchange rate differences; reference should be made to the paragraph "enterprise groups" for more details about the acquisition.

For impairment tests, the Group has identified its cash-generating units (CGUs), that substantially match with the entities operating in each country.

Goodwill divided by groups of CGUs is as follows:

Goodwill (Euro/000)	Italy and Europe	The Americas	Asia Pacific	Total
December 31, 2006	147,849	105,977	128,933	**382,759**
December 31, 2005	121,377	107,383	136,361	**365,121**

The recoverable amount of the CGUs is based on their value of use determined on estimated cash flow projections. This computation derives from five-year financial budgets, approved by management considering its expectations for market and Group development. To determine the terminal value, the cash flow projections that were obtained were actualised at a discount rate that considers the specific nature and risks of each area where the Group operates.

Cash flows beyond the five-year period are extrapolated using the perpetual estimated growth rate that does not exceed the long-term average growth rate forecast by analysts for the business in which the Group operates.

Key assumptions	"WACC" discount rate		Growth rate "g"	
	2006	2005	2006	2005
Euro area	6.4%	6.5%	1.0%	1.0%
USA area	7.2%	7.5%	1.0%	1.0%
Far East area	8.5%	8.8%	2.6%	2.0%
Australia	8.3%	8.3%	1.0%	1.0%
Japan	4.4%	4.7%	1.0%	1.0%
South Africa	10.4%	10.4%	4.5%	4.7%
India	11.1%	11.7%	5.0%	3.6%
Brazil	12.4%	13.2%	4.0%	4.9%

Enterprise groups

On November 9, 2006 the Group took over the Loop Vision chain stores, with 63 stores throughout Spain. The overall cost for the purchase by the Group company Safint B.V. is Euro 2,721 thousand (including accessory costs) for the purchase of 100% of the shares of the Luxembourg company Luxury Trade S.A., which holds the entire capital of the Spanish trading company Fashion Optic S.A. which, in turn, holds 100% of the shares in the trading company Navoptik S.A..

The transaction was posted using the acquisition method, and the difference between the purchase price and the fair value of the purchased net assets was entirely allocated to goodwill. In accordance with the provisions of IFRS n. 3, paragraph 62, the initial value for the enterprise group was determined temporarily, determining just the fair value to assign to the assets, liabilities and potential liabilities in the acquired companies. The adjustments of these

provisional values, in accordance with paragraph 62 above, will be determined within twelve months from the date of acquisition.

The assets and liabilities acquired on November 9, 2006 are as follows:

Acquired assets and liabilities	Fair value
Cash in hand and at banks	400
Trade receivables, net	431
Inventory	4,173
Other current assets	466
Property, plant and equipment	3,474
Net intangible fixed assets	184
Other non-current assets	1,215
Trade payables	(10,735)
Other current liabilities	(3,414)
Long-term loans	(20,170)
Provisions for risks	(142)
Total net assets	**(24,118)**
Goodwill	26,839
Price paid	**2,721**

Goodwill is entirely attributable to the excess income that is expected from distributing Group products through the retail chains and from the synergies that will result from the grouping. The goodwill was submitted to impairment test on both the date of purchase and at the end of the financial year, and further to the test no needs emerged to account for any reduction in value.

Despite the fact the transaction took place near to the end of the period, it was considered best to consolidate the costs and income of the companies for the period between the purchase date of the subsidiaries and the end of the 2006 financial year. Since the purchase date, there has been net sales of Euro 3.642 thousand and a loss of Euro 565 thousand. If the acquisition had been made on January 1, 2006 the Group net sales would have been higher by Euro 21,923 thousand, and the net income for the year lower by Euro 4,502 thousand.

No acquisitions were made in the previous financial year.

4.10 Investments in associates

Investments in associated companies refer to:

Company	Registered office or headquarters	% of share capital	Type of investment	Main activity
Elegance I. Holdings Ltd	Hong Kong	23.05%	Associated company	Commercial
Optifashion As	Turkey	50.00%	Non consolidated subsidiary	Commercial
TBR Inc.	USA	33.33%	Associated company	Real estate

The movements in investments in associated companies during the year were as follows:

(Euro/000)	Gross value	Revaluation (write-down)	Value at December 31, 2005	Movements for the year: Share of results and write-down of divid. of assoc. comp.	Movements for the year: Translation differences	Value at December 31, 2006
TBR Inc.	437	456	893	146	(100)	939
Elegance Ltd	5,406	6,887	12,293	434	(1,333)	11,394
Optifashion As	353	(47)	306	(104)		202
Total	**6,196**	**7,296**	**13,492**	**476**	**(1,433)**	**12,535**

There were no new investments in associated companies in 2006. The changes compared to December 31, 2005 are principally due to the gains realised in the year, net of dividends distributed. The table below shows the principal data relating to the last approved financial statements of the above-mentioned companies:

December 31, 2005 *(Euro/000)*	Assets	Liabilities	Net equity	Net sales	Profit (loss)	% Group	Group net equity
Elegance Ltd	66,254	14,671	51,583	41,902	3,684	23.05%	11,889
Optifashion As	613	170	443	1,161	85	50.00%	222
TBR Inc.	5,396	2,717	2,679	1,107	368	33.33%	893
Total	**72,263**	**17,558**	**54,706**	**44,170**	**4,137**		**13,004**

December 31, 2006 *(Euro/000)*	Assets	Liabilities	Net equity	Net sales	Profit (loss)	% Group	Group net equity
Elegance Ltd	63,007	17,337	45,670	44,305	2,860	23.05%	10,526
Optifashion As	523	87	436	1,128	97	50.00%	218
TBR Inc.	5,253	2,435	2,818	1,152	439	33.33%	939
Total	**68,783**	**19,859**	**48,924**	**46,585**	**3,396**		**11,683**

The company Optifashion A.s. with registered office in Istanbul (Turkey), a 50% held subsidiary of the Group, is not included in the consolidation scope as the amounts are considered insignificant in representing a true and fair view of the financial position and result of the Group.

4.11 Financial assets available for sale

This account represents the financial assets which may be sold. They are measured at fair value with the fair value reserve of the Shareholders' equity as counterbalance. With reference to Banca Popolare Italiana S.p.A. and Unicredit S.p.A., the value is determined referring to the prices quoted on the official markets on the balance sheet date.

(Euro/000)	Relationship	Value at December 31, 2006	Value at December 31, 2005
Banca Popolare Italiana S.p.A.	Other equity investment	3,238	5,589
Safilens S.r.l.	Other equity investment	-	209
Unicredit S.p.A.	Other equity investment	191	168
Others	Other equity investment	43	43
Total		**3,472**	**6,009**

The movements in the above assets were as follows:

	31.12.2005			Movements for the year		
(Euro/000)	Gross value	Revaluation (write-down)	Net value	Incr./Decr.	Revaluation (write-down)	Value at Dec, 31 2006
Banca Pop. Italiana S.p.A.	10,198	(4,609)	5,589	(3,343)	992	3,238
Safilens S.r.l.	209	-	209	(209)	-	-
Unicredit S.p.A.	48	120	168	-	23	191
Others	43	-	43	-	-	43
Total	**10,498**	**(4,489)**	**6,009**	**(3,552)**	**1,015**	**3,472**

In April 2006 the investment in Safilens S.r.l., recorded in the financial statement at 31.12.2005 for a value of Euro 209 thousand, was sold for Euro 66 thousand.

Also during 2006, Safilo S.p.A. sold no. 446,500 of the 746,250 shares of the investment in Banca Popolare Italiana with a corresponding income, net of costs and bank charges, of Euro 4,368 thousand.

4.12 Deferred tax assets and deferred tax liabilities

(Euro/000)	2006	2005
Deferred tax assets		
- recoverable within 1 year	24,264	22,775
- recoverable after 1 year	26,908	26,504
Total	**51,172**	**49,279**
Deferred tax liabilities		
- recoverable within 1 year	2,199	533
- recoverable after 1 year	10,883	10,436
Total	**13,082**	**10,969**
Total, net	**38,090**	**38,310**

Deferred tax assets

Deferred tax assets refer to income taxes calculated on fiscal losses recoverable in future years and temporary differences between the carrying amount of assets and liabilities and their tax basis.

