



Probi is here!





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This is Probi

Probi is a leading biotechnology company that identifies patented and effective probiotics and licences them to international companies, mainly in the fields of foodstuffs and dietary supplements.

Probi's customers include Danone, Skane Dairy, Institut Rosell, Metagenics and Health World. The global market for probiotic products is showing good growth. The trend towards health and well-being is boosting the industry, as are new insights into the benefits offered by probiotics. The media is also helping by educating and informing the public of the positive health effects of probiotics.

Probi has been offering probiotics on a commercial basis since the mid-1990's. Our product offering is based on probiotic research and development, an area in which Probi is a pioneer and one of the world's leading companies. The main areas on which Probi's research focuses are gastrointestinal disorders, the immune system, cardiovascular diseases, and stress and performance recovery.

Probi's research is well-regarded internationally and our offering is of a documented high standard. Probi's bacteria are robust and well-suited for industrialisation. Collectively, these factors allow Probi to charge higher licensing fees than those charged by the industry as a whole.

Probi is based in Lund and has 18 employees. The Probi share is quoted on the Nordic list of the Stockholm Stock Exchange.

THE YEAR IN BRIEF

- A new two-year partnership agreement was signed with Danone. The product concept with which Danone is working is commercially interesting and the new agreement removes previous limitations on Probi's other offerings.
- The growth rate in royalty revenues from sales of the ProViva fruit drinks doubled to 21 per cent in 2006 (10), and totalled SEK 21.4 million.
- There was continued substantial interest in dietary supplements based on Probi's probiotics. New distribution agreements were signed for Canada, Germany, Sweden, Norway, Finland and South Africa. Dietary supplements will be launched in the majority of these markets in 2007.
- Probi won a breakthrough order from Metagenics, which is the leading brand name for dietary supplements in the health care sector in the US. Probiotics will be sold directly to Metagenics, which means a step forward in the value chain for Probi.
- Rolf Bjerndell took over as the new Acting CEO.
- Clinical studies began on a new probiotic composition intended to reduce inflammatory disorders of the kind that can develop during cancer treatment, for example.
- A clinical trial of probiotic usage in connection with colds began in late 2006. Two of Probi's new bacterial strains will be tested, partly to see if the number of colds decreases and partly to see if the duration of the colds is reduced.

Probi's business concept and motivation

BUSINESS CONCEPT

Probi shall be a leading research and development company that supplies industrial players with commercially interesting product concepts based on bacterial cultures with a probiotic effect.

VISION

Probi shall, through its research, be the most attractive partner and supplier of probiotic concepts for leading producers of probiotic products.

FUNDAMENTAL VALUES

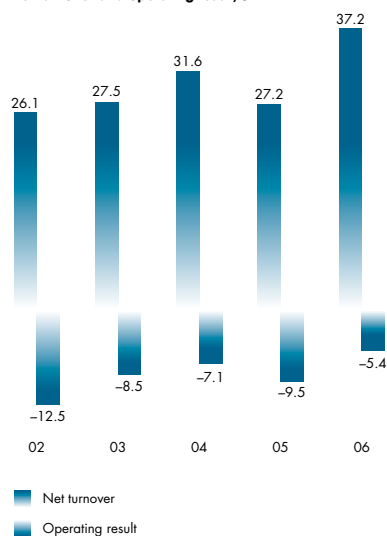
Probi aims to create health-promoting product concepts that enable people to feel better, stay healthy and live longer.

BUSINESS MODEL

Probi shall sign agreements with a variety of players for the commercialisation of bacterial cultures. The probiotics are licensed in return for royalties on ongoing sales or are sold as semi-finished goods or consumer products. The business model is based on Probi's ability to patent the results of its research in order to protect spheres of use for bacterial discoveries in a variety of functional areas.

Probi's research aims to identify, evaluate and clinically document commercially interesting bacteria and probiotic product concepts. Probi's probiotics shall have a high level of survival in their end-products and the probiotics shall be thoroughly documented, effective and clinically tested, in order to ensure that they are always regarded as the leading products in the field.

Net turnover and operating result, SEK m





What are probiotics?

Did you know that:

The food we eat affects our well-being. Which isn't that strange, considering that 70–80 per cent of our immune system is located in the gastrointestinal tract. Once the food has passed through the entire digestive tract, it has been exposed to a surface area of approximately 250 m² – the same size as a tennis court.

Probiotics are live microorganisms that have positive effects on health and which are a natural part of a human being's intestinal flora. Beneficial bacteria are found in food fermented in lactic acid, such as sauerkraut, pickled gherkins, marinated green olives, yoghurt, soured milk, cheese and salami. These foods contain large quantities of naturally occurring live bacteria in the form of lactobacilli, some of which may be probiotic, unless they are heat treated after manufacture, which is unfortunately common. Some of these naturally occurring lactobacilli may be probiotic. The shelf-life of a food product can be increased naturally by using beneficial bacteria to eliminate harmful ones.

Changes in our dietary habits and lifestyles have, however, resulted in a reduction in the amount of beneficial bacteria that people consume. Consumption of food fermented in lactic acid declined dramatically after the introduction of the refrigerator. At the same time, people's intake of a completely different type of bacteria that grows in refrigerators and which causes the body to react by becoming inflamed has increased. A shift in the digestive tract from lactobacilli to bacteria that promote inflammation can affect our immune systems, increasing the risk of disease. Not all of the causal links have been clearly established, but research is increasingly supporting linkages of this kind. Not all of the bacteria sold as probiotics have documented health effects and certain probiotic strains are more effective than others, depending on the nature of the health problem.

Probiotic research was not taken seriously until recently, when research opportunities increased dramatically with the availability of new, genetically-based methods of recognising different types of bacteria.

WHY PROBI'S PROBIOTICS?

Probi is a pioneer in terms of commercialising the findings of probiotic research. Fresh and dry foodstuffs are both capable of functioning as a host for probiotics, but because probiotics are live microorganisms, some types of food are better carriers for probiotics than others. The challenge is to keep the probiotic alive, all the way from manufacture and distribution to storage, in-store sales and, finally, consumption.

Several of Probi's patented bacterial strains are more robust than many other strains and have a good survival rate, which makes them well-suited for use as additives in fruit drinks and dietary

supplements, for example. This fact helped make Probi the first company to be able to offer fresh fruit drinks containing probiotics – something that the company is still relatively alone in being able to do. Probiotics allow both human immune systems and human metabolisms to be affected, boosting hopes that it will eventually be possible to prevent and influence not only digestive disorders, but several other prevalent endemic diseases. Probi aims to seek out, identify, evaluate and clinically document bacterial strains and probiotic product concepts in the following therapeutic areas:

STRESS AND PERFORMANCE RECOVERY

Stress, poor dietary habits, disease, lack of sleep and antibiotic treatments can all disrupt the balance between good and bad intestinal bacteria, increasing the risk of intestinal disorders and infections. Probiotics can restore the balance and can help the body recover after physical exertion.

CARDIOVASCULAR DISEASES

A constantly elevated inflammatory level in the body (systemic inflammation) increases the risk of cardiovascular diseases, among other things. Probiotics can help reduce abnormally high inflammation levels and thereby counteract disease.

IMMUNE SYSTEM

Disruptions to the body's bacterial balance can affect its immune system. If the immune system reacts incorrectly, it can lead to chronically elevated inflammation levels, whether locally or systemically, increasing the risk of cardiovascular diseases, cancer, type II diabetes, fatty liver and possibly even obesity. A person's immune system can also attack their own body (autoimmunity), which can cause type I diabetes, rheumatoid arthritis, MS, and the inflammatory bowel disease known as Crohn's disease. An over-reacting immune system can also cause allergies. Probiotics can help keep the immune system in shape.

GASTROINTESTINAL DISORDERS

Research has shown that probiotics alleviate the symptoms of people suffering from irritable bowel syndrome (IBS). Research findings also support the belief that probiotics can improve the digestive process and nutrient absorption, and that they can also counter symptoms associated with inflammatory intestinal disorders.

Probi may also expand its research into other therapeutic areas if they are deemed to have commercial potential.



Did you know that:

You should consume several billion beneficial bacteria a day to keep your intestinal tract flora healthy. One drinking glass full of ProViva corresponds to 10 billion beneficial bacteria and boosts the growth of other health-bringing bacteria.

The CEO's statement

The past year marked a turning point in Probi's development. Interest in Probi's probiotics increased during the year and will lead to, among other things, the launch of dietary supplements containing our probiotics on a number of geographic markets in 2007.

One of the more interesting agreements signed was with the American firm, Metagenics, which is the leading brand name in the field of dietary supplements for the professional health care sector in the US. Probi already has a successful partnership with Metagenic's subsidiary, Health World, which sells dietary supplements containing Probi's probiotics in Australia and New Zealand. The partnership offers additional potential in that Probi can become an important partner in tandem with Metagenic's planned expansion of its product offering.

The partnership with the French-Canadian Institut Rosell was just as successful, leading to a number of new licensing agreements for dietary supplements containing Probi's probiotics. The dietary supplements will be distributed by well-known companies, including Merck and Ferring Pharmaceuticals.

Sales of ProViva were also pleasing last year. Skane Dairy increased the scope of its marketing and this, coupled with new distribution partnerships, resulted in substantially boosted sales.

The market

Both the Swedish and foreign media have played a positive role in educating consumers by highlighting the health effects of probiotics and other food product ingredients.

We are also seeing the food industry becoming more and more concerned about having the right products on the market. Probi can make food products more nutritious, e.g. by adding probiotics or by combining probiotics with fruit, fibre or minerals to reinforce a range of health effects. Demand for more nutritious food is pushing this trend, and as a result, the food industry is adapting its products in line with what customers want in a completely new and different way than before.

Clinical documentation strategically important

Risk aversion levels are high among both existing and new customers, so the importance of the safety aspects of food product ingredients has increased.

The impending regulation of health claims within the EU will help tighten the requirements for verification of food product contents, making Probi's clinical documentation strategically important in supporting the claim that probiotics are natural, safe and have demonstrated health effects.

Customer support

We must be able to offer our customers support throughout the entire production process for new foods and food products – from taste to experience of well-being. To meet this requirement and to help our customers get on to the market quickly, we strengthened our resources in the field of application development last year. Our product development work made further progress and the results of this success include the fact that we can now add probiotics to dry foods such as breakfast cereals while maintaining the shelf-life requirements.

The Dietary Supplements business area now has a more flexible business model, as can be seen from the fact that we also started offering finished products, alongside semi-finished products and royalty-based revenues, during the year. This boosted both the top and the bottom line of our Income Statement. Our ability to offer finished products moves us a step up in the value chain and, at the same time, enhances the potential for improving both our result and our margins.

Research

Probi has focused primarily on the immune system and on an inflammation-related concept. Probi's probiotics can have a moderating effect on the substantially elevated inflammatory status that develops after radiotherapy and chemotherapy, and the focus on this research field hence has considerable potential in the health care sector. Cardiovascular diseases are also, essentially, inflammatory processes, so probiotics may be appropriate for a wide range of user groups. Overall, we believe that our research portfolio has substantial potential.

The Chairman's Statement

There is no doubt that Probi is making findings that are of considerable scientific and commercial interest, both in Sweden and internationally. Probi is a world-leading company in the field of probiotics, with several highly respected international partners and a strong research portfolio. At the consumer stage of the chain, products containing Probi's bacteria have a turnover in excess of SEK 500 million and are reporting impressive growth driven by the company's partnership launches and increasing market shares.

I will not hide the fact that getting our products out on to the market has been a tough process. Health World, our partner in Australia, and Skane Dairy, have both been very successful, but it has taken slightly longer than expected to bring new partners on board. This is why we are delighted that our efforts to increase our market orientation have already yielded results. Probi

has gained four new partners during the past six months, all of which are now on the verge of market launches. Our increased emphasis on the market demands both that we ensure we have the requisite skills and that Probi works in an even more unified manner internally – that there is a single connecting thread running all the way from research and commercialisation to the finished product and sales.

Probi will soon be able to offer finished probiotic concepts in all of its business areas. We intend to broaden the spheres of use and to offer probiotics to treat even more symptoms with the help of a body of scientific expertise that few in our field can match.

I have also noted that, in addition to our internal work on market orientation, Probi is also benefiting from an extremely positive market trend. From previously operating in a market with a few players, we now operate in one with

a whole string of players and considerably more consumers who are aware of the positive health effects of probiotics.

The Board of Directors has been heavily and actively involved in the company over the past year. The internal transformation work towards an increased market focus in a revitalised market will allow Probi to demonstrate its sustainable profitability.

Stockholm, March 2007

Peter Zakrisson
Chairman of the
Board



Outlook

We look forward to the future of the Dietary Supplements business area with considerable confidence. The growing dietary supplements market makes it easier to complement our product offering with new product alternatives. The regulatory environment is not as extensive and shelf-life is one of the reasons why it is easier to add probiotics to dietary supplements than to food products. Many dietary supplement agreements signed last year will lead to product launches in 2007.

The model for our agreement in the US, which is new to us and involves our selling directly to the customer, can also be applied in other geographic markets, so there are grounds for expecting more direct selling agreements to be signed this year.

We also, in addition to our US agreement, signed an agreement with a company called Biostime for the Chinese market. Our partner, Institut Rosell, is building a factory in China in partnership with Biostime. The factory will produce probiotics, which was part of the reason why we decided to move into the Chinese market.

We will be monitoring the launches in the various geographic markets closely and expect to sign additional licensing agreements during the course of the year. We will continue to build up the company and to position it in line with the resources demanded by existing and future customers.

It is vital that we are able to meet the demands and expectations of our customers – and we must demonstrate, in 2007, that their confidence in us is justified.

Lund, March 2007

Rolf Bjerndell
Acting CEO



Per-Ola Forsberg, Executive Vice President and CFO, and Rolf Bjerndell, Acting CEO.

Operations

Probi's market offering is divided into three business areas; Functional Food, Dietary Supplements and Clinical Nutrition.

- **Functional Food offers food producers thoroughly documented probiotic bacteria.**
- **Dietary Supplements offers manufacturers and distributors of dietary supplements well-documented, high-quality probiotics.**
- **Clinical Nutrition offers probiotic concepts for use in nutritional solutions in the health care sector.**

Probi's primary research fields are gastrointestinal disorders, immunological defence, cardiovascular disease risk factors, and stress and performance recovery. Probi chose these fields because they have an impact on many people and are areas in which probiotics can have a positive effect.



Functional Food

- **ProViva posted massively increased sales in 2006.**
- **Danone signed a new, two-year partnership agreement.**
- **Marketing activities increased in drinks and dairy products.**

OFFERING

The term “functional food” refers to food products that have been enriched with ingredients that have positive effects on health. Probi offers probiotic bacteria cultures that are robust, have well-documented positive health effects, which boost the value added of the licensees’ products and helps ensure that the customers are prepared to pay a higher price.

The probiotics are licensed for use in return for a royalty payment on ongoing sales to the retail trade.

Probi’s production technology expertise, along with its build-up of an extensive body of knowledge and expertise with regard to probiotic additives to food products, strengthen the product offering. This is important to new customers because it reduces time-to-market.

