

DANONE

06

Economic and Social Report

Interview with Franck Riboud

Building the future

Nutrition

The health imperative

Human development in emerging countries

Examples: Algeria, Egypt and Colombia



*Your Trusted Brand.
Balance in Taste & Health.*



Taste



Health



The photograph on the front cover was shot for a feature at Akbou in Algeria where Groupe DANONE has a Fresh Dairy Product plant. Algeria is a promising market for the Group, which opened plants there in 2006 in its two other business lines, Beverages and Biscuits.

Photographer:
Olivier Culmann/
Tendance Floue



In recent years Groupe DANONE, like many other companies, has published an annual business report separately from its social responsibility report. Building on the belief that both social responsibility and sustainable development must be incorporated into the daily business of the workplace and that they are neither incidental nor extraneous, DANONE has elected to publish **a single economic and social report** this year integrating all topics. This report is rounded out by two documents designed for specialist readerships: a financial reference document and a report describing social responsibility in detail, including sustainable development indicators.

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Corporate governance comprises the rules and procedures adopted by a company to reach its targets, take decisions and exercise its powers. At DANONE, governance is based on a willingness to listen.

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As the world's fifth largest food group, Groupe DANONE finds itself at the heart of health issues. Our response: make stringent health standards a principle of corporate governance.

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1966-2006: 40 years in business. A look back at an adventure initiated by BSN and pursued to this day by DANONE. We consider strategies, innovation, commitment, and the Group's ability not only to invent but also to reinvent itself.

“DANONE is a unique business that has built its success on being different. And that difference also holds the key to our future.”

FRANCK RIBOUD,
Chairman and Chief Executive Officer, Groupe DANONE



BUILDING THE FUTURE

In 2006, DANONE posted continued growth, beating targets for the year. This strong performance will underpin management's drive to build the business of the future, accelerating moves into new markets and stepping up the pace of innovation, while at the same time testing new business models. CEO **Franck Riboud** reviews highlights of the year and looks at what the future holds.

How would you sum up 2006 at DANONE?

Franck Riboud: It was another excellent year for Groupe DANONE. Organic growth was well ahead of target at close to 10%, a performance that really sets us apart in the consumer goods sector and in our highly competitive market environment.

Did temporary factors drive this performance, or do you see a more lasting basis for it?

F. R.: Market ups and downs always play a role. In 2006, for example, exceptionally strong fourth-quarter growth in China certainly had an impact, which is unlikely to last. But even allowing for that, and even if you re-weight fourth-quarter growth in China on the basis of normal levels of activity, we would still

have beaten the 6 to 8% range which we announced as our target for organic growth. That indicates that our performance was soundly based and not the result of some special event or clearly exceptional situation in one part of the world or another.

A special reason for satisfaction with 2006 results is that all regions and all business lines made a positive contribution to growth, even those that have recently run into temporary difficulties.

One example is our Biscuits line, which has suffered from slack market trends but is now back to firm growth in many countries. And looking at the geographical breakdown of sales, markets as important for us as France and Spain showed renewed pace in 2006 after going through a troubled patch.

€14

billion 2006 sales.

Number 1 worldwide in fresh dairy products

Number 2 worldwide in bottled water

Number 2 worldwide in biscuits and cereal products



“We have a responsibility to build on the good results we’ve achieved.”

FRANCK RIBOUD, age 51, Chairman & CEO of Groupe DANONE, shown here addressing a meeting of heads of Group subsidiaries in Evian (September 2006).

You have revised your target for organic growth, setting it higher for the medium term. What are the reasons behind such confidence?

F. R.: Feeling confident doesn’t mean that we can take anything for granted. We’re going to keep our eye very much on the ball. But there are also good reasons for confidence.

First of all there is the geographical balance in our business, with half of our sales outside Western Europe and a third on emerging markets. That means that our growth is not dependent on ups and downs in any one part of the world—with our broad geographical base, we can make up for the temporary lulls that are inevitable on any market.

Secondly, a growing number of countries are reporting very strong growth. When you look at DANONE’s markets you see that the subsidiaries posting the strongest growth—that is, above the 8% at the top end of our target range—are making an increasingly

important contribution to sales. In 2006 they accounted for over half the total. That will automatically generate momentum over time, which is cause for confidence. And our shareholders and investors appear to share our feeling, since DANONE shares gained over 30% last year.

Pushing into new markets and stepping up organic growth—doesn’t that weigh on profitability?

F. R.: Well, our operating margin was up for the 12th year running in 2006, which I think speaks for itself. It is a clear sign of a lastingly sound business base; proof that our growth, however strong, is under firm control and is not at the expense of profitability. Which is essential—if growth weren’t profitable it couldn’t be lasting, since we wouldn’t be able to fund it for long. That said, our business model is deliberately designed for growth. We are not going to sacrifice growth, and with it our future, so as to give margin a temporary, artificial lift. Not that it would be hard—we could add a few basis points simply by cutting a few weeks’ worth of advertising at the end of the year. But that would be putting our future at risk. What we have to do is strike the right balance between improving our profitability and growing our sales. I think we have been successful in doing just that, and it shows in our financial targets for 2007. We expect sales to grow 6 to 8% and operating income to rise by between 7 and 10%. We are thus looking forward to firm sales growth and a slightly higher rise in earnings. Which shows, first, that we are not growing at the



In Bangladesh, India, and South Africa, as in many other emerging economies, DANONE is currently developing specialties and product lines adapted to the local populations’ nutritional needs and income.

expense of profitability and, second, that improved profitability is not hampering growth and investment.

What are the main priorities in Danone’s strategy?

F. R.: We have a responsibility to build on the good results we’ve achieved. It would be a real waste if we now sat back and failed to make the most of the leeway and confidence this strong performance has given us. We need to harness current momentum to build the future. DANONE is now benefiting from the efforts we made ten years ago, and if we don’t want to find ourselves empty-handed ten years from now, we have to invent new reserves for future growth today.

That means providing vigorous support for our brands, setting up new production facilities, making major investments in research, accelerating geographical expansion and opening up future frontiers.

So moving into new countries is a major priority?

F. R.: Absolutely. Because there is enormous room for progress. Take the example of Activia. You can rightly see it as a magnificent success, with sales running at €1.3 billion and showing strong growth even on mature markets such as France and Spain, while margins are holding high with the support of a steady flow of innovation. All that is true. But if you set your sights a little higher, you see that Activia is present in only 30 countries and only a small part of its potential has been realized. If we can double the

number of countries where the Activia brand is sold and maintain the pace of organic growth, you’re looking at annual sales of potentially €5 billion a few years from now. I don’t believe that is beyond reach.

Do you have definite targets in mind when you talk about geographical expansion?

F. R.: Taking all our business lines together, Groupe DANONE is now firmly established in only around 40 countries. I think we should be able to double that number in years ahead. We have the financial resources we need to make several acquisitions every year, especially because our potential partners are generally small to medium-size operations serving local markets. Over recent months, we have moved in this direction with investments totaling €600 million. In some cases, we have reinforced our existing positions—an example being China, where we acquired an interest in Hui Yuan, the leader for fruit juices, and set up a crucial strategic partnership with Mengui, number one for milk. Similarly, in Algeria, we set up a new bottled water operation and built a new biscuit factory. At the same time, we have moved into new countries including Egypt, Thailand and Colombia for fresh dairy products and Denmark for biscuits. And there’s more to come.

Can we expect some major acquisitions?

F. R.: Not necessarily, as I’ve always said in the past. As I just noted, local businesses in our sectors are no more than medium-sized. On top of that, we now have the capacity to start out in a new country from

New markets

In 2006, DANONE invested €600 million

to raise its international profile by acquiring local players or joining forces with them. Initiatives in recent months are in China, Thailand, Ukraine, Egypt, Denmark and Colombia.

“Our business model is unashamedly designed for growth and it enjoys our full, unqualified attention.”

“At DANONE, commitment to health is structural and has led to radical strategic decisions.”

998

product launches in 2006, including 495 fresh dairy products, 272 biscuits and 231 beverages.

scratch, or almost. Which means buying or partnering with the local leader isn't the only path to rapid success. We can start out with nothing or buy the number-three or number-four business, as we did in Egypt, where our market share jumped from nil to over 12% in only a year. We also need to use the markets where we have a strong presence as regional platforms for expansion into neighboring countries. As an illustration of this, over recent months we have made a successful move into Chile from our base in Argentina.

How fast are you planning to expand?

F. R. : We're talking about three to five new countries a year. We have the expertise, the marketing concepts, the organization and the financial resources we need for that. As is often the case, pace will depend to a large extent on our success in finding the people we need to lead expansion. That's a challenge, but it's a positive challenge and one we are well equipped to meet.

Your markets are fiercely competitive. What special strengths does DANONE have to deal with that?

F. R. : I believe that DANONE has truly unique expertise in its businesses. We are the uncontested world leader for fresh dairy products, and—even more importantly—we are the only business in this sector present in some 40 different national markets, whereas our competitors are content with four or five or ten. We are also the only one to line up four dairy-product brands boasting sales of over €1 billion each—Activia,

Actimel, Taillefine-Vitalinea and Danonino, or Petit Gervais aux Fruits as it is called in France. We also have outstanding expertise in natural waters, especially mineral and spring waters, with top brands such as Evian, Volvic, Aqua and Bonafont. And we are now leveraging that expertise, the strength and the credibility of our brands, to widen their scope to new beverages that match the expectations of society and strong consumer demand for naturally healthy products.

Don't all food companies claim to sell healthy products?

F. R. : To that, I would say that our health positioning is genuinely distinctive and gives us a real lead on the competition. For DANONE, this isn't about changing our advertising in response to social concerns that we've only just become aware of. It's a longstanding commitment that you can trace back to the discovery of the benefits of Evian water in 1789 and the first sales of Danone yogurts in pharmacies in 1919. At DANONE, commitment to health is structural and ten years ago led to the most radical strategic decisions ever seen in the food industry.

We sold off operations in confectionery, packaging, ready-to-serve dishes, beer, and other segments that then accounted for 30% of our sales to focus on three core businesses, each with a special relationship to health and nutrition. That move has given us the widely recognized credibility that we now enjoy. Our approach to health also sets us apart. At DANONE, health isn't just about limiting some types of ingredient to



1/ Ukraine: DANONE supplies 8,000 small shops after expanding its fleet of trucks and revamping delivery routes. **2/** Egypt: Most DANONE products are sold in local shops. **3/** In Malaysia, modern supermarkets are already common.

make for better nutritional balance in our products. We do that too, of course—and our biscuits have made spectacular progress in that direction—but it's an essentially defensive strategy, and we look beyond it. Our goal is products that offer added health and well-being by fueling growth, for example, or by regulating digestion, what we call active health.

It sounds as if you are moving into pharmaceuticals.

F. R. : No. Medical treatment is completely beyond our scope. Our expertise is in prevention and comfort. And, of course, we are in the food industry—not chemicals or pharmaceuticals. Our concern is with natural good health, which for us is inseparable from taste and pleasure. Our researchers, biologists and development teams throughout the world look for natural ingredients that offer real benefits, as do certain cultures and fruit varieties. They then find the best way to put these benefits to work and develop recipes for tasty, appealing products that people will enjoy. We have no desire to make pills.

In many parts of the world, there are plans to tighten regulation of the food industry. Do you consider that a risk?

F. R. : On the contrary. We favor strict standards, in particular as regards health claims, which we believe should be backed by clinical trials. The structure and scale of our research teams reflect our conception of responsibility in this area. We have dozens of specialists working on these questions because scientific evidence for the health benefits

of our products is absolutely essential to lasting credibility with consumers and society at large. We take the same approach to communications and consumer information, for example in nutritional labeling. Strict standards are our responsibility—but they're also in our interest.

You have often described corporate responsibility as a source of competitive differentiation for DANONE.

F. R. : Corporate responsibility is in our genes. A look at Antoine Riboud's speeches, which have recently been republished in France, will show you that it has structured our business philosophy for the past 40 years. At that time, when people hadn't yet begun to talk about sustainability, DANONE had already adopted a dual project aiming for both business success and social progress. I stress the word "both" because what is involved is a truly integrated approach and not looking after business on the one hand and social responsibility on the other. Without that integration, corporate responsibility and sustainability wind up in the hands of a few specialists with a marginal place in the business and no leverage to effectively influence its operation. We have long been convinced that a demanding approach to corporate responsibility can be a source of strength for the business, leading to the adoption of solutions that benefit everyone.

To take a concrete example, reducing packaging volumes reduces both the environmental impact of our operations and, in a very direct way, our production costs. This integrated



Eating around the globe

DANONE has created maps covering

17 countries to identify nutritional deficiencies and surpluses by region, then adapt product formulations as a result. Example: Danonino, a dairy specialty for children, is enriched with vitamin A and zinc in Brazil, with calcium and vitamin D in Poland, and with iron and vitamin C in Mexico.



1/ Evian, a mineral water acknowledged for its health benefits, is marketed in 140 countries. 2/ Slimline dairy products Vitalinea/Taillefine were launched in France as early as 1964. 3/ Danone Biscuits China launched Jia Gai, a biscuit that has been enriched in nutrients like calcium.



“In Bangladesh I came across a way of life I knew nothing about. I was most struck by the sincerity and the sense of hope of the people I met.”

ZINÉDINE ZIDANE, ambassador of DANONE's Program for Children.

“Social responsibility and business success must be part of a single integrated approach.”

approach is also behind DANONE Way, a program we launched seven years ago to help our subsidiaries assess their own performance in the field of social responsibility. DANONE Way is based on the belief that our teams will be more motivated if they make their own diagnosis and identify room for progress themselves. This year the same commitment led us to set up a Social Responsibility Committee within the Board of Directors. This Committee, operating at the highest level in our organization, has exactly the same status as other Board Committees with more traditional business and financial concerns—for example, the Audit Committee. We are among the first to have a committee of this kind.

Presumably, this Committee's job is to oversee compliance with essential principles.
F. R.: Yes, but its scope goes beyond compliance in the strict sense of the word. Obviously we have to unfailingly abide by

the most demanding rules in areas of corporate responsibility. But that alone is not enough. DANONE owes it to itself to take things a step further, aim higher, work in new directions. We want to do more than meet requirements, we want to take the initiative for progress. In keeping with this approach, we have extended DANONE Way to include social innovation in our fundamentals, thus encouraging our subsidiaries to explore new possibilities. We have also launched danone.communities, a highly innovative program that doesn't really fit into any of the usual categories.

Could you tell us more about it?
F. R.: The project started out with thinking about our mission—bringing health through food to a maximum number of people—and our growing experience in developing countries where that mission is often a huge challenge. How can you bring products to a majority of people when a third or a half of the population live below the poverty line? Thinking along those lines has led us to launch successful initiatives with our Affordability Programs, putting our products and the health benefits they provide within the reach of people with very limited resources in China, Indonesia and other countries. But cost-cutting has its limits, and we're still unable to reach many people at the bottom of the social pyramid—the families that have to live on two euros a day or less. We realized that achieving that requires a new business model, very different from

our existing one, with different ways of doing things, different rules and different priorities. That is the thinking behind the project we launched in Bangladesh alongside Grameen, the group headed by Nobel Peace Prize winner Muhammad Yunus. Considering the interest the project has attracted and its encouraging preliminary results, we've decided to move ahead, promoting this type of initiative on a larger scale, with the participation of all interested parties. That is the idea behind the project danone.communities. In concrete terms, it involves setting up an investment fund dedicated to support and ongoing assistance for a new kind of business that makes the social impact of its operations the first priority—by reducing malnutrition and poverty, for example, or creating jobs in the local community. This fund will be open to anyone who wants to make a prudent, meaningful investment that will contribute to social development (read more about danone.communities and Grameen DANONE on pages 45 and 96).

What are Danone's reasons for launching the project? What do you expect to gain?
F. R.: Looking at the long term I would say that it is in the interest of any firm to help promote development and raise standards of living. But that's not the immediate consideration for us. This kind of initiative helps us to better understand some types of market and, most importantly, it keeps us from getting complacent. It forces us to be more innovative, more agile—and to acquire new expertise for a broader vision. It also gives us closer, more meaningful relationships with our employees and shareholders. Perhaps this will sound naive, but I would like to think that people could choose to work with us or invest in Danone not only because of our growth potential, the power of our brands, the quality of our staff or our commitment to health, but also because we want to be more than an international business, because we want to make ourselves useful in other ways too. That's certainly naive, but I think you need to be at least a little naive to move an enterprise forward.

2007 Objectives
Organic sales growth between 6% and 8%.
Operating income growth between 7% and 10%.
Operating margin of over 20 points (on a like-to-like basis and at constant exchange rates).
Earnings per share over 10%.

MUHAMMAD YUNUS, Nobel Peace Prize laureate and president of the Grameen Bank
“With DANONE we have taken a giant step.”

“The Grameen Danone Foods joint venture shows that it is possible to do business differently. It sets an example that others will perhaps follow. Profit is no longer an end in itself, but the means to social ends. The money this business generates can be reinvested and maximized, and continue to serve a cause.”



*Cada vez más gente
lo elige como postre.*



PERFORMANCE

CLOSE-UP ON GROUP BUSINESS

In 2006, Groupe DANONE posted its best performance ever in terms of organic growth. Drivers were expansion into new geographical markets, rapid deployment of brands clearly positioned for health benefits, and an unrelenting focus on new-product development. A review by business line.

9.7%

Organic growth in sales/

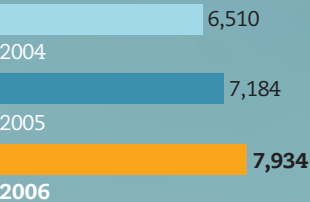
During the year sales from existing business rose 9.7% to €14,073 million, one of the strongest increases in our history. Vigorous growth was visible in all three core businesses and in all geographical markets.

KEY FIGURES

FRESH DAIRY PRODUCTS

28,757 employees
No. 1 worldwide in FDP
Sales: €7.9 billion
56.4% of total Group sales

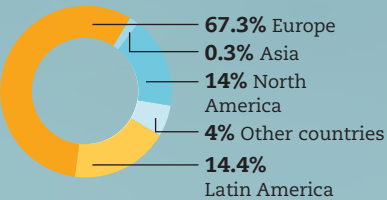
→ SALES (€ millions)



→ YEAR-ON-YEAR CHANGE IN OPERATING MARGIN

2005	13.4%
2006	14%

→ SALES BY GEOGRAPHICAL MARKET



→ SALES OF BLOCKBUSTER PRODUCTS

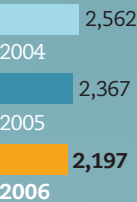
Activia: €1.3 billion
Actimel: €1 billion
Vitalinea: €900 million
Danonino: €800 million

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BISCUITS

14,740 employees
No. 2 worldwide in biscuits
Sales: €2.2 billion
15.6% of total Group sales

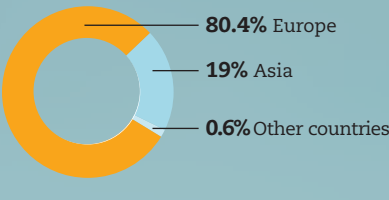
→ SALES (€ millions)



→ YEAR-ON-YEAR CHANGE IN OPERATING MARGIN

2005	13.7%
2006	13.7%

→ SALES BY GEOGRAPHICAL MARKET

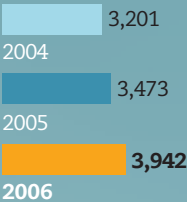


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BEVERAGES

43,253 employees
No. 2 worldwide in packaged water
Sales: €3.9 billion
28% of total Group sales

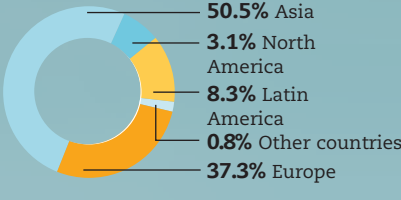
→ SALES (€ millions)



→ YEAR-ON-YEAR CHANGE IN OPERATING MARGIN

2005	12.9%
2006	12.8%

→ SALES BY GEOGRAPHICAL MARKET



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FDP business line looks to new geographical horizons

FDP's vigorous performance in 2006 rewarded two strategic priorities that had been in place for only a few months. These prioritized brands bringing strong consumer health benefits and faster geographical expansion.