		Impact on				
(Euro/000)	Balance at January 1, 2006	Income Statement	Equity	Receiv./(pay.) due to Group tax consol.	Transl. Diff.	Balance at December 31, 2006
Fiscal losses	10,664	759	-	(759)	-	10,664
ICO profit on inventory and obsol.	13,532	4,801	-	-	(1,921)	16,412
Receivables	5,641	1,320	-	-	(390)	6,571
Contingent liabilities	2,278	(318)	-	-	(16)	1,944
Employee benefits liability	2,101	61	(992)	-	(32)	1,138
Intangible assets	6,804	(368)	-	-	(2)	6,434
Property, plant and equipment	1,144	2,214	-	-	52	3,410
Unrealised exchange differences	2,150	(1,989)	-	-	-	161
Derivative instruments - fair value	1,369	(229)	(1,140)	-	-	-
Equity investments	513	(130)	-	-	(39)	343
Goodwill	1,609	221	-	-	(84)	1,746
Other payables	(57)	722	-	-	-	665
Others	1,531	25	441	-	(314)	1,683
Total	**49,279**	**7,089**	**(1,691)**	**(759)**	**(2,745)**	**51,172**

The following table shows the Group fiscal losses on which deferred tax assets have been calculated as there is a reasonable expectation of the recovery of these amounts through future assessable income:

(Euro/000)	Tax losses	Financial year	Expiring date	Calculated deferred tax assets	Transfer to holding company	Total deferred tax ass. for tax losses
	1,711	2003	2008	565	-	565
	30,602	2004	2009	10,099	-	10,099
	57,572	2005	2010	18,999	(18,999)	-
	2,300	2006	2011	759	(759)	-
Total	**92,185**			**30,422**	**(19,758)**	**10,664**

Deferred tax liabilities

Deferred tax liabilities refer to taxes calculated on the temporary differences between the book value of the assets and liabilities and the related fiscal value.

(Euro/000)	Balance at January 1, 2006	impact on Income Statement	impact on Equity	impact on Transl. Diff.	Balance at December 31, 2006
Property, plant and equipment, net	6,230	(563)	-	(139)	5,528
Goodwill	1,959	662	-	4	2,625
Equity investments	1,650	56	-	(175)	1,531
Derivative instruments - fair value	418	(248)	179	-	349
Dividends	99	363	-	-	462
Translation differences	-	1,388	-	-	1,388
Other	613	388	263	(65)	1,199
Total	**10,969**	**2,046**	**442**	**(375)**	**13,082**

The most important line item included in deferred tax liabilities principally derives from the different calculation of the depreciation for the financial statements of Safilo S.p.A. compared to the depreciation computed for fiscal purposes. In particular, in 2003 the estimates of the useful life of some assets were revised with particular reference to plant and machinery. The effects of this revision, both for fiscal purposes and for Italian Accounting Standards purposes, were adjusted in 2003, while in compliance with IFRS 1, paragraph 7, they were calculated as if the assets were always depreciated in accordance with the re-determined useful life.

4.13 Other non-current assets

The account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Receivables from holding company Safilo Group S.p.A.	19,758	20,300
Other non-current assets	1,974	1,303
TOTAL	**21,731**	**21,603**

The receivables from the parent company Safilo Group S.p.A. relate to the fiscal losses realized by Safilo S.p.A. during the financial years 2005 and 2006 and transferred to Safilo Group S.p.A. further to the "national tax consolidation". In accordance to it, Safilo Group S.p.A. is the consolidating company and Safilo S.p.A., Oxsol S.p.A., Lenti S.r.l. and Smith Sport Optics S.r.l. are the consolidated company; thanks to the agreements subscribed, the fiscal losses realized by Safilo S.p.A. are hence transferred to the consolidating company. The receivables from the parent company is the counterbalance for the fiscal benefits transferred to the consolidating company.

The other non-current assets mainly refer to down payments and other long-term receivables in the balance sheets of the Group companies. The increase compared to the previous year is mainly due to down payments for rental contracts for the stores of the new Spanish subsidiary Navoptik.

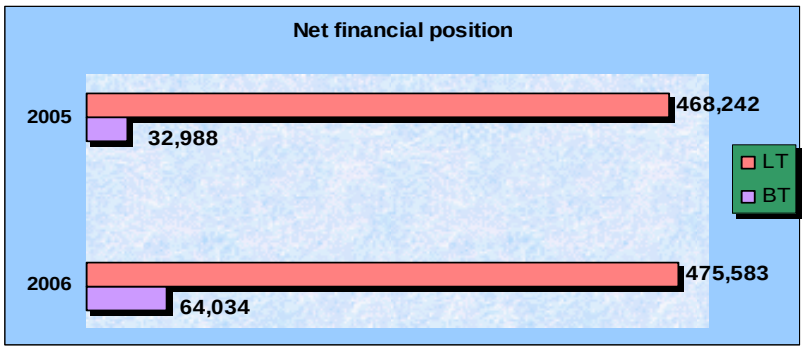
4.14 Payables to banks and loans

The account is comprised as follows:

(Euro/000)	December 31, 2006	December 31, 2005
Payables to banks and short-term loans		
Bank overdrafts	6,631	5,046
Short-term bank loans	29,813	5,000
Short-term portion of long-term bank loans	22,523	26,614
Short-term portion of High Yield bond	-	105,000
Payable for High Yield advance repayment	-	10,106
Short-term portion of financial leasing and other loans	1,121	3,944
Other short-term loans	39,589	28,296
Total	**99,677**	**184,006**
Payables to banks and medium and long-term loans		
Medium long-term loans	465,103	456,763
Payables for financial leasing	9,708	10,616
Other medium long-term loans	772	863
Total	**475,583**	**468,242**
Total borrowings and bank loans	**575,260**	**652,248**

The net financial position of the Group on December 31, 2006 compared to December 31, 2005 is as follows:

Net financial position *(Euro1000)*	Dec. 31, 2006	Dec. 31, 2005	Change
Current portion of long term borrowings	(23,644)	(135,558)	111,914
Bank overdrafts and short t. bank borrowings	(36,444)	(10,046)	(26,398)
Other short term borrowings	(39,589)	(38,402)	(1,187)
Cash and cash equivalents	35,643	151,018	(115,375)
Short term net financial position	**(64,034)**	**(32,988)**	**(31,046)**
Long term borrowings	(475,583)	(468,242)	(7,341)
Long term net financial position	**(475,583)**	**(468,242)**	**(7,341)**
Net financial position	**(539,617)**	**(501,230)**	**(38,387)**



Key:

LT= long term
ST= short term

On June 26, 2006 the Group completed an important financing operation by signing a new contract to replace the Senior Loan issued in 2002. The banking pool that coordinated the refinancing operation is formed of Banca Intesa S.p.A., Sanpaolo IMI S.p.A. and UniCredit Banca Mobiliare S.p.A..

On December 31, 2006 the new loan showed a short-term portion of Euro 18,886 thousand, a portion of Euro 272,301 thousand included in medium long-term borrowings, expires on December 31, 2011 and is divided in the following credit lines:

- Euro 200 million, for "Facility A", with six monthly amortisation starting from December 2006 until December 2011. Facility A is in turn divided in three tranches, one in Euro (tranche A1, for nominal Euro 80 million) at Euribor rate plus a spread of 0.60%; and two in US dollars (Tranche A2 and Tranche A3, for nominal USD 70.4 million an USD 80.5 million respectively) at Libor rate plus a spread of 0.60%.

- Euro 200 million for the "Revolving Facility" formed of two tranches which can also be paid in US dollars (Tranche B1 for nominal Euro 170 million, Tranche B2 for nominal Euro 30 million) used at December 31, 2006 for Euro 110 million.