THE MARKET

The global market for functional food continued to report healthy growth in 2006 with a generally strong increase in sales of health foods and value-added food products. The growing understanding of the benefits of probiotics and the continued interest in personal health are benefiting the market. Overall, the main driving forces behind the market growth are:

- New realisations of the benefits offered by probiotics.
- Greater awareness and a continued interest in personal health.
- The food industry’s efforts to achieve higher margins and growth via innovative products.
- The authorities’ efforts to achieve better standards of public health and hence lower health care costs.

The probiotic food market is dominated by dairy products, with the Japanese firm, Yakult, and the French firm, Danone, among the market’s biggest players. The highest per capita consumption of probiotic food is in Japan where probi-

otic drinks have been available for many years and where many people have a positive attitude towards the effects of probiotics.

In recent years the use of probiotic food has grown stronger in Europe than in the rest of the world. The trend is being reinforced by extensive marketing from several of the major manufacturers, including the French firm, Danone. Increased consumer marketing contributed to higher growth rates in the US market as well.

Several countries have chosen to regulate the ways in which functional food may be marketed, the aim being to protect and guide consumers. In Sweden, product-specific claims have, to date, been approved by the Swedish Nutrition Foundation, SNF, but a new, EU-adapted regulatory framework is expected to come into force in 2008. The health claims are based on the product’s scientific documentation. From a marketing perspective, probiotics can be divided into three tiers.

- Foods with product-specific health claims.
- Foods with general health claims.
- Foods without approved health claims, but with a clear health-oriented positioning.

There is a trend towards increased awareness on the part of consumers with regard to the contents of food products, therefore contents labelling is becoming increasingly important. This is expressed not only in terms of flavour, but in the increasing importance of the food product’s health and nutritional properties for the consumer.

Probi has strengthened its application development resources in order to support the company’s customers in their product development work. The reason for this was that food companies’ expertise and experience when it comes to working with bacteria in the products is not normally as extensive as those of dairies. Probi has also strengthened its marketing resources with the aim of further expanding the customer base.

Did you know that:

The global market for probiotic functional foods is valued at approximately SEK 100 billion. Probiotic food account for just under 20 per cent of the functional food market. The annual growth rate in recent years is in excess of 10 per cent, in contrast to an annual growth rate of 3–4 per cent for the food market as a whole. Probi believes that the growth rate for probiotic food will, in the future, exceed 10 per cent on a yearly basis.



Functional Food



DANONE

Danone operates in 120 countries and is a leading supplier of probiotic products. A new, two-year agreement was signed with the French food giant during the year. Probi believes that the product concept which Danone is working with is commercially interesting, and the new agreement removes the previous limitations on Probi's other offerings.

SKANE DAIRY

Royalty revenues from sales of ProViva fruit drinks increased by 21 per cent (10) in 2006, and totalled SEK 21.4 million. ProViva is available in the form of fruit drinks, fruit shots, soured milk and drinking yoghurt. The fruit drinks are the only probiotic products in Sweden to have a Swedish Nutrition Foundation-verified product-specific health claim.

"It is currently true to say that at one end of the scale, we have pharmaceutical products, and at the other, we have food products. In the future, we may well have products that are in-between these two poles, products that are both food products and pharmaceutical products – food pharmaceutical products," says Annika Åhnberg, entrepreneur and former Swedish Minister for Agriculture, Food and Fisheries.



Increased marketing and a large number of in-store demonstrations helped bring about a bigger than expected increase in sales. Skane Dairy has expanded its production capacity and has also introduced the new 300 ml packaging size. A new flavour, mango, was launched during the year, and overall, ProViva took market shares within the chilled fruit juices sector.

ProViva has been a sales success ever since its launch in 1994 and revenues have increased by over 10 per cent every year.

THE FUTURE

The health trend is helping to ensure a continued positive market performance which will benefit Probi.

Probi may also benefit from the regulations on health claims that the EU is planning to introduce, depending on how consumer-friendly they are. The details of the regulatory structure are, as yet, unclear, but it would be useful if the health claims were linked to the bacterial culture, rather than to the consumer product, because this would enable Probi to use the health claims for its probiotics in other applications as well. If the Apoteket monopoly on the sale of pharmaceutical products is abolished, Probi's sales could well benefit from the new category of pharmaceutical and health stores expected to emerge.

As Probi develops its production technology know-how, the bacterial strains and product solutions will become increasingly stable, which will pave the way for probiotics to be added to room-temperature dried food products, such as breakfast cereals or biscuits. Probi believes that this development work offers massive potential for the future in the form of new probiotic applications for both dried and liquid food products.



The fruit drink, ProViva, which contains Probi's probiotics, had a very successful year in 2006, with sales volumes increasing by a massive 16 per cent (2). One important reason for this success was the increased marketing work by its producer, Skane Dairy.

Starting in May, an advertising film began to air on TV4 and Kanal 5. A new flavour, mango, was introduced and quickly became the third best-selling ProViva drink. A new and more grip-friendly type of packaging, known as a diamond curve-type, was introduced. The campaign was supported by 400 in-store product demonstration days.

"We made a big one-off investment and many things happened simultaneously. The effects were particularly pronounced during the autumn, when ProViva's sales increased by 25 per cent. Sales increased to a far greater extent than we had dared hope," says Anders Ahlström, Brand Name Manager for ProViva at Skane Dairy.

An additional 150 product demonstration days were held during the autumn in parallel with a re-showing of the advertising film.

Skane Dairy sharpened its portfolio of ProViva products. This led to the yoghurt being removed from the product range, which was complemented instead with soured milk and drinking yoghurts, and the new 300 ml packaging size was introduced for the fruit drinks. The new size gave ProViva access to the service retail trade, thereby further expanding the brand name's exposure.

Skane Dairy has, alongside its marketing of ProViva, also initiated a long-term strategic investment in profiling health food products more clearly on store shelves. This investment has also had a marginally positive effect on ProViva's sales.



Anders Ahlström

Dietary Supplements



- **Highly competitive, with a cost-effective offering.**
- **Continued positive momentum and several new distribution agreements signed.**
- **Strategically important agreement with the American firm, Metagenics.**

PROBI'S OFFERING

Dietary supplements are foods designed to complement a normal diet and are often sold in the form of capsules, tablets or sachets. They include everything from simple products, such as vitamins and herbs, to more highly refined and documented products.

Probi's probiotics are used in products such as dietary supplements to treat gastrointestinal disorders. Manufacturers and distributors of dietary supplements are offered well-documented, high-quality probiotics in the form of ingredients, semi-finished or consumer products. The probiotics are licensed in return for royalty payments on ongoing sales, or are sold as semi-finished or consumer products.

If the ingredients need to be documented, there are certain synergy benefits with the Functional Food business area, which can help to lower Probi's development costs.

OPERATIONS

The strategy is to commercialise bacterial strains that Probi has successfully documented. Probi primarily targets pharmaceutical companies with non-prescription products, nutrition companies and companies that have established sales channels to the above. The credibility of the offering is strengthened by acquiring reference customers among pharmaceutical companies and recommendations from the medical profession.

Probi's offering has attracted considerable interest for several years now, and in 2006, this was confirmed in the form of a number of new licensing agreements for various geographic markets. Working with partners to cut costs has generated greater flexibility in the pricing structure, resulting in increased competitiveness. The business area obtained additional resources for marketing purposes during the year.

Dietary supplements containing Probi's probiotics are currently being launched in Germany, South Africa, Canada, the US, Norway and Finland as a result of the agreements signed during the year, and in early 2007, an agreement was signed for the Chinese market. Dietary supplements containing Probi's probiotics are already sold in France, the UK, Australia and New Zealand.



The French-Canadian firm, Institut Rosell, which has been working with Probi since 2003, sees great potential in the use of dietary supplements to treat the commonly occurring gastrointestinal disorder, irritable bowel syndrome (IBS). The company intends to launch dietary supplements containing Probi's Lp299v bacterium in several geographic markets during 2007.

"The field is a demanding one and Probi's probiotics are well-documented. We have received good response from the market and have never regretted choosing Probi's probiotics. I'm very enthusiastic about the year ahead," says Patrice Malard, Head of Business and Product Development at Institut Rosell.

Pharmaceutical companies are interested in complementing their product range with dietary supplements. Institut Rosell distributes dietary supplements to major pharmaceutical companies such as Merck, Merckle Recordati and Ferring. Institut Rosell also targets not only the pharmaceutical companies, but industry representatives who are well-positioned to recommend dietary supplements, such as moulders of public opinion and doctors.

Institut Rosell is particular about the quality of its products and has its own research and development facilities in Canada and France, and a global research partnership with other institutes and universities. Institut Rosell complements its efforts to position its products with marketing, clinical documentation, information and education.



Patrice Malard

METAGENICS

At the end of 2006, Probi signed a partnership agreement with the American firm, Metagenics, which is the leading brand name for dietary supplements in the professional health care sector. The agreement is a breakthrough for Probi in the US, because it involves Probi selling a consumer product directly to Metagenics. This change has advanced Probi's position in the value chain. The launch is expected for the first half of 2007.

HEALTH WORLD

Health World, Australia's largest supplier of probiotic dietary supplements, reports extremely successful sales of dietary supplements containing Lp299v in Australia and New Zealand. The products include powders and capsules that can be marketed exclusively for the treatment of irritable bowel syndrome (IBS). Health World is now a subsidiary of Metagenics.

INSTITUT ROSELL

The French-Canadian firm, Institut Rosell, is one of the leading suppliers of probiotic dietary supplements in the US and Europe. Institut Rosell markets and sells dietary supplements containing Probi's Lp299v bacterium. The agreement gives Institut Rosell the exclusive right to market dietary supplements in the therapeutic area of irritable bowel syndrome (IBS). Distribution is handled by market-leading players, including Merck KgaA in France, Merckle Recordati in Germany, and Ferring Pharmaceuticals in Canada. Probi has been working in partnership with Institut Rosell since 2003.



THE FUTURE

The preconditions for signing further licensing agreements, both for new geographic markets and with new distributors and customers, have improved as a result of the cost-cutting, efficiency-enhancing measures implemented. The potential exists to use probiotics for creating different types of combination products, opening up new opportunities. Overall, Probi views the future potential of the dietary supplements market in a strongly positive light.

Did you know that:

The global market for dietary supplements, excluding vitamins, totals approximately SEK 155 billion, of which probiotic dietary supplements account for around SEK 7 billion. The probiotic dietary supplements sector is, however, growing faster than the rest of the dietary supplements market, reporting an annual growth rate of 10 per cent. The growth rate will, in Probi's view, remain high.



The Australian firm, Health World, distributes dietary supplements containing Probi's probiotics under the brand name Metagenics to physicians, homeopaths and other health care specialists in Australia and New Zealand. The dietary supplement is sold in pharmacies and health food stores under the Ethical Nutrients brand name.

"The customers expect effects when they take dietary supplements. We chose Probi's Lp299v bacterial strain for its therapeutic benefits," says Health World's Sales Manager, Graeme Joiner.

Health World, which is now part of the American firm, Metagenics, has, among other things, produced a commercial to market the dietary supplement which alleviates problems associated with irritable bowel syndrome (IBS).

The dietary supplement, which has been approved by the Australian authorities, has attracted a great deal of very positive attention in the media.



Graeme Joiner

Clinical Nutrition

- **Additional clinical data is required for commercialisation.**
- **Study of side-effects in conjunction with radiotherapy and chemotherapy to begin in 2007.**

Clinical nutrition products are specialised nutritional products intended for use in inpatient and outpatient care. Clinical tests of probiotics used in clinical nutrition have shown excellent potential for both improving health and saving money in the medical sector. The bacterial flora of patients in intensive care units at hospitals is often substantially reduced as a result of intense courses of antibiotics treatment, etc. This increases the risk of patients developing complications, such as inflammations or serious infections. Nutrient solutions that contain probiotics can help to restore the bacterial flora in these patients' digestive tracts.

THE MARKET

The most advanced market for clinical nutrition is the Japanese one, where work on products of this kind is already underway. The market for clinical nutrition is otherwise still largely immature and must be delineated and defined in terms both of size and potential.

A successful product launch requires Probi's offering to be supported by clinical data with proven health effects. The documentation facilitates effective marketing and is a prerequisite if the product is to be covered by the subsidies usually paid for nutrition products. Other factors that demand answers before the launch include any local regulatory limitations, distribution, packaging and shelf-life.

THE FUTURE

Viewed from a longer term perspective, it is probable that a market for clinical nutrition products containing probiotics could emerge, primarily driven by the following factors:

- Demand for shorter treatment period and reduced use of antibiotics.
- Efforts to reduce infections and complications resulting from surgery.
- New opportunities to reduce inflammations.
- Increased knowledge and documentation of the health effects of probiotics.
- An ageing population with a growing number of patients.

If antibiotic usage can be reduced by giving patients probiotics for preventative reasons, the risk of antibiotic-resistant bacteria developing in hospitals can be reduced. It is this objective that forms the background of a three-year intensive care study of Probi's probiotic concepts that has been taking place at a university hospital in the Netherlands since 2005. The study aims to discover, among other things, whether patients who receive probiotics require routine treatment with strong antibiotics.

There are numerous illnesses where established therapeutic methods can wipe out large parts of the intestinal microflora. This is true, for example, of cytostatic treatment (chemotherapy) and radiation, where probiotics can reduce both the problems and side-effects associated with the treatment. Probi is planning to launch a study in this field in 2007.



Research portfolio

RESEARCH AND DEVELOPMENT

Probi's research and development forms the basis for the commercialisation of product concepts. The research focuses on live microorganisms with scientifically demonstrated health-bringing effects.

Research in the probiotics field has successively increased over the past 20 years, focusing both on discovering probiotic effects and on identifying the most effective probiotic strains. The research also focuses on establishing the effects of imbalances between the 400–500 species, or a total of approximately two kilos of bacteria present in the gastrointestinal tract. Disruptions to the bacterial balance may lie behind many prevalent endemic diseases.

RESEARCH ACTIVITIES, 2006

Studies have demonstrated that one of Probi's bacteria reduces infections in intensive care from 40 to 10 per cent and that stays in intensive care units (ICU) can be reduced by up to two days. The year 2006 saw a continuation of the ongoing partnership with a group of researchers in Maastricht in the Netherlands regarding treatment of ICU patients. The programme's goal is to include 500 subjects in the trial over the course of three years, which will provide a far more extensive statistical base than previous studies. If the programme confirms the indications from previous studies, it could offer substantial commercial potential in the field of intensive care.

A clinical trial of probiotic usage in conjunction with colds began at the end of 2006. During the spring of 2007, approximately 500 volunteers will test two of Probi's bacterial strains to see if the number of colds is reduced and if the duration of the illness is shortened.

Application development and product development work have also been carried out in partnership with the licensees and other players.

THE RESEARCH PROCESS

Commercialisation of product concepts is founded on Probi's structured research and development processes, from initial research to launch. The bacteria are tested on a laboratory scale and suitable bacteria are selected. The bacteria's properties are then characterised with the aid of a variety of test methods. Selected bacteria then undergo additional investigation and testing.

Phase one of the clinical trials entails identifying and characterising interesting bacteria that meet important requirements, such as survival in the gastrointestinal tract and the absence of side-effects. Probi's clinical trials then enter phase two, in which tests are conducted on a small group of patients

with the help of the company's partnerships with various academic research groups. This enables the effects of Probi's probiotics to be further documented. The goal of the clinical studies is approval for a product-specific health claim. In the final stages of the process, Probi's customers develop the consumer product, normally with the assistance of Probi in the form of documentation, production technological know-how and experience.

