# AMREST HOLDINGS N.V.

# DIRECTORS' REPORT FOR H1 2006

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# 1. Company Profile

## 1.1. Key Services Provided by the Group

AmRest Holdings N.V. operates KFC restaurants (in Poland, the Czech Republic and Hungary), Pizza Hut restaurants (in Poland and Hungary) and Ice*Land units in Poland. Moreover, two new restaurant chains – FreshPoint and Rodeo Drive – were launched in the first half of 2006. With the new brands, the Company will diversify its services and guarantee customer satisfaction with its broad range of products.

AmRest restaurants feature services like dine-in, take-away, drive-through and home delivery. Our aim is to provide tasty food at competitive prices, while ensuring quality service and a dining experience that is comfortable and friendly. The products offered at AmRest restaurants include proprietary menu items that are prepared from fresh ingredients according to unique recipes and standards of KFC and Pizza Hut chains, as well as on the basis of original concepts (FreshPoint and Rodeo Drive).

The KFC and Pizza Hut brands are franchised to AmRest by Yum! Brands Inc. The other brands, namely Ice*Land and the new FreshPoint and Rodeo Drive, are proprietary brands of AmRest.

### a) KFC

KFC is a quick service restaurant chain operating in Poland, the Czech Republic, and – since July 2006 – in Hungary, offering miscellaneous chicken meals, such as spicy or mild tasting chicken wings, breasts and drumsticks, as well as various fresh seasonal salads, biscuits and desserts, originally cooked corn, and hot and cold beverages. In terms of revenue and number of restaurants, KFC AmRest is one of the largest restaurant chain operators in Central and Eastern Europe.

KFC seeks to strengthen its brand extending its offering by fresh salads. This trend is continued by introducing new menu items that are perceived as prepared from fresh ingredients.

KFC strategy is based on ensuring top quality of products and services while retaining the high cleanliness standards, so that – by following the Customermania programme (seeking to ensure that the customers' expectations are met at the fullest) – a distinctive brand would be developed on the market.

### b) Pizza Hut

Pizza Hut is one of the largest casual dining chains in Central and Eastern Europe, offering a wide range of various dishes in restaurants with waiter service. Pizza Hut serves traditional pan pizzas and Italian thin-crust pizzas, typical for its brand, with a selection of toppings and sauces, as well as different dips, salads – both ready-made and prepared by the customers at salad bars – tortillas, hot and cold starters and sides, cakes and ice-cream desserts, a wide selection of wines, freshly squeezed juices, various types of coffees and other cold and hot drinks.

The Pizza Hut restaurant chain focuses its activities on strengthening the perception of Pizza Hut as a casual dining brand. The extensive renovation plan gave the restaurants a new look, with a new salad bar and a self-service stand for preparing pastas being the main innovations. The changes demonstrate the brand's commitment to serving top quality fresh dishes.

### c) Ice*Land

Ice*Land is a chain of ice-cream bars offering a variety of products and desserts based on multi-flavoured ice cream as well as coffee beverages and cakes. The Ice*Land units are usually situated within KFC or Pizza Hut restaurants, and support their sales by supplementing the range of dishes with desserts. The revenue of this business segment is the highest in the summer months. Some of the Ice*Land sites operate only in summer, and their sales are included in the results of their host restaurants. That is why no separate presentation of the Ice*Land's results is provided.

### d) FreshPoint

FreshPoint is a new chain of small restaurants operating in locations with high pedestrian traffic. The restaurant's menu is based on fresh sandwiches served directly from the oven, to eat in or take out. The staff prepares the sandwiches in front of the customers, who may decide on the selection of ingredients. The menu also includes fresh salads, juices, yoghurts and a choice of beverages.

Currently, there are two FreshPoint restaurants, both located in Warsaw.

### e) Rodeo Drive

The other new concept, Rodeo Drive (American Bar & Grill), is a casual dining restaurant serving meals based mostly on grilled meat and a wide range of beverages. The restaurants will operate in attractive locations and will be able to serve 150–250 customers.