DANONE's Fresh Dairy Products (FDP) line, which represents 56% of Group sales, chalked up another successful year in 2006, with sales rising 9.2%* to €7.9 billion. Growth came primarily from a significant increase in volumes, up 355,000 metric tons for the year. Profitability also rose sharply, with operating margin up seven basis points to nearly 14%. This good performance consolidates DANONE's position as worldwide leader in the sector, with 2006 market share averaging more than 35% wherever the Group does business.

GROWTH BY REGION

In Europe, growth made a comeback in 2006. A rise in French sales reflected the performances of Activia, Danette and Petit Gervais brands and the success of new launches, especially in ranges with reduced fat and sugar. In Spain, the largest single source of FDP sales revenues, volumes rose a further 3%, while Northern Europe saw growth of 8%. On surging Central European markets, sales were

up 21%, with a record 35% increase for Russia and continued double-digit growth in Poland. In the North Africa/Middle East region, the Group continued to build a solid network. DANONE is expanding rapidly in this region, investing steadily and posting across-the-board growth of around 10%. Turkey, a star performer in 2005, was the only exception amid fallout from political troubles in 2006. Latin America made another strong showing, with sales growth averaging more than 20% in Argentina, Mexico and Brazil. In 2006, our primary focus in these countries was on productivity to counter the impact of inflation. The strategy worked: prices for Danone products edged up only 0.5% on average, enabling Danone to be more competitive than other local manufacturers and make steady gains in market share. The United States saw a major breakthrough for the Group's health concept. Sales of both DANONE FDP companies in the US—Stonyfield, the leading organic producer, and Dannon—were up more than 10%, with Stonyfield holding on a firm

track and Dannon benefiting from the successful launch of Activia, which posted sales of \$130 million in its first year on the market (see p. 42). This first launch of a probiotic line in the US signals the start of a trend that will gain pace in coming years.

TWO ACTIVE HEALTH BRANDS TOP €1 BILLION

The FDP growth model relies largely on four blockbuster brands that stand apart from their competitors with clearly identified, scientifically proven health benefits: Activia to favor regularity, Actimel to strengthen the body's natural defenses, Vitalinea-Taillefine to aid weight control and Danonino to promote healthy growth in children. Together, these concept brands account for 53.2% of FDP sales. All four show double-digit growth—averaging over 15% in 2006—and are expanding into new countries every year. Activia confirmed its potential with a 48% rise in sales to €1.3 billion in

* like-for-like

(cont. page 21) → → →



1/ Launched in 2003, **Activia Laban** sold in 1-liter cartons (Saudi Arabia, 3 riyals or €0.6).
2/ New in 2006: **Taillefine Mousse aux fruits** (France, €2.10 per 4-pack, 88g servings).
3/ **Blueberry Actimel** (UK, £2.34 for an 8-bottle pack, or €3.45) 4/ 2007 innovation: **Essensis** (France, €2.05 per 4-pack). 5/ 2006 launch by Dannon: **Activia** (USA, \$2.49 per 4-pack, or €1.89). 6/ Turkish version of Danonino: **Danonino** (Turkey, 0.184 new lira per 4-pack, 75g servings; €0.99).

3 billion

or, more precisely, "3 x 1 billion". In 2006, for the first time, two brands—Activia and Actimel—each recorded over €1 billion in sales. FDP operating profit also reach €1 billion.

Infant food—Blédina/ Net sales of Blédina baby food rose 6.6% from €442.2 million in 2005 to €471.5 million. At year-end 2006, the brand accounted for 48.6% of all infant foods sold in large and medium-size supermarkets in France, up 1.9% from 2005. Full-year, Blédina's market share rose 1.4% in 2005 to 47.7%.



1/ Milkuat, enriched with 5 vitamins and calcium (Indonesia, 1,000 rupiahs or around €0.1). 2/ Yogurísimo sold under the La Serenisima brand (Argentina, 1kg bag, 2.39 pesos or €0.48). 3/ Danone Nature (Egypt, 0.97 Egyptian pounds per 120g tub, or €0.13). 4/ White-chocolate flavor Danette (Brazil, 1.89 reals, or €0.68). 5/ Launched in 2004: Danacol (France, €3.49 per 6-pack). 6/ Launched in 2006: Shoktidoi (Bangladesh, 5 takas or around €0.06 per serving).



2006, while Actimel scored the second highest growth with sales up 12% to €1 billion. Vitalinea and Danonino also made good progress, reporting sales of over €900 million and €800 million, respectively. Leveraging our experience with these four brands, we have developed new products with a marked focus on health benefits backed by a significant research commitment. These efforts paid off in late 2004, when we launched Danacol, a dairy product that helps fight bad cholesterol. Today, Danacol is sold in ten countries, bringing in sales revenues of over €100 million. In 2006, the Group moved into dermo-nutrition, a new niche in the active health market, as FDP prepared for the launch of Essensis. Fortified with borage oil and other nutrients, plus green tea for its antioxidant effects, this new dairy product helps keep skin cells hydrated. Launched almost simultaneously in Belgium, Spain, Italy and France in early 2007, it has received an enthusiastic response from retailers and is off to a strong start.

STEPPING UP GEOGRAPHICAL EXPANSION

FDP plans to double tonnage sold over the next few years, with acquisitions and new businesses providing much of the momentum. Since early 2006, Danone has established a presence in Ukraine, launched operations in Egypt and signed a joint venture agreement in Colombia. Several acquisitions quickened the pace of FDP's Asian expansion in 2006. A joint venture with Mengniu will

As markets open up in new countries, business is set to double.

help the Group tap the potential of the Chinese market (see below) and in 2007 Danone will launch several flagship products in Thailand under an agreement with Dutch Mill Co. In Japan, Danone recently acquired full control of the joint venture set up several years ago with local companies Calpis and Ajinomoto, clearing the way for the new Danone Japan to begin an investment drive backing the growth of Group brands. Fresh Dairy Products also plans to expand through a new hub system that will leverage Danone's production tools in large countries, using exports to establish an initial presence on neighboring markets prior to investing in local plants. In the short and medium term, Argentina could, for example, serve as a base for supplying fresh dairy markets in Chile, Uruguay and other Latin American countries. With this hub strategy and selected acquisitions, the business line plans to move into an average of three to five new countries annually over the next few years. ●

2 million

bottles of Milkuat are sold daily in Indonesia. Sixty percent of Indonesians live on less than \$3 a day (about €2.25) while many are paid daily wages and thus buy only small quantities at a time. Priced at 1,000 rupiahs (€0.10), Milkuat is tailored to local purchasing power and consumer habits, while its formulation—30% protein, and enriched with five vitamins and calcium—is adapted to nutritional needs. In 2006, Milkuat sales rose 70%.

Tackling markets nationwide in China/ In China, 2006 brought a joint venture between DANONE and the country's leading producer of fresh dairy products, Mengniu Dairy Company Limited. While per capita consumption of FDPs remains low, consumers are increasingly health and diet-conscious, which makes for major growth potential. The new company is positioning itself to develop, produce and distribute FDPs nationwide. Mengniu is listed on the Hong Kong Stock Exchange and has sales of €1 billion. A young company, it is expanding 25 to 30% a year and currently operates 20 plants in 15 provinces. DANONE plans to leverage these to build a distribution network covering all of China.

BISCUITS business line enters a new phase of growth

Number two worldwide and number one in 75% of the countries where it does business, DANONE's Biscuits line strengthened its position around the globe with rising sales and consistently high operating margins in 2006.

After two years of consolidation, repositioning, and reshaping its product portfolio, the Biscuits line posted organic growth topping 3% in 2006, up from 1.5% in 2005. Buoyant European sales made a strong contribution, rising 15.5% in Poland, 11.5% in Spain, 10% in the Netherlands and around 5% in both Italy and Greece.

Performance also benefited from a turnaround in France, which accounts for over 40% of sales. LU was the only brand to grow faster than the market, outpacing competitors with rises in both volumes and revenues to bolster its number-one place.

Results were more mixed in Hungary, the Czech Republic and Russia, where the Biscuits line has begun an overhaul of its brand portfolio on the basis of the model that has proved so successful in the rest of Europe. The new portfolio will focus on more premium or added value products, where DANONE's expertise in production,

marketing and research put the Group ahead of competitors.

In Asia, which accounts for nearly 20% of DANONE's total biscuit sales, the Group is solidly positioned as No. 1 or a strong No. 2 in Malaysia as well as in Indonesia, China and India, the continent's three largest markets. Malaysian and Chinese sales were particularly robust, with respective gains of 14% and 10%. Success in China stems partly from the winning affordability strategy pursued over the past few years. This offers nutritionally fortified products at low prices alongside higher-end brands.

SIX BRANDS, 17% OF SALES

The success of our Biscuits business line is largely attributable to the strategy we adopted in 2003, focusing on a few simple principles: optimizing production capacity, improving the nutritional profile of our products and stepping up marketing and advertising efforts to emphasize the high nutritional value of biscuits, especially their high grain content.

Our strategy also targets expansion into new geographical markets such as Algeria, where we are currently building a plant.

Finally, we are working to expand our network of neighborhood outlets, including service stations and vending machines, which offer enormous potential and account for only 4% of sales.

The business line's strong showing in 2006 also reflected good performances from Tuc, Mini-Star, Mikado, Ourson, Petit-Déjeuner and Cracotte, six star brands based on concepts that can be adapted to a variety of international markets. Each has a distinctive feature rooted in DANONE expertise—a special shape, a health benefit, or a production process—that sets it apart from competitors and makes it hard to imitate. These high-power brands have also shown that they can sell successfully in similar versions across a wide range of countries. In 2006, they accounted for 17% of the business line's sales outside Asia and posted average growth of 15%, underscoring their potential. ●

Mikado/ Mikado's strong performance (sales up over 10% in 2006) stems directly from the brand's steady stream of new products—including, in France, a milk-chocolate variety in 2003, caramel chocolate in 2005 and chocolate hazelnut in 2006—combined with successful repositioning as a specialty for young adults. Advertising reflects this focus, with a fresh, irreverent tone underscoring Mikado's appeal for consumers aged 18 to 35. To meet demand in the nine countries where these chocolate-dipped stick biscuits are sold, a new production line was inaugurated at year-end 2006 at the LU plant in Cestas in southwestern France.



1/ New in 2006: **Mini Jaffa** (Finland, 11.70 marks per 100g, or €1.29). 2/ **Mikado** (Italy, €1.32 per 75g pack) 3/ **Sesame TUC** (France, €0.99 per 100g pack). 4/ **Oro Tuffi** (Italy, €1.98 per 240g packet). 5/ Individually wrapped **Ourson** (France, €1.56 per 150 g). 6/ Czech variety of Mini-Star, sold as **Diskito** (Czech Republic, 1.89 koruny or €0.68). 7/ New in 2006: **Twisties** (Malaysia, 1.75 ringgits per 6-pack (10 x 60 g), €0.38). 8/ Raspberry **Craquinette** (France, €1.62 per 200g). 9/ Redesigned for Chinese consumers: **Prince** (China, 8.3 yuan renminbi per 360g pack, €0.80). 10/ Available in family-size package: **Bébé Dobre rano** (Czech Republic, 400g 8-pack for 50.7 koruny or €1.8). 11/ The ever-popular **Véritable Petit Beurre** (France, 200g pack for €0.97).

BEVERAGE line creates momentum for growth

DANONE's Beverage line reported like-for-like growth of 14.8% in 2006, benefiting from firm trends in some regions and leveraging the strength of natural water brands to grow new markets for functional and flavored products.

Beverages made a decisive contribution to the Group's business growth in 2006, with sales rising by some €500 million. Operating margin edged down amid sustained rises in prices for packaging raw materials, but held close to 13% at 12.8%.

All parts of the world contributed to this fine showing, with rapid growth in Europe driven by rises of 10% in both Germany and Spain, 26% for Poland, and Turkey and the UK recording smaller increases. Trouble spots were limited to the French market—and even there the Group's leading brands, Evian and Volvic, gained market share.

As in 2005, Asia and Latin America turned in the strongest performances. Asia, which accounts for 50% of beverage sales—and 60% of production volume—posted a growth rate of around 22% thanks to buoyant markets in China and Indonesia, where sales were up 26% and 18%, respectively, and in Japan.

Following an impressive 30% increase in 2005, Latin America provided continued growth with sales up more than 20% for the region as whole, 26% in Argentina and 20% in Mexico.

In Argentina, two major innovations—V energy drink, inspired by a successful concept from New Zealand, and flavored mineral water under the Villa del Sur brand—pumped up performance in the first half of the year.

In Mexico, the Bonafont natural-water brand further consolidated its lead, taking sales to the billion-liter mark and dominating the home and office delivery (HOD) market.

In both countries, DANONE applied the growth strategy used by the Beverages business line worldwide, capitalizing on the strength, name recognition and credibility of the Group's natural-water brands with functional and flavored products—new market segments where demand is particularly robust.

The Group's natural waters and local mineral waters have positioned

DANONE as a highly credible health brand on these segments, giving our new products a critical advantage over the competition.

NEW COUNTRIES, NEW MARKETS

The Beverages line is also targeting international expansion and opening markets in new countries, as illustrated by a number of tie-ups with leading local companies in 2006. In Denmark, for example, the Group acquired a 49% stake in the Aqua d'Or bottled water company, and in Algeria DANONE stepped up its local presence, breaking into bottled water with the acquisition of Tessala and bringing the first bottles of Hayet—the Arabic word for "life"—to market in November. Danone Tessala's goal is to develop a family brand that will set the standard for quality but remain affordable for a majority of Algerian consumers, replicating the model DANONE has used successfully in several emerging countries. •

Asia—focus on functional beverages/ Strong demand in Asia is linked to the Group's strategy of innovating in functional beverages. Example: Indonesia, where Aqua, the region's leading producer of bottled water, launched Mizone in 2006. First developed by Frucor in New Zealand and adapted for the Chinese market in 2004, this energy drink shot to the head of its category in just a few months. Likewise dairy/fruit juice beverage Nutri-Express, where sales hit €200 million a scant year after its launch by Wahaha. Finally, in Japan demand for functional beverages soared 20% following the launch of Alcalyon in tandem with Japan's Kirin.



1/ Flavored water sold under Bonafont brand **Levité** (Mexico, 1.5l bottle for 10.5 pesos or around €0.7). 2/ Pioneering design from **Evian** (France, 1 liter for €0.44). 3/ **Aqua** (Indonesia, 2,000 rupiahs for 600ml bottle, or €0.17). 4/ New in 2006; **Ser Vivactiv** (Argentina, 1.89 pesos, or around €0.45). 5/ Rolled out at year-end 2006: **Hayet**—"life" in Arabic (Algeria, 1.5-liter bottle for 25 dinars, or €0.27). 6/ Energy drink **Mizone**, a success in New Zealand, then in China; rolled out in Indonesia in 2006 (Indonesia, 3,000 rupiahs for 500ml, or €0.25).

20%

growth for Bonafont (Mexico) fueled by new product development and communications built around natural spring water. Altogether, beverages account for 28% of Group sales, up 15% on a like-for-like basis. Division sales are nearly €4 billion. Asia is the division's fastest-growing single market, up 25% in 2006.



BOARD OF DIRECTORS

Franck Riboud, 51,
Chairman and Chief
Operating Officer

Jacques Vincent, 61,
Vice Chairman and
Chief Operating Officer

Bruno Bonnell¹, 48,
Chairman, Infogrames
Entertainment

Michel David-Weill, 74,
Chairman of Supervisory
Board, Eurazeo

Emmanuel Faber, 43,
Executive Vice-President
Asia-Pacific

Richard Goblet d'Alviella¹,
58, Chief Executive Officer,
Sofina SA

Bernard Hours, 50,
Executive Vice-President
Fresh Dairy Products

Christian Laubie¹, 68,
member, Haut Conseil du
commissariat aux comptes

Jean Laurent¹, 62,
Chairman of the Board,
Calyon SA

Hakan Mogren¹, 62,
Deputy Chairman,
Astra Zeneca

Jacques Nahmias¹, 59,
Chairman,
Pétrofrance Chimie SA

Benoît Potier¹, 49,
Chairman of
Management Board,
Air Liquide SA

Naomasa Tsuritani², 62,
Senior Managing Director,
Yakult Honsha

1. Independent director.
2. Co-opted at the Board Meeting
of 14 February 2007 to replace
Hirokatsu Hirano, who resigned.
Naomasa Tsuritani will sit on the
board until the Annual General
Meeting of Shareholders in 2008,
when Hirokatsu Hirano's mandate
was due to expire.

CORPORATE GOVERNANCE

THE DANONE MODEL

Corporate governance comprises the rules and procedures adopted by a company to reach its targets, take decisions and exercise its powers. At DANONE, governance is based on a willingness to listen.

In recent years the quality of governance in big international corporations has come in for increasingly close scrutiny. Highly publicized business failures associated with fraud, mismanagement and unethical behavior, albeit exceptional, have made this a fundamental concern not only for shareholders but also for society at large. Strictly speaking, corporate governance refers to the rules and procedures adopted to achieve two fundamental goals: compliance with applicable law and regulations, and effective risk control. As a result, the concept of corporate governance is often viewed as practically identical with internal controls and risk management. Danone takes a broader view. In keeping with the principles of our DANONE Way process

for engagement with all stakeholders to drive progress at Group subsidiaries in areas under their responsibility—from labor policies to product quality to supplier and client relations—we consider decision-making as a whole. Thus, good corporate governance certainly means effective controls to ensure proper implementation of decisions. But it should also provide for decision-making processes based on willingness to listen, on dialog and on the capacity to look ahead and allow for a full range of challenges, risks and opportunities.

EFFECTIVE INTERNAL CONTROL
Good governance is impossible without mechanisms for effective control and secure operation. This

imperative defines the core mission of the Group Risks department, which combines the Internal Audit and Risk Management units and reports to the Group Secretariat General. The Group Risks department's primary responsibility is to monitor all Group companies and organizations for compliance with applicable laws and regulations, as well as with management principles, procedures, policies and other internally defined requirements. The department also assists the Group's general management and Board of Directors with the assessment and ongoing improvement of internal control and risk management procedures.

(cont. page 31) → → →



Franck Riboud and Benoît Potier,
Chairman of Air Liquide SA,
at the meeting of Group executives
at Evian in September 2006.



Activities of the Board of Directors

In 2006, efforts to enhance the efficiency of Board operation continued. The Board met five times during the year for an average of three hours per meeting. In addition to recurrent matters such as business reviews, Group finances, treasury, guarantees and endorsements granted, share buybacks and cancellation, and the adoption of financial statements, the Board considered significant acquisitions and divestments at various stages of advancement. Following a first self-assessment in 2004, a number of changes were introduced in 2005 and a new self-assessment was conducted in 2006. This led to the adoption of revised internal Board regulations at the meeting held December 15, 2006.

INTERNATIONAL AUDIT COMMITTEE

The Audit Committee met six times. It reviewed procedures adopted for the monitoring and valuation of non-current assets, in particular those relating to home-and-office deliveries in Europe, progress on Sarbanes Oxley compliance, risk monitoring and assessment, approval of internal and external audit plans, and policies for pre-approval of the statutory auditor's assignments other than those for audit purposes.

NOMINATION AND COMPENSATION COMMITTEE

The Committee met once in 2006, conducting a detailed review of all compensation and benefits granted to members of the Executive Committee. At its meeting on December 15, the Board of Directors adopted internal regulations for the Committee, defining its various assignments. In particular, it is charged with drawing up proposals

for the Board of Directors regarding the appointment of Directors; preparing deliberations of the Board on governance issues; conducting, at their request, assessments of the Board of Directors and the Audit Committee; proposing criteria for all forms of executive compensation; making proposals to the Board for the grant of stock options or free allotments to senior executives; proposing the distribution of Directors' fees; and, in a general way, drawing up any recommendations on group compensation policies that the Board may ask for.

MANAGEMENT COMPENSATION

Management compensation is made up of a fixed salary and a variable bonus representing between 40 and 60% of the total. Bonuses are determined on the basis of business, staff development and individual targets. For all members of the Executive Committee, bonuses are based on a combination of quantitative business targets and qualitative assessments of strategy pursued over the year. In the cases of the Chief Executive and Chief Operating Officer, the business criteria for bonuses are the Group targets for sales, operating margin on ordinary business, free cash flow and net ordinary income per share announced to financial markets. The business criteria used in the calculation of the bonuses of Executive Committee members in charge of a Business Line are based on the Business Line's budget targets for sales, operating income on ordinary business, free cash flow and operating margin on ordinary business.