FOCUS ON LACTOBACILLUS PLANTARUM

Maintaining research on several fronts is resource-intensive and Probi has therefore decided to focus primarily on the species known as *Lactobacillus plantarum*. As a leader in its field Probi will complement with research into other bacteria in order to meet other health requirements and to maintain breadth in the product offering.

Probi cooperates with a network of researchers at universities and institutions in Sweden and abroad in order to optimise the costs and direction of the research and development work. Probi utilises research capacity on a project basis and also applies for grants for its research, e.g. from the EU.

The financial goals that relate to Probi's operating margin include a requirement that R&D costs (as of 2009) shall not exceed 30 per cent of income.

PATENTS

Patents provide value and protection for both Probi and the company's customers. Probi currently holds patents for numerous probiotic strains and also holds complementary patents with regard to the probiotics' effects. The company has a total of 124 patents, taking into account all of its geographic markets. The patent portfolio is analysed regularly from a strategic viewpoint with a view to optimising the existing protection, e.g. via documentation and studies.

As a general rule, licensing revenues are determined by the effective patent duration, i.e. the patent duration remaining when the product is launched. Broad commercial agreements often include numerous patents, however, and when this is the case, Probi has sought solutions whereby royalties are paid with no reduction for as long as there is a patent in force. The strain patent for Lp299v, which is the most important patent in terms of Probi's existing commercial agreements, expires in 2012.

In 2006, Probi was awarded 21 patents, three of which refer to bacterial strains and 18 of which refer to applications (including via the European Patent Office). Probi submitted four new applications for patents in respect to new application areas in 2006.

Organisation and employees

Today's Probi is an efficient organisation with 18 employees. Probi works in partnership with international and regional partners who can cover various geographic markets.

The partner companies handle production, distribution and marketing to the consumer, and a small sales organisation is thus sufficient to meet Probi's requirements in this respect. The fact that much of the research is conducted via a network that includes Swedish and international universities also helps to keep the organisation small and cost-effective. Some of the research is also partially financed by scholarships and other research grants. When extra capacity is required, the services are bought in temporarily on a consultancy basis.

EXPERIENCED RESEARCH PERSONNEL

Probi's operations focus on probiotic research and Probi has therefore, among other things, invested heavily in attracting staff with in-depth research experience. The company employs research personnel with experience in the fields of medicine, microbiology and food chemistry. One-third of the company's employees have doctorates, and one-third of the employees also have a multicultural background, which helps to create a more dynamic organisation, not least in the context of Probi's research work. Probi's headquarters are located in the Ideon Research Park in Lund – a location that enables research and information exchanges, as well as contacts between universities and companies.

Over and above its research and marketing organisations, Probi also has finance, administration, production and product development units. In terms of gender breakdown, the company's employees consisted of ten women to eight men at the end of 2006. The average term of employment was 4.2 years (3.8). The age distribu-

tion is shown in the diagram below. Probi strives to have a workplace that is attractive to both existing and potential employees.

Total sickness absence in relation to total number of hours worked in 2005 was 5.0 per cent (0.9). One long-term period of sickness absence has a relatively major impact because Probi is a small organisation.

FLEXIBILITY

Given its relatively small number of employees, Probi's organisation must be flexible if it is to conduct successful research and commercialisation within several different therapeutic areas. Accordingly, Probi strives to maintain an open dialogue within the company and to support a continuous exchange of knowledge between different functions. The ability of Probi's employees to familiarise themselves quickly with work that has already been performed is crucial.

VALUES

Probi shall be characterised by:

Know-how and expertise

Probi shall be characterised by know-how and expertise in all areas. This is what Probi's partners demand and what attracts personnel and other partners, making them keen to work with Probi.

Dedication

Dedication to working with Probi's products means a level of commitment over and above the norm. It involves dedication to research and to the development and marketing of products that improve people's health.

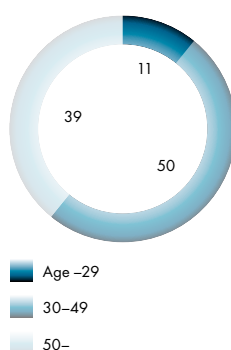
Credibility

Credibility is the key if partners are to choose Probi and end-consumers are to be keen to buy the products.

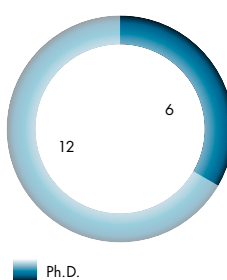
Curiosity

Probi started as a research company that was born from a discovery. Curiosity is a strong driving force and Probi's work entails continuously exploring new paths.

Age distribution, %



Education level, number



Ethics and quality

Probi follows the same high standards for clinical trials with regard to ethics as the pharmaceutical industry. This means that no clinical trials of Probi's bacteria are performed until an ethics committee has approved the trial's experimental plans. Approval of this kind secures the ethical aspect of Probi's trials with regard, for example, to the target group, the object of the tests, the tests to be performed and the methods to be used.

CERTIFICATION

Wherever possible, Probi has adhered to the same requirements as its customers, the food industry and the medical sector industry, with regard to quality assurance.

Probi has tailored its activities to the EU's requirements whereby all foods must be traceable at all stages of the production, processing and distribution chains. Probi has also tailored its operations to the Hazard Analysis Critical Control Point (HACCP) monitoring programme, which is a quality assurance system for the entire production process. The HACCP programme specifies that the company must, among other things, determine and set threshold values for the critical points in the production process and have an action programme in place to deal with any errors that may occur.

In 1998, Probi received its first quality certification from SWEDAC (the Swedish Board for Accreditation and Conformity Assessment). SWEDAC's representatives perform annual inspections to ensure that quality requirements are being met, and an inspection on a larger scale is performed every fourth year prior to renewed accreditation. The most recent such inspection was performed at Probi in 2004. The accreditation means that Probi, in common with other accredited laboratories, gains international acceptance in 40 or so countries for its test reports and calibration certificates in accordance with the EN ISO/IEC 17025 standard.

PRODUCTION QUALITY

In addition to all the standard monitoring functions, Probi also performs extensive analyses of every new batch of bacterial cultures produced. Microbiologists ensure, among other things, that the bacterial content is correct and that hygiene maintains the highest possible standards. Identity analyses are also performed during which fermentation patterns and genetic profiles are checked against the original culture. This process also includes tests of the bacterium's function.

Probi produces its bacteria in its cultivation facility at the Ideon Research Park in Lund. The production units are capable of handling a substantial increase in volume using existing capacity and can also, if necessary, quickly be scaled up without the need for significant investments. The production of dry products, such as dietary supplements, is outsourced to the external production units of quality assured subcontractors.

ENVIRONMENT

Probi's research and production have a negligible effect on the environment in that no harmful by-products are generated.

Risk factors

RELIANCE ON A FEW PARTNERS

Probi has only a few partners who are expected, within the foreseeable future, to provide the company with significant royalty revenues. If one or more of these partnerships were to be terminated or prove unsuccessful, it would have a negative impact on Probi's revenue streams, results and financial position. The customer, Skane Dairy, still accounts for a dominating share of the company's revenues.

STRATEGIC RESEARCH PARTNERSHIPS

Probi's research is based on both internal competence and external resources provided via Swedish and international researchers linked to Probi. The external partnerships have made a significant knowledge contribution to Probi's development work. There are no guarantees, however, that these partnerships will result in new discoveries, or that Probi will have the exclusive rights to any such discoveries.

KEY INDIVIDUALS AND EMPLOYEES

Probi's operations are heavily dependent on the competence of key individuals and specialists within the company. The company's potential for expansion is closely linked to Probi's ability to retain these employees and to attract new and highly qualified members of staff.

PROBIOTIC REGULATION

The functional food market is at present under-regulated with regard to health claims. The introduction of international regulations is, however, expected within the next few years, and these will apply equally to probiotics. These regulations are expected to boost demand for high-quality products, but they could also increase the cost of the manufacturing processes.

PROBIOTICS FOR THE MEDICAL SECTOR

Probi's focus on clinical nutrition presupposes a usage of probiotic nutrient solutions in the medical sector that does not currently exist. Probi believes that there is a medical need for probiotic products in the medical sector. Establishment of this usage could, however, take time, and this would mean that the development expenses incurred by Probi would not be covered through commercial agreements within the immediate future.

DOCUMENTATION AND PATENT PROTECTION

Probi's commercial successes are largely dependent on its ability to protect patents and to continue generating positive research findings of high quality. It is vital that Probi is on the cutting edge in this respect since the requirements for a high degree of inventiveness and innovation will continue to increase as interest, activity and regulation levels grow within the probiotics sector.

SECURITY

Probi signs confidentiality agreements with both its personnel and external consultants, and the company strives to generate a high level of awareness with regard to sensitive information. Continuous supervision of systems, firewalls and virus protection provide protection against unauthorised access to Probi's IT network and data. Probi also works actively with operational reliability and monitors its security functions to ensure that they are managed efficiently and function smoothly.

COMPETITION

International competition from probiotics suppliers has increased in all of Probi's business areas. The markets in the probiotic functional food and clinical nutrition sectors verge on oligopolies. Competition in the probiotic food field also comes from other products that are endeavouring to achieve the same sort of health benefits.

COMPETING RESEARCH INCREASING

Threats to market growth include substitute products, less serious players and a trivialisation of probiotics.

FUTURE CAPITAL REQUIREMENTS

Probi's focus on biotechnology means that the company will always be burdened with substantial research and development expenses. These expenses are currently largely covered by commercial revenues. If opportunities for faster growth that entail a capital requirement arise, Probi may be forced to acquire additional capital by means of a new share issue, for example.

FINANCIAL RISKS

Probi's partnerships with international customers entail revenues in several different currencies, and these are affected by exchange rate fluctuations. The primary source of revenue at present is Skane Dairy, and under the terms of the contract, these revenues are always paid in SEK, irrespective of whether they derive from royalties in countries other than Sweden. A large proportion of revenues during 2006 was in EUR and derived from payments made by Danone. Revenues in foreign currencies will increase as royalty revenues from new agreements grow. Probi has borrowed approximately SEK 4 million on the production facility in Sösdala at a variable interest rate. An increase of 1 percentage point in the interest rate would mean an increase of approximately SEK 40,000 in interest expenses. The company has no interest-bearing operating liabilities.

Annual checks (impairment tests) are carried out to determine whether any write-down requirement exists for patents and licenses. The European rights are amortised linearly from the acquisition year until 2012. Probi closely monitors product launches by its partners, together with development work for impending launches. The assessment of this information forms the basis for decisions as to when the company performs write-down evaluations.

Five-year overview

FIVE-YEAR OVERVIEW						
Summary of the income statement, SEK k		2006	2005	2004	2003	2002
Net turnover		37,215	27,236	31,619	27,462	26,063
Total operating income		38,417	27,666	31,915	27,470	27,257
Total operating expenses		-43,824	-37,165	-39,003	-35,998	-39,768
Operating result		-5,407	-9,499	-7,088	-8,528	-12,511
Result after financial items		-4,834	-8,833	-6,675	-8,180	-14,128
Net result for the year		-4,834	-8,833	-6,675	-8,180	-14,128
Key ratios		2006	2005	2004	2003	2002
	Definition					
Equity/assets ratio, %	1	85.9	91.1	90.1	80.8	88.3
Debt/equity ratio, %	2	5.1	4.8	4.5	6.7	6.2
Return on capital employed, %	3	-6.1	-10.4	-8.6	-12.0	-14.6
Return on equity, %	4	-6.6	-11.0	-9.4	-13.1	-19.2
Cash liquidity, %	5	589	1,161	903	247	487
Share in operating income of research costs, %		40	56	46	50	50
Average number of employees		18	18	17	15	17

The data for 2002 and 2003 have not been recalculated in accordance with IFRS. A recalculation would have a positive effect on the operating result of SEK 691,000 per annum for reduced goodwill depreciation.

1. Shareholders' equity as a percentage of balance sheet total.
2. Interest-bearing liabilities as a percentage of shareholders' equity.
3. Operating result plus financial income as a percentage of average balance sheet total less non-interest-bearing liabilities and provisions.
4. Pre-tax profit as a percentage of average shareholders' equity.
5. Total current assets, excluding stock in trade, as a percentage of current liabilities.



Probi's share

On 29th December 2006, the closing price for the Probi share was SEK 23.90 (32.00), corresponding to a market value of SEK 224 million (300). The highest price paid during the year was SEK 33.60 (4th January), and the lowest was SEK 18.00 (7th November). A total of 2,981,226 shares were traded in 2006, corresponding to 31.8 per cent of the total number of outstanding shares. Probi's share has been quoted on the Nordic list of the Stockholm Stock Exchange since December 2004, after having been previously quoted on the NGM Equity list of shares.

SHARE CAPITAL

Probi's share capital at the end of 2006 totalled SEK 46,826,500 (46,826,500), spread over 9,365,300 shares with equal voting rights. The nominal value of the share is SEK 5. Probi's shareholders' equity totals SEK 70.7 million after the net result for the year.

NUMBER OF SHAREHOLDERS AND OWNERSHIP BREAKDOWN

The total number of shareholders registered with VPC (the Swedish CSD) on 31st December 2006 was 4,192 (4,654). At the turn of the year, Probi's ownership broke down as follows: 41.5 per cent private ownership, 11.9 per cent owned by institutions, and 20.5 per cent foreign ownership. Probi's two principal owners, Skane Dairy and H&B Capital, jointly control approximately 26 per cent of the votes and capital.

STOCK OPTIONS ISSUED

The principal owners issued 20,000 stock options on market terms to the Executive Vice President, Per-Ola Forsberg. The options entitle their holders to buy shares at a price of SEK 44 during the period from 1st January 2007 to 31st August 2007.

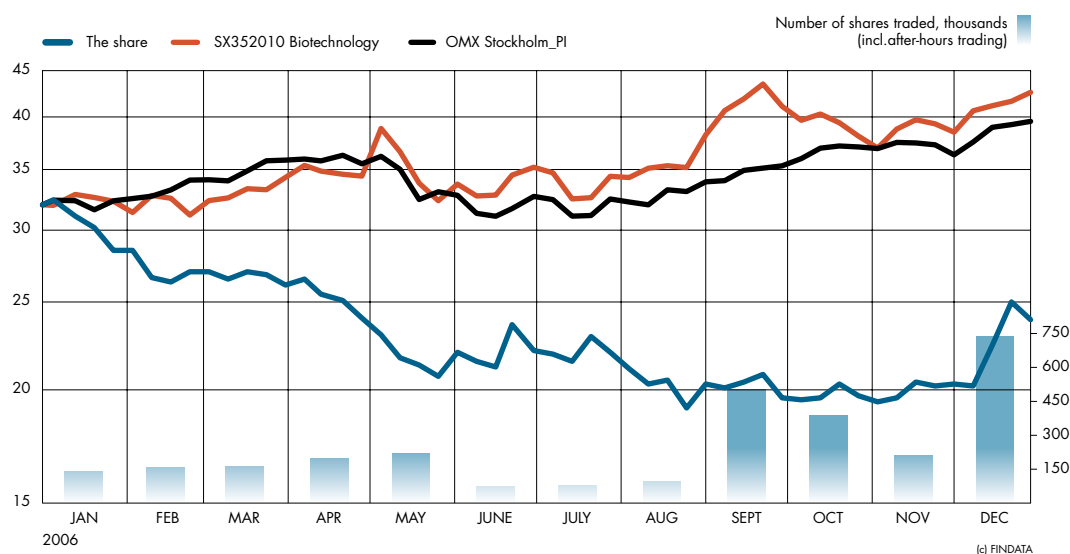
Probi currently has no outstanding conversion loans or any outstanding warrants.