Currently, one Rodeo Drive restaurant is in operation, situated in the main market square in Wrocław.

FreshPoint and Rodeo Drive, AmRest's new dining concepts, are currently in the testing stage. The menu is constantly modified and the customers' opinions are verified. Both concepts have been developed by AmRest, therefore sales in these restaurants are not charged with franchise fees.

## 1.2. Revenue Structure

In the first half of 2006, the sales revenue of the AmRest Group rose by 22.9% (PLN 280m relative to PLN 228m in H1 2005). The majority of AmRest Holdings N.V.'s revenues are generated on the KFC brand, which accounted for 76.0% of the Company's total revenues in H1 2006. In the corresponding period of 2005, the share of KFC in the Company's total revenues stood at 73.8%. Higher sales are related to the chain's good performance and opening of more KFC restaurants than Pizza Hut units.

Table: AmRest Holdings N.V. sales structure by brand

| **BRAND** | **Jan-Jun 2006** | | **Jan-Jun 2005** | |
|---|---|---|---|---|
| | **PLN '000** | **share (%)** | **PLN '000** | **share (%)** |
| **KFC** | 212,710 | 76.0% | 168,125 | 73.8% |
| **PH** | 66,833 | 23.8% | 59,738 | 26.2% |
| **New brands** | 466 | 0.2% | 0 | 0.0% |
| **Total** | **280,009** | **100.0%** | **227,863** | **100.0%** |

Revenue of multi-branded restaurants is divided in the following proportion: 60% – KFC, 40% – PH.

In H1 2006, 71.6% of AmRest Holdings N.V.'s revenues were generated in Poland, compared with 71.7% in the corresponding period of 2005. The Czech Republic's share in the Group's revenue also remained at the same level (slight increase from 28.3% in H1 2005 to 28.4 % in H1 2006). The revenues generated by restaurants acquired in Hungary will contribute to the Company's revenues starting from the third quarter of 2006.

Table: AmRest N.V. sales structure by country

| **COUNTRY** | **Jan-Jun 2006** | | **Jan-Jun 2005** | |
|---|---|---|---|---|
| | PLN '000 | share (%) | PLN '000 | share (%) |
| **Poland** | 200,530 | 71.6% | 163,416 | 71.7% |
| **Czech Republic** | 79,479 | 28.4% | 64,447 | 28.3% |
| **Total** | **280,009** | **100.0%** | **227,863** | **100.0%** |

Revenue of multi-branded restaurants is divided in the following proportion: 60% – KFC, 40% – PH.

## 1.3. Customers

AmRest's products are addressed to a large number of individual customers and are offered through a chain of proprietary restaurants situated mainly in cities or in their vicinity.

The target market for AmRest in Poland and the Czech Republic is 15-39 year olds. Based on the available national statistics, as at the end of 2005 this segment comprised ca. 31% of Poland's and ca. 44% of the Czech Republic's populations. Over 70% of customers of AmRest restaurants in Poland completed at least secondary-level education and over 60% live in cities with a population in excess of 20,000. In the case of customers of AmRest restaurants in the Czech Republic, ca. 41% of them completed at least secondary-level education and over 60% live in cities with a population in excess of 20,000.

The above figures are based on the research carried out in 2005 by SMG/KRC TGI in Poland (January–December 2005) and by MML TGI in the Czech Republic (June–November 2005).

## 1.4. Suppliers

AmRest's strategy for food and packaging purchases assumes ensuring quality and high level of service, as well as being competitive on the market – subject to fulfillment of the first two requirements. The Company has in place a strict programme for approving new suppliers and products, as well as for monitoring the existing suppliers. Such a system ensures that the products supplied to AmRest restaurants meet all the required parameters.