Quantitative criteria for other Committee members relate to Group budget targets for operating margin on ordinary business, net ordinary income per share and operating expense. The compensation of the Chief Executive Officer and the Chief Operating Officer is set by the Board of Directors on the basis of the recommendations of its Nomination and Compensation Committee. Policies governing compensation of other Executive Committee members are reviewed annually by the same Committee. Total direct and indirect compensation attributed to Directors and the 19 members of the Board of Directors and Executive Committee for the 2006 financial year came to €11.4 million. Of this, €11.1 million was attributed to Executive Committee members in connection with their functions on the Committee, an amount including €6 million in variable compensation. Other benefits, including supplementary pension entitlements allocated to the same members in 2006, totaled €0.6 million. Compensation of each of the four members of the Executive Committee who are also members of the Board of Directors was as follows in 2006: Franck Riboud, Chairman and Chief Executive Officer, €2,579,100; Jacques Vincent, Deputy Chairman

and Chief Operating Officer, €1,592,980; Emmanuel Faber, Executive Vice-President Asia-Pacific, €998,084; Bernard Hours, Executive Vice-President Fresh Dairy Products, €1,364,170.

MANAGEMENT COMPENSATION

At the end of 2006 the Board of Directors decided to create a third governing body, the Social Responsibility Committee. Its mission will include the following tasks: examine the main environment-related risks and opportunities facing the Group; carry out assessments of the labor policies which the Group conducts; review reporting systems; and ensure the implementation of ethics rules defined by the Group. As regards the Group's investment in social action programs, the Committee's mission is to evaluate their impact both on local communities and on the Group; to examine how the rules drawn up by the Group have been implemented in social investment and programs; to prevent any conflicts of interest between social investment and the rest of the Group's activities; and, more broadly, to prepare and explain the Committee's work in social investment and action programs.

1/ DANIEL CARASSO
Honorary Chairman

2/ JEAN LAURENT
Chairman of the Board, Calyon SA

3/ BRUNO BONNELL
Chairman, Infogrames Entertainment

4/ MICHEL DAVID-WEILL
Chairman of the Supervisory Board, Eurazeo

5/ CHRISTIAN LAUBIE
Member, Haut Conseil du commissariat aux comptes

6/ HIROKATSU HIRANO

Adviser of the International Business division, Yakult Honsha. Naomasa Tsuritani was co-opted at the Board Meeting of 14 February 2007 to replace Hirokatsu Hirano, who had resigned. Naomasa Tsuritani will sit on the board until the 2008 Annual General Meeting, when Hirokatsu Hirano's mandate was due to expire.

7/ HAKAN MOGREN

Deputy Chairman, Astra Zeneca

8/ JACQUES NAHMIAS

Chairman, Pétrofrance Chimie SA

9/ RICHARD GOBLET D'ALVIELLA

Chief Executive Officer, Sofina SA

**AUDIT COMMITTEE**

Benoît Potier*, Chairman
Richard Goblet d'Alviella*
Christian Laubie*

**NOMINATION AND
COMPENSATION COMMITTEE**

Michel David-Weill, Chairman
Jean Laurent*
Hakan Mogren*

SOCIAL RESPONSIBILITY COMMITTEE

Jean Laurent*, Chairman
Bruno Bonnell*
Emmanuel Faber

* Independent director.



The Group Audit Charter allows internal audit teams to intervene independently and audit any group organization at any time. Moves are now afoot to streamline structures even further—not only at Group level, but also through support for each subsidiary to develop its own internal control organization.

Recent initiatives have included circulation of an updated version of Danone's Business Conduct Policies Guide (see sidebar) to each of our 9,000 managers, and publication of a Risk Management Charter to raise employee awareness and help them to assess and anticipate business-related risks more effectively.

Two thousand and six also saw the deployment of Vestalis, a software package that ranks and maps risks of all kinds—industrial, financial, environmental and regulatory—for an overview that favors quicker, more reliable decision-making.

**CONSTRAINTS
AND OPPORTUNITIES**

Throughout the year, we continued to improve our system of controls. Progress included a new employee alert system that stepped up existing anti-fraud mechanisms. Yet Sarbanes-Oxley compliance, an obligation for Danone as an NYSE listed company, remained the biggest single project. Under the terms of the Act, all companies publicly traded in the US must provide detailed information on controls, together with related tests and assessments, and although this entails significant constraints, it also offers an opportunity to gain a firmer grasp on business processes. Compliance is clearly a basic component of any governance structure, but it is no guarantee of enlightened governance, which requires a decision-making process designed to consider a full range of issues and points of view in order to reach the best possible response.

**A BROADER BASE FOR INFORMED
DECISION-MAKING**

Danone management has thus adopted working methods to open up the process, avoiding the dangers of a too narrowly focused approach and

There can be no good governance if there is no dialog with stakeholders.

gaining access to new input for more broadly based strategic thinking and better informed decisions.

In concrete terms, this starts by drawing inspiration from the ideas of local managers. Most of the ten members of the Danone Executive Committee have direct experience of operational management with at least one subsidiary, but given the fundamental role of geography in the food industry, it is crucially important to be aware of local concerns and factor these into business planning. This is the idea behind our International Committee, an informal grouping with no fixed membership that brings together the Executive Committee and some 30 managing directors heading subsidiaries in all parts of the world.

The Committee meets for three days every year, each time at a different location conducive to reflection and exchange. Participants conduct an in-depth review of strategic issues with particular relevance to current developments. Formal presentations take a backseat to open discussion allowing participants to express their points of view, clarifying points of disagreement as well as agreement. This input fuels debate within Group management throughout the year, including the annual management conference at Evian and the DANONE Way committee, helping to shape the priorities identified for discussion by the Board of Directors. At the end of September, the outcome of this process is presented to the managing directors in charge of subsidiaries and important business functions at Evian meeting—a session also attended by Board members who thus have an opportunity for direct

**Principles of
Business Conduct**

First drawn up in 1996 and updated in 2006, DANONE's Principles of Business Conduct are widely circulated among staff members worldwide. They state non-negotiable obligations for individuals and business entities. Referring to such internationally recognized texts as the Universal Declaration of Human Rights and ILO (International Labour Organization) conventions, the Principles define rules of governance and set out DANONE's commitments to consumers, customers, suppliers, employees and shareholders, along with responsibilities for the environment and to the countries where we operate. They also define the duties of employees as regards relationships with people from outside the business, confidentiality, conflicts of interest and trading in DANONE shares.



Sarbanes Oxley compliance

The US Sarbanes Oxley Act, adopted in the wake of financial scandals associated in particular with the Enron case, is intended to provide business and the financial community in general with reasonable assurance of the reliability of financial reporting. Applicable from 2006 on to all listed companies in the US and thus to DANONE, traded on the New York Stock Exchange, the Act requires a full description of internal controls, which must be tested and assessed. Meeting these requirements has been the occasion for DANONE to reinforce its internal controls and operational procedures. Against this backdrop, the group also launched Dialert, a system enabling all employees to report to group management any breaches of accounting and financial rules that might affect the reliability of accounts, and any failure to abide by our Principles and procedures or comply with anticorruption rules.

discussions with operational teams. This model for decision-making based on dialog and interchange favors the continued evolution and ripening of strategies that managers can readily accept as their own.

STAYING IN TOUCH WITH THE WORLD AT LARGE

Cultivating dialog with the broader social environment is a well established tradition at Danone. It became part of stated policy in the early 1970s and then the focus of systematic procedures as part of the DANONE Way social responsibility program (see page 30). Over time, dialog has played an increasingly important role in our governance, providing as it does the essential basis for decision-making and management processes open to the realities and ideas of society and the world at large. Dialog takes place through structures that begin at local level, requiring directors of all the Group's factories—some 200 in all—to participate actively in

community life through regular contacts with elected officials and associations, at the same time reaching out to create new opportunities for fruitful exchange. The aim in each case is to multiply opportunities for discussion. Relationships with nutritionists are one case in point.

Every year, heads of French subsidiaries hold a meeting with 12 highly reputed nutrition scientists to present their ideas and projects and hear the scientists' comments and suggestions. The following year, they come back to report on how these suggestions have been put into practice. This procedure has proven its worth in generating practical measures with significant impact. For example, dialog between Danone and consumer groups resulted in the elimination of dangerous allergens from the production cycle—just one illustration of the many benefits of a management model that makes willingness to listen a fundamental principle. ●

PHILIPPE-LOIC JACOB, DANONE Corporate Secretary “Attentive to society”

What makes DANONE attentive to its stakeholders?

To begin with, this is an integral part of our dual commitment to social progress and business success, which was clearly stated a good 35 years ago. This aspect of our approach to governance is also borne out in ratings and indexes that recognize our performance in this area.

Why is dialog with society at large important?

Listening to other people is an effective way to avoid upsets that can be put down to poor or non-existent communications

with stakeholders. Being attentive to society at large and more particularly to consumers also helps us to detect emerging trends with possibly lasting effect that can be negative—or instead offer new opportunities. To take one example, through DANONE's social watch procedure, we realized over five years ago that obesity was going to become a major social issue and that we would have to take action. Which had important implications for product development.

What about relationships with EU institutions?

For a long time we were

not much involved, but over the past few years we have been working to build stronger links. Before it adopts any new laws or regulations, the European Commission calls for input from stakeholders including businesses and consumer groups, which offers DANONE an opportunity to put its points of view and arguments. This must also bring positive effects for consumers. An example are the new restrictions on nutritional claims. While this law obviously has an impact on our business, we were in favor of it because we believe that consumers should never be misled.

DANONE Way ahead and going even further



98%

is the percentage of DANONE subsidiaries in which DANONE Way had been deployed by the end of 2006. In addition, over 800 actions had been undertaken worldwide since 2001.

DANONE Way is a unique management tool based on self-assessments covering quality, ethics, management, environmental standards and other aspects of operations within each subsidiary. Initiated in 2001, it calls on the participation of executive committees, managers and staff at all levels to provide the broadest possible base for findings. Subsidiaries' self-assessments are used to identify both strong points and areas for improvement, which are then the object of targeted action plans.

PERFORMANCE AND RESPONSIBILITY

Now, five years on, the benefits are clear in terms of business performance, staff commitment, public awareness of the DANONE group and recognition for its appeal. DANONE Way has also enabled individual

subsidiaries to gain a 360° view of their business, favoring new awareness of the progress to be made in areas relating to sustainable development, social responsibility and constructive dialog with all stakeholders. Example: DANONE Way findings helped Danone France take new initiatives to reach out to stakeholders outside the business and thus gain a clearer understanding of their perceptions and its own image. The conclusion was that while it is a recognized leader with a powerful image, Danone France is also considered remote from the concerns of its stakeholders. Action plans set up response to these findings focused in particular on reinforcing ties to consumers and customers as well as raising awareness of the broader environment within the business. Danone France's initiatives are among the 800 DANONE Way action plans adopted by Group business around the world, with 98% of these already leading to improved links to the community.

A FRESH STEP FORWARD

DANONE Way is now ready for fresh progress with a new version dubbed DANONE Way Ahead. This will pursue the twin goals of defending the Group's reputation and favoring social innovation. The first of these goals is defined in terms of 16 fundamentals that make up the essential underpinnings of socially responsible business operation. These will be applied by all Group entities and be subject to independent audits. The second goal, social innovation, involves adopting a methodical approach across the Group, with projects conducted in association with NGOs and other representatives of civil society aimed at benefiting both society at large and the business over the medium to long term. One example of this kind of project already under way in Poland is the Share Your Meal program to combat malnutrition; another is the factory built by DANONE and Grameen Bank in Bangladesh (see pages 45 and 96).

Snapshots

Executive Committee

Evian, September 2006. Members of the Group’s Executive Committee pass on the DANONE strategy to the subsidiaries at the meeting of 150 executives that takes place at Evian every year at the end of September.

- 1/ **JACQUES VINCENT**, 61
Deputy Chairman and Chief Operating Officer

2/ **FRANCK MOUGIN**, 49
Executive Vice-President Human Resources

3/ **PHILIPPE-LOÏC JACOB**, 42
Corporate Secretary

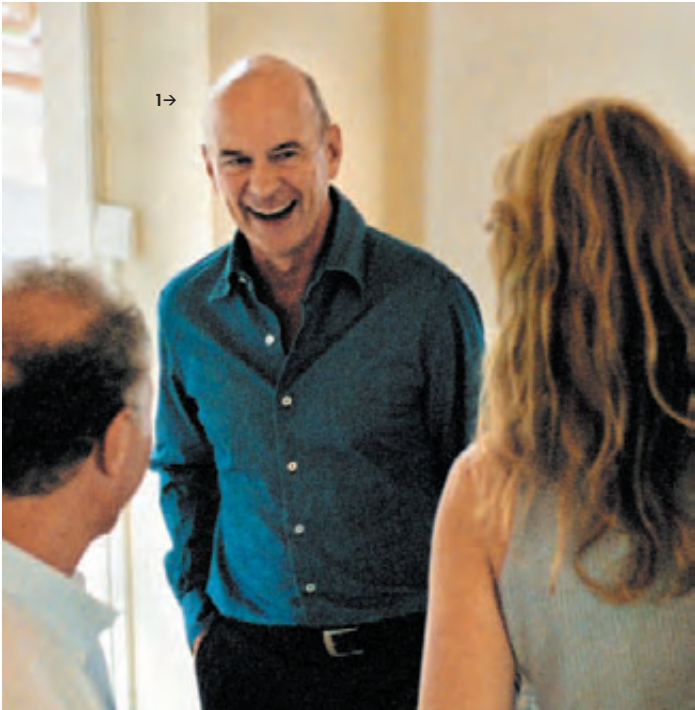
4/ **GEORGES CASALA**, 65
Executive Vice-President Biscuits and Cereal Products

5/ **SVEN THORMAHLEN**, 50
Executive Vice-President Research & Development
- 6/ **ANTOINE GISCARD D’ESTAING**, 46
Executive Vice-President Finance, Strategy and Information Systems

7/ **THOMAS KUNZ**, 49
Executive Vice-President Beverages

8/ **EMMANUEL FABER**, 43
Executive Vice-President Asia-Pacific

9/ **BERNARD HOURS**, 50
Executive Vice-President Fresh Dairy Products





THE HEALTH IMPERATIVE

Food and nutrition have become critical public health issues. As the world's fifth largest food group and a leader in healthy food, Groupe DANONE finds itself at the heart of the issue. Our response makes stringent health standards a principle of corporate governance.

50%

of the world's population —some three billion people—live on less than two euros (\$2.60) a day. According to the World Health Organization (WHO), over two billion suffer from inadequate vitamins or minerals or other dietary deficiencies. A serious situation compounded by the fact that 300 million people around the world suffer from obesity and roughly one billion are overweight.

Public health issues directly or indirectly related to nutrition have captured enormous attention over recent years, with the result that most food companies now factor health into their strategies. This is nothing new for DANONE. Concern for health has shaped the history of our group and our brands, and the DANONE name is synonymous with good health. The same is true of our core product, yogurt: developed from a Nobel laureate's work on the benefits of dairy cultures¹ in foods, it was sold only in pharmacies in the 1920s. Our focus on health is neither opportunistic nor defensive. Health plays a defining role in all our major innovations and in the long-term strategy behind the current scope and makeup of our business. The decision we made in 1996 to sharpen our focus and reduce our business lines from nine to three was a direct consequence of a conscious, pioneering commitment to nutrition and health. Today, that same commitment shapes our day-to-day operations and is built into governance principles that call for unfailing vigilance to prevent any compromise on health. Defined in terms of providing healthy food for as many people as possible, DANONE's mission makes special demands.

To ensure continuing progress towards this ideal and underpin our concrete contribution to public health, we have adopted specific, publicly stated rules to structure governance in relation to nutrition and the continuing dialog with civil society this supposes. These rules define an approach emphasizing self-regulation, close links to society at large and focused research.

PRINCIPLES OF GOVERNANCE FOR HEALTH AND NUTRITION

To meet commitments including, in particular, those set out in our Food, Nutrition and Health Charter (see sidebar opposite), DANONE has adopted specific requirements in this area, providing a clear framework for all our subsidiaries. For each product category, our International Nutrition Guidelines define maximum and minimum content for ingredients and nutrients such as sugars, fats, proteins, vitamins and minerals, in strict compliance with the recommendations of the World Health Organization, FAO² and the European Union's Eurodiet³ program. Similarly, Communications Guidelines for our marketing teams and local advertising agencies define standards for translating scientific data into advertising and presenting our major health brands to the general public, whether in the form of verbal claims



or in visuals or graphics illustrating the effects of our products.

Drawn up by multidisciplinary teams including experts from our Research & Development and Compliance departments, these guidelines set unambiguous standards. In the case of Activia, for example, they allow references to proven benefits for intestinal regularity but prohibit any reference to digestion, purification or elimination of toxins.

PRODUCTIVE TIES TO CIVIL SOCIETY

The second mainstay of DANONE's principles of governance for health and nutrition concerns relationships with the world outside our business. We support—and even initiate—national and international projects that bring business, public institutions and civil society together in constructive dialog, particularly where these projects contribute to consumer education or encourage responsible eating habits. In the same spirit, DANONE has given whole-hearted support to the recently adopted EU regulations requiring a sound scientific basis for all health and nutrition claims—which even in that case will only be allowed if the products concerned also comply with the basic prin-

ciples of a balanced diet. This means that a product with too much fat or sugar cannot be advertised for its health benefits even if it is rich in vitamin A or C. DANONE has also taken the initiative to enhance transparency, teaming up with seven other food companies to introduce nutritional labeling on the European market over the coming two years. This will apply standards recommended by CIAA, the European food industry confederation, for labels indicating calories and nutrients per portion and as a percentage of the recommended daily allowance. DANONE already has experience with this approach through our operations in the UK, where we have developed a system of easy-to-read labels for all products. The front of each package shows calories per portion and as a percentage of the recommended daily average, and a full list of nutrients appears on the back. The same principle will be extended to France in 2007, then to other parts of Europe in the near future. Obviously, the aim is not to point a finger at products that are intended mainly for pleasure, as these can perfectly well fit into a balanced diet provided enjoyment does

DANONE R&D is made up of many disciplines: biologists, microbiologists, immunologists, development engineers, sensor analysis specialists and gastroenterologists.

The Charter

A touchstone for DANONE employees worldwide, our Food, Nutrition and Health Charter reflects our willingness to make public commitments. In addition to reaffirming five core values—balance, variety, pleasure, sociability and information—the Charter commits to:

- offering products that combine good nutrition with taste appeal
- cultivating dialog with scientists
- supporting research
- promoting information-sharing with the scientific community, healthcare professionals and the general public
- being attentive to public opinion
- providing consumers with clear, transparent information
- backing product claims with scientific evidence
- practicing responsible advertising
- encouraging physical activity.

A long tradition in nutrition and health

1789/ Discovery of the benefits of Evian natural spring water by the Marquis de Lessert.

1846/ Creation of LU biscuits, packed with wholesome grains and synonymous with healthy, convenient nutrition.

1906/ Birth of Blédine, the baby food of choice for generations. Blédine's success was to lead to the foundation of Blédina in 1965.

1919/ Creation of the first Danone yogurts by Isaac Carasso in Barcelona. Made with lactic bacteria from the Pasteur Institute, these were sold in pharmacies.

1964/ Launch of Taillefine fat-free fromage frais.

1987/ Launch of Activia, a fermented dairy product that promotes regularity when eaten daily.

1991/ Founding of the first Danone Institute.

1994/ Launch of Actimel, a fermented dairy product that strengthens the body's natural defenses when eaten daily.

1996/ Strategic refocus on the Group's three core business lines: fresh dairy products; water and beverages; and biscuits and grain products.

1997/ Launch of Taillefine/Vitalinea biscuits.

1999/ Launch of Biskuat biscuits in Indonesia as part of a DANONE affordability initiative

aimed at offering highly nutritious products tailored to the purchasing power and health needs of people in the developing world.

2000/ Launch of Taillefine/Vitalinea beverages and slow energy-release biscuits.

2001/ Acquisition of an interest in Stonyfield Farm, a US maker of 100% organic yogurt.

2004/ Launch of Danacol, a dairy product fortified with plant sterols to help reduce bad cholesterol.