DIVIDEND POLICY

The Board of Directors has proposed to the Annual General Meeting that no dividend be paid for the 2006 financial year. Probi's operations over the next two years will require considerable resources and the company therefore believes that no dividend will be paid until after 2008.

Provided that Probi has achieved a suitable capital structure after this period, and that it is deemed that the company's financial goals can be maintained, Probi estimates that its share will thereafter yield a dividend totalling 30–50 per cent of the result after tax.

PROBI'S SHARE



SHARE CAPITAL DEVELOPMENT

Event	Year	Issue price	Increase in no. of shares	Total no. of shares	Nominal value per share	Increase in share capital	Share capital
Formation	1991		500	500	100	50,000	50,000
Scrip issue 1:1	1997		500	1,000	100	50,000	100,000
Directed share issue ¹	1997		150	1,150	100	15,000	115,000
Split from 100 to 1	1997		113,850	115,000	1.00	0	115,000
Scrip issue 34:1	1998		3,910,000	4,025,000	1.00	3,910,000	4,025,000
Directed share issue ²	1998		1,006,250	5,031,250	1.00	1,006,250	5,031,250
Scrip issue 15:10	1998		7,546,875	12,578,125	1.00	7,546,875	12,578,125
Directed share issue ³	1998	12	1,721,875	14,300,000	1.00	1,721,875	14,300,000
Scrip issue 13:10	1998	–	18,590,000	32,890,000	1.00	18,590,000	32,890,000
New share issue with preferential rights	2000	10	8,222,500	41,112,500	1.00	8,222,500	41,112,500
Reverse split 5:1	2004		–	8,222,500	5.00	–	41,112,500
New share issue	2004		1,142,800	9,365,300	5.00	5,714,000	46,826,500

¹ The issue was directed at founders and senior executives.

² The issue was directed at Skane Dairy's ownership group and at Probi AB.

³ The issue was directed at participation holders in Skane Dairy, Probi AB and Skane Dairy personnel, and certain other associated parties.

DATA PER SHARE

	2006	2005	2004	2003	2002
Number of shares on 31/12, thousand	9,365	9,365	9,365	8,223	8,223
EPS, SEK	-0.52	-0.94	-0.71	-0.99	-1.72
Shareholders' equity per share, SEK	7.55	8.06	9.01	7.10	8.09
Cash flow per share, SEK	-0.56	-0.77	2.86	0.10	-3.64
Share price on 31/12 (final price paid), SEK	23.90	32.00	30.00	40.00	15.00
Price/Shareholders' equity per share, multiple	3.17	3.97	3.33	5.64	1.85
P/E ratio, multiple	neg.	neg.	neg.	neg.	neg.
Dividend, SEK	–	–	–	–	–
Market capitalisation on 31/12, SEK k	223,831	299,690	280,959	328,900	123,338

The values in the above table do not correspond to those in the formal accounts because they have been recalculated for the 5:1 split employed.

SHAREHOLDERS

	Number of shares	Percentage of share capital and votes, %
H & B Capital Lp	1,212,542	12.95
Skane Dairy Ek för	1,170,903	12.50
The Pecunia fund	909,500	9.71
KI chem AB	566,333	6.05
Molin, Göran with companies	426,241	4.55
Jeppsson, Bengt	407,517	4.35
Morgan Stanley & Co	244,000	2.61
Ahrné, Siv	214,073	2.29
Douglas, Gustaf	200,000	2.14
Nordea	162,250	1.73
Other	3,851,941	41.12
Total	9,365,300	100.00

SHAREHOLDING PER SHAREHOLDER

Share distribution	No. of owners	No. of shares	Percentage of shares, %
1–500	3,119	547,087	5.84
501–1,000	531	410,462	4.38
1,001–5,000	432	985,129	10.52
5,001–10,000	60	441,118	4.71
10,001–15,000	14	173,062	1.85
15,001–20,000	5	82,640	0.88
20,001–	31	6,725,802	71.82
Total	4,192	9,365,300	100.00

Directors' Report

The Board of Directors and the CEO of Probi Aktiebolag (publ), company reg. no. 556417-7540, the registered offices of which are in Lund, Sweden, hereby present the annual accounts and the consolidated accounts for 2006.

Probi was founded in 1991 and is now a leading player in the field of probiotic research and development. The company's research relates to live microorganisms with scientifically demonstrated health-giving effects. The main fields of research are: Gastrointestinal complaints, Immunology, Risk factors for cardiovascular disease and Stress and performance recovery.

Probi's business concept is based on offering effective and well-documented probiotic product concepts with extensive patent protection, thereby creating the potential for higher royalties than in the industry as a whole. Probi's share is quoted on The Nordic Exchange.

FUNCTIONAL FOOD

Royalty income from Skane Dairy's ProViva fruit drinks in Sweden increased during the year to SEK 21.4 million (17.7), corresponding to an increase of 21 per cent. The pronounced increase was mainly due to increased marketing activities by Skane Dairy.

Probi renegotiated its agreement with Danone during the fourth quarter. The royalty levels remain unchanged under the new agreement from those under previous ones, but the new licensing agreement no longer limits Probi's opportunities to cooperate with other parties in the dairy products and fruit drinks fields. Probi received a payment of SEK 8.7 million in conjunction with the expiry of the previous licensing agreement. The new agreement gives Danone the scope to launch a product containing Probi's probiotics within the next two years.

Danone has operations in 120 countries and is Europe's leading supplier of probiotic products. The product development work carried out by Danone in order to optimise a product containing Probi's Lp299v probiotics has taken longer than originally anticipated. Probi believes that the product concept with which Danone is working continues to be commercially interesting.

Gastrointestinal disorders are currently the functional area with the highest demand for probiotic food products. Spheres of use are

expanding as research makes new advances, and potential future spheres of use include diabetes, cholesterol reduction, infections, influencing immunological functions and inflammatory conditions, lowering blood pressure, and a variety of metabolic fields. The development of methods that allow bacteria to be added to non-chilled foods is continuing and will further expand the market potential. Probi expects, as a result of positive developmental results, to be able to initiate new partnerships with regard to probiotics in non-chilled food products during the course of the year.

DIETARY SUPPLEMENTS

Income increased in the Dietary Supplements business area to SEK 4.6 million during the year, corresponding to an increase of 30 per cent in comparison with the previous year. The business area posted an operating loss for the year of SEK -0.4 million (-1.2).

Probi has signed agreements to sell its probiotics in the form of dietary supplements directly under the Metagenics brand name. Metagenics is the US's leading brand name for dietary supplements in the health care sector. The product is based on Probi's Lp299v bacterium and the launch is scheduled for the first half of 2007. This constitutes a breakthrough for Probi, partly because Metagenics is the leading brand name in dietary supplements for the professional health care sector in the US, and partly because the agreement was signed directly with Metagenics, Inc. Probi can see additional potential in the partnership due to Metagenics' plans to expand its product offering and to Probi's ability to become an important partner in this expansion.

The fact that the product will be sold directly to Metagenics means an advance in Probi's position in the value chain. Probi already has a successful licensing agreement whereby Metagenic's subsidiary, Health World, sells dietary supplements containing Probi's probiotics in Australia and New Zealand.

Institut Rosell signed a new distribution agreement during the period with Ferring Phar-

maceuticals – an internationally highly reputed pharmaceutical company – in the field of gastrointestinal disorders. The agreement grants the company exclusive rights to sell a dietary supplement based on Probi's Lp299v bacterium in the Canadian market. The product will be launched in the spring of 2007.

Institut Rosell has also signed distribution agreements that grant the pharmaceutical company, Merck, exclusive rights to sell a dietary supplement containing Probi's Lp299v bacterium in the Swedish, Norwegian and Finnish markets. The launches in Norway and Finland are scheduled to take place during the year, while in Sweden, the product is awaiting completion of the registration process, before a launch can be possible.

Merck has established itself in France as a strong player in the field of probiotics and the company has already implemented a successful launch of Probi's product in the French market. The company intends to further strengthen this position by marketing high-quality probiotic products on other markets. Approximately 25 per cent of sales in France are prescription-based, which generates credibility for other sales of the product as well.

Probi's partner, Institut Rosell, has also signed a new distribution agreement that grants the pharmaceutical company, Merckle Recordati, exclusive rights to sell a dietary supplement on the German market. The product is based on Probi's Lp299v bacterium and will be launched in the spring of 2007. The fact that it is the pharmaceutical company, Merckle Recordati, that will be launching the product on one of the bigger European markets is significant, because the company is a strong player in the gastrointestinal disorders field. This is the third distribution agreement in connection with Lp299v entered into in Europe during the past twelve-month period. The quality of the players and the increased rate at which agreements are being signed shows both that there is a considerable need for products targeting gastrointestinal disorders, and that Probi has a competitive offering.

Institut Rosell has also launched dietary supplements in South Africa during the year, through Nutrilida, which is the leading health food company in the field in that country.

The new agreements mean that sales of dietary supplements containing Probi's probiotics are now being built up in the UK, France, Germany,

Scandinavia, the US, Canada, South Africa, Australia and New Zealand. The total global market for probiotic dietary supplements is valued at approximately SEK 7 billion and has shown an annual growth rate of over 10 per cent in recent years. The fact that highly reputed companies are prepared to invest resources in building a new, high-quality dietary supplement market across large geographic markets helps establish a consolidation process that can only benefit Probi.

CLINICAL NUTRITION

The Clinical Nutrition business area has not yet issued any invoices and operating costs for the year fell to SEK –5.4 million (–77). The costs principally refer to development work and clinical trials.

No concrete discussions with counterparties with regard to the commercialisation of findings in the business area are currently in progress. The results of the ongoing clinical studies are important in generating the preconditions for more in-depth discussions of commercial partnerships and licensing agreements within the Clinical Nutrition field. A major intensive care study is being carried out in the Netherlands and is scheduled for completion in 2008.

RESEARCH AND DEVELOPMENT

Probi has commenced clinical trials on the subject of colds. Approximately 500 volunteers in Lund and Uppsala are scheduled to test two of Probi's bacterial strains during the spring, to see, firstly, whether the number of colds decreases, and secondly, whether the duration of the colds is reduced.

The majority of the probiotic foods currently available focus on counteracting diseases and disorders of the gastrointestinal tract. Probi is behind the beneficial stomach bacteria present in ProViva drinks, but also owns several other bacterial strains. The two that will now be tested in the colds study belong to the *Lactobacillus plantarum* – the same family as the bacterium present in ProViva – and *Lactobacillus paracasei* species. Animal testing and smaller scale studies on humans have already shown that the bacteria seem to be able to strengthen the immune system against viruses. The new study is financed partly with money from the Swedish government agency Vinnova's subsidy programme, Forska&Väx, and is scheduled for completion in the autumn.

Directors' Report

Probi has developed a technique that can enrich dried food products with effective amounts of probiotics. The successful test results increase the potential for commercialisation in the Functional Food business area.

In the Clinical Nutrition business area, the intensive care study being carried out in the Netherlands has been expanded to another hospital in order to accelerate the rate of patient inclusion. The study is scheduled to run for a total of three years and is investigating whether routine preventative treatment with powerful antibiotics can be reduced using probiotics. A new probiotic product targeting inflammation is currently being studied in initial clinical trials on patients with bowel inflammation.

PERSONNEL

Probi had 18 employees at the end of the year, 10 of whom are women and 8 of whom are men. The average number of employees during the year was 18 (18). The company now employs 6 (8) researchers who have defended their doctoral theses. In November 2006, Probi's Board of Directors decided to appoint Rolf Bjerndell to the position of Acting CEO in conjunction with the former CEO resigning his position. The recruitment process has begun for a new CEO.

TURNOVER AND RESULTS

The Group's net turnover during the year totalled SEK 37.2 million (27.2), corresponding to an increase of 37 per cent. Probi received a payment from Danone of SEK 8.7 million in conjunction with the expiry of a former licensing agreement during the period.

Operating expenses increased during the year and totalled SEK -43.8 million (-37.2). The increase is primarily due to severance pay totalling SEK -4.6 million disbursed to the former CEO and to disposals of patents and write-downs of production equipment collectively totalling SEK -1.3 million.

Earnings per share during the year were SEK -0.52 (-0.94).

CASH FLOW AND FINANCIAL POSITION

Probi's cash flow for the year was SEK -5.3 million (-7.2). The cash flow from operating activities totalled SEK -3.1 million (-4.9). Liquid assets at the end of the reporting period totalled SEK 34.4 million (39.7). The increase in operating receivables

comprises the payment from Danone received after the period end and the increase in operating liabilities comprises severance pay to the former CEO. Probi invests significant amounts in research and development, and the company has therefore reported a loss. R&D expenses, excluding raw materials and consumables, comprised 44 per cent (46) of total costs during the year.

The company's accumulated fiscal loss on 31st December 2006 is SEK 71.2 million. The accumulated loss entails a deferred tax receivable of SEK 19.9 million, which can be utilised in future once the company starts reporting a profit. The company has not booked this deferred tax receivable in the accounts.

There are no unreported undertakings in respect of former Board Members or senior executives. The company was not involved in any legal proceedings in 2006.

EVENTS AFTER THE CLOSING DATE

No significant events have occurred after the closing date.

FUTURE DEVELOPMENT

Probi's business model is based on conducting research and development, patenting and documenting probiotic bacteria and product concepts, and producing probiotic bacteria. Probi offers licenses to companies that produce, distribute and market products based on Probi's patented bacteria and product concepts. The company will continue to operate according to its stated plan.

ENVIRONMENTAL IMPACT

The Group is not engaged in any operations for which a permit is required pursuant to the Swedish Environmental Code.

SUBSIDIARIES

Probi AB has two wholly owned subsidiaries, Probi Food AB and Probi Feed AB. Both companies are dormant.

PROPOSED ALLOCATION OF LOSS

The Parent Company's accumulated loss totals SEK -4,834 thousand and it is proposed that this be offset in its entirety against the share premium reserve. According to the consolidated Balance Sheet, the Group's accumulated loss totals SEK -73,384 thousand.

CORPORATE GOVERNANCE

The Board of Directors and its rules of procedure

The Board of Directors and management of Probi strive to live up to the requirements of the company's shareholders and other stakeholders with regard to good corporate governance by means of openness, effective control and efficiently functioning internal routines.

Composition of the Board

Probi's Board of Directors is appointed once a year at the Annual General Meeting. The Board of Directors for 2006 comprised six ordinary Members: Peter Zakrisson (11 of 11), Mats Lidgard (11 of 11), Göran Molin (11 of 11) and Hilde Furberg (7 of 11). Rolf Trulsson (4 of 5) and Lars Backsell (3 of 5) replaced Rolf Bjerndell (5 of 6) and Berthold Lindqvist (4 of 6), who resigned in conjunction with the Annual General Meeting in May 2006. The figures in parentheses refer to attendance at Board Meetings.