Supplies of food products to the restaurants are coordinated by SCM Sp. z o.o., a company spun off from the AmRest Group in 2005. The strategy of consolidating purchases enables the Group to improve efficiency throughout the whole supply chain and constitutes a competitive advantage in its Central European operations. Today, SCM Sp. z o.o. provides services not only to AmRest, but also to other Yum! franchisees in Central Europe.

AmRest's key supplier is McLane. This company supplies the Polish restaurants with packaging and all food products, excluding chicken, which is supplied directly by producers, and vegetables (in the case of some restaurants). In March 2005, after comparing service prices within Yum!'s European network, a decision was made to extend the agreement with McLane for another two years, until the end of July 2008 (for detailed information see Regulatory Announcement No. 8/2006 of March 24th 2006 concerning an annex to the abovementioned agreement).

## 2. COMPANY'S SHAREHOLDERS

### 2.1. Shareholder Structure

According to the information available to the Company, as at the date of filing the semi-annual report (September 29th 2006), the following shareholders submitted information on holding directly or indirectly (through subsidiaries) at least 5% of the total vote at the General Shareholders Meeting of AmRest Holdings N.V.

Table: Shareholder structure of AmRest Holdings N.V.

| Shareholder | No. of shares | % of share capital held | No. of votes at GM | % of the total vote at GM |
|---|---|---|---|---|
| IRI LLC * | 5,068,000 | 37.54% | 5,068,000 | 37.54% |
| BZ WBK AIB AM ** | 1,396,179 | 10.34% | 1,396,179 | 10.34% |
| ING Nationale – Nederlanden Polska OFE | 838,046 | 6.21% | 838,046 | 6.21% |
| ING TFI S.A. | 706,227 | 5.23% | 706,227 | 5.23% |
| AIG OFE | 698,535 | 5.17% | 698,535 | 5.17% |
| BZ WBK AIB TFI | 688,231 | 5.10% | 688,231 | 5.10% |

* IRI LLC is wholly-owned by ARC.

** BZ WBK AIB AM manages assets including funds controlled by BZ WBK AIB TBI.

### 2.2. Changes in the Shareholder Structure

Set forth below is a summary of material changes in the Company's shareholder structure that have taken place since the beginning of 2006.

On January 18th 2006, International Restaurants Investments LLC, the main shareholder in AmRest Holdings N.V., reduced its holding by 45,000 shares and held 5,338,000 shares representing 39.54% of the Company's share capital and conferring the right to 5,338,000 votes at the General Shareholders Meeting, i.e. 39.54% of the total vote.

Prior to the change, IRI held 5,383,000 shares representing 39.87% of the Company's share capital and conferring the right to 5,383,000 votes at the General Shareholders Meeting, i.e. 39.87% of the total vote.

On March 6th 2006, investment funds managed by ING Towarzystwo Funduszy Inwestycyjnych S.A. acquired shares in AmRest Holdings N.V., thereby increasing their aggregate shareholding to 706,227 shares, representing 5.23% of the Company's share capital and conferring the right to a total of 706,227 votes at the General Shareholders Meeting, i.e. 5.23% of the total vote. Prior to the change, the investment funds managed by ING TFI S.A. held, in aggregate, 641,227 shares in AmRest Holdings N.V., representing 4.75% of the Company's share capital and conferring the right to a total of 641,227 votes at the General Shareholders Meeting, i.e. 4.75% of the total vote.

As a result of share acquisition settled on March 16th 2006, customers of BZ WBK AIB Asset Management S.A. became owners, in aggregate, of 724,911 shares in AmRest Holdings N.V., representing 5.37% of the Company's share capital and conferring the right to a total of 724,911 votes at the General Shareholders Meeting, i.e. 5.37% of the total vote. Prior to the change, the customers of BZ WBK AIB Asset Management S.A. held, in aggregate, 674,911 shares in AmRest Holdings N.V., representing 4.999% of the Company's share capital and conferring the right to a total of 674,911 votes at the General Shareholders Meeting, i.e. 4.999% of the total vote.