Transparent labeling

Over 90% of DANONE products sold in Europe display nutritional information on their packaging, showing—as a minimum—calories, protein, carbohydrate and fat per 100g (3oz) serving. On July 11, 2006, Groupe DANONE and six other food industry leaders gave the European Union an undertaking to further extend the range of nutritional information provided. Under this new commitment, the front of each package will show calories per portion and as a percentage of daily requirements. The back will present a more detailed nutritional breakdown for each portion, specifying values for protein, fat (including saturated fat), carbohydrates (including sugars), fiber and sodium, both in grams and as a percentage of recommended daily intake. This is in keeping with our goal of transparency—to educate consumers and give them the information they need to make informed purchases.

not lead to excess. This is the point of view of nutritionists generally, and DANONE will continue to count such products in its lineup. The important thing is to ensure that relevant information is clearly presented, giving consumers the facts they need to make their own choices.

FOUR KEY RESEARCH PRIORITIES

Clearly, none of our commitments could be met without the support of the credible advanced scientific expertise that plays a central role in the various stages in the business process. DANONE's R&D teams are thus the most important—or at least the most demanding—contributors to health and nutrition governance within our group, ensuring a sound scientific basis for the quality of our products and the benefits they provide. DANONE R&D counts over 900 people from more than 20 different countries around the world. Among them are some 700 researchers with advanced know-how in fields that include biology, microbiology, molecular biology, gastroenterology, nutrition and food safety. These researchers pool their expertise to focus on four key priorities: active health, or a product's demonstrable bene-

fits on human health; nutrition and the continuing drive to improve the nutritional quality of our products; affordability, through the use of new techniques and ingredients to put products within reach for as many people as possible, even in developing countries; and, finally, the sheer pleasure of food, which remains essential—no matter how healthy the product, if it has no taste appeal it will simply go uneaten, and its benefits will be lost.

In line with these priorities, our first concerns are health and nutrition, which together account for four out of five projects. Most partnerships with science institutes outside the business also focus on the same themes.

OVER 200 RESEARCH PARTNERSHIPS

Partnerships with science institutes in the public and private sector make a key contribution to DANONE'S R&D strategy, reflecting our awareness of the complexities of progress in health and nutrition, which calls on advanced expertise in a wide range of highly specialized fields. To gain access to these essential resources, we forge many differ-

(cont. page 43) → → →



The Daniel Carasso Centre houses the "Atelier", a consumer space opened in 2006. It is designed to involve consumers in product and packaging development processes. The Atelier is also a source of new ideas serving all three business lines.

AGNÈS MARTIN, Director of Nutrition and International Coordination at the Danone Institutes

Danone Institutes: championing the cause of nutrition



Agnès Martin reviews the missions and operations of the independent non-profit Danone Institutes.

What is the role of the institutes?

The 16 Danone Institutes around the world have three goals: promoting research to increase nutrition knowledge, keeping healthcare and education professionals informed, and raising public awareness of important food issues. In short, they enhance, update and disseminate scientific knowledge of nutrition. Each institute sets up programs addressing local issues, organizes workshops and symposia, and develops and disseminates publications on nutrition themes. DANONE set up the Institutes in 1991, continuing and reinforcing a close, long-term involvement in health issues. They also illustrate our commitment to making a contribution to community life that goes well beyond making food products. Altogether, Danone

Institutes now count more than 220 recognized nutrition experts, who work in public organizations, hospitals, universities and research centers.

How do the Danone Institutes work?

Every institute has a six- to 25-member Scientific Council that defines programs and communications priorities. Strategic and financial decisions are made by a Board of five to eight scientists and DANONE representatives, who also serve as the institute's contacts with the press and other organizations. I should also stress the importance of ethics for the institutes. And of course their programs have no commercial content of any kind.

What sort of projects are the institutes involved in?

In 2006, for example, Italy's Danone Institute began providing doctors with training in pediatric nutrition—and that's in addition to the annual nutrition programs for pediatricians that the Institute has offered since 1998. In Germany, the Danone Institute has just released a series of television commercials on child nutrition. And since 2004 the Institute in France has run a program encouraging French healthcare professionals to track children's weight so that obesity risks can be detected as early as possible. On the research front, the Institutes sponsor a wide variety of projects on food, nutrition and child development in different parts of the world. Since their creation in 1991, Danone Institutes have sponsored over 700 research programs worldwide. The Institutes have also organized more than 135 conferences, brought out 75 publications, and set up 72 public education programs.

Danone Nutrition Prize

Since 1998 the Danone Institute has awarded its Danone International Prize for Nutrition. Every two years it rewards a researcher or research team whose work in the field of nutrition has made a major contribution to improving public health.

16

Danone Institutes worldwide

Germany, Belgium, Canada, China, Spain, the United States, France, Israel, Italy, Japan, Mexico, Poland, the Czech Republic, Russia, Turkey, and the International Institute.

For more information/ Each Institute has its own website, providing a wealth of information in the language of the host country for professionals and laypeople alike. Visitors to these sites can find answers on local health and nutrition issues, subscribe to e-newsletters, and download books, newsletters, educational kits and other documentation. Links to all of the sites can be found at www.danoneinstitute.org

Activia takes the American market by storm



The New York Times, December 28, 2005. A front-page article spotlights the benefits of Activia.

Danone's association with probiotics goes back nearly 90 years, to our first yogurt product. Spurred by health concerns and numerous scientific discoveries, the probiotic segment is now among the most dynamic in the market for fresh dairy products. Activia is a perfect example of this trend. Daily consumption of Activia yogurt, made with the probiotic bacterial strain Bifidus Essensis, helps restore regularity in just two weeks. Its scientifically proven benefits are now winning favor around the globe. Americans—who consume only 6kg (13 pounds) of dairy products annually, compared with nearly 33kg (73 pounds) for the French—first discovered Activia in 2006. In a country where a healthy diet is often equated with supplement pills and 70 million people suffer from irregularity, Danone US faced the challenge of making the public aware of the then little-known benefits of probiotics and the science behind them. Despite these handicaps, the new concept was a resounding success with distributors and consumers alike. With sales reaching \$130 million in just one year, Activia has gone down as one of the most spectacular product launches in US history.

FIGURES SPEAK FOR THEMSELVES
This formula has proved equally successful in other countries. Mexicans bought nearly 80,000 metric tons (90,000 tons) of Activia in 2006, and the product also did well in Brazil and China. In Russia, 2006 saw the launch of affordably-priced Activia Kefir, a traditional cheese-flavored fermented milk drink. After posting annual sales growth of 25% in 2001-2003 and 36% in 2004-2005, Activia reached worldwide sales of €1.3 billion in 2006—a success built on universal appeal and health positioning backed by clearly presented scientific evidence.



12 million children from around the world have participated in the Danone Nations Cup since 1999. Promoted by French soccer legend Zinedine Zidane and organized by DANONE, this World Cup soccer tournament for kids brings home the benefits of exercise for young people. Other events are held locally throughout the world.



rent partnerships each year, creating ties to the world's leading specialists. These partnerships focus primarily on the special demands of basic research, an area where we rely entirely on outside resources, but they also cover some applied research projects as well as in vitro and vivo tests. All clinical trials are outsourced. DANONE currently has over 200 agreements for scientific cooperation in different parts of the world. In the area of probiotics⁴, we have formed a four-year partnership with the Pasteur Institute to study how these strains act on the human body. DANONE is also working with the University of Washington on a project exploring the role of intestinal flora in health. Finally, DANONE research teams are also involved in a number of international projects under the aegis of the European Union. These include Eurostarch, a study on digestion of different types of starch and their

use by the body; Healthgrain, which explores the nutritional potential of grains; and the EU's Childhood Obesity program, which is testing a hypothetical relationship between protein intake in infancy and the incidence of obesity among children

PARTNERSHIPS FOR THE FUTURE
DANONE Research is also forming partnerships for education. An example of this is our association with the Heart and Arteries Foundation, designed to encourage research into the relationship between nutrition and cardiovascular disorders and to develop public-awareness and prevention campaigns. This effort is in the same spirit as the Group's not-for-profit initiatives in support of nutrition information and training. The 16 Danone Institutes that have opened in different parts of the world since 1991



80%

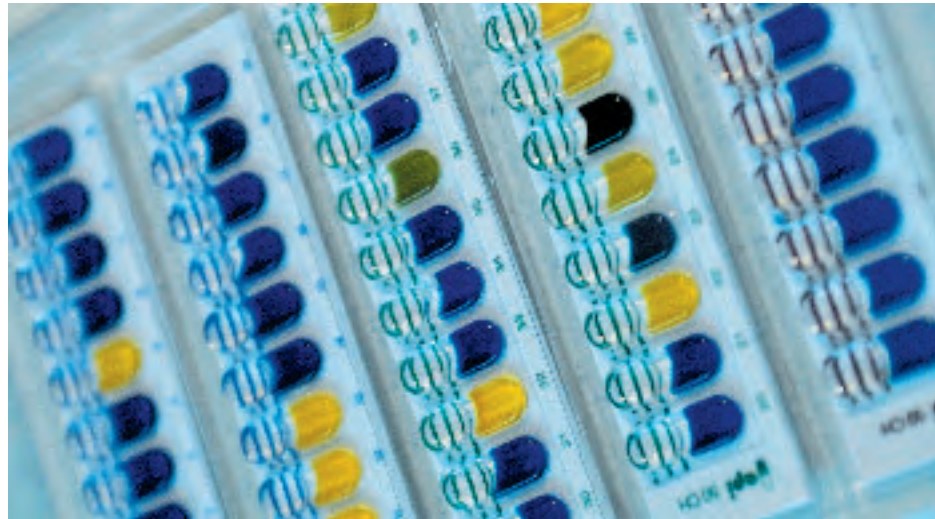
of DANONE research projects focus directly on health and nutrition. Fifty percent of the research budget is devoted to probiotics. In 2006 the R&D budget stood at €140 million or 1% of Group sales — a rise of 8% over the previous year.

600

products are currently undergoing renovation to upgrade their nutritional profile. LU France, for example, has in the last six years reduced the saturated fat content of its biscuits by 14% and their sugar levels by 9%, while increasing their cereal content by 15%.

Biochemical array test for the characterization of strains.

Each well contains a particular strain in a specific culture medium. The color change of the culture medium indicates a biochemical modification which enables the identification of each particular strain.



→ → →

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health and nutrition professionals throughout the world help ensure that subsidiaries communicate nutritional and health claims reliably, while providing scientific validation through close work with the scientific community.

play a central role in this (see page 41). With the dramatic rise in obesity, our subsidiaries are also encouraged to participate in local programs promoting good eating habits and active lifestyles. Initiatives include Dannon's Next Generation program, launched last year, which offers financial support for US associations involved in nutrition programs for children. A recent initiative in Bulgaria features a play with children helping the main character discover the basics of a healthy balanced diet, the importance of fruit and vegetables, and the benefits of exercise. All these initiatives are not just a feel-good exercise. They result from our continuing effort to make health an integral part of the daily life of our business. It is on this basis

that we have patiently built trust with consumers and credibility with scientific and regulatory institutions. It is up to us to continue earning that trust and credibility every day, ensuring that our principles of health and nutrition governance have true meaning and substance.

1. Cultures are live microorganisms such as bacteria or yeast.
2. FAO: the Food and Agriculture Organization of the United Nations.
3. Eurodiet is a European Commission project involving some 100 European experts. Its purpose is to develop a European program promoting health through nutrition.
4. Probiotics—the term literally means “for life”—are cultures that provide health benefits when ingested in sufficient quantities.

Affordability/ The healthiest foods are often the most expensive—and yet the people who need them most are generally the poorest. Over the last few years DANONE has worked to resolve this contradiction with affordability initiatives focused on developing countries. Our goal is to offer highly nutritious, affordably priced products that can be sold by the unit or serving and be distributed in all local outlets. Our first experiment, calcium- and vitamin-fortified Biskuat biscuits, began selling in Indonesia in 1999 for only 1,000 rupiah (10 eurocents). Using the same model, we launched our Milkuat dairy drink in 2004, also in Indonesia. Since then, the Indonesian model has spread to China, South Africa, Morocco, and in 2006 to Bangladesh.

Poverty, nutrition and health



In 2006 DANONE and Grameen Bank, the world's leading micro-credit lender, pooled their expertise to create Shoktidoi, a yogurt developed specifically to meet the nutritional needs of Bangladeshi children.

THE CHALLENGE

Bangladesh is one of the poorest countries in the world. Some 56% of Bangladeshi children under five suffer from moderate to serious malnutrition; of those, 21% are significantly underweight. The core problem of malnutrition leads to deficiencies in iron, vitamin A, and a variety of other nutrients. Grameen Danone Foods, created in March 2006 as a joint venture between Grameen and DANONE, has the twofold mission of providing healthy food to disadvantaged Bangladeshis with nutritional deficiencies, and helping to reduce poverty by implementing a business model based on close ties to the local community.

THE STRATEGY

In late 2006 Grameen Danone Foods took its first step, launching Shoktidoi yogurt at the very affordable price of 5 BDT (around 6 eurocents). For Grameen Danone, the goal is to help the poorest children in Bangladesh grow up healthy and strong by providing a wholesome, nutritious product they can eat every day. In keeping with this goal,

Shoktidoi was formulated specifically for the nutritional deficiencies of children living in the region where the first Grameen Danone plant is located. Shoktidoi was developed in partnership with the Global Alliance for Improved Nutrition (GAIN*), which is also helping Grameen Danone Foods develop a nutrition campaign.

THE SOLUTION

Shoktidoi—Bengali for “yogurt that makes you strong”—is made from locally produced cow's milk and date molasses and is a natural source of the calcium and protein children need for strong bones and healthy growth. Shoktidoi's live cultures also reduce the severity and duration of diarrhea. One 80g (3oz.) cup meets 30% of a child's daily requirement of vitamin A (for good vision and a strong immune system), iron (to prevent anemia), zinc (to encourage normal weightgain and protect the immune system) and iodine (for healthy growth and brain development). In early 2007, GAIN launched an efficacy study designed to measure the benefits of regular Shoktidoi consumption.

* A non-governmental organization dedicated to improving nutrition in populations at risk.

147

million people live in Bangladesh. Though data show income rising sharply and food quality improving even for the very poor, nearly half of all Bangladeshis live below the poverty line. Bangladesh remains one of the poorest countries on the planet.

30%

of a child's daily requirement for vitamin A, iron, zinc and iodine is met by one serving of Shoktidoi yogurt—no small feat in itself, since each serving is only 80g (3 oz.). Affordably priced at only 6 eurocents, Shoktidoi is accessible to the great majority of Bangladeshis.

Health and products

A fresh look at biscuits



For several years Group R&D has been working to reduce sugar content and use healthier fats in DANONE biscuits. Whole grains are now an equal priority.

THE GOODNESS OF GRAIN

Whole grains contain complex carbohydrates and provide more fiber, vitamins and minerals than refined grains. A vital part of a balanced diet, they favor regularity, help manage appetite, and contribute to daily fiber and micronutrient requirements. In 2006, top international experts reaffirmed the health benefits

of whole grains in symposia co-organized by LU at the annual conference of the International Union of Food Science and Technology and at Medec, a leading annual event for the medical professions in France. As a result, the nutritional value of DANONE biscuits has come into the spotlight in France, Belgium, Spain, Poland, Hungary, the Czech Republic and a growing number of other countries.



Beverages: less sugar, more pleasure

The trend to lower sugar content reflects a central nutritional concern in Europe. Volvic, the top seller of flavored waters in France with a 33.7% market share, has responded to this concern with innovation and transparency, launching Volvic Sans Sucre, its first sugar-free flavored mineral water, in May 2006. Sweetened with

sugar substitutes, the new product line comes in strawberry, tropical fruit and red fruit flavors. Like Volvic Gourmande and Volvic Zest, those used to sweetened drinks can enjoy sugar-free Volvic Sans Sucre with its low sugar content and less pronounced sweet taste—the first step, especially for youngsters,

towards kicking the sugar habit. In the interest of transparency, a sugar scale on each bottle rates the sugar content of Volvic beverages relative to water and sweet beverages such as sodas and fruit juices. This information allows consumers to make informed, responsible choices among sweetened, low-sugar

and unsweetened beverages. Our research to reduce the sugar content and sweetness of our beverages is only one part of DANONE's broad commitment to offering the best possible products, reducing fat and sugar and increasing fiber, vitamins.



Eating the right foods at the right age

In September 2006, Blédina launched a new line specifically for children 18 months to three years old. These groundbreaking products offer toddlers a balanced diet and introduce them to a wide variety of foods in portions the right size for their age.

INNOVATION BUILT ON SCIENCE

In France an estimated 84% of food eaten by French toddlers aged between 18 months and three years old is not produced to meet their specific needs. Jacques Ghisolfi, an academic and member of the French Pediatric Society's Nutrition Committee, underscores the concrete implications of this statistic: "Children under three aren't just miniature adults: their bodies are literally

under construction. As a result, they have special dietary needs—and their parents have a special responsibility to meet these." Between the ages of 18 and 36 months, height increases 20%, weight goes up 40%, and the brain gains an ounce every two weeks. This means that, in proportion to their weight, young children need six times more essential fatty acids and three to five times more iron than adults.

MEETING CHILDREN'S NEEDS

Blédina has responded to these needs with Petits Grands, a balanced line of tasty foods that promote psychosensory and psychomotor development in children 18 months to three years old. In stores since September 2006,

the new line offers a variety of main courses, desserts and snacks tailored to toddlers' nutritional needs, including ravioli stuffed with meat or vegetables, which contain three times less salt than traditional ravioli*, 100% fruit purees, dairy and chocolate-flavored drinks, and biscuits. Blédina also believes in making fun part of the experience, and its Petits Grands products not only provide opportunities to discover different ways of eating, from forks to straws, but come with free educational games. Nutrition information naturally appears on each package. Future products will round out the line to offer children complete meal solutions.

* source: Ciquel 2001

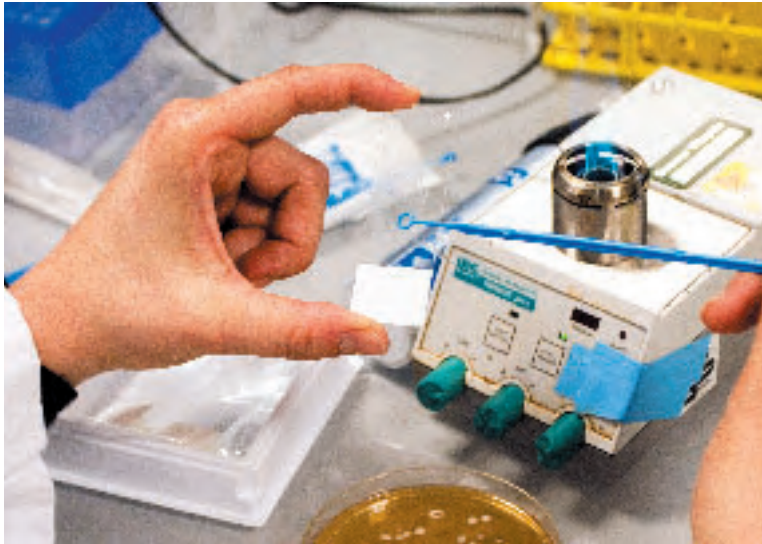
The right nutrients for the right country

The nutritional content of Danonino, DANONE's leading children's brand, has been varied to match specific needs in 14 different countries. In Brazil, where anemia and undernutrition coexist with obesity, Danonino is fortified with calcium, iron, vitamins A and D, and zinc to meet the requirements of local children. In Mexico, the product is fortified with iron; in Japan, with vitamins A and D; in Spain, with calcium; and in France, where Danonino is sold as Petit Gervais aux fruits, with vitamin D. Though the nutrients vary, the goal is always the same: to help children grow up strong and healthy.



Health and science

Benevolent bacteria



DANONE has been studying probiotic bacteria—bacterial strains with health benefits—for over 20 years. Our research into these microorganisms has enabled us identify their relationships with their hosts and to understand how they take their place in the body, how they grow, and how they work. The human digestive tract contains some 100 billion bacteria per gram of content. These bacteria help the body digest

food and keep the digestive system balanced and healthy. Microorganisms such as yeasts and molds also play an active role in the fermentation process used to preserve foods and to improve their flavor and nutritional properties.

NATURAL PROCESSES

Science has for centuries been interested in the processes involved in alcoholic fermentation—the conversion of sugar

into alcohol—along with the yeast fermentation used to make bread, the fermentation of pickles, chocolate and cheeses, and finally milk fermentation, which relies on lactic bacteria to produce cultured milk and yogurt. DANONE Research selects lactic bacteria with the right technical, organoleptic and probiotic properties for use as cultures in our fresh dairy lines, developing products based on specific probiotic properties. The two most striking examples of these probiotic products have been a worldwide success—Activia, which contains the DN 173-010 strain of the Bifidus family to promote regularity, and Actimel, formulated with the DN 114-001 strain of *Lactobacillus casei* to help strengthen the body's natural defense system.