This operation offers better conditions than the previous loan both in terms of guarantees and repayment terms, and with regards to the margins applied to the interest parameter (EURIBOR or LIBOR), with an initial spread of 0.60% yearly with respect to the previous spread which, depending on the tranches, ranged from a minimum of 2.25% to a maximum of 3.25%.

With the income from the new contract, the Group repaid the previous Senior Loan with an overall payment of Euro 300,340 thousand. The settlement of the loan brought about posting non-recurring financial charges to the income statement for an overall amount of Euro 7,749 thousand further to speeding up amortisation of the charges relative to the extinguished loan, and Euro 1,210 thousand for the fair value of the interest rate swaps contracts, that were not addressed to hedge cash flows from the new loan (see note 4.5 for further details).

The agreements relative to loans granted to some companies of the Group by Banca Intesa S.p.A., San Paolo IMI S.p.A. and UniCredit Banca Mobiliare S.p.A. include a series of operational and financial obligations. In particular, predefined levels must be respected relative to certain covenants, which are calculated on the basis of figures at the balance sheet date on a half-year basis. If these covenants are not respected, conditions will be negotiated with the lenders to be able to continue with the loan agreement, or rather the opportune waivers or adjustment changes to the covenants. Otherwise, there is risk of an event of default which could result in the forced advanced repayment of the loaned sums.

The covenants in the current medium long-term loan contract are calculated as the ratio between the net financial position and EBITDA and between EBITDA and the relative financial interests.

With regards to the High Yield bond, the short-term portion at December 31, 2005 was repaid on January 13, 2006 by the Luxembourg subsidiary Safilo Capital International S.A. for 35% of the nominal value of Euro 300 million. The outstanding portion of the bond of nominal Euro 195 million is included in the account medium long-term borrowings. The debt for advance payment of the High Yield bond in the balance sheet at December 31, 2005 refers to the additional charges paid in January 2006 to the bondholders further to the above advance repayment.

The above loans are valued with the amortised cost method and are mainly guaranteed by security on shares in Safilo S.p.A. and guarantees from the directly financed companies.

The expiry dates for the medium and long-term loans are as follows:

(Euro/000)	December 31, 2006	December 31, 2005
Within 2 years	38,693	30,464
Within 3 years	39,656	33,564
Within 4 years	39,822	20,471
Within 5 years	163,739	131,068
Beyond 5 years	193,673	252,675
Total	**475,583**	**468,242**

Below the bank loans and borrowings is given divided by currency:

(Euro/000)	December 31, 2006	December 31, 2005
Short term		
Euro	84,857	162,641
US Dollars	11,160	19,205
Brasilian Real	2,265	-
Hong Kong Dollars	1,395	2,160
Total	**99,677**	**184,006**
Medium long-term		
Euro	383,359	402,980
US Dollars	90,950	65,262
Yen	1,274	-
Total	**475,583**	**468,242**
Total borrowings	**575,260**	**652,248**

The following table shows the bank credit lines granted to the Group, the usage and credit lines available on December 31, 2006, net of factoring and leasing operations:

(Euro/000)	Credit lines granted	Uses	Credit lines available
Credit lines on bank accounts and short-term bank loans	149,540	34,179	115,361
Credit lines on long-term bank loans	391,687	301,687	90,000
Total	**541,227**	**335,866**	**205,361**

Below is a summary of the main features of the more significant medium long-term borrowings in being on December 31, 2006 and December 31, 2005:

December 31, 2006 *(Euro/000)*	Currency	Nominal interest rate	Internal interest rate	Current value	Expiry
Facility A1	*EURO*	Euribor + 0.60%	4.8704%	79,078	31/12/2011
Facility A2	*USD*	Libor + 0.60%	6.6615%	47,522	31/12/2011
Facility A3	*USD*	Libor + 0.60%	6.4706%	54,588	31/12/2011
Revolving facility	*EURO*	Euribor +0.60%	4.4094%	110,000	31/12/2011
High Yield	*EURO*	9.625%	10.6887%	215,381	15/05/2013

December 31, 2005 (Euro/000)	Currency	Nominal interest rate	Internal interest rate	Current value	Expiry
Senior Loan - Term B	*EURO*	Euribor + 2.75%	6.2402%	134,400	31/12/2010
Senior Loan - Term C	*EURO*	Euribor + 3.25%	6.7288%	61,226	31/12/2011
Senior Loan - Term A1 - T2	*USD*	Libor + 2.25%	8.4636%	40,670	31/12/2009
Senior Loan - Term A2	*USD*	Libor + 2.25%	8.2889%	45,890	31/12/2009
Capex line	*EURO*	Euribor + 2.50%	4.6460%	7,000	31/12/2009
Capex line	*EURO*	Euribor + 2.50%	4.6426%	14,000	31/12/2009
High Yield	*EURO*	9.625%	10.6887%	337,013	15/05/2013
Loan in YEN	*YEN*	Tibor + 0.54%	Tibor + 0.54%	2,148	27/03/2006

The current value of the loans is represented by the outstanding nominal value at the balance sheet date, except for the High Yield loan which has the current value represented by the market value on December 31, 2006.

The debts for financial leasing refer to property, plant and equipment purchased through leasing contracts by some companies of the Group. The residual life of the leasing contracts is around 8.5 years. All the leasing contracts in being at the date of this report should be repaid through a constant installment plan and no changes are forecast to the original plan.

The following table shows the short-term shares and medium long-term shares relative to financial leasing contracts in being on December 31, 2006:

(Euro/000)	December 31, 2006	December 31, 2005
Financial leasing payables (short term share)	1,121	3,436
Financial leasing payables (long term share)	9,708	10,616
Total debt	**10,829**	**14,052**

Some companies in the Group have stipulated operational leasing contracts. The relative instalments are recorded in the income statement under “Cost of sales” (note 5.2), “Selling and marketing expenses” (note 5.3) and “General and administrative costs” (note 5.4).

The other medium and long-term loans mainly refer to a loan granted to the holding company Safilo S.p.A. valid under law 46/82 at a rate of 0.705%.

With regards to bank borrowings and short-term loans, it is noteworthy to be mentioned that the account *"Other short-term loans"* includes Euro 38,096 thousand for a payable to a primary factoring company derived from a contract stipulated by Safilo S.p.A..

4.15 Trade payables

The account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Purchase of raw materials	51,295	42,098
Purchase of finished products and subcontractors	93,438	71,299
Commissions and royalties	25,524	26,725
Advertising and marketing costs	24,054	17,456
Services received from third parties	30,123	21,756
Payables for purchase of property, plant and equipment and intangible assets	3,912	3,299
Total	**228,346**	**182,633**

The increase in trade payables for "purchases of raw materials" reflects the higher internal production levels; the increase in "purchase of finished products and subcontractors" reflects the greater supplies of finished products to back up the sales in the last quarter of the financial year and to increase warehouse stocks in view of the forecast increase in sales in 2007.

4.16 Tax payables

Tax payables at December 31, 2006 amount to Euro 20,716 thousand and refer for Euro 10,363 thousand to income taxes for the year, for Euro 3,008 thousand to VAT payables and for the remainder to advanced and various tax liabilities and local taxes.

The accrual for current income taxes is disclosed in the note relative to income taxes (5.10).

4.17 Other short-term liabilities

The account is comprised as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Payables to personnel and social security institutions	31,935	44,913
Premiums to clients	20,541	17,195
Agent fee payables	2,202	2,962
Accrued advertising & sponsorship costs	520	2,746
Accrued interests on long term payables	7,302	3,628
Other accruals and deferred income	3,314	2,898
Due to Shareholders for dividends	19,553	2,170
Payable to the holding company Safilo Group S.p.A.	1,085	959
Other current liabilities	3,336	1,952
Total	**89,788**	**79,423**

Payables to personnel and social security institutions principally refer to salaries and wages for December and for holidays matured and not taken.