On April 4th 2006, as a result of acquisition of shares, AIG Otwarty Fundusz Emerytalny became the owner of 698,535 shares in AmRest Holdings N.V., representing 5.17% of the Company's share capital and conferring the right to 698,535 votes at the General Shareholders Meeting, i.e. 5.17% of the total vote. Prior to the change, AIG OFE held 625,397 shares in AmRest Holdings N.V., representing 4.63% of the Company's share capital and conferring the right to 625,397 votes at the General Shareholders Meeting (4.63% of the total vote).

As at April 5th 2006, PZU Asset Management S.A.'s holding in the share capital of AmRest Holdings N.V. fell under 5% as a result of disposal of the Company shares held in portfolios of PZU AM customers. As a consequence, the share of PZU AM in the total vote at the Company's General Shareholders Meeting also fell under 5%. Prior to the change, securities portfolios managed by PZU AM contained, in aggregate, 676,618 shares in the Company, representing 5.01% of the share capital and conferring the right to 676,618 votes at the General Shareholders Meeting of the Company, i.e. 5.01% of the total vote.

On July 12th 2006, the funds managed by BZ WBK AIB TFI S.A. came to hold 688,231 shares in AmRest, representing 5.10% of the Company's share capital and conferring the right to 688,231 votes at the General Shareholders Meeting of the Company (5.10% of the total vote). Prior to the change, the funds managed by BZ WBK AIB TFI held 635,537 shares in AmRest, representing 4.71% of the Company's share capital and conferring the right to a total of 635,537 votes at the General Shareholders Meeting of the Company (4.71% of the total vote). BZ WBK AIB TFI commissioned BZ WBK AIB Asset Management S.A., pursuant to Art. 46.1.1 of the Act on Investment Funds of May 27th 2004, to manage the investment portfolios of the investment funds controlled by BZ WBK AIB TFI. Consequently, BZ WBK AIB AM's notification on having exceeded 5% of the total vote in AmRest on March 16th 2006 also concerned AmRest shares held by the funds controlled by BZ WBK AIB TFI.

On August 23rd 2006, as a result of disposal of 270,000 shares in AmRest Holdings N.V., IRI LLC reduced its holding to 5,068,000 shares, representing 37.54% of the Company's share capital and conferring the right to a total of 5,068,000 votes at the General Shareholders Meeting, i.e. 37.54% of the total vote. Prior to the change, IRI held 5,338,000 shares in AmRest, representing 39.54% of the share capital and conferring the right to a total of 5,338,000 votes (54% of the total vote) at the General Shareholders Meeting.

On September 6th 2006, customers of BZ WBK AIB Asset Management S.A. acquired shares in AmRest Holdings N.V. and came to hold, in aggregate, 1,396,179 shares representing 10.34% of the Company's share capital and conferring the right to a total of 1,396,179 votes at the General Shareholders Meeting of the Company, i.e. 10.34% of the total vote. Prior to the change in the holding, the customers of BZ WBK AIB Asset Management S.A. held, in aggregate, 1,345,056 shares in AmRest Holdings N.V., representing 9.96% of the Company's share capital and conferring the right to a total of 1,345,056 votes (9.96% of the total vote) at the General Shareholders Meeting of the Company. BZ WBK AIB Asset Management S.A.'s notification read as follows "(…) over 12 months from the date of the notification the equity holdings of BZ WBK AIB Asset Management S.A. customers in AmRest Holdings N.V. may increase or decrease. Decisions on acquisition or disposal of shares in the company will depend on its standing, assessment of the standing, and on market conditions. The decision on acquisition or disposal of shares in AmRest Holdings N.V. will also be influenced by the value of assets managed by BZ WBK AIB Asset Management S.A. Acquisitions of shares in AmRest Holdings N.V. by BZ WBK AIB Asset Management S.A. on behalf of its customers are made exclusively to ensure growth in the value of the customers' investment as a result of realising the fundamental value of the shares."