INNOVATION FOR HEALTH

In this way, DANONE develops new products using 100% natural dairy cultures. Working in partnership with internationally recognized scientific institutes (see p. 48), our research teams focus on immune function, digestive well-being, and the interaction of probiotics with resident intestinal flora and the body as a whole. We are also studying the possibility of producing active molecules—vitamins, for example—that benefit human health.



What about biscuits ?/ In a move to offer consumers biscuits made with real yogurt—and with the taste and goodness of yogurt—DANONE R&D developed a patented process for making biscuits with living ferments. The biscuits keep from six to nine months at room temperature. They are marketed under the brand name Liga in the Netherlands.



Probiotic Conference: Moving science forward

The knowledge shared among scientists provides the essential base for **consensual progress**, a fact well illustrated by the fourth annual Probiotic Conference. In early 2006, 160 experts from 30 countries gathered in Paris to review the latest advances in probiotic science and assess their practical applications. Each year, this event has attracted greater interest and more participants. Reflecting the quality and authority of contributions, proceedings have been published in a number of scientific journals, among them *The American Journal of Clinical Nutrition* in 2002, *Current Nutrition and Food Science* in 2003, and the *European Journal of Nutrition* in 2004 and 2005.

NICOLAS GAUSSERES, Director of Health and Nutrition Research

“Every health claim must be backed by clinical studies.”



“Clinical studies provide scientific evidence of our products’ benefits, and Danone has always seen them as critical. And with the advent of new European regulations on health claims, the strategic

advantage that they give us is more important than ever. Clinical studies are essential in demonstrating the reliability of our scientific arguments. An in-house team sets up the studies, oversees them and analyses the results, and each protocol is reviewed by ethics committees. At year-end 2006, we had about 40 studies under way worldwide, with 50 to 1000 participants in each. All studies are run in partnership with independent research entities. Finally, we always have several clinical studies to support each health claim. These safeguards are what enables us to guarantee the validity of the claims that we make to consumers, so the stakes couldn't be higher.

What's more, regulators require us to retain study records over a period of 15 years. The biggest challenge is having to prove that any effect we claim is produced by the product as sold, and not by a specific nutrient which it contains.”

30

patents were filed by DANONE in 2006, of which 20 were for Fresh Dairy Products.

16

clinical studies were launched in 2006, eight related to Actimel and four to Activia. In five years the clinical studies budget has grown fifteen-fold.



NATURE LOVERS

In recent years the environment has become a major concern for both the public at large and government. National and international regulations have grown ever more stringent, while consumers are increasingly drawn to environmental concerns and natural products—for ecology or health-related reasons. For Groupe DANONE, which puts nature at the heart of its product range, business development that fails to take the environment into consideration is simply inconceivable.

Spring water—a **wealth** of health and our natural heritage

Eighty percent of planet Earth is made up of water. Yet fresh water resources account for only 3% of that 80, making conservation critical. As the world's leading producer of bottled spring water, DANONE is doubtless more sensitive than anyone to this issue and invests heavily to preserve the quantity of natural water and protect its quality.

Bottling spring or mineral water is not a threat to fresh water resources but an opportunity—a paradox in appearance only. The reasons are simple. First, because a major producer like Groupe DANONE takes only 0.0014% of global fresh water reserves, or some eight billion liters in 2006. Secondly, because bottled water producers are in the front line, more directly affected than anyone by the need to protect and conserve a resource that lies at the very heart of their business. DANONE has deliberately turned this into concrete commitments spelled out in its Charter for the Protection of Groundwater Resources.

The prime principle underlying this Charter is to not use more water than nature produces annually. "We carry out hydrogeological surveys at all our springs," explains Jean-Christophe Bligny, head of Environment and Water Resources at Danone Waters France. "Which means studying the full water cycle and limiting the amount we take to ensure that groundwater levels always remain the same."

ENLISTING LOCAL PARTNERS

Groupe DANONE is thus careful never to make excessive demands on any of its 100 springs. Instead it adopts a rational approach so as not to deplete resources, while protecting spring quality and avoiding changes in the composition of groundwater. To this end, DANONE enlists local farmers, authorities and companies.

At the Villavicencio site in Argentina, for example, a nature reserve was set up in partnership with local tourism authorities. At the same site, constructive dialog has led to an understanding with mining companies, which now factor conservation of the natural heritage into their mining practices. At Lanjarón in Spain, the municipality and other users have joined forces in a foundation to share and manage water resources more efficiently, funding local infrastructure and other projects. At Evian in France, consultation has led to the creation of an association for the protection of the mineral water catchment area. This funds wastewater treatment plants, chlorine-free road salting programs, green weed control using

no chemical pesticides, and upgrades to livestock buildings.

But DANONE's commitment goes beyond protecting its own springs and immediate interests. As a signatory of the international Ramsar Convention since 1998* and founding member of the DANONE/Evian Fund for Water in 2003, it contributes to the protection of wetlands threatened by urban sprawl and drainage. It also funds public awareness-raising campaigns, an example being the Ramsar Game program in Indonesia. Launched in partnership with Unesco, this is used as a teaching aid in hundreds of schools. Groupe DANONE's latest water conservation commitment is to reduce its own consumption at production sites and not discharge wastewater into the natural environment. This is the purpose of the Danone Water Footprint program which has helped save over 3.5 billion liters of water in the past five years. ●

* An intergovernmental treaty for national and international action and cooperation for the conservation and rational use of wetlands and their resources.

Groupe DANONE's contribution/ 100 springs in operation worldwide. / 8 billion liters of mineral water sold every year. / 3.6 million cubic meters of water saved in 5 years by Groupe DANONE's production sites. / 1 liter for 10 liters: in Germany, then France, DANONE has committed to financing access to 10 liters of drinking water for people in Ethiopia and Niger for every liter of Volvic water it sells. In the first half of 2007, six new wells will be bored in Niger, providing 1.6 billion liters of water per annum for 16,000 people. In 2007 the program will be extended to Japan.

At Klaten on the Indonesian island of Java, local DANONE company Aqua bottles water from an underground spring at the foot of the famous Merapi volcano. When farmers in the region experienced a water shortage that affected irrigation of their rice paddies, geological surveys confirmed that Aqua's deep-well drilling had no impact on the surface water they used. But to resolve the nascent dispute, DANONE nevertheless turned to French agricultural research and development body CIRAD. In 2006 a consultation process began, with all stakeholders coming together to share their points of view on water resources. In parallel, research into the water shortage and remedial plans of action got underway. Initial solutions are expected in early 2007.

PACKAGING:

doing better with less

Reducing the environmental impact of packaging is a challenge that Groupe DANONE is addressing in the long term, since packaging solutions must both protect products and comply with marketing and environmental constraints.

The food industry is at the heart of an equation that is apparently insoluble. As consumers, people now demand ever greater food safety and favor individual packaging, turning away from family-size formats for greater convenience. But as citizens they are quite rightly worried about the growing volume of packaging waste, much of which is not biodegradable. Resolving this contradiction has become a priority for Groupe DANONE in recent years, through initiatives ranging from support for recycling to research into new materials and reductions in the weight of individual packaging. Historically Groupe DANONE has been a pioneer in the promotion of recycling. In the early 1970s it launched litter collection campaigns including "Vacances Propres", aimed at encouraging French vacationers to pick up their trash, and is now actively involved in over 20 recycling organizations nationwide. Six years ago, Groupe DANONE decided to go one step further and tackle the problem at its source. The aim was clear—to reduce the overall

weight of product packaging by 10% over a 10-year period. To do so, DANONE subsidiaries monitor a key indicator—the ratio of product weight to packaging weight.

MATERIALS OF THE FUTURE

In practical terms, each subsidiary must ensure that packaging gets lighter for identical product weight. Results are very encouraging, especially for flagship products: the weight of an Actimel bottle has dropped from eleven to 6.5 grams, and that of an Evian bottle from 43 to 30 grams. Progress has been made possible by substantial investment and major technological breakthroughs, including yogurt cartons made from foam plastic containing more air bubbles and less solid material.

Today Groupe DANONE is on course to meet its target: over five years, it has reduced packaging weight by 5%. Yet there are limits to how light packaging can become and still afford adequate protection for the products it contains.

The Group has thus widened its approach, investing in research into

new types of more environmentally friendly materials that break down more easily for recycling. The Biscuits business line has made enormous strides using recycled cardboard. There are promising developments in bottled waters, too, when legislation allows the use of PET plastic containers. In Germany, for example, lengthy research has made Groupe DANONE the first company of its kind to produce high-quality bottles made of 25% recycled PET, thus cutting plastics production in years to come. Germany is a test case that may help bring about changes in legislation in countries such as France and Spain.

The next step could be widespread use of bioplastics—biodegradable plastics made from plants (see box). First trials are now underway in Bangladesh, with cartons made of a corn-starch derivative (see page 96). ●

Key figures/ 757,000 metric tons is the weight of (primary and secondary) packaging required for products in DANONE's three business lines. The aim is to reduce that figure by a further 5% in five years. / €63 million is DANONE's contribution to packaging waste collection in Europe. / 72% of Europeans claim they are willing to sort their waste so that it can be recycled. / Between 500,000 and one million tons is the projected size of the bioplastics market in the European Union by 2010. The figure was 23,000 tons in 2000 (source Eco Emballages, Pro Bip Report).



“Plastic is fantastic”

was the hook of an ad promoting this then-revolutionary material when it was launched in the 1960s. But plastic has two drawbacks: first, it is derived from oil, a non-renewable resource of which reserves may run out by 2050. Secondly, it takes years to break down. Because consumers are not always willing to change their lifestyles, industry has had to look for alternatives. It now has the technical know-how needed to replace traditional plastic by a plant-based substitute, bioplastic—a material offering one solution to packaging needs in the 21st century. The fruit of technology and research, bioplastic is made from natural, renewable, fully biodegradable matter that poses no threat to the planet's non-renewable resources. First trials are just starting in Bangladesh (page 96), and other initiatives are set to get underway in 2007 with packaging made from polylactic acid (PLA), a bioplastic derived from corn starch. However even PLA has its limits: producing a high-quality non-petroleum-based plastic that is at once rugged, durable and affordable continues to pose a serious challenge to researchers.

Farmers cultivate sustainable progress

Although the farming industry is vital to our way of life, it is responsible for nearly 25% of greenhouse gases, and accounts for 70% of all water consumption and 40% of groundwater pollution. For nearly ten years Groupe DANONE has worked with farmers to develop sustainable farming practices.

Although DANONE uses only 0.8% of the world's milk output—some four billion liters nonetheless—it is still a major player in the dairy product chain in over 20 countries, with 15,000 pickup points worldwide. Against that background, it is difficult not to feel concerned by the challenge of making the dairy industry as environmentally friendly as possible. “We’re working steadily, making progress step by step,” says Guillaume Thomas, environment project manager in DANONE’s Sustainable Development and Social Responsibility department. “Our prime objective is to encourage all farmers to move ahead together in adopting more responsible practices,” he adds. This long-term commitment got underway in 1997 against a global backdrop of food scares, with consumers becoming increasingly vocal in their demands for quality and traceability. The Group opted to strengthen its dairy quality and security program (DQSE) which includes 42 expert-defined criteria, seven directly related to the environment. Part of a quality and sustainable farming-based strategy, this involves stricter

hygiene, more stringent milking regulations, limited use of pesticides, and respect for the well-being of livestock.

MUTUAL SUPPORT

To give farmers the support they need, DANONE’s specialists audit all 15,000 farmers with whom the Group works directly at two-year intervals. Technicians conduct on-site inspections at farms and check, for example, that animal waste is stored in a way that does not contaminate the environment; that water used to clean milking equipment is regularly inspected; and that farmers have been properly informed of the types of incident they must report to DANONE. Examples include cattle diseases, tank malfunctions and trace substances found in milk. “An audit is a critical opportunity,” says Guillaume Thomas. “It gives DANONE a chance to state its environmental requirements and lets farmers discuss problems they are having. We advance together: we receive flawless raw materials and farmers benefit from our specialists’ advice. In countries where legislation is less stringent than our standards, as in Romania, farmers can even get financial assistance to upgrade. It’s a

win-win proposition.”

Each interview between DANONE auditors and farmers culminates in a progress plan balancing DANONE’s quality criteria with farmers’ own profitability. Yet when DANONE asks farmers to limit water consumption, they soon notice that their water bills are down, and when they are encouraged to recycle organic waste rather than buy chemical pesticides and fertilizers, they make similar savings. So by anticipating tighter national regulations through compliance with the highest quality and environmental standards, farmers are actively improving their own prospects.

“In some countries, like France and Germany,” says Thomas, “farmers can write off their investment over a longer period and are less likely to find themselves with their back to the wall.”

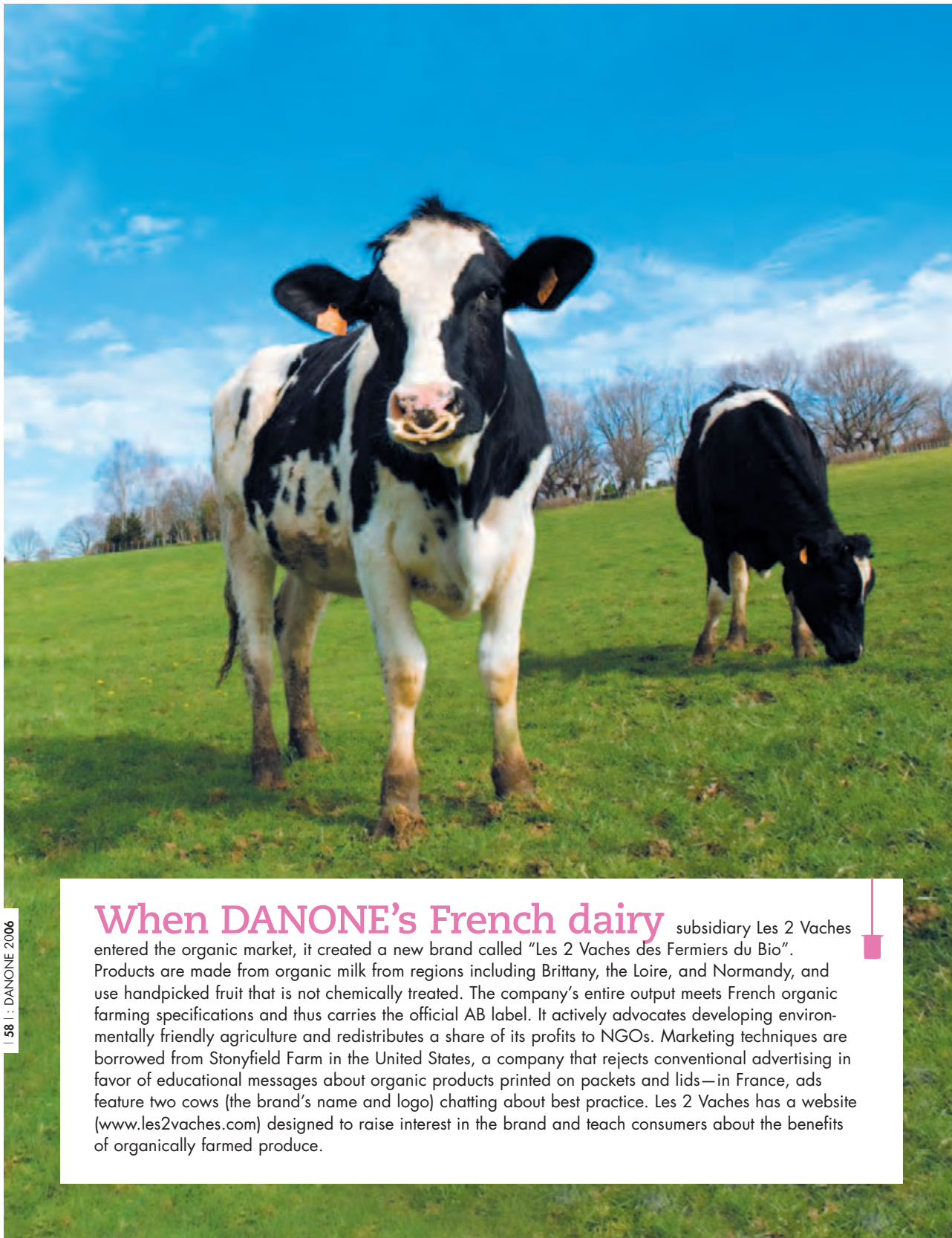
A guide for farmers willing to undertake environmental upgrades has just been published. This explains the thinking behind the DANONE approach and provides examples of good practice at each step in the process.



How can you cut costs without affecting the quality of output?

What if farmers were given a means to identify and analyze each cost in milk production—from animal feed and water to electricity and more? And what if they could compare their costs to those of other farmers in the region? “Perspective” does just that: this program enables suppliers to tap into fellow farmers’ best practices, lowering consumption, optimizing production and making substantial savings along the way. Proof that Group DANONE’s requirements can also help them create wealth.

Milk consumption/ Groupe DANONE buys 0.8%—i.e. four billion liters—of the milk produced worldwide.



Danone also offers organic products. Taking its cue from Stonyfield in the United States, French brand Les 2 Vaches has built its media campaign on an educational message with a touch of humor.



In 2006, the focus was on waste management, including recycling in the production processes used for some foods.

In Spain, for example, the Gota Verde program helps farmers learn about the environment and gain a better understanding of environmental legislation. Training is organized in each milk collection area.

Content reviews regulatory issues, introduces best practices and guides farmers through the processes needed to qualify for Common Agricultural Policy subsidies, now tied to compliance with environmental, food safety, animal welfare and occupational safety standards.

ORGANIC EXPERIENCE

While promoting sustainable farming measures designed to help all farmers gradually improve their environmental performance, Groupe DANONE has also worked with a small number to develop organic farming.

First moves in this direction came in the United States in 2001, when Stonyfield Farm, an organic yogurt producer since 1983, joined the Group. In a winning partnership all

around, the US organic subsidiary has recorded growth of 70% in recent years.

Building on this success, DANONE created Stonyfield Europe in June 2006 as a means of making organic products available to more European consumers. The initiative was also intended to attract new customers and, above all, to secure a market in France for the 40% of organically farmed milk carrying the AB label; without buyers, this is marketed as ordinary milk.

In June 2006, Stonyfield Europe bought 37% of Ireland's leading organic dairy producer and invested €5 million to boost its production capacity. In France it has launched the Les 2 Vaches des Fermiers du Bio brand, with marketing based on consumer education in organic products (see opposite).

Will dairy production ever be 100% organic? For DANONE, sustainable and organic farming are not contradictory, and there is no need to shift from one to the other. What's more, both models are constantly evolving, due in particular to changes in the regulatory context that force traditional farms to take greater account of

the environment in their operations. This is entirely in line with Groupe DANONE's support for sustainable farming as reflected in the DQSE program. The priority is to make conventional farming more environmentally friendly while maintaining high output and quality standards. By focusing on initiatives in this direction, Groupe DANONE seeks to move out of small-scale organic ventures into more wide-ranging, environmentally virtuous practices capable of meeting demand from hundreds of millions of consumers every day. ●

When DANONE's French dairy

subsidary Les 2 Vaches entered the organic market, it created a new brand called "Les 2 Vaches des Fermiers du Bio". Products are made from organic milk from regions including Brittany, the Loire, and Normandy, and use handpicked fruit that is not chemically treated. The company's entire output meets French organic farming specifications and thus carries the official AB label. It actively advocates developing environmentally friendly agriculture and redistributes a share of its profits to NGOs. Marketing techniques are borrowed from Stonyfield Farm in the United States, a company that rejects conventional advertising in favor of educational messages about organic products printed on packets and lids—in France, ads feature two cows (the brand's name and logo) chatting about best practice. Les 2 Vaches has a website (www.les2vaches.com) designed to raise interest in the brand and teach consumers about the benefits of organically farmed produce.

DANONE and the environment/ In 2006 Groupe DANONE's environmental investment totalled €25 million, i.e. 3% of the group's entire industrial investment. / Waste recycling rate: 81% (not counting sludge from wastewater treatment plants). / Production plant objectives for 2000-2010: water consumption down 30%, energy consumption down 20%, packaging weight down 10%, 90% waste recycling.



MANAGEMENT

INSIDE STORIES

Human resource management has long played a central role at Groupe DANONE. Which is hardly surprising given our well-known commitment to dual success—improving overall performance while maintaining a healthy balance between business success and personal quality of life.