The Chairman of the Board, Peter Zakrisson, is also a partner in Probi's largest owner, H&B Capital. Rolf Trulsson was, up to the end of September 2006, the CEO of the second largest owner, Skane Dairy. No Board Member is employed by the company. The company's CEO and Executive Vice President also attend the majority of Board Meetings, although they are not entitled to vote.

Remuneration to the Board of Directors and management

The Annual General Meeting determines the principles and threshold limits for directors' fees. A Member of the Board may, for a brief period of time, provide consulting services on behalf of Probi, but only after a Board resolution to this effect and only provided that it is deemed to be the most cost-effective and advantageous alternative for the company. Any such consulting fees are reported in the Annual Report.

The Directors' fees for 2006 were set at SEK 650 thousand, SEK 150 thousand of which is payable to the Chairman of the Board, while SEK 100 thousand is payable to each of the other Board Members. See Notes 9 and 27 for details of remuneration paid to the Board.

The working procedures of the Board of Directors

Each year, the Board of Directors draws up the rules of procedure that regulate the division of

labour and responsibility between the Board, the Chairman and the CEO. The Board of Directors shoulders ultimate responsibility for Probi's organisation and the administration of the company's affairs. It makes decisions on significant organisational and operational changes and on the appointment and dismissal of the CEO. The duties of the Board also include determining and evaluating strategies, business plans and budgets. The Board also adopts interim reports and preliminary financial statements.

It is incumbent upon the Chairman of the Board to monitor the company continuously and ensure that all Board Members receive the ongoing information required to assess and evaluate Probi. The Chairman of the Board shall also consult the CEO on strategic issues, chair the Board Meetings, and ensure that the handling of items on the agenda of Board Meetings does not contravene the disqualification rules laid down in the Swedish Companies Act.

The Board shall draft a set of instructions for the CEO every year, containing guidelines on the ongoing management, bookkeeping and administration of funds, as well as internal checks and balances within the company. The instructions shall also include the extent of the CEO's authority and his or her obligation to supply the Board of Directors with information.

Pursuant to the Articles of Association, the Board of Directors shall hold at least five ordinary Meetings per year, over and above the statutory company meeting. In 2006, the Board has held eleven meetings and has focused particularly on following up on Danone's launch-related activities and the start of Institut Rosell's launches in the Dietary Supplements sector, as well as on monitoring the company's efforts to further commercialise its business areas.

Audit Committee

Probi's Audit Committee comprises the Board of Directors. The Board maintains continuous contact with the auditors, who present their audit reports and observations twice a year in person. At these meetings, the auditors also provide details of the areas that are due to be specifically addressed by the next audit while the Board informs the auditors about issues or areas to which the Board wishes particular attention to be paid.

Directors' Report

Remuneration Committee

Probi's Remuneration Committee comprises the Board of Directors. The Chairman of the Board drafts a proposal relating to directors' fees ahead of the statutory company meeting. The proposal is checked and approved by the Nomination Committee. The Remuneration Committee also determines the salary and remuneration payable to the CEO, and the principles governing salaries and remuneration payable to other senior executives. The Remuneration Committee monitors conditions of employment and benefits for the company's senior executives on an ongoing basis.

Probi shall offer a market-based total remuneration package that enables senior executives to be recruited and retained. The remuneration paid to the company management shall comprise a fixed salary, pension and other remuneration. Collectively, these components make up the individual's total remuneration package.

The salary shall take into account the individual's spheres of responsibility and experience. Other remuneration and benefits shall be market-based and shall help promote the executive's ability to carry out his or her duties.

The company management's contracts of employment include termination provisions. These contracts state that employment may usually be terminated at the employee's request with a three to six month notice period and, at the company's request, with a six to twelve month

notice period. The individual's salary shall remain unchanged during the notice period.

The Remuneration Committee shall be entitled to waive the above-mentioned guidelines if, in the opinion of the Board, and on a case-by-case basis, special grounds exist to justify such a departure.

Nomination Committee

The Annual General Meeting elects the Nomination Committee, which shall comprise representatives of the two biggest owners and one representative of the other owners. The Committee currently comprises Lars Gatenbeck (H&B Capital), Jan Persson (Skane Dairy) and Carl Henrik Shah.

The Chairman of the Board and the Nomination Committee present a proposal for a new Nomination Committee for the period up to the next Meeting. A representative of the biggest owner shall convene the Nomination Committee well in advance of the Annual General Meeting in order to submit proposals to the Meeting concerning the ordinary Board Members, any Deputy Members and the auditors. Their recommendation shall also be submitted to the Board of Directors in January/February.

Ownership Structure

According to VPC (the Swedish CSD), Probi had 4,192 shareholders (4,654) on 29th December 2006. The company currently has no outstanding conversion loans or outstanding warrants.

Operational goals

- Probi shall, within the next year, develop and commercialise additional product concepts for the food and nutrition market.
- Probi shall retain its position as a successful supplier of clinically documented probiotics.
- Probi shall, through high-quality documentation and extensive patent protection, endeavour to receive higher royalty revenues for its probiotics than the industry as a whole.

Financial goals set in conjunction with the listing on the Stockholm Stock Exchange in December 2004

- Probi's organic growth in terms of net turnover during the next five years shall reach an average of 25 per cent per year.
- Probi's operating margin, excluding R&D expenses, shall be a minimum of 60 per cent. After a five-year period, R&D shall not exceed 30 per cent of income.
- Probi's result before tax for the year as a whole shall be positive by 2007. The net margin shall exceed 25 per cent in the long term.
- Probi's cash flow shall be positive by 2007, and shall subsequently total at least 50 per cent of the operating result.
- Probi's operations shall, over the next three years, be financed by means of shareholders' equity.

Financial statements

INCOME STATEMENTS					
SEK thousand	Note	The Group		The Parent Company	
		2006	2005	2006	2005
Operating income					
Net turnover	6	37,215	27,236	37,215	27,236
Other income		1,202	430	1,202	430
Total operating income	5, 27	38,417	27,666	38,417	27,666
Operating expenses					
Change in stock in trade		-55	-344	-55	-344
Raw materials and consumables		-1,302	-1,247	-1,302	-1,247
Staff overheads	9	-18,509	-15,004	-18,509	-15,004
Other external costs	7, 8	-16,845	-14,646	-16,845	-14,646
Depreciation and write-downs of fixed assets	10, 15, 17, 18	-6,645	-5,757	-6,645	-5,757
Other operating expenses		-468	-167	-468	-167
Total operating expenses		-43,824	-37,165	-43,824	-37,165
Operating result		-5,407	-9,499	-5,407	-9,499
Result from financial investments					
Financial income	11	718	810	718	810
Financial expenses	11	-145	-144	-145	-144
Total result from financial investments		573	666	573	666
Result before tax		-4,834	-8,833	-4,834	-8,833
Tax on the result for the year	12	0	0	0	0
NET RESULT FOR THE YEAR		-4,834	-8,833	-4,834	-8,833
Number of shares		9,365,300	9,365,300		
EPS, SEK		-0.52	-0.94		

There have been no changes in the number of the company's shares and the average number of shares in 2006 was hence the same as the total number of shares, namely 9,365,300.

The company currently has no outstanding conversion loans or outstanding warrants.

Financial statements

CONSOLIDATED BALANCE SHEETS			
SEK thousand	Note	The Group	
		2006	2005
ASSETS	5		
Fixed assets			
Intangible fixed assets			
Patents, licenses and similar rights	15	24,145	27,569
Goodwill	16	2,762	2,762
		26,907	30,331
Tangible fixed assets			
Buildings and land	17	3,795	3,956
Inventories, tools and installations	18	2,508	3,899
		6,303	7,855
Total fixed assets		33,210	38,186
Current assets			
Stock in trade, etc.			
Finished goods		985	1,040
Total stock in trade		985	1,040
Current receivables			
Accounts receivable	20	12,559	3,053
Other current receivables		202	0
Prepaid costs and accrued income	21	973	963
Total current receivables		13,734	4,016
Liquid assets	22	34,436	39,702
Total current assets		49,155	44,758
TOTAL ASSETS		82,365	82,944

CONSOLIDATED BALANCE SHEETS

SEK thousand	Note	The Group	
		2006	2005
SHAREHOLDERS' EQUITY AND LIABILITIES			
Shareholders' equity	5		
	23		
Share capital		46,827	46,827
Other capital contributed		97,290	97,290
Loss brought forward		-73,384	-68,550
Total shareholders' equity		70,733	75,567
Long-term liabilities			
Other long-term liabilities		3,450	3,610
Total long-term liabilities	24	3,450	3,610
Current liabilities			
Current part of long-term liability	24	156	152
Accounts payable		1,836	1,051
Other liabilities		404	687
Accrued costs and prepaid income	25	5,786	1,877
Total current liabilities		8,182	3,767
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		82,365	82,944

Financial statements

BALANCE SHEETS – THE PARENT COMPANY			
SEK thousand	Note	The Parent Company	
		2006	2005
ASSETS	5		
Fixed assets			
Intangible fixed assets			
Patents, licenses and similar rights	15	24,145	27,569
		24,145	27,569
Tangible fixed assets			
Buildings and land	17	3,795	3,956
Inventories, tools and installations	18	2,508	3,899
		6,303	7,855
Financial fixed assets			
Participations in Group companies	19	4,031	4,031
Total fixed assets		34,479	39,455
Current assets			
Stock in trade, etc.			
Finished goods		985	1,040
Total stock in trade		985	1,040
Current receivables			
Accounts receivable	20	12,559	3,053
Other current receivables		202	0
Prepaid costs and accrued income	21	973	963
Total current receivables		13,734	4,016
Liquid assets	22	34,436	39,702
Total current assets		49,155	44,758
TOTAL ASSETS		83,634	84,213

BALANCE SHEETS – THE PARENT COMPANY

SEK thousand	Note	The Parent Company	
		2006	2005
SHAREHOLDERS' EQUITY AND LIABILITIES			
Shareholders' equity	5		
Restricted equity	23		
Share capital		46,827	46,827
Statutory reserve		25,974	34,807
Total restricted equity		72,801	81,634
Profit/loss brought forward		0	0
Net result for the year		-4,834	-8,833
Total loss brought forward		-4,834	-8,833
Total shareholders' equity		67,967	72,801
Long-term liabilities			
Other long-term liabilities		3,450	3,610
Liabilities to Group companies		4,035	4,035
Total long-term liabilities	24	7,485	7,645
Current liabilities			
Current part of long-term liability	24	156	152
Accounts payable		1,836	1,051
Other current liabilities		404	687
Accrued costs and prepaid income	25	5,786	1,877
Total current liabilities		8,182	3,767
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		83,634	84,213

Financial statements

CHANGES IN SHAREHOLDERS' EQUITY – THE GROUP

SEK thousand	Share capital	Other capital contributed	Loss brought forward	Total shareholders' equity
Opening balance, 1st Jan 2005	46,827	97,290	-59,717	84,400
Net result for the year			-8,833	-8,833
Opening balance, 1st Jan 2006	46,827	97,290	-68,550	75,567
Net result for the year			-4,834	-4,834
Shareholders' equity, 31st Dec 2006	46,827	97,290	-73,384	70,733

The VAT totalling SEK 750,000 reversed from 2004 was initially reported against the loss carried forward, but has been adjusted in the Group's shareholders' equity in the opening balance for 2005 against other capital contributed, as it referred to VAT reversed in conjunction with the new share issue in 2000.

CHANGES IN SHAREHOLDERS' EQUITY – THE PARENT COMPANY

SEK thousand	Share capital	Premium reserve	Statutory reserve	Non-restricted shareholders' equity	Total shareholders' equity
Opening balance, 1st Jan 2005	46,827	40,672	60	-5,925	81,634
Transfer from premium reserve to statutory reserve		-40,672	40,672		
Allocation of previous year's result			-5,925	5,925	0
Net result for the year				-8,833	-8,833
Opening balance, 1st Jan 2006	46,827	0	34,807	-8,833	72,801
Allocation of previous year's result			-8,833	8,833	0
Net result for the year				-4,834	-4,834
Shareholders' equity, 31st Dec 2006	46,827	0	25,974	-4,834	67,967

There are a total of 9,365,300 shares with a no-par value of SEK 5.

CASH FLOW STATEMENT

SEK thousand	Note	The Group		The Parent Company	
		2006	2005	2006	2005
Operating activities					
Result before tax		-4,834	-8,833	-4,834	-8,833
Depreciation and write-downs		6,645	5,757	6,645	5,757
Disposal of intangible fixed assets		379	153	379	153
Cash flow from operating activities before change in operating capital		2,190	-2,923	2,190	-2,923
Change in stock in trade		55	344	55	344
Change in operating receivables		-9,718	-532	-9,718	-532
Change in operating liabilities		4,415	-1,813	4,415	-1,813
Cash flow from operating activities		-3,058	-4,924	-3,058	-4,924
Investment activities					
Acquisition of intangible fixed assets		-1,283	-2,022	-1,283	-2,022
Acquisition of tangible fixed assets		-769	-105	-769	-105
Cash flow from investment activities		-2,052	-2,127	-2,052	-2,127
Financing activities					
Amortisation		-156	-171	-156	-171
Cash flow from financing activities		-156	-171	-156	-171
Change in liquid assets	22	-5,266	-7,222	-5,266	-7,222
Opening liquid assets		39,702	46,924	39,702	46,924
Closing liquid assets		34,436	39,702	34,436	39,702
Interest received and paid					
Interest income, as per Income Statement		718	810	718	810
Interest expense, as per Income Statement		-145	-144	-145	-144

No prepaid or accrued interest effects affect the interest income and interest expenses reported above.

Notes to the Accounts

Amounts in SEK thousand unless otherwise indicated.

NOTE 1 GENERAL INFORMATION

Probi Aktiebolag (publ), corporate ID no. 556417-7540, the registered offices of which are in Lund, Sweden and the address of which is Ideon Gamma 1, Sölvegatan 41, SE-223 70 Lund, Sweden, was founded in 1991 and is now a leading player in the field of probiotic research and development.

The company's research relates to live microorganisms with scientifically demonstrated health-giving effects. The main fields of research are: Gastrointestinal complaints, Immunology, Risk factors for cardiovascular disease and Stress and performance recovery. Probi's business concept is based on offering effective and well-documented probiotic product concepts with extensive patent protection, thereby creating the potential for higher royalties than in the industry as a whole.

The Group comprises the Parent Company, Probi AB, and two dormant subsidiaries, Probi Food AB and Probi Feed AB. Probi's share is quoted on The Nordic Exchange.

These consolidated accounts were approved by the Board of Directors for publication on 13th February 2007.

NOTE 2 ACCOUNTING AND VALUATION PRINCIPLES

The consolidated accounts have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU, and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) approved by the European Commission.