Payables to Shareholders refer for Euro 16 million to dividends approved by the Safilo S.p.A. Shareholders' Meetings held on November 13, 2006 to be distributed to the only Shareholder Safilo Group S.p.A. and not paid on the balance sheet date. The outstanding part relates to dividends to be distributed to minority Shareholders, in accordance with the resolutions of some companies of the Group. The said amounts, even if deliberated, have not been paid as at the balance sheet date.

4.18 Provisions for risks and charges

The account is comprised as follows:

(Euro/000)	Balance at January 1, 2005	Increases	Decreases	New acquisition	Translation Differences	Balance at December 31, 2005
Product warranty provision	3,119	312	(312)	-	-	3,119
Agents' severance indemnity	2,861	416	(116)	-	3	3,164
Litigation	-	2,000	-	-	-	2,000
Other provisions for risks and charges	376	191	(251)	-	45	361
Provisions for risks - long term	**6,356**	**2,919**	**(679)**	**-**	**48**	**8,644**
Provisions for risks - short term	**136**	**-**	**(8)**	**-**	**-**	**128**
Total	**6,492**	**2,919**	**(687)**	**-**	**48**	**8,772**

(Euro/000)	Balance at January 1, 2006	Increases	Decreases	New acquisition	Translation Differences	Balance at December 31, 2006
Product warranty provision	3,119	682	-	-	-	3,801
Agents' severance indemnity	3,164	612	(87)	-	-	3,689
Litigation	2,000	-	(812)	-	-	1,188
Other provisions for risks and charges	361	1,373	-	117	(51)	1,800
Provisions for risks - long term	**8,644**	**2,667**	**(899)**	**117**	**(51)**	**10,478**
Provisions for risks - short term	**128**	**675**	**-**	**25**	**-**	**828**
Total	**8,772**	**3,342**	**(899)**	**142**	**(51)**	**11,306**

The product warranty provision was made against the costs to be incurred for the replacement of products sold before the balance sheet date.

The agents severance indemnity was created against the risk deriving from the payment in the case of termination of the agency agreement. This provision has been calculated based on existing laws at the balance sheet date considering all the future expected financial cash flows.

4.19 Employee benefits

The account shows the following movements:

(Euro/000)	Balance at Jan. 1, 2005	Posted to income statement	Actuarial differences	Use	Translation Differences	Balance at Dec. 31, 2005
Employee benefit liability	34,607	3,968	3,207	(2,417)	-	39,365
Total	**34,607**	**3,968**	**3,207**	**(2,417)**	**-**	**39,365**

(Euro/000)	Balance at Jan. 1, 2006	Posted to income statement	Actuarial differences	Use	Translation Differences	Balance at Dec. 31, 2006
Employee benefit liability	39,365	7,395	(3,006)	(2,786)	(88)	40,880
Total	**39,365**	**7,395**	**(3,006)**	**(2,786)**	**(88)**	**40,880**

The amount refers to different forms of defined benefit and defined contributions pension plans, in line with the local conditions and practices in the countries in which the Group carries out its activities.

The amounts posted to the income statement (operating and financial components) and to net equity (actuarial differences) are divided as follows:

(Euro/000)	Dec. 31, 2006	Dec. 31, 2005
Service cost	6,304	3,312
Interest cost	1,091	656
Actuarial gain/(loss)	(3,006)	3,207
Total	**4,389**	**7,175**

Actuarial estimates used for calculating the Staff Severance Fund are based on a system of probable factors based on:

a) demographic parameters;

b) economic parameters;

c) financial parameters.

Demographic parameters are normally summarised in tables based on samples deriving from different institutes (Istat, Inail, Inps, National Accounts, etc.).

Economic parameters principally refer to long-term inflation rates and financial yield rate, crucial for the revaluation of amounts accrued in the Staff Severance Fund.

Economic parameters also include compensation dynamics of the workforce in question. Personnel compensation average increase has been taken into account considering the employee's service life and the professional qualification (blue collars, white collars and intermediaries, middle management and executives).

The most important financial parameter is the discount rate. For the present value of the discount rate, the structure of the zero coupon rate terms has been used derived from the swap rates interest on December 31, 2006.

On January 1, 2007 the new Financial bill and implementing decrees introduced changes to the discipline governing Staff Severance Funds (TFR), including the choice of the worker as to how his or her accruing TFR should be allocated. In particular, the new flows of TFR can be allocated by the worker to selected pension funds or kept in the company reserves (in which case the company pays the TFR contributions into a treasury account set up with INPS). At the moment, the uncertain interpretation of this new law, the various different interpretations of the qualification according to IAS n. 19 of the accruing TFR and the subsequent changes to the actuarial calculation of the accrued TFR, and the total impossibility of begin able to estimate how the employees will decide to allocate their accruing TFR (each employee has until June 30, 2007 to make his or her choice), would make any idea of changing the actuarial calculation of the TFR that had accrued at December 31, 2006 rather premature.

4.20 Other non-current liabilities

The other non-current liabilities at December 31, 2006 amount to Euro 5,172 thousand and include:

- Euro 4,416 thousand for the medium long-term portion of payables to licensors further to current contracts for the production and marketing of designer products;

- Other long-term payables for the difference in the balance sheets of Group companies.

4.21 Share capital

On December 31, 2006 the share capital of the parent company Safilo S.p.A. stood at Euro 35,000,000, divided in no. 35,000,000 shares with a nominal value of Euro 1.00 each. Therefore no changes were made in the capital since December 31, 2005.

4.22 Share premium reserve

The share premium reserve amounts to Euro 53,350 thousand and consists of:

- Euro 29,000 thousand, the higher price paid, compared to the nominal value of the increase in share capital, deliberated by the Extraordinary Shareholders' meeting on April 30, 2003;

- Euro 24,350 thousand, the higher price paid, compared to the nominal value of the increase in share capital, deliberated by the Extraordinary Shareholders' meeting on May 19, 2004;

4.23 Retained earnings (losses) and other reserves

The retained earnings and other reserves include both the reserves of the subsidiary companies generated after their inclusion in the consolidation area and the currency differences deriving from the translation into Euro of the financial statements of consolidated companies denominated in currencies other than Euro.

(Euro/000)	January 1, 2005	Previous year's profit allocation	Impact on equity	Impact on P&L	Dividends distribution	Change in consolid. area	December 31, 2005
Group translation difference	(4,738)	-	9,946	-	-	-	5,208
Translation difference - Minority Interests	(105)	-	207	-	-	-	102
Total	**(4,843)**	**-**	**10,153**	**-**	**-**	**-**	**5,310**
Other reserves - Group	(35,394)	21,610	292,207	1,695	-	-	280,118
Other reserves - Minority Interests	2,055	3,123	-	62	(3,025)	-	2,215
Total	**(33,339)**	**24,733**	**292,207**	**1,757**	**(3,025)**	**-**	**282,333**
Total	**(38,182)**	**24,733**	**302,360**	**1,757**	**(3,025)**	**-**	**287,643**

(Euro/000)	January 1, 2006	Previous year's profit allocation	Impact on equity	Impact on P&L	Dividends distribution	Change in consolid. area	December 31, 2006
Group translation difference	5,208	-	(17,473)	-	-	-	(12,265)
Translation difference - Minority Interests	102	-	(104)	-	-	-	(2)
Total	**5,310**	**-**	**(17,577)**	**-**	**-**	**-**	**(12,267)**
Other reserves - Group	280,118	10,442	(14,503)	-	-	294	276,351
Other reserves - Minority Interests	2,215	3,220	(34)	-	(3,063)	(294)	2,044
Total	**282,333**	**13,662**	**(14,537)**	**-**	**(3,063)**	**-**	**278,395**
Total	**287,643**	**13,662**	**(32,114)**	**-**	**(3,063)**	**-**	**266,128**

4.24 Fair value and cash flow reserves

The account is comprised as follows:

(Euro/000)	Balance at January 1, 2005	Impact on equity	Impact on P&L	Balance at December 31, 2005
Cash flow reserve	(3,637)	(2,780)	3,637	(2,780)
Fair value reserve	(2,705)	(452)	2,038	(1,119)
Total	**(6,342)**	**(3,232)**	**5,675**	**(3,899)**

(Euro/000)	Balance at January 1, 2006	Impact on equity	Impact on P&L	Balance at December 31, 2006
Cash flow reserve	(2,780)	2,533	1,468	1,221
Fair value reserve	(1,119)	1,016	741	638
Total	**(3,899)**	**3,549**	**2,209**	**1,859**

The cash flow reserve refers to the current value of the interest rate swap contracts and to the current value of the forward currency contracts, while the fair value reserve refers to the current value of the investments classified under financial assets available for sale.