Fundamental tasks facing human resource professionals start with creating effective organizational structures for growth: implementing payroll policies that encourage employees to give their all; fostering constructive industrial relations; identifying and recruiting candidates able to rise to the challenges of the business; and organizing training and development opportunities. The ability to meet these challenges makes HR teams a crucial partner at all subsidiaries. But they must also perform the role that Groupe DANONE originally attributed to them—ensuring a healthy balance between profitable business and the well-being of employees. As guardians of DANONE values and

culture, HR officers embody our Group's founding values and conviction that the well-being of people is both the means to and end of growth. This is a commitment they must stand up for, even in the face of conflict or pressure from shorter-term business imperatives. The same commitment is expressed in the daily routine within each production plant, team and subsidiary, currently formalized in the Group's key priorities. These include occupational safety, a policy that aims to halve a workplace accident rate that is still too high (page 66). Another example: efforts to improve the workplace atmosphere Group-wide by making companies the place where everyone does and feels their best (page 62). Another focus is decentralization—

encouraging countries and subsidiaries to network to enhance the responsiveness and informal style that are the hallmarks of Groupe DANONE (page 64). These concerns are perhaps even more visible in new subsidiaries in emerging markets where the prime challenge is less related to finance, marketing and business than to human resources per se. How can we find local staff or qualified expatriates to build a business from next to nothing? How can we adapt our social priorities to different contexts, or incorporate new subsidiaries into a group with global reach while allowing them to remain local businesses? These questions are addressed every day and in themselves sum up the issues at play in DANONE's human resources function (page 69).

Job motivation: A great place to work?

To attract and retain talent and foster conditions conducive to high performance and self-realization, the HR function has risen to the challenge of making DANONE a great place to work. First step: the decision to assess conditions by conducting a survey every two years, with subsidiaries taking part in comparative local polls. To that end DANONE chose to work even more closely with the American research and management consultancy Great Place to Work® Institute. With offices in numerous countries, it assesses workplace climates and employee well-being through questionnaires that address a wide range of issues (work conditions, equity, respect for staff, relations with management, staff diversity, etc.). It then draws up league tables of the best places to work in each country and continent. In 2006, 22 DANONE subsidiaries worked with Great Place to Work® Institute or were involved in similar surveys with other firms in countries where it did not have offices. In Romania, for example, the Group measured employee satisfaction in 2005 by taking part in polls by the magazine Capital—highly reputed in Romania—and in those of the Hewitt institute in 2006. The aim is that all subsidiaries get involved in such assessments—

not in order to throw the spotlight on those which perform best, but to undertake action plans that will help everyone improve. By committing to constant progress in this way, each subsidiary can move ahead and address its shortcomings. Experience shows that when companies make progress their employees feel pride and their sense of motivation grows. Workplace assessments thus give companies an edge over their competitors. DANONE's ultimate aim is to make its subsidiaries more attractive. By becoming the greatest places to work in each country where the Group does business, they will foster a feeling of pride and sense of belonging among employees.

Personal views/ Importance of a good workplace atmosphere

Between well-being and health

At Danone UK we launched the "Danone Active Health" plan.

As part of the plan we organize training sessions on topics like stress management. We also urge employees to adopt healthy diets through lectures and by offering them breakfast with

cereal, fruit, and dairy products every morning—and making sure a basket of fruit is at their disposal. The idea is simple: just as it does for consumers, Danone commits to the health of its employees.

ANNE-CATHERINE MORADPOUR, French, HR manager, Danone UK

Diversity: working towards a more representative company

Danone Waters France believes that welcoming diversity and allowing it to blossom make the company more dynamic. In 2006

we signed an agreement with employee representatives on the issue of diversity. The aim was to improve equality in the workplace between men and women and to ensure that people with disabilities, employees of different origins, and the elderly were smoothly

integrated into the company. We have been taking action to promote diversity for two years. At Evian, for example, a training course has been put in place, designed to enhance the career prospects of female factory workers, while people with physical disabilities account for 9% of recruitment since 2005. At the Amphion plant near Evian, sign language classes have helped workers with impaired hearing to fit in.

Greater diversity in teams changes perceptions of things. We become more receptive to a greater variety of profiles. So in Marketing, for example, people with a more diverse range of qualifications help us come at business issues in a less standardized way and to be more in tune with market expectations.

CÉCILE DIVERSY, French, Human Resources, Danone Waters France



Transparency

Surveys carried out at Danone Romania have revealed a lack of information on strategy, career prospects, and salaries. Now that the problem has been identified, corrective measures are in place. To ensure that employees are aware of business strategy, conventions with non-managerial staff have been organized. We have also communicated the salary grid to employees and by 2008 all will benefit from systems of personal development. These actions will demonstrate that equity within the company is a reality which deserves to be reinforced.

MIRCEA MATESCU, Romanian, Human Resources, Danone Romania and the Adriatic Region

XAVIER LIÑAN, Spanish, Organization and Development Director "It is an opportunity to motivate employees"

Every year since 2003 Danone Spain has taken part in the survey conducted by Great Place to Work® Institute. We are always rated among Spain's top two companies and in 2005 we were actually one of Europe's top five. Every survey is of course an opportunity to improve working conditions, but more importantly to motivate employees, and foster a sense of pride in belonging to Danone Spain.



Networking for **high** performance

Sharing knowledge is a key factor in the business performance of large companies and the self-realization of all employees. Since 2002, Groupe DANONE has developed what it calls “the networking attitude”—a mindset that makes it second nature for managers from different subsidiaries to share good practices directly with each other, from one subsidiary to another, rather than going through traditional channels. Networking makes sense because it connects people who have experience of a good practice—givers—with people who need to learn about it—takers. The prime aim is to secure gains in efficiency: networking saves time and reduces risk by focusing on solutions that have already proved themselves in the field. Initially, networking was introduced and developed by organizing events and gatherings designed and staged to provide opportunities for sharing experience

in a relaxed atmosphere. Marketplaces are one example. They mimic real-life markets, with givers of smart ideas “selling” their wares at stalls and trying to talk takers into “buying” them. In 2006 networking entered its next phase. This is the Group’s dual ambition of involving employees and external partners in a networking approach along with the 9,000 managers and of developing new tools for building solutions together.

Personal views/ The benefits of networking

Working and building together

At the Beverages business line convention in Seville, Spain, in June 2006, I took part in a networking session. There were seven stands where Group subsidiaries presented their projects in progress and we could come up with ideas to improve them. It is worth noting that even if ideas are not taken on board wholesale, they can bring inspiration. Sometimes we get too

involved in a project, and fresh input from someone on the outside can prove very positive in helping to get us thinking again. Last but not least, the networking session was an opportunity to meet colleagues from all over the world and to fill my group address book. That’s part of networking, too.

FRANKIE SUEN, China, managing director, Export Division, Beverages, China



Sharing and deciding

The biscuits Business line has set itself the objective of cutting its energy consumption by €1 million in 2007. Against that backdrop we held a networking session devoted to energy saving in November 2006. It took place at the Herentals plant in Belgium. Around 40 managers from the division supply chain took part. They included plant, engineering, and environment managers.

Subsidiaries thus got the chance to introduce projects they were deploying internally and to ask attendees for the benefit of their experience or for new ideas in order to improve them. Countries like France, Italy, Poland, the Czech Republic, Belgium, and Germany presented their projects—ten in all. They included the purchase of new infrared burners which reduce gas consumption by 15% and

the recovery of dissipated energy to heat buildings. The session saw much sharing of ideas and experience. And it resulted in some unanimous decisions being taken. One such decision concerned the oven inspection method designed in France, which will be applied to all the plants in the Biscuit business line.

PATRICK ROCHER, French, process and technology director, Biscuits.

Some figures/ To transmit the networking mindset to all subsidiaries, DANONE gives employees tools such as marketplaces and an intranet that help them connect with each other. In 2006 a total of 191 good practices were presented for deployment (over 600 since 2003) and 1,000 new ideas registered. In addition, over 70 sharing networks are active in every sphere of the Group’s activities.

Communicating

There is often one or two of us in charge of public relations, “which is very useful to progress in information sharing between subsidiaries. Every six weeks we hold phone conferences and share our experience and compare viewpoints. Through our intranet site we share best practices and understand group positions on some sets of issues. For the launch of Activia in the US, my colleagues’ experience was very valuable.”

MICHAEL NEUWIRTH, American, director of public relations, Dannon US.

Opening

We organized an Innovation Day with our packaging and raw materials suppliers. They showed us the solutions they had designed to meet our precise specifications. Sixteen suppliers unveiled their ideas at a marketplace. Of them 120 were demonstrated and 10% brought to market.

KATARZYNA HUTNA, Polish, purchasing manager, Danone Poland.

Safety: a business everybody should mind

At DANONE we naturally consider safety to be a basic, universal human right. As such, it is every employee's business and is not restricted to a group of experts. To continue to improve results which, at times, did not live up to our ambitions, DANONE initiated a safety-specific approach in 2004. Called "Wise", this was first deployed in the Biscuits business line before being extended to Beverages and Fresh Dairy Products. Designed in partnership with the DuPont group, a global pioneer of safety culture, it is defined by a cross-functional approach that seeks primarily to change people's behavior. A full 90% of accidents are caused by inappropriate behavior and could therefore be prevented. For that reason Wise puts management and dialog at the core of Groupe DANONE's safety focus on, as they are the most effective ways of driving progress in the long term.

MOBILIZING IN THE FIELD

In the course of 2006 all DANONE subsidiaries launched initiatives aimed at changing employee behavior. These included displaying the number of accidents and the number of consecutive accident-free days in production plants; running campaigns promoting basic rules and the importance of protecting oneself in the workplace; safety marketplaces (see page 64) where participants—who included machine operators, supervisors, maintenance

technicians and human resource directors, among others—shared good practices; exhibitions of photographs taken in production facilities to raise awareness of the need to obey safety instructions; and safety information displays at many sites which convey simple but essential ideas. Another priority is communicating the safety message directly. This is the practice, for example, at Bonafont, the Group's Beverage subsidiary in Mexico. At the Toluca plant management, machine operators, and trade unions have formed working groups and drawn up safety standards. Using the Wise approach, managers and their teams meet four times a year to address safety issues and ensure that everyone obeys the rules. When an incident that could degenerate into an accident occurs, communication is once again crucial in preventing the same situation from occurring again: a video simulating the accident which could have happened is thus filmed and screened on the plant's televisions. The aim is first and foremost to raise each employee's awareness of the risks to which he or she is exposed and of the most effective forms of protection.

It is still a little early to measure the impact of the Wise safety policy in Beverages and Fresh Dairy Products. But, in the Biscuits business line, the accident rate fell 37% in 2005 and 11% in 2006. Groupe DANONE was the recipient of a Safety Award at DuPont Leaders Forum of Safety and Performance in 2006. The Group was singled out for the speed and commitment with which its managers rolled out the safety drive. ●

zero

accidents: the only acceptable goal. To achieve that goal, it is important to create a safety-first culture.

Mexico/ The Toluca Beverages plant, which employs 250, recorded 560 accident-free days in a row at the end of 2006—a record. Safety is value number one at Toluca, ahead of quality, customer services and competitiveness.



Key figures

74

factories and warehouses have joined the Wise occupational safety drive.

Since the Wise safety procedure went operational in 2004, the workplace accident rate has dropped by 30% (like-to-like).

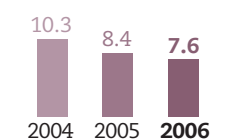
59

safety audits were conducted in 2006.

On every site audits were carried out by a DuPont auditor and a DANONE auditor trained by DuPont. (About 20 DANONE auditors have been trained to date.) Auditors draw up assessments built on 12 criteria which make up the safety management system.

The most interesting aspect of this approach, however, is that auditors put forward recommendations for action plans to improve safety. Eighteen months on, a new audit takes place to measure progress made and determine avenues of further improvement.

The workplace accident rate*



* Number of accidents resulting in at least one day of sick leave for every one million hours worked.

Emerging countries: the human challenge

Groupe DANONE recorded over 90% of its sales in the developed world a scant ten years ago, but by 2006 emerging countries accounted for a full one-third of business. Clearly, our growth strategy has undergone a radical change—that is only just beginning. Our ambition today is to double our geographical spread by moving into 40 additional countries in just a few years. In this, our main challenge is not financial but human: we must identify the talent we need and manage human resources effectively.

BUILDING BUSINESS

Whether DANONE moves into a new country by leveraging a local partnership—the usual practice—or starts a business from scratch, a crucial stage in creating a new subsidiary is finding the right general manager. For this strategic position, DANOE seeks candidates who combine entrepreneurial qualities with a sense of adventure and a sound understanding of the Group, its methods and its competencies. Successful candidates must create and put to work a management team that strikes a balance between expats and local staff. The former bring DANONE know-how with them, passing on our Group's corporate culture and practices. The latter provide indispensable knowledge of the local market and consumer habits. Such recruitments are far from simple—and of decisive strategic importance. Economic and political conditions in some countries can make it difficult to attract the right

expatriates, while young local managers often lack the training to be immediately operational. In addition, they are often relatively few in number, and aggressively recruited by rival companies. If all of a country's managers are already in employment, the shortage becomes very acute.

COMMITMENT TO TRAINING

Such situations prompt new subsidiaries to invest heavily in training, with a dual rationale: on the one hand, training makes new recruits operational more quickly, either through traditional courses or by leveraging our “networking attitude” (page 64), with employees from new subsidiaries “groomed” by managers from other entities. The second purpose is to transmit DANONE culture, and in so doing trigger an attachment to our company that leads to a fierce sense of loyalty.

**Personal views/
Reports from five countries
where Groupe DANONE
is present**



New frontiers/ The “new frontiers” concept first appeared in 2003 to designate the Group's most powerful potential “growth relays”, i.e., countries with large populations where product consumption is still low and economic growth firm, where there is major scope for nutritional and health-oriented food products, and where DANONE has a sound base. The five new frontiers identified at the time – China, Indonesia, Russia, Mexico, and the USA (for dairy products) today account for 25% of Group sales and they are growing at an annual rate of nearly 20%. More than 35,000 employees work in those countries. In 2006 tomorrow's new frontiers began to take shape in Latin America, North Africa, and Middle East. Business growth is still in its early stages, but the potential is obvious. The Group is investing heavily in these countries to rapidly make them into new engines of growth.



Egypt/

Creating a management committee



I supervised the creation of our management committee. Aside from the financial director and myself, the directors are all Egyptian and were hired in 2006. By the end of the year, our team easily stood comparison with other management committees in the Group.

CHARLIE CAPPETTI,
Dutch, general manager,
Danone Egypt.

In the field



To launch the Danone brand we went out to meet families to better understand their needs. We made a point of presenting our fresh dairy products as world leaders—the kind of argument that always carries weight in Egypt. We stressed health benefits, but didn't overdo it and used humor. This is not the approach DANONE usually adopts, but it works in Egypt.

HISHAM EZZ-EL-ARAB,
Egyptian, marketing director
of Danone Egypt.



Complementary competencies

Fresh Dairy Products' move into Egypt began in late 2005 with the purchase of a production plant. The first step was to set up a management team that combined the skills of expatriates with those of local managers. The idea was that the former would introduce DANONE know-how and

the latter identify discrepancies between DANONE's culture and that of the company it had taken over. The entire management team was then sent for training in other Group subsidiaries to better understand working practices specific to DANONE.

Adapting to an international group/ When Jordanian national Ismail Al Qalawi arrived as financial director at Danone Egypt after a long stint in the US, his first task was to bring the new company into line with Group standards. He then had to put together a team, motivate it, and teach it to work to the rules of an international group.

Colombia/

The industrial view

The plant to be built in Colombia will comply with a concept new to DANONE: that of a production facility designed especially for emerging markets. Although these cost around 30% less than the Group's classic plants, there are absolutely no shortcuts when it comes to safety and quality standards. "To cut costs I work mainly with local industrial goods suppliers

and choose equipment with low levels of automation," says Danone Colombia manufacturing director Yvan Moliner. "When I have to deal with a problem, I phone colleagues whom I think may have developed the solution I need in their subsidiaries. Every week I organise two or three such meetings. And the savings in time and money are invaluable."



MARCELO PALMEIRO,
Brazilian, general manager
of Danone Colombia.

Adapting to act local

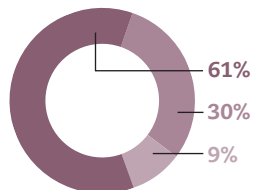
Danone will operate its Colombian plant through a joint venture company created with local partner Alqueria, which leads the Colombian milk and fruit juice markets. The first products are due to come to market by the end of 2007, the strategy being to gradually introduce DANONE flagship products adapted to match Colombian tastes. 2006 saw a host of job interviews since, with the exception of three DANONE expats, managers will be Colombians trained to conduct business the DANONE way.

In emerging markets

8

the number of emerging countries where DANONE has moved in or strengthened its presence since the beginning of 2006: Bangladesh, Colombia, Thailand, Algeria, China, Egypt, Mexico and Argentina.

Breakdown of sales



● Europe
● Emerging countries
● Other countries

Algeria/

Training



We decided to double our budget for training both the managers who were already in place and those who would be joining us. The Group works with local recruitment consultants, of course. But we also urge our managers to network, in other words to "sell" the company around them. In fact, networking is now our prime means of recruitment. Within the company, finally, we undertake many initiatives to transmit the Group's corporate culture because it enables us to attract employees and strengthen their loyalty. It also boosts performance and personal development.

PAOLO TAFURI, Italian, general manager, fresh dairy products, Algeria.

A market with strong potential

2006 was a key year for Danone FDP in Algeria. The main challenge was to sustain business growth and to manage the rise of the Algerian FDP market which is growing by an average 20% a year. Throughout the year the Algerian subsidiary continued to launch Danone-branded products which gradually replaced those in the old ranges. Results were encouraging in light of the constraints that weigh on business in Algeria: the country began opening up to

market economics and foreign investment only ten years ago, which has led to a legal framework that can stifle business. The job market is still somewhat inflexible, and finding candidates with the right profiles remains difficult because university curricula do not always meet needs. There is no shortage of good technicians, but the country lacks marketing, supply chain, and human resources managers.



Facts and Figures/ The Algerian market: 33 million inhabitants / Rising purchasing power: dairy product consumption of 9kg per capita (compared to 33kg in France) Danone Djurduja: sales of around €70 million / Danone 35% market share / 700 employees / Output of 100,000 tons in 2006 compared to 36,000 in 2002 / DANONE and its three business lines have been present in Algeria since 2006/

China/



ELLEN RUAN, Chinese, director of human resources DANONE China.

Attract and retain

It has become essential for us to both attract managers in China and to hold on to them. Between now and 2020 the Chinese economy will need 75,000 managers every year. Yet today there are only between 3,500 and 5,000 graduates a year. "To retain managers we conduct in-depth analyses with them of the career prospects the Group can offer. We then draw up a career path for the next three years. Then, as we do in other countries in the Asia-Pacific zone, we train the most promising young talent to become directors in 18 months."

Indonesia/

Grooming young talent

Indonesia is Groupe DANONE's newest frontier. It is present there in all its three business lines. Although the country posts an economic growth rate of around 5%, unemployment is close to 10%. DANONE's local Beverages subsidiary Aqua is seeking candidates

who are able to work in a company that was originally a family business and now belongs to an international group. In Fresh Dairy Products, we are looking for managers who have experience in the dairy products and can launch the company. The idea is thus

to build up a pool of talented young people who will develop as the business evolves and who will be very closely involved. To train these future managers the ideal solution is to send them to foreign subsidiaries like New Zealand or the United States.

In emerging countries

€695

million investment in plant. Increased production capacity for facilities in Mexico and Argentina and a new Biscuits plant built in Algeria.

In 2006 DANONE drew up a new model for production in emerging countries. Plants cost around 30-40% less than those which DANONE traditionally builds, while complying with DANONE's quality and safety standards. Plant design factors in production volumes and the cost of manpower in the countries concerned. The aim is to arrive at the level of investment needed to operate a facility at the lowest possible cost for the highest possible safety level. Modular solutions mean that the Group can move a plant elsewhere if necessary or extend it. The first facility to be designed and built in this way will be in Colombia.

NUEVA LEVITÉ[®] DE BONAFONT[®].



Todas las bondades de tomar
agua Bonafont[®] y un delicioso
sabor, **sin calorías.**

TOMA 2 L. DE AGUA AL DÍA.