A number of standards and interpretations have been published, but not yet come into force, in conjunction with the preparation of the consolidated accounts on 31st December 2006. Below is a preliminary assessment of the effect that the introduction of these standards and interpretations could have on Probi AB's financial reports:

IAS 1 addendum – presentation of financial statements: Capital Disclosures

The addendum comes into force on 1st January 2007. This addendum is currently expected to entail augmented supplementary disclosures with regard to, among other things, the definition of capital, capital structure and capital management policies.

IFRS 7 Financial instruments: Disclosures

The standard comes into force on 1st January 2007. For Probi, this standard is not expected to entail any requirement to make additional supplementary disclosures.

*IFRS 8 Operating segments**

The standard comes into force on 1st January 2009 and applies to financial years that begin as of this date. The standard addresses the division of the company's operations into different segments. The standard states that the company shall take this as its starting point in the structure of its internal reporting and shall determine the reportable segments on the basis of this structure. Probi's preliminary assessment is that no changes in the segment reporting will be presented in the 2009 annual accounts.

IFRIC 7 Applying the restatement approach under IAS 29

Financial reporting in hyperinflationary countries

The interpretation came into force on 1st March 2006 and applies to financial years that began after 1st March 2006. Probi currently has no operations in countries where a transition to hyperinflationary reporting is imminent.

IFRIC 8 Scope of IFRS 2

The interpretation came into force on 1st May 2006 and applies to financial years that began after 1st May 2006. According to IFRIC 8, the provisions of IFRS 2 include goods and services received in exchange for equity instruments, even if these goods or services, either wholly or in part, cannot be specifically identified. This interpretation is not applicable to Probi, as this type of transaction does not occur.

IFRIC 9 Reassessment of embedded derivatives

The interpretation came into force on 1st June 2006 and applies to financial years that began after 1st June 2006. The interpretation constitutes a clarification of IAS 39 with regard to embedded derivatives, primarily with regard to an amended assessment of embedded derivatives resulting from changes in market conditions. Probi has no such instruments.

*IFRIC 10 Interim Financial Reporting and Impairment**

The interpretation came into force on 1st November 2006 and applies to financial years that begin after this date. The interpretation states that impairment losses in a previous interim report cannot be reversed in a subsequent interim or full year report. Probi will apply IFRIC 10 as of 1st January 2007, but this is not expected to have any effect on the Group's accounts.

*IFRIC 11 IFRS 2 Group and Treasury share transactions**

The interpretation comes into force on 1st March 2007 and applies to financial years that begin after this period. The interpretation clarifies the treatment of the classification of share-related payments in which the company buys its own equity instruments in order to regulate its share-based payment obligation and the reporting of stock option programmes in subsidiaries that apply IFRS. Probi will apply IFRIC 11 as of 1st January 2008, but this is not expected to have any effect on the Group's accounts.

*IFRIC 12 Service concession arrangements**

The interpretation comes into force on 1st January 2008 and applies to financial years that begin after this date. The interpretation addresses those arrangements in which a private company shall establish an infrastructure for providing public services for a specific period of time and the company receives payment for this service for the term of the contract. Probi will apply IFRIC 12 as of 1st January 2008, but this is not expected to have any effect on the Group's accounts.

* These standards/interpretations have not been adopted by the EU as of this date.

2.1 Prerequisites for preparing the consolidated financial reports

The Parent Company's functional currency is the Swedish krona, which is also the reporting currency for both the Parent Company and the Group. Unless otherwise indicated, all amounts shown have been rounded off to the nearest thousand kronor. The consolidated accounts have been prepared in accordance with the acquisition value accounting method, with the exception of applicable cases where financial assets are valued at their true value.

The most important accounting principles applied when these consolidated accounts were prepared are shown below. These principles have been applied consistently for all the years presented, unless otherwise indicated.

The Parent Company applies the same accounting principles, other than with regard to the exceptions and additions stipulated in recommendation RR 32, "Accounting for legal entities", issued by the Swedish Financial Accounting Standards Council. The accounting principles for the Parent company are detailed in the section entitled "The Parent Company's accounting principles".

2.2 Consolidated accounts

The consolidated annual accounts comprise the annual accounts for the Parent Company and all subsidiaries. All companies in which the Group holds or controls more than 50 per cent of the votes or in which the Group contractually exercises an exclusive determining influence are consolidated as subsidiaries. Subsidiaries are consolidated as of and including the day on which the Group gains control of the company, and sold subsidiaries are included in the consolidated accounts up to and including the day on which the Group retains control over the company.

The consolidated accounts are prepared using the acquisition method. Shareholders' equity in subsidiaries acquired is calculated on the basis of a market valuation of assets and liabilities at the time of acquisition (known as an acquisition analysis). If the market valuation of assets and liabilities yields values that differ from the acquired Group book values, these market values constitute the Group's acquisition value. If the acquisition value for the subsidiary's shares exceeds the estimated value of the net assets at the time of acquisition, the difference is reported as consolidated goodwill. If the acquisition value is less than the value of the net assets, the difference is reported as consolidated negative goodwill.

The effects of all intra-Group transactions and Balance Sheet items, such as unrealised profits on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction constitutes proof of the existence of a write-down requirement for the asset transferred.

2.3 Segment classification

Lines of business comprise products or services that are subject to risks and returns that differ from those of other lines of business. Geographic markets supply products or services within a distinct economic environment that is subject to risks and returns that differ from the risks and returns that apply to units operating in other economic environments. Lines of business are classified as primary segments in the Group, while geographic areas are classified as secondary segments.

2.4 Income

Income comprises the true value of what is obtained or will be obtained in return for the company's own or licensed goods sold within the framework of the Group's operations. Income is reported excluding Value Added Tax, returns and discounts and after the elimination of intra-Group sales.

Probi reports an income when the amount can be reliably measured, it is probable that future economic benefits will accrue to the company and special criteria have been met for each of the company's operations, as described below. The income amount is not deemed capable of reliable measurement until all obligations with regard to the sale have been met or expired. Probi bases its assessments on historic results and takes into account, in connection therewith, the type of customer, type of transaction and special circumstances, on a case-by-case basis.

Royalty revenues: Royalty revenues are reported as a percentage on the basis of the licensee's reporting of the sale value of consumer products containing Probi's products and ingredients. The accounting process is carried out at the end of every month. Licensing revenues arising from down payments made in conjunction with the signing of the contract are periodised over the period until the date when Probi expects a launch to occur in a territory in order to cover the company's organisation costs. The percentage of licensing revenues that does not correspond to costs is reported directly.

Interest income: Interest income is recognised as revenue over the term, applying the effective interest method.

2.5 Loan costs

Loan costs are taken up as income in the period to which they refer, irrespective of the use to which the borrowed funds have been put. Interest is capitalised in the acquisition value of assets.

2.6 Income tax

Income taxes reported comprise tax payable or receivable in respect of the year in question, together with adjustments made in respect of current tax for previous years. Valuation of all tax liabilities/receivables is effected at nominal amounts and in accordance with the tax regulations and tax rates instituted or announced and likely to be confirmed.

Associated tax effects are also reported in the Income Statement for items reported therein. Tax effects of items booked directly to shareholders' equity are reported against shareholders' equity.

Deferred tax is calculated using the Balance Sheet method on all temporary differences arising between reported and fiscal values of assets and liabilities. Deferred tax receivables in respect of deficit deductions or other future fiscal deductions are reported to the extent that it is likely that the deduction can be offset against surpluses in conjunction with future taxation. Deferred tax receivables attributable to fiscal loss deductions have not been reported pending product launches arising from new agreements.

2.7 Intangible assets

Goodwill: Goodwill comprises the amount by which the acquisition value exceeds the true value of the Group's participation in the acquired subsidiary's identifiable net assets at the time of the acquisition. Goodwill on the acquisition of subsidiaries is reported as intangible assets. Goodwill reported separately is tested annually (impairment testing) to identify any write-down requirements and are reported at the acquisition value less accumulated write-downs. Goodwill write-downs are not reversed. Profits or losses on the sale of a unit include the residual reported value of the goodwill that refers to the unit sold.

Goodwill is distributed between cash-generating units when conducting impairment tests. The distribution is made to the cash-generating units or groups of cash-generating units that have given rise to the goodwill item.

Accounting principles in respect of research and development expenses: Research expenses are booked as expenses on a rolling basis. Development expenses are reported as assets from the date when it is deemed that the project or activity to which they relate will lead to a technically and commercially launchable product and where Probi has decided to seek a partner or in some other way attempt to launch the product. Probi conducts research and development work in the probiotics field. Probi's licensees use this probiotic in their own products and these are in turn further developed for launch and commercial use. Probi provides assistance, but is not the party that completes the development of the end-product. Probi may, in certain cases, develop a product solution with the intention of presenting a potential licensee with an opportunity in new areas. Probi does not however control the launch or the choice of product solution.

When Probi deems that the criteria with regard to identifiability, control, future economic benefit and the ability to calculate the acquisition value in a satisfactory manner have been met, it capitalises these development costs. Customer-controlled development projects in relation to existing launches with Probi's probiotics will probably meet the requirements for capitalising development expenses.

Other intangible assets: Patent and licensing expenses are reported at their acquisition value and are amortised linearly over their contractually regulated useful life. The useful life of the assets is reviewed annually. The following amortisation periods are applied:

- Patents – 10 years
- Licenses – 12 years, in respect of acquisitions of European rights where the initial contractual period is 12 years.

Annual charges and other additional fees are carried as expenses on a rolling basis.

2.8 Tangible fixed assets

Land and buildings are reported at a value that is tested annually, less depreciation of buildings effected thereafter. All other tangible fixed assets are reported at the acquisition value less depreciation. The acquisition value includes expenses directly attributable to the acquisition of the asset. Additional charges are only added to the reported value of the asset or reported as a separate asset, depending on what is appropriate, when it is likely that the future economic benefits associated with the asset will accrue to the Group and the acquisition value of the asset can be measured in a reliable way. The reported value for the part replaced are eliminated from the Balance Sheet. All other forms of repairs and maintenance are reported as costs in the Income Statement during the period when they arise.

Notes to the Accounts

Land is not depreciated. Linear depreciation methods are used for all types of asset, as shown below.

- Buildings – 25 years
- Inventories, tools and installations – 3-10 years

Profits and losses on the disposal of tangible fixed assets are reported under Other operating income and Other operating expenses, respectively.

2.9 Write-downs of tangible assets

Assets that have an undefined useful life are not depreciated; rather they are reviewed annually with regard to any requirement for a write-down (impairment testing). Assets depreciated are evaluated with regard to a reduction in value whenever events or changes in circumstances indicate that the reported value may not be recoverable. A write-down is effected in the amount by which the asset's reported value exceeds its recovery value. The recovery value is whichever is the higher of an asset's true value less selling expenses, and the value in use. When conducting impairment testing, the assets are grouped at the lowest level at which separate identifiable cash flows (cash generating units) exist.

2.10 Leasing

Leasing agreements are classified within the Group as either financial or operational leasing. Leasing agreements in respect of fixed assets whereby the Group has, in every significant respect, assumed the same risks and enjoys the same benefits as it would in conjunction with direct ownership, are classified as financial leasing.

Operational leasing agreements: Leasing of fixed assets where the lessor, in every significant respect, continues to hold the title to the asset, are classified as operational leasing. The leasing charge for operational leasing is carried as an expense linearly over the leasing period.

Financial leasing agreements: When the leasing agreement results in the Group, in its capacity as lessee, in every significant respect enjoying the economic benefits and assuming the economic risks attributable to the leasing object, the object is reported as a fixed asset in the consolidated Balance Sheet. A corresponding undertaking to pay leasing charges in the future is reported as a liability. All leasing agreements, irrespective of whether they are operational or financial, are reported in the Parent Company as rental agreements (operational leasing agreements).

All of the company's leasing agreements are operational in nature.

2.11 Financial instruments

Consolidated financial instruments reported in the Balance Sheet include liquid assets, accounts receivable and accounts payable, as well as loan liabilities.

Accounts receivable: Accounts receivable are non-derivative financial assets with fixed or fixable payments that are not quoted on an active market. They are distinguished by the fact that they arise when the Group supplies monies, goods or services directly to a customer without intending to trade in the receivable that arises. They are included under Current assets, with the exception of items with a due date that falls more than 12 months after the closing date, which are classified as Fixed assets. Accounts receivable are booked under the Accounts receivable item in the Balance Sheet. Accounts receivable are booked in the amount that the Group expects to receive, based on an individual assessment of doubtful accounts receivable.

Loan costs: Loan costs are initially reported in the amount received after deductions for transaction costs. This ensures that on the due date, the reported amount corresponds to the amount to be repaid. Financial liabilities do not cease to be reported until the debts have been settled by means of repayment or the loan being remitted. All transactions are reported on the settlement date.

2.12 Stock in trade

Stock in trade is valued, using the first-in-first-out (FIFO) principle at whichever is the lower of the acquisition value and the net sales value

on the closing day. The acquisition value of finished goods comprises the cost of raw materials, direct salaries, other direct costs and indirect manufacturing costs attributable to them (based on normal manufacturing capacity). Loan costs are not included. The net sales value comprises the estimated sale price in the day-to-day operations, less applicable floating sales overheads.

2.13 Accounts receivable

Accounts receivable are reported at their true value, less any provision for depreciation and thereafter at the accrued acquisition value applying the effective interest rate method, less any provision for a reduction in value. Provision for the depreciation of accounts receivable is made when there is objective proof that the Group will be unable to obtain the full amount due in accordance with the original terms of the receivable. The size of the provision is determined by the difference between the reported value of the asset and the current value of estimated future cash flows, discounted using the effective interest rate. The provision amount is reported in the Income Statement.

2.14 Liquid assets

Liquid assets comprise cash and bank balances. Liquid assets include no short-term investments.

2.15 Foreign currencies

Transactions in foreign currencies are converted to the functional currency at the exchange rate on the transaction date. Monetary assets and liabilities in foreign currencies are converted at the closing date rate. Exchange rate differences arising in conjunction with the conversion are reported in the Income Statement. Non-monetary assets and liabilities reported at historic acquisition values are converted at the exchange rate on the transaction date.

2.16 Provisions

Provisions are reported when the Group has, or may be deemed to have, an obligation as a result of events that have occurred, and where it is likely that disbursements will be required in order to meet the obligation. A further requirement is that it is possible to make a reliable estimate of the amount to be disbursed. Provision for potential restructuring measures is made once a detailed, formal plan for the measures has been drawn up and well-founded expectations have been generated among those who will be affected by the measures.

2.17 Pensions

All of the company's pension plans are defined contribution plans. Under defined contribution plans, the company's legal or informal obligations are limited to the size of the contribution that the company agrees to make. The Group's disbursements in respect of defined contribution plans are reported as a cost over the period during which the employees performed the services to which the contribution relates.

2.18 Cash flow statement

The cash flow statement is compiled using the indirect method. The reported cash flow only comprises transactions that entail payments being received or made. Bank deposits and petty cash are defined as liquid assets.

2.19 The Parent Company's accounting principles

The Parent Company's financial reports have been prepared in accordance with the provisions of the Swedish Annual Accounts Act (ÅRL) and recommendation RR32, Reporting for legal entities, of the Swedish Financial Accounting Standards Council, whereby the Parent Company shall, wherever possible within the framework of ÅRL and taking into account the link between reporting and taxation, apply the International Financial Reporting Standards (IFRS) approved by the EU. No differences between the reporting of the Parent Company and the Group have been identified.