4.25 Stock option plans

On March 25, 2003, the Extraordinary Shareholders' Meetings of Safilo Holding S.p.A. (now Safilo Group S.p.A.) approved the "Stock Option Plans of Safilo Holding S.p.A. and Safilo S.p.A. for 2003-2007" (in short 2003 Plan), which provides for the free vesting of rights for the subscription of new shares issued at the current value of the company, to some employees and consultants of the companies of the Group.

On November 24, 2004, the Extraordinary Shareholders' Meeting of Safilo Group S.p.A. approved a new plan, the "Stock Option Plan of Safilo Group S.p.A. and Safilo S.p.A. 2004–2008" (in short 2004 Plan), which provides for the free vesting of rights for the subscription of new shares issued at the current value of the company, to some employees and consultants of the companies of the Group.

Further to the mandate granted by the Extraordinary Shareholders' Meeting on October 24, 2005, the Board of Directors of Safilo Group S.p.A. resolved to increase the share capital on May 31, 2006 to a maximum nominal figure of Euro 2,125,296.25 by issuing up to a maximum of 8,501,185 ordinary shares of a value of Euro 0.25 each, with a share premium of Euro 4.16. These shares had been and will be available for subscription by the beneficiaries listed in the new "Stock Option Plan of Safilo Group S.p.A. 2006-2010" that was approved by the above Board (in short 2006 Plan). This plan is valid for 4 financial periods (2006 – 2010) and, like the previous ones, is addressed to certain directors, executives and consultants of the Safilo Group and provides accruing option rights equal to ¼ for each financial period in the Plan. The accrual criteria for the options is based on reaching certain conventional EBITDA consolidated levels in the balance sheet of Safilo Group S.p.A., that have been fixed by the Board of Directors.

The fair value of the options, in accordance with the requirements of IFRS, is recorded under personnel costs with a corresponding increase in a specific equity reserve over the duration of the maturity period, as the stock option plans are on an "equity-settled" type. In compliance with the requirements of IFRS 2, irrespective of which company issues the new shares, the stock option costs is recorded in the company in which the employees carry out their employment. The amount received, net of the costs directly attributable to the transaction, will be credited to the share capital (nominal value) and the share premium reserve, when the options are exercised.

With reference to the first stock option plan (2003 Plan), the Group has decided to apply the exemption for share-based payments. In substance, IFRS 2 is applied from January 1, 2004 for all the options issued after November 7, 2002 but not matured ("vested") before January 1, 2005. The application of this exemption results in the recording of only the third tranche of the 2003-2007 Stock Option Plan as a cost in the income statement of the Group.

In December 2005 the holders of the options relative to the 2003 Plan and 2004 Plan, in consideration of the quotation of Safilo Group S.p.A. on the Italian Stock Market, exercised 50% of the rights in their possession. The beneficiaries can exercise the remaining rights in the possession respectively within June 20, 2007 and September 20, 2008.

The total of the costs allocated to the income statement in 2006 and 2005 can be summarised as follows:

(Euro/000)	December 31, 2006	December 31, 2005
2003 Plan	-	79
2004 Plan	389	1,635
2006 Plan	138	-
Total	**527**	**1,714**

The following table shows the main elements relative to the stock option plans in force:

SOP 2003-2007	2006 Strike	2006 no. shares	2006 no. rights	2005 Strike	2005 no. shares	2005 no. rights
At January, 1	2.5325	909,400	227,350	2.5325	3,932,540	983,135
Issued	-	-	-	-	-	-
Granted	-	-	-	-	-	-
Cancelled	-	-	-	-	-	-
Forfeited	-	-	-	-	-	-
Exercised	-	-	-	2.5325	(3,023,140)	(755,785)
At December 31	2.5325	909,400	227,350	2.5325	909,400	227,350
- Tot. Exercisable	*2.5325*	*909,400*	*227,350*	*2.5325*	*909,400*	*227,350*
- Max res. life (years)			*0.5*			

SOP 2004-2008	2006 Strike	2006 no. shares	2006 no. rights	2005 Strike	2005 no. shares	2005 no. rights
At January, 1	3.5438	3,037,832	759,458	3.5438	4,016,316	1,004,079
Issued	-	-	-	-	-	-
Granted	-	-	-	-	-	-
Cancelled	-	-	-	-	-	-
Forfeited	-	-	-	3.5438	(54,372)	(13,593)
Exercised	-	-	-	3.5438	(924,112)	(231,028)
At December 31	3.5438	3,037,832	759,458	3.5438	3,037,832	759,458
- Tot. Exercisable	*3.5438*	*3,037,832*	*759,458*	*3.5438*	*3,037,832*	*759,458*
- Max res. life (years)			*1.7*			

SOP 2006-2010	2006 Strike	2006 no. shares	2006 no. rights	2005 Strike	2005 no. shares	2005 no. rights
At January, 1	-	-	-	-	-	-
Issued	4.4100	8,501,185	8,501,185	-	-	-
Granted	4.4100	3,548,817	3,548,817	-	-	-
Cancelled	-	-	-	-	-	-
Forfeited	4.4100	(34,014)	(34,014)	-	-	-
Exercised	-	-	-	-	-	-
At December 31	4.4100	3,514,803	3,514,803	-	-	-
- Tot. Exercisable	-	-	-	-	-	-
- Max res. life (years)			*4.0*			

TOTAL	2006 Strike	2006 no. shares	2006 no. rights	2005 Strike	2005 no. shares	2005 no. rights
At January, 1	3.3108	3,947,232	986,808	3.0435	7,948,856	1,987,214
Issued	4.4100	8,501,185	8,501,185	-	-	-
Granted	4.4100	3,548,817	3,548,817	-	-	-
Cancelled	-	-	-	-	-	-
Forfeited	4.4100	(34,014)	(34,014)	3.5438	(54,372)	(13,593)
Exercised	-	-	-	2.7693	(3,947,252)	(986,813)
At December 31	4.1690	7,462,035	4,501,611	3.3108	3,947,232	986,808
- Tot. Exercisable	*3.3108*	*3,947,232*	*986,808*		*3,947,232*	*986,808*
- Strike range (min)	*2.5325*					
- Strike range (max)	*4.4100*					
- Max avg. Res. Life (years)			*3.4*			

5. Notes to the Consolidated Statement of Operations

5.1 Net sales

Group sales in 2006 amounted to Euro 1,121,983 thousand and report an increase of 9.4% compared to Euro 1,025,274 thousand the previous year. The slight change in the average Euro/US dollar exchange rate in 2006 compared to 2005 did not result in any significant changes: the increase with equal exchange rates would have been 9.8%.

Group sales in financial year 2005 amounted to Euro 1,025,274 thousand and report an increase of 8.5% compared to Euro 944,740 thousand recorded in the previous year. The slight change in the average Euro/US dollar exchange rate in 2005 compared to 2004 did not have a significant impact on net sales.

Refer to note 5.12 "Segment Information" for further details regarding the sales trend compared to the previous year.