KEY FIGURES

CLOSE-UP GROWTH IN 2006

In 2006, business was on the rise for all three DANONE business lines and in all geographical regions. With trading operating income up 10.1% despite a rise in raw-material prices, net current income up 15.6% and diluted current net income up 17.9%, we posted one of the strongest performances in our history.

15.8%

Net income on current business

was up from €1,031 million in 2005 to €1,194 million in 2006, a rise that reflects the combined benefits of higher trading operating income and lower financing costs associated with a decline in average net debt, as well as optimization of tax rates.

DANONE WORLDWIDE

NORTH AMERICA*

2,326 employees
No. 1 in Fresh Dairy Products (FDP)
Sales: €1.23 billion
8.8% of total sales
* USA and Canada

WESTERN EUROPE

20,688 employees
No. 1 in FDP
No. 1 in bottled water
No. 1 in biscuits
and cereal products
Sales: €7 billion
50% of total sales

CENTRAL AND EASTERN EUROPE

11,696 employees
No. 1 in FDP
No. 1 in bottled water
No. 1 in biscuits
and cereal products
Sales: €1.56 billion
11% of total sales

ASIA-PACIFIC

34,023 employees
No. 1 in bottled water
No. 1 in biscuits
and cereal products
Sales: €2.43 billion
17.3% of total sales

LATIN AMERICA

15,558 employees
No. 1 in FDP
No. 1 in bottled water
No. 1 in biscuits
and cereal products
Sales: €1.49 billion
10.5% of total sales

AFRICA AND MIDDLE EAST

3,833 employees
Sales: €320 million
2.3% of total sales

→ FINANCIAL HIGHLIGHTS

	2004	2005	2006	CHANGES 2006/2005
€ millions				
Income statement data				
Net sales	12,273	13,024	14,073	+8.1%
Organic growth	–	+6.7%	+9.7%	
Trading operating income	1,608	1,738	1,914	+10.1%
Trading operating margin	13.1%	13.35%	13.6%	32 bp ⁽¹⁾
Net income (excl. non-current items)	910	1,031	1,194	+15.8%
Net income (attributable to the Group)	449	1,464	1,353	
Cash flow data				
Cash flow provided by operations	1,574	1,716	1,891	
Capital expenditure	(520)	(607)	(692)	
Purchase of businesses and other investments ⁽⁴⁾	(98)	(636)	(575)	
Free cash-flow ⁽²⁾	1,204	1,303	1,516	+16.4%
Financial position				
Net debt	4,538	3,572	2,902	
Stockholders' equity (including minority interests)	4,506	5,621	6,069	
Debt/equity ratio	100.7%	63.5%	47.8%	
Current per-share data (€)				
EPS (fully diluted)	3.57	4.14	4.88	+17.9%
Dividend per share	1.35	1.78	2 ⁽³⁾	+17.7%

Market

No. of shares at Dec. 31 ('000)	268,095	264,235	260,865
Share price at Dec. 31 (€)	68	88	114.8
Market capitalization at Dec. 31 (€ millions)	18,217	23,252	30,000

Personnel

Total employees	89,449	88,184	88,124
Western Europe	22,492	20,985	20,688
Outside W. Europe	66,957	67,199	67,436

(1) At constant structure and exchange rates.

(2) Cash flow from operations less change in working capital and capital expenditures (net of disposals)

(3) Subject to the approval of the General Meeting of Shareholders.

(4) Net of cash acquired

→ NET SALES BY BUSINESS LINE

	2005	2006	rise on like-to-like basis
€ millions			
Fresh Dairy Products	7,184	7,934	+9.2%
Beverages	3,473	3,942	+14.8%
Biscuits and Cereal Products	2,367	2,197	+3.1%
GROUP TOTAL	13,024	14,073	+9.7%

→ NET SALES BY REGION

	2005	2006	rise on like-to-like basis
€ millions			
Europe	8,179	8,582	+5.1%
Asia-Pacific	2,235	2,429	+20.6%
Rest of the World	2,610	3,062	+16%
GROUP TOTAL	13,024	14,073	+9.7%

9.7% growth

Organic growth—that is, the rise in sales at constant scope of consolidation and exchange rates—reached 9.7% to set 2006 sales at €14,073 million.

Trading operating income rose 10.1%, net income on current items 15.8% and diluted net income per share 17.9%. Drivers for these performances included a strategic focus on innovation, DANONE's strengths in food for health, the leading market positions of our three business lines, and geographical expansion.

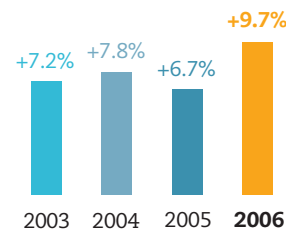
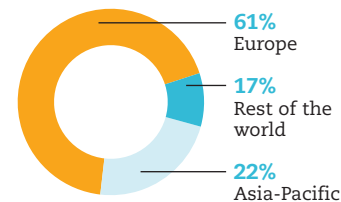
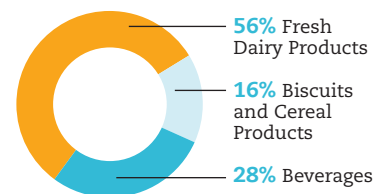
→ TRADING OPERATING INCOME

	2005	2005 ⁽¹⁾	2006 ⁽¹⁾
By business line (€ millions)			
Fresh Dairy Products	1,019	965	1,109
Beverages	474	448	504
Biscuits and Cereal Products	343	325	301
Unallocated expenses	– 98	0	0
GROUP TOTAL	1,738	1,738	1,914

→ TRADING OPERATING INCOME

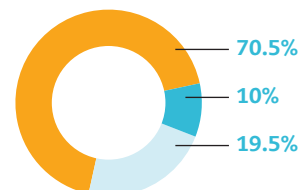
	2005	2005 ⁽¹⁾	2006 ⁽¹⁾
By region (€ millions)			
Europe	1,266	1,204	1,295
Asia-Pacific	256	239	244
Rest of the World	314	295	375
Unallocated expenses	– 98	0	0
GROUP TOTAL	1,738	1,738	1,914

(1) Unallocated expenses spread across subsidiaries.

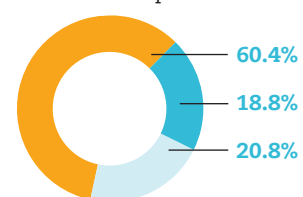


Net sales by business line and region

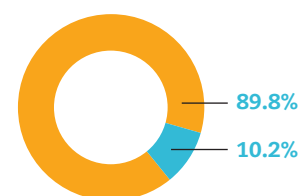
Eastern Europe



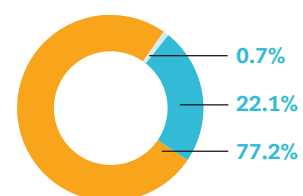
Western Europe



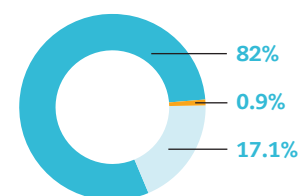
North America



Latin America



Asia-Pacific



● Biscuits and Cereal Products
● Beverages
● Fresh Dairy Products

13.6% margin

Operating margin was up for the 12th year in a row in 2006, showing a rise of 25 basis points from the previous year. At constant scope of consolidation and exchange rates, the rise was an even stronger 32 basis points. This reflects value-added product innovation, productivity gains, and optimization of fixed costs, which together fully offset the impact of higher raw material prices and an unfavorable geographical mix at Group level.

→ TRADING OPERATING MARGIN BY BUSINESS LINE*	2005	2006	change on like-to-like basis
Fresh Dairy Products	13.4%	14%	+68 bp
Beverages	12.9%	12.8%	-20 bp
Biscuits and Cereal Products	13.7%	13.7%	-1 bp
GROUP TOTAL	13.35%	13.6%	+32 bp

* After unallocated expenses have been allocated to business lines.

→ TRADING OPERATING MARGIN BY REGION*	2005	2006	change on like-to-like basis
Europe	14.7%	15.1%	+33 bp
Asia-Pacific	10.7%	10%	-15 bp
Rest of the World	11.3%	12.2%	+125 bp
GROUP TOTAL	13.35%	13.6%	+32 bp

* After unallocated expenses have been allocated to business lines.

15% growth

Growth in sales of Fresh Dairy Products exceeded 15%, driven by four star products—Actimel, Activia, Danonino and Vitalinea.

Fresh Dairy Products gathered further momentum in 2006, with its four blockbuster products providing continued impetus.

The vigor of these brands reflects their strong health image backed by dedicated research. A strategic priority for DANONE in the years ahead will thus be to increase capacity for health-related research and continue successes illustrated

by products such as Activia, Actimel, Vitalinea and Danonino. In keeping with this strategy, our Group has followed up the development of products targeting health concerns relating to growth, intestinal transit, obesity, immunity and cholesterol levels with the launch of Essensis, a unique fresh dairy product with scientifically proven cosmetic properties.

PER CAPITA CONSUMPTION

WATER (liters/year)

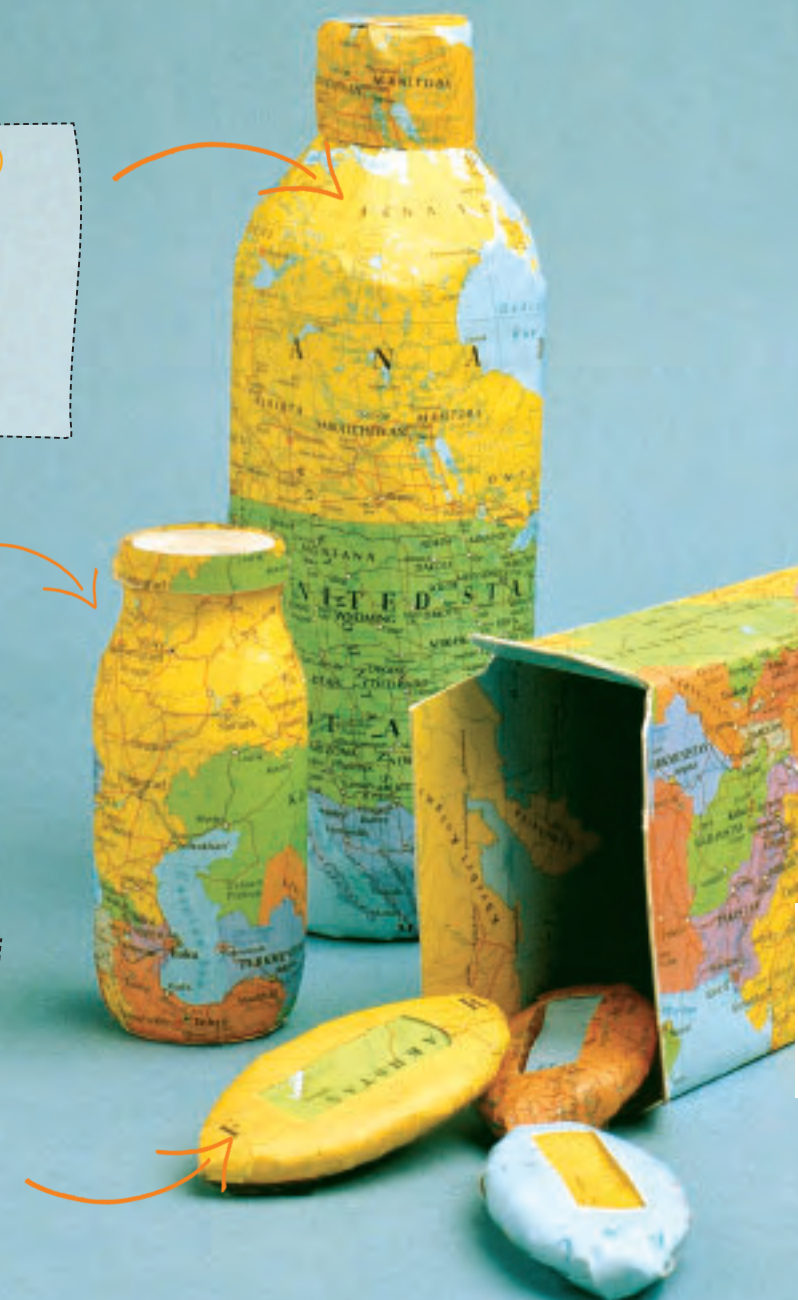
28: Average worldwide
110: Western Europe
30: Eastern Europe
95: North America
55: Latin America
13: Asia-Pacific
14: North Africa and Middle East

FRESH DAIRY PRODUCTS (kilos/year)

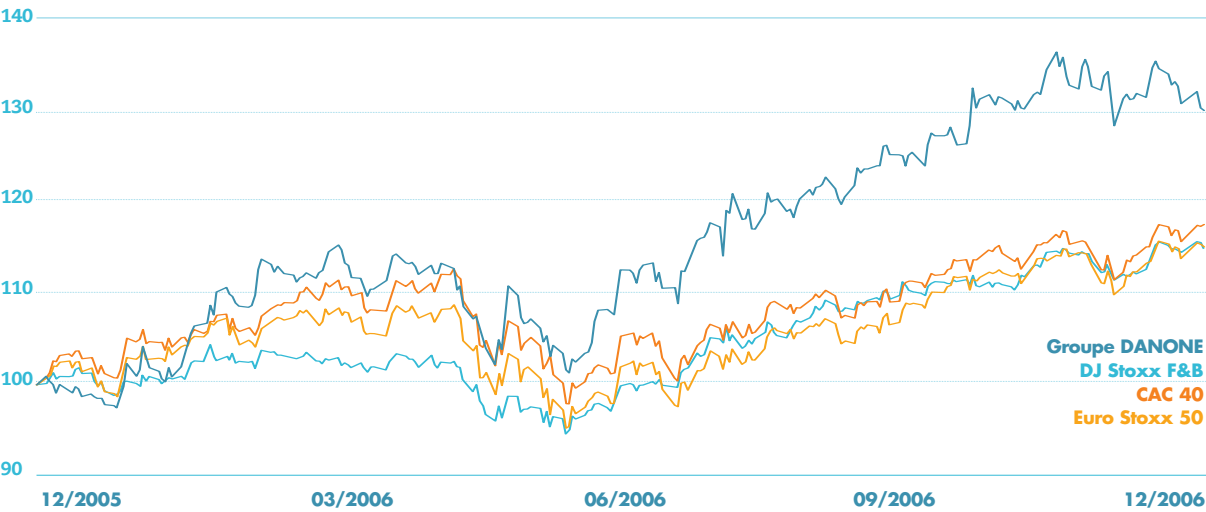
3.4: Average worldwide
20.7: Western Europe
6.1: Eastern Europe
7.6: North America
4.4: Latin America
1: Asia-Pacific
1.5: North Africa and Middle East

BISCUITS (kilos/year)

22: Average worldwide
7: Western Europe
4.2: Eastern Europe
8.2: North America
4.5: Latin America
1.0: Asia-Pacific
0.6: North Africa and Middle East



→ MAJOR STOCKMARKET INDEXES (FROM DEC. 30, 2005 TO DEC. 31, 2006)



→ KEY MARKET DATA AT 12/31	2002	2003	2004	2005	2006
€ thousands					
Market capitalization at Dec. 31	17,606	17,466	18,230	23,252	30,000
€					
Closing price for the year	64	65	68	88	114.8
High for the year	75	69	73	96	121.1
Low for the year	55	52	62	68	85.2
thousands of shares					
Average number of shares traded daily	1,574	1,599	1,271	1,427	1,212

→ DIVIDEND PER SHARE	2002	2003	2004	2005	2006
thousands of shares					
Thousands of shares	274,670	269,950	268,095	264,235	260,865
€					
Net dividend per share (excluding tax credit) ⁽²⁾	1.15	1.22	1.35	1.70	2.0 ⁽¹⁾

(1) Subject to the approval of the Annual General Meeting.
(2) Depending on legislation applicable to beneficiary; calculation based on 50% rate.

→ DIVIDEND AND SHARE BUYBACKS

Stock markets had a very good year in 2006, bouncing back from a mid-June low to set 12-month rises to December 31 at 17.5% for the CAC 40, 15.10% for the Eurostoxx and 15% for the DJ Stoxx Food & Beverage index. Danone shares outdid their benchmark indices with a rise of 30.2% over the year, providing renewed confirmation of the soundness of our Group's model for profitable growth.

Against this backdrop, the Board of Directors decided to ask the Annual General Meeting on April 26, 2007 to approve a dividend of €2 per share for the 2006 financial year, 17.7% more than the dividend paid for 2005. This dividend will be made payable from May 10, 2007. Considering its strong financial position, the company is planning to undertake an active program of share buybacks in 2007.

→ SHARE OWNERSHIP AT 12/31/2006

Groupe DANONE share ownership:

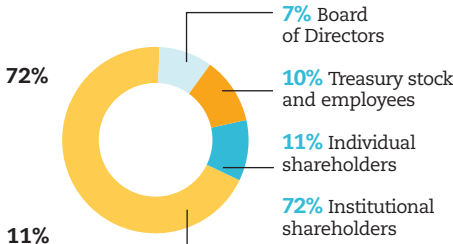
Institutional investors 72%

- France 27%
- US 17%
- UK 10%
- Other 18%

Individual investors 11%

Board of Directors 7%

Treasury stock and employees 10%



→ MAIN SHAREHOLDERS AT 12/31/2006	% of capital	% of voting rights
Eurazeo	5.4%	9.1%
Caisse des Dépôts et Consignations	3.6%	3.6%
Sofina and Glaces de Moustier	2.0%	2.5%
Predica	1.7%	1.7%

For more information

www.danone.com
17, bd Haussmann, 75009 Paris

Toll-free information number for investors calling in France: 0800 320 323

E-mail: finance@danone.com

Share buybacks and cancellations

4 million shares cancelled in August and December 2006.

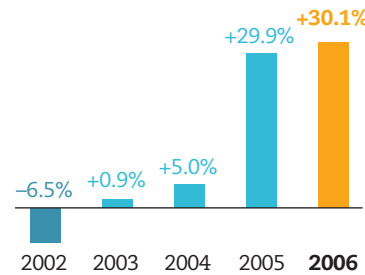
7,073,266 Group shares bought back in 2006.

20,455,171 own shares held at 31/12/2006.

A Group program to buy back 10% of its capital stock.*

* Subject to the approval of the Ordinary and Extraordinary Annual General Meeting on April 26, 2007.

→ SHARE PRICE 2002-2006



→ GROUPE DANONE SHARE DATA

Nominal: €0.50 per share (at December 31, 2006)
Number of shares: 260,864,746 (at December 31, 2006)
Markets: Danone shares are traded on Euronext Paris, on the Swiss Stock Exchange, and the New York Stock Exchange in the form of American Depositary Shares.

KEY FIGURES FOR ASIA

39% OF GROUP EMPLOYEES ARE BASED IN THE ASIA-PACIFIC REGION

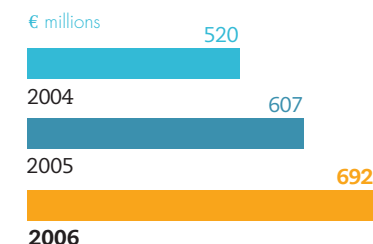
China 20,816
Indonesia 11,425
New Zealand 521
Malaysia and Singapore 1,092
Australia 169
Total 34,023

KEY FIGURES (€ '000)

FDP sales 21,879
Biscuit sales 416,315
Beverage sales 1,991,268
Total sales 2,429,462
Share of total Group sales 17.3%

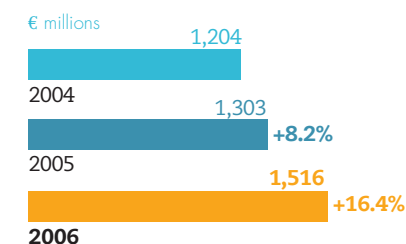
→ INVESTMENT IN PLANT AND EQUIPMENT

Capital expenditure rose from 607 million—or 4.7% of sales in 2005—to €692 million or 4.9% in 2006, reflecting a reinforcement of production and logistic capacities in high-growth regions. Net financial debt declined from €3,572 million at December 31, 2005 to €2,902 million at the same date in 2006.



→ FREE CASH-FLOW

Free cash flow showed a further rise of 16.4% in 2006, reflecting the combined impact of a rise in cash flow from operations and continuing efforts to optimize working capital requirement.



+15.9%

net current income per share

Diluted net current income per share was up 17.9% from €4.14 in 2005 to €4.88 in 2006.