NOTE 3 FINANCIAL RISK FACTORS

Probi's partnerships with international customers entail income in several different currencies that are affected by exchange rate fluctuations. Revenues from Skane Dairy currently dominate, and contractually, these are always paid in SEK. In 2006, a smaller percentage of revenues were in EUR, but as the agreements with Danone and Institut Rosell generate royalty payments, revenues in foreign currencies are expected to increase.

Probi has borrowed approximately SEK 3.6 million on the production facility in Sösdala at a variable interest rate. An increase of 1 per cent in the interest rate would mean an increase of approximately SEK 40,000 in interest expenses. The company has no interest-bearing operating liabilities.

NOTE 4 IMPORTANT ESTIMATES AND ASSESSMENTS FOR ACCOUNTING PURPOSES

Probi's deferred tax receivable attributable to fiscal loss deductions has not been reported, pending product launches arising from new agreements and the company's ability to generate a taxable profit. The company's accumulated fiscal loss deductions as of 31st December 2006 totalled SEK 71.2 million. The accumulated loss entails a deferred fiscal receivable of SEK 19.9 million that can be utilised in future when the company reports a profit.

Impairment tests have been carried out within Probi in 2006 to secure the value, as of 31st December 2006, of patents, licences and similar rights. Probi closely monitors its partners' launches, and their development work and product positionings for impending launches. The information obtained from this material forms the basis for the information used when the company performs impairment tests. The tests carried out have indicated that no write-down requirement exists.

The Group investigates whether any write-down requirement exists for goodwill on an annual basis, in accordance with the accounting principle described in Note 2.9. The recovery value for cash-generating units has been determined by calculating the value in use. These calculations require certain estimates to be made. The remaining useful life is 6 years (7), 12 per cent (12) has been used as the discount rate and growth has been estimated at 10 per cent (10).

NOTE 5 SEGMENT INFORMATION

The Group works within three main business areas: Functional Food ("FF"), Dietary Supplements ("DS"), and Clinical Nutrition ("CN").

The FF business area has existed since the first licensing agreement was signed in 1993. DS became an independent business area in 2002. The company launched CN as an independent business area in 2003.

"Other" comprises unallocated research and business development costs, general administrative costs, other central costs, and financial items.

There are no sales or other transactions between the various lines of business.

Income statement per line of business

The Group	2006				Total
	FF	DS	CN	Other	
Total operating income	33,557	4,583	0	277	38,417
Total operating expenses	-28,802	-5,006	-5,402	-4,614	-43,824
Operating result	4,755	-423	-5,402	-4,337	-5,407

NOTE 5 Cont.

Income statement per line of business

The Group	2005				Total
	FF	DS	CN	Other	
Total operating income	24,143	3,517	0	6	27,666
Total operating expenses	-24,495	-4,755	-7,738	-177	-37,165
Operating result	-352	-1,238	-7,738	-171	-9,499

Balance Sheet per line of business

The category "Other" comprises assets and liabilities attributable to joint research and business development activities, Group-wide activities and items of a financial nature.

Balance sheet per line of business

The Group	2006				Total
	FF	DS	CN	Other	
Total assets	42,861	1,352	1,451	36,701	82,365
Long-term liabilities	0	0	0	3,450	3,450
Current liabilities	2,203	236	271	5,472	8,182
Total liabilities	2,203	236	271	8,922	11,632
Shareholders' equity	0	0	0	0	70,733
Investments	2,052	0	0	0	2,052
Depreciations	-5,061	-219	-472	0	-5,752
Amortisation	-893	0	0	0	-893

The Group	2005				Total
	FF	DS	CN	Other	
Total assets	37,598	1,533	1,769	42,044	82,944
Long-term liabilities	0	0	0	3,610	3,610
Current liabilities	1,479	92	494	1,702	3,767
Total liabilities	1,479	92	494	5,312	7,377
Shareholders' equity	0	0	0	0	75,567
Investments	2,022	0	45	60	2,127
Depreciations	-5,055	-217	-461	-177	-5,910
Amortisation	0	0	0	0	0

Operating income, assets and investments broken down by geographical area

The Group	2006			Total
	Nordic region	Europe, other	Global, other	
Operating income	25,121	9,857	3,439	38,417
Assets	52,014	29,964	387	82,365
Investments	1,010	460	582	2,052

The Group	2005			Total
	Nordic region	Europe, other	Global, other	
Operating income	20,815	4,131	2,720	27,666
Assets	54,923	25,377	2,644	82,944
Investments	485	624	1,018	2,127

Notes to the Accounts

NOTE 6 BREAKDOWN OF NET TURNOVER

	The Group		The Parent Company	
	2006	2005	2006	2005
Goods	1,985	2,086	1,985	2,086
Royalties, licenses, etc.	35,230	25,150	35,230	25,150
Total	37,215	27,236	37,215	27,236

NOTE 7 AUDITORS' FEES

	The Group		The Parent Company	
	2006	2005	2006	2005
Audits	314	342	314	342
Non-audit assignments	17	38	17	38
Total	331	380	331	380

The term, audit assignment, refers to the auditing of the Annual Report, the bookkeeping and the administration by the Board of Directors and CEO, other duties incumbent upon the company's auditors, and the provision of advice or other assistance occasioned by observations in conjunction with such auditing, or the execution of other such duties. Everything else is classified as Non-audit assignments.

NOTE 8 RESEARCH AND DEVELOPMENT

	The Group		The Parent Company	
	2006	2005	2006	2005
Research and development expenses booked as costs	15,391	15,240	15,391	15,240

NOTE 9 AVERAGE NUMBER OF EMPLOYEES, SALARIES, OTHER REMUNERATION AND PAYROLL OVERHEADS

	The Group		The Parent Company	
	2006	2005	2006	2005
Average no. of employees				
Women	10	10	10	10
Men	8	8	8	8
Total	18	18	18	18
Salaries and remuneration:				
The Board of Directors and CEO	2,088	2,095	2,088	2,095
Other management	2,480	2,589	2,480	2,589
Other employees	4,430	5,032	4,430	5,032
Total	8,998	9,716	8,998	9,716
Payroll overheads, total:	4,750	5,061	4,750	5,061
Of which pension costs for the Board and CEO	482	478	482	478
Of which pension costs for other management personnel	574	610	574	610
Of which pension costs for other employees	442	481	442	481
Salary and pension premiums for CEO:				
Salary, former CEO	1,304	1,485	1,304	1,485
Pension premiums, former CEO	482	478	482	478
Salary, Acting CEO	50	0	50	0
Pension premiums, former CEO	0	0	0	0

NOTE 9 Cont.

	The Group		The Parent Company	
	2006	2005	2006	2005
Salaries and remuneration for the Board				
Salary and remuneration for the Chairman of the Board	150	142	150	142
Salaries and remuneration for other Board Members	500	468	500	468

Salary payments made to the CEO of the company in 2006 totalled SEK 1,304 thousand and salary payments made to the Acting CEO totalled SEK 50 thousand. The company has also paid SEK 482 thousand in pension premiums for the former CEO. There is currently no bonus programme for the CEO and other senior executives. There are currently no bonus programmes for the CEO and other senior executives. The period of notice for the CEO was six months if notice is given by the CEO and twelve months if notice was given by the company. Severance pay shall also be payable in the sum of twelve months' salary when notice is given by the company. The retirement age for the CEO is 65. The current Acting CEO is employed for a fixed period of time. The period of notice for the Deputy CEO is twelve months if notice is given by Probi and six months if notice is given by the Deputy CEO.

The period of notice for other senior executives is six months if notice is given by Probi and three months if notice is given by the employee.

The company has no severance pay or pension agreements other than those described above.

The CEO's salary is set by the Board of Directors while those of the rest of the management are set by the CEO and the Chairman of the Board.

There are no share-based benefits within the company. The principal owners of Probi have issued 20,000 stock options at the market price, using the Black Scholes valuation model, to the Deputy CEO. These stock options entitle their holder to acquire shares at a price of SEK 44 during the period from 1st January 2007 to 31st August 2007.

The Company has no outstanding and unreported pension undertakings since all pensions are premium-based. There is no share-based remuneration in the company. The company management is exclusively male.

Absence due to sickness

Parent Company	2006	2005
Total absence due to sickness	5.0 %	0.9 %

No breakdown is provided because there are fewer than 10 employees in each sub-category.

NOTE 10 DEPRECIATION AND WRITE-DOWNS OF FIXED ASSETS

Tangible and intangible fixed assets have been depreciated in the amounts shown below:

	The Group		The Parent Company	
	2006	2005	2006	2005
Depreciation and write-downs	6,645	5,757	6,645	5,757

NOTE 11 FINANCIAL INCOME AND EXPENSES

	The Group		The Parent Company	
	2006	2005	2006	2005
Interest income	718	810	718	810
Interest expenses	-145	-144	-145	-144

NOTE 12 INCOME TAX

Tax is calculated at a tax rate of 28 per cent.

	2006	2005
Result before tax	-4,834	-8,833
Fiscal effect, calculated at the national tax rate	-1,354	-2,473
Review of previous years' taxation	37	0
Non-taxable income	0	0
Non-deductible expenses	24	12
Fiscal deficit for which no deferred tax receivable has been reported	1,293	2,461
Tax expense	0	0

NOTE 13 DEFERRED TAX

	The Group		The Parent Company	
	2006	2005	2006	2005
Non-booked tax receivable in respect of unutilised deficit deductions	19,947	18,654	19,947	18,654

There is no time limit on the use of the non-booked tax receivable in respect of unutilised deficit deductions. On 31st December 2006, Probi had SEK 71.2 million in unutilised deficit deductions, corresponding to an as yet unbooked deferred tax receivable of SEK 19.9 million. Probi will consequently have a corresponding deduction entitlement when the company shows a profit. Probi's ability to realise all or part of the value of the loss deduction depends on the company's ability to generate taxable profits.

NOTE 14 OPERATIONAL LEASING AGREEMENTS

Operational leasing agreements comprise rental agreements for premises, office equipment and car leasing. The nominal value of future minimum leasing charges in respect of operational leasing agreements breaks down as follows:

	The Group		The Parent Company	
	2006	2005	2006	2005
Year's leasing charges	1,918	1,959	1,918	1,959
Falls due for payment within one year	1,895	1,910	1,895	1,910
Falls due for payment after more than 1 but fewer than 5 years	457	182	457	182
Falls due for payment after more than 5 years	0	0	0	0

NOTE 15 PATENTS, LICENSES AND SIMILAR RIGHTS

Patents and licenses	The Group		The Parent Company	
	2006	2005	2006	2005
Opening acquisition value	53,515	51,730	53,515	51,730
New acquisitions	1,283	2,022	1,283	2,022
Disposals	-543	-237	-543	-237
Closing accumulated acquisition value	54,255	53,515	54,255	53,515
Opening depreciation	-25,946	-21,832	-25,946	-21,832
Disposals	162	83	162	83
Depreciation for the year	-4,326	-4,197	-4,326	-4,197
Closing accumulated depreciation	-30,110	-25,946	-30,110	-25,946
Closing residual value according to plan	24,145	27,569	24,145	27,569

NOTE 15 Cont.

Patents, licenses and similar rights are primarily attributable to the buy-back of the European rights from Skane Dairy for SEK 40 million in 2001, the book value of which, as on 31st December 2006, was SEK 20.4 million. The European rights are depreciated linearly from the acquisition year up until 2012, which is the year when the patent for the bacterial strain in question expires.

Write-down tests (or impairment tests) have been carried out within Probi during 2006 to determine the value of patents, licenses and similar rights on 31st December 2006. Probi closely monitors its partners' launches, and their development work and product positionings for impending launches. The information obtained from this material forms the basis for the information used when the company performs write-down tests.

The tests carried out have indicated that no write-down requirement exists. The discount rate used was 12 per cent.

The Group has reviewed the useful life of its intangible assets in accordance with the provisions of IAS 38. This process has not occasioned any adjustments.

NOTE 16 GOODWILL

	The Group		The Parent Company	
	2006	2005	2006	2005
Opening acquisition value	2,762	2,762	-	-
Closing residual value according to plan	2,762	2,762	-	-

The goodwill item is related to the strategic acquisition in 1998 of outstanding shares in Probi Food AB and is, therefore, reported under the Functional Food segment. Goodwill is tested every year with regard to any write-down requirement, as of the 2004 financial year. Such tests are also conducted when there are indications of a write-down requirement.

The Group carries out tests every year to determine whether any write-down requirement exists for goodwill, in accordance with the accounting principle described in Note 2.9. The recovery value of cash-generating units has been determined by calculating the value in use. Certain estimates must be made for the purposes of these calculations. Because the remaining useful life is 6 years (7), forecasts are based on periods of more than five years. 12 per cent (12) has been used as the discount rate, and growth has been calculated at 10 per cent (10), which was also the growth rate reported for the license agreement in question in 2006.

Impairment tests have been carried out within Probi during 2006 to determine the goodwill value on 31st December 2006. The tests carried out have indicated that no write-down requirement exists.

NOTE 17 BUILDINGS AND LAND

	The Group		The Parent Company	
	2006	2005	2006	2005
Opening acquisition value	4,642	4,642	4,642	4,642
Closing accumulated acquisition value	4,642	4,642	4,642	4,642
Opening depreciation	-686	-525	-686	-525
Depreciation for the year	-161	-161	-161	-161
Closing accumulated depreciation	-847	-686	-847	-686
Closing residual value	3,795	3,956	3,795	3,956
Rateable value, land in Sweden	1,123	561	1,123	561
Rateable value, buildings in Sweden	1,638	1,339	1,638	1,339

The value of land accounts for SEK 1,247 thousand of the total reported value. An independent valuation in 2004 indicates that the market value of buildings and land exceeds the book value.

Notes to the Accounts

NOTE 18 INVENTORIES, TOOLS AND INSTALLATIONS

Inventories	The Group		The Parent Company	
	2006	2005	2006	2005
Opening acquisition value	13,269	13,164	13,269	13,164
Purchases	769	105	769	105
Closing accumulated acquisition value	14,038	13,269	14,038	13,269
Opening depreciation	-9,370	-7,972	-9,370	-7,972
Depreciation for the year	-1,267	-1,398	-1,267	-1,398
Closing accumulated depreciation	-10,637	-9,370	-10,637	-9,370
Opening write-downs	0	0	0	0
Write-downs for the year	-893	0	-893	0
Closing accumulated write-downs	-893	0	-893	0
Closing residual value	2,508	3,899	2,508	3,899

NOTE 19 PARTICIPATIONS IN GROUP COMPANIES

	The Parent Company			
	2006		2005	
Book value	4,031		4,031	
Specification of the Parent Company's shareholdings in Group companies				
	Share in capital	Share in votes	No. of shares	Book value
Probi Food AB 556354-1951, Lund	100 %	100 %	10,000	3,931
Probi Feed AB 556540-4364, Lund	100 %	100 %	1,000	100
No purchases or sales have been made between the Group's companies during the year.				

NOTE 20 ACCOUNTS RECEIVABLES

Probi's accounts receivable are related to a few major licensing partners. The company does not deem there to be any significant credit risk in respect of these partners. Probi has used letters of credit or payment in advance when selling to companies without licensing agreements.