5.2 Cost of sales

The account is comprised as follows:

(Euro/000)	2006	2005	2004
Purchase of raw materials and finished goods	368,522	282,892	263,126
Change in inventories	(68,411)	(7,770)	(36,722)
Payroll and social security contributions	100,500	91,278	95,846
Capitalisation of costs for increase in property, plant and equipment (-)	(10,002)	(9,851)	(7,475)
Subcontracting costs	37,313	23,275	33,473
Depreciation	20,126	25,382	24,800
Rental and operating leases	789	766	956
Other industrial costs	9,676	10,533	7,525
Total	**458,513**	**416,505**	**381,529**

The increase in the cost of materials and finished products, associated with the increase in inventories compared to December 31, 2005, is more than proportional with respect to the sales trends. This increase is the consequence of the high product demand from the market and the need to increase raw material stocks to back up the increased production levels. The increase in purchases of raw materials and finished goods in 2005 compared to 2004 relates mainly to the higher quantities of finished products acquired as a consequence of both increased sales and the "outsourcing" strategy of the company.

The changes in inventories are comprised as follows:

(Euro/000)	2006	2005	2004
Finished products	(61,170)	(913)	(36,674)
Work-in-progress	(119)	1,321	252
Raw materials	(7,122)	(8,178)	(300)
Total	**(68,411)**	**(7,770)**	**(36,722)**

With respect to the previous year, payrolls and contributions increased for the production staff of the Group increased further to the additional employees in the production departments and due to the normal trend in labour costs. Payroll and social security contributions in 2005 decreased by approximately 4.8% compared to 2004, mainly as a result of the decrease in the average number of employees in the production facilities of the Group.

The total workforce of the Group at December 31, 2006, 2005 and 2004 is broken down as follows:

	December 31, 2006	December 31, 2005	December 31, 2004
Headquarters in Padua	845	765	707
Production facilities	4,573	4,192	4,561
Commercial companies	1,083	1,053	1,024
Retail	854	374	221
Total	**7,355**	**6,384**	**6,513**

The average number of employees per category is summarised as follows:

	2006	2005	2004
Executives	77	76	76
Clerks and middle management	2,263	1,967	1,810
Factory workers	4,461	4,280	4,636
Total	**6,801**	**6,323**	**6,522**

Costs for external processing which, while being burdensome in economic terms, granted rapid increase in production capacity and guarantees good future flexibility, increased considerably compared to 2005. Compared to 2004 the costs for subcontracting costs decreased by Euro 10,198 thousand, due to the Group carrying out some of the processes directly, as previously some of these processes had been outsourced.

The other industrial costs include energy, industrial services, and maintenance and consultancy services relating to the production area.

5.3 Selling and marketing costs

The account is comprised as follows:

(Euro/000)	2006	2005	2004
Payroll and social security contributions	90,830	81,817	73,852
Commissions to sales agents	79,080	74,725	65,585
Royalty expenses	98,517	91,040	79,980
Advertising and promotional costs	88,818	78,493	76,482
Amortization & depreciation	3,227	2,545	2,360
Logistic costs	18,009	14,259	12,968
Consultants fees	3,731	3,849	4,040
Rental and operating leases	7,614	5,873	4,606
Utilities	1,276	713	347
Provision for risks	1,941	2,919	1,109
Other sales and marketing expenses	22,215	23,186	22,738
Total	**415,258**	**379,419**	**344,067**

The increase in payrolls and contributions is further to the increase in the after-sales structure, to the development of the chain of American stores and to the normal salary increases.

The increase in commissions is directly related to the increased sales, while the marketing costs increased over 2005 due to higher advertising costs to develop the sales of brands that will replace those that have expired licences, and to reinforce the image of the brands belonging to the Group.

The increase of selling and marketing expenses in 2005 compared to the previous year is a result of the increase in the after-sales structure, the development of the American retail chain Solstice and the normal salary increases. The growth in commissions to sales agents and royalty expenses is directly related to the increase in sales. The amount of royalties has been impacted by a mix of sales more focused on licensed products.

5.4 General and administrative expense

The account is comprised as follows:

(Euro/000)	2006	2005	2004
Payroll and social security contributions	54,177	48,416	52,165
Allowance for doubtful accounts	4,356	1,904	4,566
Amortisation & depreciation	13,485	7,270	8,345
Consultants fees	11,548	9,706	9,927
Rental and operating leases	6,811	6,226	5,464
EDP costs	3,743	3,543	3,469
Insurance costs	2,497	2,091	1,893
Utilities, security and cleaning	6,172	3,486	3,486
Taxes (other than on income)	2,135	2,227	2,298
Other general and administrative expenses	12,875	17,253	15,266
Total	**117,799**	**102,122**	**106,879**

The increase in personnel costs is due to the normal salary trends and increased number of employees in the Padua headquarters.

General and administrative expenses for the different Group companies decreased by about 4% as a result of cost containment activities taken by the Group during 2005 financial year.

5.4.1 Remuneration (including all possible and deferred remuneration) and benefits in kind received by Directors and Statutory Auditors

All forms of remuneration paid to the Directors and the Statutory Auditors for the year ended December 31, 2006 who were in office at the balance sheet date and also carried out their activities for the subsidiaries, amounted to Euro 12,101 thousand and Euro 83 thousand, respectively.

Name and surname	Office	Period of office	Expiry of office
Directors			
Vittorio Tabacchi	Chairman	all 2006	Approval of financial statements as at 31/12/2008
Giannino Lorenzon	Vice Chairman	all 2006	Approval of financial statements as at 31/12/2008
Claudio Gottardi	Chief Executive Officer (*)	from 3/8 to 31/12/2006	Approval of financial statements as at 31/12/2008
Massimiliano Tabacchi	Co-Chief Executive Officer (*)	from 3/8 to 31/12/2006	Approval of financial statements as at 31/12/2008
Roberto Vedovotto	Chief Executive Officer	from 1/1 to 31/7/2006	
Ennio Doris	Director	all 2006	Approval of financial statements as at 31/12/2008
Carlo Gilardi	Director	all 2006	Approval of financial statements as at 31/12/2008
Riccardo Ruggiero	Director	all 2006	Approval of financial statements as at 31/12/2008
Charles Paul Pieper	Director	from 1/1 to 15/2/2006	
Julian Masters	Director	from 1/1 to 15/2/2006	
Colin Taylor	Director	from 1/1 to 15/2/2006	
Thompson Dean	Director	from 1/1 to 15/2/2006	
Board of Statutory Auditors			
Franco Corgnati	Chairman	all 2006	Approval of financial statements as at 31/12/2008
Lorenzo Lago	Regular Auditor	all 2006	Approval of financial statements as at 31/12/2008
Paolo Mazzi	Regular Auditor	all 2006	Approval of financial statements as at 31/12/2008

(*) On August 3, 2006 the Board of Directors co-opted to replace Dr. Roberto Vedovotto, Chief Executive Officer who had resigned for personal reason, with Ing. Claudio Gottardi, whose office had been confirmed by the Shareholders' meeting on November 13, 2006. The Board of Directors meeting of August 3, 2006, also confirmed the

office and powers that had been granted on April 27, 2006 to the Chairman and Vice Chairman, and assigned the office of Chief Executive Officer to the Director Claudio Gottardi and Co-Chief Executive Officer to the Director Massimiliano Tabacchi.

5.4.2 Stock options attributed to the members of the Board of Directors and to the Statutory Auditors

Name and surname	Office	Options at the beginning of the financial year	Options assigned during the year	Options exercised during the year	Options expired during the year	Options at the end of the financial year
Directors						
Vittorio Tabacchi	Chairman	-	-	-	-	-
Giannino Lorenzon	Vice Chairman	134,909	-	-	-	134,909
Claudio Gottardi	Chief Ex. Officer	110,422	1,047,614	-	-	1,158,036
Massimiliano Tabacchi	Co-Chief Ex. Officer	19,015	306,121	-	-	325,136
Ennio Doris	Director	-	-	-	-	-
Carlo Gilardi	Director	-	-	-	-	-
Riccardo Ruggiero	Director	-	-	-	-	-
Statutory auditors						
Franco Corgnati	Chairman	-	-	-	-	-
Lorenzo Lago	Regular auditor	-	-	-	-	-
Paolo Mazzi	Regular auditor	-	-	-	-	-

5.5 Other income and expenses, net

The account totals Euro 1,384 thousand and is comprised as follows:

- Euro 272 thousand relating to the gain on assets disposals by the Austrian subsidiary Carrera Brillen (Traun), being wound up, further to selling the building where the company operated (see note 4.4).
- The remaining part mainly comes from casual profits and gains on insurance repayments.