Net income on current items rose 15.8% from €1,031 million in 2005 to €1,194 million in 2006, reflecting a rise of 10.1% in trading operating income combined with the lower financing costs associated with a decline in average net debt, as well as optimization of tax rates. Net income attributable to the parent to €1,353 million, a lower figure than in 2005, reflecting the impact of the divestment of sauce business during the year. This included a capital gain on the sale of Amoy Foods, which followed that of HP Foods in 2005.

Net extraordinary income on current business for the year came to €11 million, a figure which includes:

- a net capital gain of around €30 million on the sale of Griffins in New Zealand, and Home and Office Delivery business in Canada;
- value impairment of around €170 million relating to Robust in China and Home and Office Delivery business in Europe;
- use of a loss carryforward of approximately €150 million relating to Home and Office Delivery business in the US.

Key figures



→ SALES: TOP TEN COUNTRIES

€ millions

2,917
France

1,538
Spain & Canary Islands

1,493
China

972
United States

705
Mexico

604
Germany

542
Benelux

513
UK and Ireland

466
Italy

450
Argentina

SOCIAL AND ENVIRONMENTAL INDICATORS

→ WORKFORCE
AT DEC. 31, 2006

20,688
people
in Western Europe

11,696
people
in Eastern Europe

3,833
people
in Africa-Mideast

34,023
people
in Asia-Pacific

15,558
people
in Latin America

2,326
people
in North America

For a total
of **88,124**
employees worldwide

→ ENVIRONMENTAL INDICATORS	2005	2006
Production (000 metric tons)	17,848	18,266
Agricultural raw materials (000 metric tons)	5,297	5,811
Consumption of primary and secondary packaging, excluding reused bottles and demijohns (000 metric tons)	735	757
Recyclability of plastic bottles	100%	100%
Proportion of plastic bottles actually recycled	22% in Europe	22.7% in Europe
Recyclability of paper and cardboard containers	100%	100%
Proportion of paper and cardboard containers actually recycled	100% in Europe	77% in Europe
Surface area of land owned in richly biodiverse habitats (in hectares)	74,000 (Villavicencio)	74,000 (Villavicencio)
Production sites		
Total number	200	186
Cover rate	76%	77%
Total number of sites certified compliant with ISO 14001	84	90
Thermal energy consumption (000 MWh)	2,371	2,385
Electricity consumption (000 MWh)	1,668	1,744
Total energy consumption (000 MWh)	4,039	4,129
Total amount of waste generated (000 metric tons)*	239	238
Total amount of waste eliminated through specific waste management path (000 of metric tons)	180	192
Proportion of waste eliminated through specific waste management path*	75%	81%
Water consumption (000 of cubic meters)**	33,658	35,628
Wastewater COD (chemical oxygen demand) in 000 metric tons	4,103	5,576
Significant emission incidents (chemical and hydrocarbons)	none	3
Emissions of greenhouse gases (CO ₂ , CH ₄ , N ₂ O, CFC, etc.) in metric kilotones CO ₂ equivalent	520	510
SO _x (sulfur oxide emissions) in metric tons SO ₂ equivalent	2,608	2,128
NO _x (nitrogen oxide emissions) in metric tons NO ₂ equivalent	1,136	1,221
Gases depleting the ozone layer (in kilograms CFC equivalent)	1,579	791

*Excluding sludge from wastewater plants.

**Water consumed by plants, excluding water put into bottles and containers.

→ EMPLOYMENT INDICATORS

	2005*	2006
Net rise in employment		404
Europe		-280
Asia		-525
Rest of the world		1,209
Employees by region		
Europe	37%	37%
Asia	39%	39%
Rest of the world	24%	24%
Total employees at Dec. 31	87,720	88,124
Average permanent employees for the year	83%	84%
Average temporary employees for the year	17%	16%
Managers	11%	11%
Other	89%	89%
Male managers	62%	61%
Female managers	38%	39%
Other employees, men	70%	73%
Other employees, women	30%	27%
Permanent employees at Dec. 31		
< age 18	0.1%	0.1%
18 to 25	16%	15%
26 to 35	41%	40%
36 to 45	26%	27%
46 to 55	14%	14%
> age 55	4%	4%
Turnover of permanent employees as % of total workforce	17%	18%
% of business units whose employees are covered by a company or multi-sector collective agreement	76%	78%
% of business units with employee representatives (elected or appointed by a union)	83%	81%
Number of labor disputes with work stoppages	46	55
Number of workplace accidents with stoppages	1,106	1,070
Number of fatal accidents	1	0
Frequency of workplace accidents	8.4	7.6
% of employees insured for major risks (death/incapacity)	94%	97%
% of business units with profit-sharing agreements	44%	45%
Number of employees receiving training during the year	48,687	56,812
Managers	8,515	8,381
Other	40,172	48,431
Men	nd	na
Women	nd	na
Average number of training hours in the year	22	19
Managers	46	41
Other	18	16

* 2005 at comparable basis.



Frollini Vitasnella.
Fatti del bene ogni giorno.



Per il tuo benessere, scegli un'alimentazione quotidiana equilibrata. I Frollini Vitasnella, ricchi di gusto e con l'apporto nutrizivo delle fibre, ma con il 25% di grassi in meno* al giorno dopo giorno ti aiutano a stare in forma. Scegli tra Frollini Latte e Miele, ai frutti rossi e ai cereali. Da Saiwa.

HISTORY



40 YEARS OF PIONEERING SPIRIT

transformed French glass company BSN into DANONE, the international food group of today. The adventure that began under the bold, visionary leadership of Antoine Riboud in 1966 continues with the teams led by his son Franck since 1996 — now building on 40 years of achievement and openness to the world.

Pioneering spirit

At DANONE pioneering spirit means accepting risks, daring to strike out in new directions, and a capacity to overcome setbacks and move on to new successes.

Strategy

From geographical boundaries to business categories, nothing is ever taken for granted. For DANONE as for BSN, strategy has always meant being on the move.

1966

Birth of BSN After lengthy talks, two little-known French companies—flat glass specialist Glaces de Boussois and container glass manufacturer Souchon-Neuvesel—announce merger plans, setting the stage for the rise of DANONE. Antoine Riboud is named CEO of the new company, which adopts the name BSN a year later.

1968

A failed takeover bid and a new strategic direction Aiming to win new global reach for the French glass industry, Antoine Riboud seeks an agreement with glass manufacturer Saint-Gobain, but talks fall through. In late December 1968, Riboud mounts a hostile takeover bid—a first in France. The controversial move fails, but thrusts BSN and its CEO into the limelight. Antoine Riboud learns from the setback and rebounds, revising his strategy to expand downstream into the food industry.

From BSN to DANONE

No one could have foreseen it in 1966 but over the next 40 years French glass manufacturer BSN would become the world leader for fresh dairy products and number two for both bottled water and biscuits, its workforce rising ten-fold from the 8,800 employees it began with. In the late 1960s, supermarkets were springing up all over France, and consumption of bottled mineral water was skyrocketing. Anticipating the trend away from glass, Antoine Riboud, then CEO of BSN, shifted business focus from container to content, taking control of brewer Kronenbourg, Société Européenne de Brasserie and Evian in the early 1970s, and taking advantage of the 1973 Danone-Gervais merger to add fresh dairy products to the product portfolio. Drawing strength from successes in the food sector, from 1974 to 1979 the Group responded to economic changes with a sweeping overhaul of production facilities, and in 1979 sold off flat-glass manufacturer Boussois.

BSN was determined to achieve international scope and made a string of acquisitions in the world food industry, beginning in Western Europe and moving on to buy Dannon USA in 1981. Starting in 1990, the Group stepped up the pace of global expansion with a focus on Eastern Europe, Southeast Asia and Latin America, targeting categories where it could rival or outperform the world's top contenders. These sectors—biscuits, dairy products and bottled water—would become DANONE's three core business lines.



Danone shop, Moscow. When the Berlin Wall fell on November 9, 1989, it opened up a "strategic opportunity"—400 million people in search of better food. Three years later a Danone shop opened a few steps from Red Square.

New markets, new international reach

Specialized in fresh dairy products with Gervais fromages frais and Danone yogurts and desserts, the Gervais Danone group had already diversified with moves including the acquisition of Panzani pasta by the time it merged with BSN in 1973, giving it access to new markets. At 52% of sales, food was the primary activity of the new BSN-Danone group, which took its place as France's number-one food company. The Group first acquired Amora and Maille (sauces and condiments), Vandamme (cakes) and La Pie qui chante (confectionery), followed by Liebig (soups), Viandox (beef extract) and Materne (jams and compotes). It then took diversification one step further in 1986 with the acquisition of General Biscuit and its famous LU brand, following this

up in 1989 with that of Nabisco's European subsidiaries—Biscuits Belin in France, Jacob's in the UK and Saiwa in Italy. In less than 20 years, BSN-Danone's acquisition strategy had secured the number-three place in the European food industry, and the Group continued to expand its growth horizons. Having long foreseen the emergence of China and Southeast Asia, Antoine Riboud made a personal visit to China in September 1983 and a Danone team arrived in the country a year later. The launch of Guangzhou Danone Yoghurt Company Ltd. in 1987 gave the Group its first industrial presence in China, and this was followed by numerous initiatives in Poland, Turkey, Algeria, New Zealand and other countries. Today Asia, Latin America and Eastern Europe together account for over 40% of Group sales.

1994

BSN becomes DANONE At a meeting on July 7, 1994, BSN-Danone shareholders vote to change the name of the Group from BSN to DANONE. Already the world leader in fresh dairy products, the DANONE brand is present in more than 30 countries and accounts for nearly 25% of consolidated sales, projecting an image of natural health, pleasure and innovation exactly matching the Group's mission. A new logo—a child looking up at a star—symbolizes a new course. The little boy evokes every parent's desire to raise a healthy, well-nourished child, while the star is a universal symbol of hope and optimism.



1996

New focus Antoine Riboud steps down in May 1996 as President of DANONE as it celebrates its 30th anniversary. His son Franck takes over. Over the next ten years, the Group turns its full attention to three health-oriented business lines with maximum potential—fresh dairy products, biscuits and beverages. It makes some 50 international acquisitions and strategic partnerships in these sectors and sheds other activities. The sale of Amoy to Ajinomoto completes the strategic shift in 2006.

Innovation

At **DANONE** innovation means more than new ideas—it is also the courage to put them to work on a grand scale.

1994

Actimel A cultured milk drink in a distinctive bottle, Actimel is the result of ten years of research. Its special benefits derive from *L. casei* *defensis*, a probiotic culture that boosts the body's natural defenses when taken daily, as independent studies have confirmed. Sixty researchers continue to explore the strain's potential.



2000

Mizone This innovative energy drink for sports enthusiasts was created by Frucor, the Group's New Zealand Beverages subsidiary, and sales have soared since China-based Robust adapted it for sale on the Chinese market under the name Maidong. With added vitamins and sports-bottle packaging, the product appeals to active city dwellers who want the most out of life. A year after its launch in April 2003, Maidong took the top spot in the energy-drink segment and was named China's beverage of the year. In 2006 the product went on to make a strong start in Indonesia under the Mizone brand.



2004

Danacol A dairy product fortified with plant sterols that can help reduce bad cholesterol when consumed as part of a balanced diet, Danacol is now sold in ten countries, posting sales of €100 million in 2006. Strong health positioning and taste appeal have made it number one in the highly competitive cholesterol-reduction market and scope for continued growth means that Danacol has the makings of a top performer for Fresh Dairy Products in the future.



2007

Essensis: the beauty product in the dairy case

A fresh dairy product that nourishes skin from the inside, Essensis is a revolutionary new link between nutrition and cosmetics. The Group's R&D teams put all their resources to work over two years to develop ProNutris®, a groundbreaking formula that combines exclusive probiotic cultures with the beneficial omega-6 fatty acids in borage oil and the antioxidant power of green tea and vitamin E. Because ProNutris® works deep below the surface where skin cells regenerate, it benefits the entire skin and thus the entire body. Eating Essensis for six weeks improves the quality of the skin, making it healthier and more attractive. Before the launch of Essensis in Belgium, Spain, Italy and France, DANONE called on the support of two independent laboratories, one specialized in dermatology and the other in nutrition, to conduct clinical trials with the participation of 72 women over six months.



1995



1999

LU P'tit Déjeuner More than ten years of research went into P'tit Déjeuner, a range of slow energy release biscuits with sugar and fat content to complement a balanced breakfast. Packed with wholesome grains and slow-baked, P'tit Déjeuner provides sustained energy with slowly digested carbohydrates and a low glycemic index. When enjoyed as part of a healthy breakfast, it helps to keep appetite in check throughout the morning. Several versions of the product are on sale in more than ten countries.



Evian introduces an exclusive, revolutionary new technology to cut packaging volumes with breathtaking simplicity—a squeeze of the hands brings the compactable bottle down to 25% of its original size.

1987

Activia "Works on the inside, shows on the outside." Activia built its reputation on this slogan. Now sold in various versions in more than 25 countries, this milk product with the active bifidus ferment promotes regularity when consumed daily—a health claim backed by four clinical studies.

Commitment

Economic activity is there to serve people: embracing this common-sense principle consistently for 40 years has often made DANONE a pioneer.



Guiding principles, guiding lights

In a 1972 speech to the French employers' federation, Antoine Riboud declared his determination not to sacrifice people to profits, setting the course for Group policy to this day. Although DANONE's geographical boundaries and business divisions have changed, the Group has remained true to Riboud's vision, closely linking corporate values, management style and social responsibility. Riboud quickly put his principles to work. As early as 1975, for example, the Group began redeveloping sites affected by reorganization and closures, and in 1988 the vast majority of the Group's employees in France logged less than a 37-hour work week. Since 2001, our DANONE Way program (see page 33) has systematically and continuously fostered progress with all our partners employees and shareholders, customers and consumers, suppliers and local communities. We launched our first major environmental initiative—an anti-litter campaign—in 1971, long before sustainable development was in the news, and in 1992 the Group was instrumental in the adoption of a French eco-packaging decree making businesses responsible for final disposal of their packaging. Today, DANONE continues to make an active contribution to economic and social development with pioneering social and environmental policies.

1972

Speech in Marseilles "The company's responsibility does not stop at the factory gates or office door. Its action has repercussions throughout the whole community and influences every citizen's quality of life. The jobs that it generates condition individuals' whole lives. Their future and that of their children depend on the possibilities of change and promotion that the company offers. Through the energy and raw materials that it consumes, through the nuisances that it generates, it gradually changes the appearance of our planet and even its balance. The public see to it that we are reminded of these responsibilities in this industrial society. [...] It is clear that growth should no longer be an end in itself, but rather a tool used to serve the quality of life without ever being detrimental to it."



2006

Fighting malnutrition in Poland

Danone Poland began its campaign against malnutrition in 2002 forming a partnership with two Polish scientific institutes to launch Poland's first national study of nutrition in four-year-olds, and later raising public awareness of the problem by organizing the country's first national conference on malnutrition. In another important move, Danone fortified Danonki—the local version of Danonino—with essential nutrients, calcium and vitamin D. In 2006, DANONE took the next step with the launch of Mleczny Start, a porridge with extra minerals and vitamins D, C, E and B6 to provide a nutritious breakfast for schoolchildren. Poland's first nutritional product targeting social progress, Mleczny Start was developed by Danone Poland in partnership with Lubella, which leads the Polish market for grain products; Biedronka, the number-one discount distributor; and the Mother and Child Institute, a major Polish institution for medical research. In a strategy devised by Groupe DANONE, Lubella produces Mleczny Start, the Mother and Child Institute verifies its nutritional content and Biedronka distributes the product through its nationwide network. Each partner agreed to slash margins to the minimum, making Mleczny Start—priced at around 15 eurocents per packet—affordable for even the most disadvantaged families. The product is the first of its kind for European consumers.

1987

Groupe DANONE becomes the world's first corporation

to open international talks with the International Union of Food Workers' Associations (IUF). The dialog produces six agreements establishing joint international guidelines on the exercise of union rights, qualification training, working conditions, business changes that affect jobs, and other issues. The closely monitored agreements were updated in 2005 to address the Group's geographical expansion and incorporate the fundamental social principles contained in the International Labour Organization Convention.

1971

Vacances propres launched in France. The program aims to reduce litter by encouraging tourists to use prominently placed striped bags for trash. In 2006, some 65,000 collection points were set up in 1,300 vacation venues with the support of the business community.

2004

The Evolution program set up to back employability of Group staff members. In a rapidly changing job market where no employer can guarantee a job for life, Evolution has two goals: to bolster the Group's performance by continually enhancing the skills of employees, and to promote active job security by fostering mobility and professional development. Designed for the 89% of our staff who are not managers, Evolution helps employees lay the foundations for new opportunities at DANONE—and beyond.

(Re)invention

DANONE joins micro-credit specialist Grameen for a groundbreaking initiative in Bangladesh, experimenting with new models for local development and inventing a whole new way of doing business.



Ribbon-cutting

Grameen Danone Foods officially began operations in Bogra, Bangladesh on November 8, 2006. On hand to open the new plant were Grameen President and Nobel laureate Muhammad Yunus, DANONE CEO Franck Riboud, and French soccer star Zinedine Zidane, DANONE's goodwill ambassador for children's programs. "This isn't charity," said Riboud. "We want to develop a genuinely community-based business model in Bangladesh. The Group's strong financial results give us room to experiment with projects combining business performance and social progress." Yunus applauded the creation of "a business with a strong social component that will combine concern for the local population with profitability." After signing the official plaque, Zidane joined youngsters in Kamar Basuli village for a soccer match.

Building a social business

The mission of Grameen Danone Foods speaks for itself: to reduce poverty by bringing health through food to children using a unique community-based business model. A joint venture launched by DANONE and Grameen in March 2006, Grameen Danone Foods is a business—and as such must turn a profit—but its priorities are reversed. While the purpose of a traditional business is to maximize profits without losing sight of impact on the community, Grameen Danone Foods seeks to maximize community benefits without losing sight of profits.

Without profitability the project cannot expand, since income from the first group of plants will fund construction of the next, but its success will be judged primarily on largely non-financial criteria.

These include the number of direct and indirect jobs created upstream among dairy producers and downstream among small retailers and the door-to-door saleswomen known as Grameen Ladies; better child health as measured by an independent non-governmental organization; improved living conditions in the communities around the plant; and positive impact on the local environment.

DANONE's experiment with this pioneering model is a meaningful step towards fulfilling our mission—bringing health through food to a majority of people—but it also affirms the Group's longstanding commitment to development and moves us closer to the business model of the future.

For more on Shoktidoi, our new product in Bangladesh, see page 45.



Doing business differently

"For years I've worked to build bigger, more sophisticated plants with more and more automation and capacity measured in hundreds of millions of tons. In Bogra I had to build a plant with a tiny fraction of the capacity—only 3,000 metric tons—50 to 100 times smaller than a typical plant in three months for just €700,000. We also had to keep automation to a minimum to create as many jobs as possible and reduce the number of qualified personnel needed to run the unit. So I did the opposite of everything I'd ever done before. I couldn't get ideas from existing plans or use standard equipment, which is generally European. I found new suppliers in Asia and asked our usual suppliers to come up with creative solutions. The challenge really energized us. Having to slash operating costs and make a positive environmental impact also forced us to find new solutions, like lighting the plant with gas from our compost

and using biodegradable PLA packaging (see p. 55) for the first time in the Group's history. We also had to re-examine our product concept. For example, using sugar would have meant importing it—an expensive proposition with no benefit to the local economy. So we used locally produced date molasses and adapted the recipe. Another problem was the lack of refrigeration between milk collection points and the plant, but we managed to find the perfect product to maintain milk quality in transit. The challenges we face here have forced us to think more creatively and question our assumptions. And I know that some of these atypical ideas will be adapted in other parts of the Group."

GUY GAVELLE, Industrial Director,
Danone Asia

Investing in danone.communities

The launch of Grameen Danone Foods quickly generated strong interest, not only among advocates of the social business model, but also within the DANONE community—our partners, suppliers, customers, investors and individual shareholders. To involve as many interested parties as possible and lay the groundwork for expanding and adapting the project in other parts of the world, the Group is setting up danone.communities, a unique investment fund for anyone interested in making a meaningful, prudent* investment designed to promote new models for development and at the same time ensure at least a minimum return. The first investments in danone.communities will fund new Grameen Danone plants in Bangladesh and new projects on other continents.

* Structured by Crédit Agricole, a leading European bank, the danone.communities fund aims for a return equal to the money-market rate less actual management expenses.





5

40 countries continents

2,5 million children

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