None of the accounts receivable have been deemed doubtful, and hence no depreciation has been effected in 2006.

NOTE 21 PREPAID COSTS AND ACCRUED INCOME

	The Group		The Parent Company	
	2006	2005	2006	2005
Prepaid rent	404	437	404	437
Other items	569	526	569	526
Total	973	963	973	963

NOTE 22 LIQUID ASSETS

The Group's liquid assets refer to cash and bank balances.

NOTE 23 SHAREHOLDERS' EQUITY

A specification of changes in shareholders' equity can be found in the report entitled "Changes in shareholders' equity", which follows directly on from the Balance Sheets.

No. of shares	Class A	Class B	Common share class	Total number
No. on 31st Dec 2005	0	0	9,365,300	9,365,300
No. on 31st Dec 2006	0	0	9,365,300	9,365,300

The no-par value of the shares is SEK 5.

NOTE 24 OTHER LONG-TERM LIABILITIES

	The Group		The Parent Company	
	2006	2005	2006	2005
Liabilities to credit institutions, 1-5 years	624	608	624	608
Liabilities to credit institutions, >5 years	2,826	3,002	2,826	3,002
Liabilities to Group companies, >5 years	0	0	4,035	4,035
Total	3,450	3,610	7,485	7,645

Liabilities refer to variable interest rate loans for industrial premises. Interest rate adjustments are made in conjunction with changes in the general level of interest rates. At the turn of the year, the effective interest rate was 4.9 per cent. The company has no significant profits or losses attributable to financial liabilities.

NOTE 25 ACCRUED COSTS AND PREPAID INCOME

	The Group		The Parent Company	
	2006	2005	2006	2005
Accrued holiday pay	297	222	297	222
Social security contributions	381	358	381	358
Severance pay	4,252	0	4,252	0
Other items	856	1,297	856	1,297
Total	5,786	1,877	5,786	1,877

NOTE 26 PLEDGED ASSETS AND CONTINGENT LIABILITIES

	The Group		The Parent Company	
	2006	2005	2006	2005
Real estate mortgages	3,300	3,300	3,300	3,300
Floating charges	800	800	800	800
Total pledged assets	4,100	4,100	4,100	4,100

The company has no contingent liabilities.

NOTE 27 TRANSACTIONS WITH ASSOCIATED COMPANIES

Transactions with associated companies reported in the Income Statement	The Group		The Parent Company	
	2006	2005	2006	2005
Skane Dairy (royalty revenues)	23,969	22,166	23,969	22,166
Skane Dairy (services)	17	0	17	0
Total income	23,986	22,166	23,986	22,166
Skane Dairy (royalty costs)	-359	-107	-359	-107
H&B Capital Advisors AB (fee)	-334	0	-334	0
H&B Capital Advisors AB (reimbursement of expenses)	-229	-367	-229	-367
GMF AB, associated party: Göran Molin	-78	-114	-78	-114
Lowenzahna AB, associated party: Rolf Bjernell	-749	0	-749	0
Total costs	-1,749	-588	-1,749	-588

Transactions with associated companies reported in the Balance Sheet	The Group		The Parent Company	
	2006	2005	2006	2005
Operating receivables				
Skane Dairy	2,741	2,098	2,741	2,098
Total operating receivables	2,741	2,098	2,741	2,098
Operating liabilities				
Skane Dairy	-2	-2	-2	-2
H&B Capital Advisors AB	0	-98	0	-98
GMF AB, associated party: Göran Molin	-17	-18	-17	-18
Lowenzahna AB, associated party: Rolf Bjernell	-635	0	-635	0
Total operating liabilities	-654	-118	-654	-118

Skane Dairy and H&B Capital are Probi's biggest shareholders. The transactions have been conducted on commercial terms and at market value. The Parent Company has an agreement with Skane Dairy comprising licensing and service agreements. Royalties from Skane Dairy are based on these long-term agreements. The transactions otherwise refer to consultancy fees.

NOTE 28 EVENTS AFTER THE CLOSING DATE

No significant events have occurred after the closing date.

The Income Statement and the Balance Sheets will be submitted to the Annual General Meeting of the shareholders of the company for adoption on 8th May 2007.

Lund 2007-02-13


 Peter Zakrisson
 Chairman


 Lars Backsell


 Hilde Furberg



 Mats Lidgard



 Göran Molin


 Rolf Trulsson


 Rolf Bjernell
 Acting CEO

Our Auditors' Report was submitted on 16th February 2007
PricewaterhouseCoopers AB


 Lars Helgesen
 Authorised Public Accountant
 Principal Accountant


 Magnus Jönsson
 Authorised Public Accountant

Auditors' Report

To the Annual General Meeting of the shareholders of Probi AB (publ), Swedish Company Registration Number 556417-7540

We have audited the annual accounts, the consolidated accounts, the accounting records and the administration of the Board of Directors and the CEO of Probi AB (publ) for the financial year 2006. The company's annual accounts can be found on pages 20–39 of the printed version of this document. These accounts and the administration of the company are the responsibility of the Board of Directors and the CEO, as is ensuring that the Swedish Annual Accounts Act is applied to the preparation of the annual accounts, and that IFRS international accounting standards, as adopted by the EU, and the Swedish Annual Accounts Act are applied to the preparation of the consolidated accounts. Our responsibility is to express an opinion on the annual accounts, the consolidated accounts and the administration based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Sweden. These standards require that we plan and perform the audit to obtain high, but not absolute, assurance that the annual accounts and the consolidated accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and their application by the Board of Directors and the CEO, as well as evaluating the significant estimates made by the Board of Directors and the CEO when preparing the annual accounts and the consolidated accounts, and evaluating the overall presentation of information in the annual accounts and the consolidated accounts. As a basis for our opinion concerning discharge from liability, we examined significant decisions, actions taken and circumstances of the company in order to be able to determine the liability, if any, to the company of any Board Member or the CEO. We also examined whether any Board

Member or the CEO has, in any other way, acted in contravention of the Swedish Companies Act, the Swedish Annual Accounts Act, or the Articles of Association. We believe that our audit provides a reasonable basis for our opinion as set out below.

The annual accounts have been prepared in accordance with the Swedish Annual Accounts Act and thereby give a true and fair view of the company's financial position and results in accordance with generally accepted accounting principles in Sweden. The consolidated accounts have been prepared in accordance with IFRS international accounting standards, as adopted by the EU, and the Swedish Annual Accounts Act and thereby give a true and fair view of the Group's financial position and results. The Directors' Report is compatible with the other sections of the annual accounts and the consolidated accounts.

We recommend to the Annual General Meeting of Shareholders that the Income Statement and the Balance Sheet of the Parent Company and the Group be adopted, that the loss of the Parent Company be dealt with in accordance with the proposal in the Directors' Report, and that the Members of the Board of Directors and the CEO be discharged from liability for the financial year.

Malmö, 16th February 2007

PricewaterhouseCoopers AB



Lars Helgesen
Authorised Public Accountant
Principal Accountant



Magnus Jönsson
Authorised Public Accountant

The Board of Directors



Peter Zakrisson

Born in 1961. Chairman of the Board since 2002. Member of the Board since 2001. Education: Business Administration degree from Lund University/Stockholm University. Founding partner of H&B Capital since 2000. Other directorships: Besthand AB, G Z Holding AB, et al. Holding in the company: 0 shares.



Lars Backsell

Born in 1952. Member of the Board since 2006. Education: Business Administration degree from the Stockholm School of Economics. Founder and CEO of Recip AB. Formerly worked within the Pharmacia group of companies in a variety of managerial positions. Other directorships: Recip AB, Chairman of IVA's Trade and Industry Advisory Board. Holding in the company: 0 shares.



Hilde Furberg

Born in 1958. Member of the Board since 2005. Education: B.Sc. in Medical Technology, University of Oslo. Vice President & General Manager of Nordic/Benelux Genzyme. Other directorships: none. Holding in the company: 0 shares.



Mats Lidgard

Born in 1954. Member of the Board since 2004. Education: LL.B., Lund University, 1980. Deputy CEO of SBL Vaccin AB. Other directorships: Synphora AB. Holding in the company: 1,000 shares.



Rolf Trulsson

Born in 1941. Member of the Board since 2006. Education: B.A. in Social Sciences from Lund University. Former CEO of Skane Dairy. Other directorships: Chairman of the Board of Busspågarna AB. Holding in the company: 3,390 shares.



Göran Molin

Born in 1949. Member of the Board since 1998. Education: Doctorate from the Royal College of Veterinary Surgeons in Stockholm, 1976. Reader in microbiology at Lund University, 1984. Professor of Food Hygiene at Lund University. Göran Molin was part of the group of researchers who founded Probi AB. Holding in the company: 426,241 shares.

Auditors

PricewaterhouseCoopers AB.
Principal Accountant: Authorised Public Accountant,
Lars Helgesen, Malmö.
Authorised Public Accountant:
Magnus Jönsson, Malmö

The senior management



From the left: Niklas Bjärüm, Håkan Peterson, Per-Ola Forsberg and Rolf Bjørndell.

Niklas Bjärüm

Born in 1963. Director of Marketing and Sales, Functional Food. Education: Degree in International Economics from Lund University. Background: Niklas Bjärüm was employed in February 2001 and was put in charge of the company's marketing and sales. Since taking his degree in 1988, Niklas Bjärüm has worked in a number of positions in Marketing, Sales and Business Development of both an operational and a strategic nature at international food companies, such as Nestlé and Masterfoods (Mars Inc.). In 1998, he changed industry and worked at Ericsson Mobile Communications for three years, where he was responsible for Business Development for the European market. Holding in the company: 2,000 shares.

Håkan Peterson

Born in 1960. Director of Marketing and Sales, Dietary Supplements. Education: Degree in International Economics from Lund University. Background: Håkan Peterson was employed in November 2006 and was put in charge of the company's marketing and sales for dietary supplements. Immediately prior to this, Håkan Peterson was employed by the medical engineering company, Gambro, where he was in charge of sales and marketing for Central and Eastern Europe. He has wide-ranging experience of international work in a number of medical engineering companies where he has worked in senior positions in the fields of marketing and sales. Holding in the company: 2,000 shares.

Per-Ola Forsberg

Born in 1961. CFO, Executive Vice President. Education: Degree in Economics and Business Administration from Lund University. Background: Per-Ola Forsberg was employed in November 2000 as CFO and Head of Administration. Immediately prior to this, Per-Ola Forsberg was the Controller at Rexam Beverage Can Fosite AB, and before that, he was employed as Head of Administration at PolyPeptide Laboratories (Sweden) AB. Holding in the company: 5,400 shares and 20,000 stock options. See also under Note 9 on page 36.

Rolf Bjørndell

Born in 1951. Acting CEO of Probi. Chairman of the Board of Probi 1996–2000 and Member of the Board 2000–2006. Education: Degree in Business Administration from Lund University. CEO of Skane Dairy, 1994–2005. Other directorships: the Chamber of Commerce and Industry of Southern Sweden, Malmö Incubator AB, Swedish Oat Fibre AB, Ideon Agro Food, et al. Holding in the company: 6,775 shares.

Probi's senior management group also includes the Head of Research – a position that is currently vacant.

Glossary

Bacterial strain

Bacteria are microscopic organisms that consist of a single cell. A bacterial strain comprises bacteria with the same genetic identity.

Clinical documentation

Documentation of clinical trials.

Clinical nutrition

Specialised nutritional and food products intended for use in hospitals and outpatient care with patients whose general health is poor or who are seriously ill.

Clinical trials

Studies of food or pharmaceutical products on humans.

Dietary supplement

Food intended for use as a complement to a normal diet and which comprises concentrated sources of nutritional substances or other substances with a nutritional or physiological effect, whether separately or collectively. Dietary supplements are sold in individual doses, e.g. capsules, tablets or portion sachets.

Enteral nutrition

Medical concept involving the supply of nutrition to the stomach or intestine via a feeding tube or by mouth.

Functional food

Food products that have been enriched with one or more ingredients that have positive effects on health over and above the normal nutritional value of the product.

IBS

Irritable Bowel Syndrome, the condition is regarded as one of biggest public health problems in the western world.

Lactobacilli

A strain of bacteria that is part of the lactic acid family of bacteria, which is closely associated with various types of human mucous membrane and is often used in the acidification of foods.

Patent

Intellectual property right that protects inventions or technical solutions. Patents grant sole right to use the patented item commercially.

Probiotics

Living microorganisms that have positive effects on human health when ingested in sufficient quantities.

Product concept

A concept or product prototype that requires development before it becomes an end-product.

Product-specific health claims

A health claim for a unique product whose scientific documentation has been reviewed by the Swedish Nutrition Foundation, for example.

Royalty

Payment for use of an intellectual property right where the amount paid is linked to the scale of the sales.

Swedish Nutrition Foundation (SNF)

The Foundation's objective is to promote scientific research into nutrition and associated fields and to promote the practical utilisation of advances made in this field of research. It is responsible for reviewing scientific documentation that forms the basis for product-specific health claims for functional food.

Therapeutic field

Sphere of use or treatment of a product, e.g. problems relating to the immune system or IBS.

Thoroughly documented

The term is used to refer to a product's demonstrated positive effects on health, as proven in extensive clinical studies.

Type I diabetes

A type of diabetes whereby the body's own insulin production has ceased, either wholly or in part.

Type II diabetes

A type of diabetes whereby the body is still able to produce small amounts of insulin, but where the insulin's effects are limited. The disease is also known as adult-onset diabetes.

The Annual General Meeting

THE ANNUAL GENERAL MEETING

The shareholders of Probi AB (publ) are hereby notified of the Annual General Meeting of the company's shareholders to be held on Tuesday 8th May 2007 at 3 p.m. (CET) in Edison Park, Emdalavägen 16, in Lund.

ENTITLEMENT TO PARTICIPATE

In order to be entitled to participate in the Meeting, shareholders must both be registered in the Register of Shareholders maintained by VPC AB (the Swedish CSD) in respect of circumstances obtaining on Wednesday 2nd May 2007, and shall have notified Probi of their intention to participate in the Meeting no later than 4 p.m. (CET) on Wednesday 2nd May 2007.

Shareholders whose shares are nominee-registered must temporarily re-register their shares in their own name with VPC in order to be entitled to participate in the Meeting. Such registration must be effected no later than Wednesday 2nd May 2007, and shareholders must therefore notify the nominee of their request to that effect in good time.

APPLICATIONS TO PARTICIPATE

Applications to participate in the meeting shall be submitted in writing to Probi AB (publ), Ideon, SE-223 70 Lund, Sweden, by fax on +46 (0)46 286 89 28, by phone on +46 (0)46 286 89 20 or by e-mail to probi@probi.se.

Applications shall include the applicant's name, civic ID number or company registration number, the number of shares held, a daytime telephone number and, where relevant, the number of assistants (a maximum of two) who will accompany the applicant to the meeting. If a shareholder intends to be represented by a proxy, a power of attorney and other authorisation documents should be appended to the application.

FINANCIAL REPORTING DATES

Interim Report, Q1	25th April
2006 Annual General Meeting	8th May 3 p.m. (CET)
Interim Report, Q2	24th July
Interim Report, Q3	25th October
Preliminary financial statement for 2007	13th February 2008
2007 Annual General Meeting	8th May 2008





Probi AB

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