5.6 Non-recurring operating expenses

This item amounts to Euro 6,000 thousand and mainly refers to the “extraordinary” costs further to the resignation of Mr. Roberto Vedovotto, Chief Executive Officer who resigned during 2006.

5.7 Share of income (losses) of associates

The account amounts to Euro 1,513 versus Euro 1,532 thousand in 2005 and –42 thousand in 2004, and consists of the profits and losses deriving from the equity valuation of the holdings in associated companies (note 4.10).

5.8 Financial charges, net

The account is comprised as follows:

(Euro/000)	2006	2005	2004
Interest expense on loans	22,044	34,954	34,734
Interests expense and charges on High Yield	18,651	29,773	29,575
Bank commissions	3,882	4,820	4,700
Foreign exchange rate differences	10,268	21,125	8,015
Financial discounts	5,312	5,262	4,715
Losses on disposal and write-down on financial assets	138	3,370	-
Other financial charges	2,081	237	2,879
Total financial charges	**62,376**	**99,541**	**84,618**
Interest income	1,089	820	437
Foreign exchange rate differences	13,110	11,740	17,792
Gains on financial assets disposal	282	-	-
Dividends	6	229	-
Other financial income	648	1,480	239
Total financial income	**15,135**	**14,269**	**18,468**
Total financial charges, net	**47,241**	**85,272**	**66,150**

Financial expenses are considerably lower than 2005 further to lower Group debts and reduced negative effects caused by the fluctuations in foreign currency that had greatly affected the previous year.

During 2005, the impairment of the value of the investment held in Banca Popolare Italia S.p.A., to adjust the book value to its current fair value, was recorded in the income statement for a total amount of Euro 3,370 thousand.

5.9 Non-recurring financial charges

(Euro/000)	2006	2005	2004
Accelerated fees for advance repayment	7,749	9,401	-
Fair value of non-hedging IRS	1,210	-	-
Penalty on High Yield advance repayment	-	10,106	-
Total	**8,959**	**19,507**	**-**

As already stated in note 4.14, the refinancing operation concluded by the Group on June 26, 2006 involved, pursuant to the IFRS provisions, the recording in the income statement of non-recurring financial charges for a total of Euro 7,749 thousand for accelerated fees for the advance payment of the redeemed loan.

Furthermore, as stated in notes 4.5 and 4.14, due to the same refinancing operation, some derivative contracts to hedge the cash flows for interest charges on the previous Senior Loan were not reallocated by the Group

to hedge the flows derived from the new loan, with their fair value recorded in the income statement under "non recurring financial charges".

The advance repayment of the Senior Loan and a third of the High Yield convertible bond, by using the proceeds from the Stock Exchange listing of the Group, had the following effect on the 2005 income statement:

- higher financial charges due to the accelerated amortisation of charges related to the above borrowings, in accordance with IFRS;

- a penalty to be paid to High Yield bondholders.

5.10 Income tax expenses

(Euro/000)	2006	2005	2004
Current taxes	(32,960)	(35,366)	(31,192)
Deferred taxes	2,838	23,993	10,718
Total	**(30,122)**	**(11,373)**	**(20,474)**

The year ended December 31, 2006 was characterised by a significant increase in the amount of fiscal charges compared to the previous year, due to increased profits during 2006. All the 3 financial periods were marked by a largely higher percentage than the theoretical tax rates.

Theoretical income taxes are calculated using a 33% rate on the estimated taxable income for the year. The above percentage represents the tax rate (IRES) that the income of the Italian holding company is subject to. Effective income taxes can be reconciled with the theoretical income taxes as follows:

(Euro/000)	%	2006	%	2005	%	2004
Income before taxation	***100.0***	**71,110**	***100.0***	**25,035**	**100.0**	**45,207**
Tax calculated at domestic tax rate	*33.0%*	23,454	*33.0%*	8,262	33.0%	14,918
IRAP and other taxes	*10.6%*	7,544	*27.7%*	6,926	14.3%	6,470
Effect of foreign tax rates	*-4.0%*	(2,820)	*-12.1%*	(3,034)	-	-
Income not subject to tax	*-0.5%*	(355)	*-2.3%*	(575)	-12.1%	(5,449)
Non deductible costs	*2.1%*	1,528	*13.4%*	3,347	1.8%	792
Advance taxes not earmarked	*0.6%*	420	*4.3%*	1,069	-	-
Use of tax losses carried forward	*0.0%*	(18)	*-18.7%*	(4,692)	-	-
Other permanent differences	*0.5%*	369	*0.3%*	70	8.3%	3,743
Effective tax charge	***42.4***	**30,122**	***45.4***	**11,373**	**45.3%**	**20,474**

5.11 Dividends

During the financial year ended on December 31, 2006, the Shareholders' meeting of the holding company Safilo S.p.A., on November 13, 2006, deliberated a dividend distribution of Euro 16,000,000 to its only Shareholder Safilo Group S.p.A.. The By-Law, underwritten on May 15, 2003, of the convertible bond denominated "High Yield" issued by Safilo Capital International S.A. (Luxembourg), subsidiary of Safilo S.p.A., foresee, among other conditions, limits to dividend distribution by Safilo S.p.A.. The distribution is subjected to defined parameters, given the possibility for Safilo S.p.A. to distribute dividends for amounts not higher than 6% of the proceeds Safilo Group S.p.A. received from the IPO, on a yearly basis. The amount Safilo S.p.a. has deliberated to distribute does not exceed the limits provided by the High Yield By-Laws.

During 2005 and 2004, the holding company Safilo S.p.A. has not paid any dividends to its Shareholders.

5.12 Segment information

The following information is provided with reference to the geographical areas where the Group operates. The geographical area has been identified as the primary segment. The criteria used in identifying the primary segment have been based on the modality of which management operates the Group and the way it attributes managerial responsibilities. In particular, such criteria are based on the grouping by geographical areas which are defined by the location of the registered office of each Group Company. Therefore, the sales identified in accordance with this segmentation are determined by origin of invoicing and not by target market.

At the date of the present report no secondary segments were identified. In particular, the secondary segments could be related, also in consideration of market practices, to the "distribution" system. In the circumstances, however, the distribution of the products is almost exclusively wholesale; in fact the distribution activity through points of sales directly controlled by the Group (retail sales) is marginal.

December 31, 2006 *(Euro/000)*	Italy (1)	Europe (2)	America (3)	Asia (4)	*Corporate* (5)	Eliminat.	Total
Net sales							
-to other segments	342,674	48,238	1,925	45	-	(392,881)	-
-to third parties	268,625	312,462	411,721	129,175	-	-	1,121,983
Total Net Sales	**611,299**	**360,700**	**413,646**	**129,220**	**-**	**(392,881)**	**1,121,983**
Gross Profit	**245,065**	**144,541**	**214,131**	**61,932**	**-**	**(2,200)**	**663,470**
Operating income	**44,237**	**26,799**	**37,196**	**18,899**	**(32)**	**(1,301)**	**125,797**
Interest expense							(71,196)
Interest income							14,996
Share losses of inv. - equity method	-	(1)	-	-	(104)		(105)
Share income/(loss) of associates	-	-	146	1,046	426		1,618
Income taxes							(30,122)
Net income							**40,988**
Gross profit margin	*40%*	*40%*	*52%*	*48%*			*59%*
Operating income margin	*7%*	*7%*	*9%*	*15%*			*11%*
Other information							
Segment assets	492,405	305,832	331,613	184,797	1,907		1,316,553
Investment in equity method assoc.	-	-	939	11,393	202		12,535
Unallocated corporate assets							54,084
Consolidated total assets							**1,383,172**
Segment liabilities	233,628	45,057	49,891	16,750	1,046		346,370
Unallocated corporate liabilities							639,476
Consolidated total liabilities							**985,846**
Capital expenditure	20,385	6,633	14,372	1,369	27		42,786
Depreciation & amortization	25,584	5,526	4,664	1,068	21		36,861
Non-cash expenses other than depreciation	8,835	5,681	1,723	834	-		17,073

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

December 31, 2005 *(Euro/000)*	**Italy (1)**	**Europe (2)**	**America (3)**	**Asia (4)**	***Corporate* (5)**	**Eliminat.**	**Total**
Net sales							
-to other segments	280,865	37,540	1,833	977	-	(321,215)	-
-to third parties	240,196	288,389	376,899	119,786	4		1,025,274
Total Net Sales	**521,061**	**325,929**	**378,732**	**120,763**	**4**	**(321,215)**	**1,025,274**
Gross Profit	**207,167**	**143,100**	**199,029**	**60,930**	**4**	**(1,461)**	**608,769**
Operating income	**32,128**	**51,341**	**40,996**	**20,960**	**727**	**(17,870)**	**128,282**
Interest expense							(116,164)
Interest income							14,755
Share losses of inv. - equity method	(3,370)						(3,370)
Share income/(loss) of associates			123	1,398	11		1,532
Income taxes							(11,373)
Net income							**13,662**
Gross profit margin	*40%*	*44%*	*53%*	*50%*			*59%*
Operating income margin	*6%*	*16%*	*11%*	*17%*			*13%*
Other information							
Segment assets	560,156	255,475	284,324	183,560	4,265		1,287,780
Investment in equity method assoc.			893	12,293	306		13,492
Unallocated corporate assets							89,478
Consolidated total assets							**1,390,750**
Segment liabilities	214,585	34,783	39,947	16,699	1,798		307,812
Unallocated corporate liabilities							697,182
Consolidated total liabilities							**1,004,994**
Capital expenditure	26,406	5,688	5,544	1,027	-		38,665
Depreciation & Amortization	24,999	5,615	3,601	961	21		35,197
Non-cash expenses other than depreciation	5,666	2,793	457	887	-		9,803

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

December 31, 2004 *(Euro/000)*	**Italy (1)**	**Europe (2)**	**America (3)**	**Asia (4)**	***Corporate* (5)**	**Eliminat.**	**Total**
Net sales							
-to other segments	275,951	44,587	1,088	348	30	(322,004)	-
-to third parties	221,801	280,398	342,699	99,815	27		944,740
Total Net Sales	**497,752**	**324,985**	**343,787**	**100,163**	**57**	**(322,004)**	**944,740**
Gross Profit	**192,258**	**137,793**	**181,174**	**54,454**	**58**	**(2,526)**	**563,211**
Operating income	**33,577**	**32,426**	**32,708**	**22,539**	**659**	**(10,510)**	**111,399**
Interest expense							(84,619)
Interest income							18,469
Share income/(loss) of associates	2			(111)	67		(42)
Income taxes							(20,474)
Net income							**24,733**
Gross profit margin	*39%*	*42%*	*53%*	*54%*			*60%*
Operating profit margin	*7%*	*10%*	*10%*	*23%*			*12%*
Other information							
Segment assets	405,944	254,780	265,193	175,743	1,343		1,103,003
Investment in equity method associates				9,871	296		10,167
Unallocated corporate assets							58,439
Consolidated total assets							**1,171,609**
Segment liabilities	178,045	37,769	42,433	16,747	5,466		280,460
Unallocated corporate liabilities							822,590
Consolidated total liabilities							**1,103,050**
Capital expenditure	21,949	5,921	2,210	972	169		31,221
Depreciation & Amortization	23,989	6,893	3,848	762	13		35,505
Non-cash expenses other than depreciation	4,522	3,852	4,261	1,202	-		13,837

(1) Includes operating companies with registered office in Italy.
(2) Includes operating companies based in European countries other than Italy, in India and South Africa.
(3) Includes companies based in USA, Canada and Brazil.
(4) Includes companies based in the Far East and Australia.
(5) Non-operating companies.

6. Transactions with related parties

The nature of the related party transactions is given in the following table:

Related parties *(Euro/000)*	Relationship	December 31, 2006	December 31, 2005	December 31, 2004
Receivables				
Elegance International Holdings Ltd	(a)	-	750	525
Optifashion As	(b)	4	-	-
Safilens S.r.l. (*)	(a)	-	207	-
Total		**4**	**957**	**525**
Payables				
Elegance International Holdings Ltd	(a)	10,360	8,533	10,715
Safilens S.r.l. (*)	(a)	-	22	-
Total		**10,360**	**8,555**	**10,715**

Related parties *(Euro/000)*	Relationship	2006	2005	2004
Revenues				
Elegance International Holdings Ltd	(a)	611	578	4
Optifashion As	(b)	221	179	268
Safilens S.r.l. (*)	(a)	-	2	-
Total		**832**	**759**	**272**
Costs				
Elegance International Holdings Ltd	(a)	27,192	20,673	21,654
Safilens S.r.l. (*)	(a)	-	81	387
TBR Inc.	(a)	1,152	1,107	1,054
Total		**28,344**	**21,861**	**23,095**

(a) associated companies
(b) unconsolidated subsidiaries;
(*) investment transferred during 2006 (see note 4.11).

These transactions relate to commercial relationships on the basis of prices defined at normal market conditions, similar to transactions with third parties.

Safilo USA rents its headquarters and distribution centre in the USA (New Jersey), based on a rental contract with TBR Inc., a company one third owned by Vittorio Tabacchi, Chairman of the Board of Directors and shareholder of Safilo Group S.p.A., one third by a subsidiary of the Safilo Group S.p.A. and one third by a third party. Safilo Group S.p.A. indirectly acquired the holding in TBR Inc. in 2002 for Euro 629 thousand. In 2006 the Group paid rent of Euro 1,152 thousand to TBR Inc. The price and other conditions of the rental contract are in line with market conditions for similar contracts.

Safilo Far East Limited, a subsidiary of Safilo Group S.p.A., holds 23.05% of Elegance International Holdings Limited ("Elegance"), a company listed on the Hong Kong Stock Exchange. Elegance is a producer of eyewear products in Asia, to which the Group assigns part of its production. The price and other conditions of the production contract between Safilo Far East Limited and Elegance are in line with those applied by Elegance to its other clients. Massimiliano Tabacchi, director of Safilo Group S.p.A., and Mario Pietribiasi, executive of the Group, are non-executive

directors of Elegance. In addition, Mario Pietribiasi is also a shareholder of the company with a holding of less than 0.5%.

7. Contingent liabilities

The Group does not have any significant contingent liabilities that have not been discussed in the previous notes or not covered by appropriate provisions.

Nevertheless, at the balance sheet date, various claims and legal actions that involve companies of the Group are pending. The company considers that these claims and actions are groundless, nevertheless a negative outcome of them beyond estimates could have adverse effects on the financial results of the Group.

Among the most important claims in monetary terms, we highlight: (*i*) a June 2005 claim against Safilo S.p.A. in legal fees allegedly owed to an Italian law firm for legal services provided to various companies in the Group from 1999 to 2001 related to the OPA; (*ii*) a claim alleging unfair business practices against Safilo S.p.A. by one of our clients, who later filed bankruptcy. The claim has been taken over by the plaintiff's receiver, who seeks damages; *(iii)* 2 companies, (having the same owner) that are clients of the Group, filed two claims seeking damages for breach of contract. We filed a claim against the same two companies, seeking payment owed to us for products sold.

8. Commitments

At the balance sheet date, the Group had no significant purchase commitments.

9. Subsequent events

In the period subsequent to December 31, 2006, there were no events that could be considered to significantly affect the data contained in this report.