# 3. COMPANY'S MANAGEMENT AND SUPERVISORY BOARD

The composition of the Management and Supervisory Boards of AmRest Holdings N.V. is presented below.

## a) Management Board

Composition of the Company's Management Board is as follows:

Henry McGovern

Wojciech Mroczyński

## b) Supervisory Board

Composition of the Company's Supervisory Board is as follows:

Christian Richard Eisenbeiss,

Donald Macintosh Kendall Sr.,

Donald Macintosh Kendall Jr.,

Przemysław Schmidt,

Jan Sykora, and

Per Steen Breimyr.

## 4. ORGANISATION OF THE GROUP

The current composition of the AmRest Group is presented in Note 1a to the Financial Statements as at June 30th 2006 and for the six months ended on that day. The changes which took place in the composition of the Group in this period are presented below.

On February 3rd 2006, the subsidiary company American Restaurants Sp. z o.o. acquired 10% of shares in SCM Sp. z o.o., and thus increased its interest in SCM Sp. z o.o. to 45%. SCM provides American Restaurants Sp. z o.o. with services consisting in intermediation and negotiation of the terms of product supplies to the restaurants, including negotiation of the terms and conditions of distribution agreements.

On June 30th 2006, American Restaurants Sp. z o.o., subsidiary of AmRest, acquired from Central European Franchise Group, Ltd. 100% of shares in Kentucky System, Kft of Budapest. Upon the acquisition, AmRest became the owner of 13 Pizza Hut restaurants and 4 KFC restaurants in Hungary. In September 2006, the company's name was changed to American Restaurants, Kft.

The Group has offices in Wrocław, Poland, and operates restaurants in Poland, the Czech Republic and Hungary.

# 5. COMPANY'S FINANCIAL STANDING AND ASSETS

## 5.1. Assessment of the Company's Performance and the Balance Sheet Structure

Table: Financial highlights (H1 2004–2006)

| PLN '000, unless stated otherwise | H1 2006 | H1 2005 | H1 2004 |
|---|---|---|---|
| Sales revenue | 280,009 | 227,863 | 226,808 |
| EBITDA* | 39,359 | 26,198 | 23,344 |
| *EBITDA margin* | 14.1% | 11.5% | 10.3% |
| Operating profit/(loss)* | 18,412 | 10,533 | 7,808 |
| *Operating margin (EBIT margin)* | 6.6% | 4.6% | 3.4% |
| Pre-tax profit/(loss)* | 22,082 | 6,457 | 1,062 |
| *Pre-tax margin* | 7.9% | 2.8% | 0.5% |
| Net profit/(loss)* | 18,951 | 9,891 | (284) |
| *Net margin* | 6.8% | 4.3% | (0.1%) |
| Equity | 139,473 | 107,910 | 9,533 |
| *Return on equity (ROE)* | 14% | 16% | (3%) |
| Balance-sheet total | 299,649 | 244,642 | 218,797 |
| *Return on assets (ROA)* | 6% | 4% | (0%) |

* *For 2004-2005, the profit is calculated without the one-off IPO-related expenses.*

*Definitions:*

- *EBIDTA margin: EBITDA (earnings before interest, tax, depreciation and amortisation) to sales revenue;*
- *Operating margin: operating profit to sales revenue;*
- *Pre-tax margin: pre-tax profit to sales revenue;*
- *Net margin: net profit to sales revenue;*
- *Return on equity (ROE): net profit to average equity;*
- *Return on assets (ROA): net profit to average assets.*

## Table: Liquidity (H1 2004–2006)

| PLN '000, unless stated otherwise | H1 2006 | H1 2005 | H1 2004 |
|---|---|---|---|
| Current assets | 46,295 | 42255 | 36,716 |
| Inventories | 7,416 | 5635 | 5,443 |
| Current liabilities | 74,296 | 64954 | 183,554 |
| *Quick ratio* | *0.52* | *0.56* | *0.17* |
| *Current ratio* | *0.62* | *0.65* | *0.20* |
| Cash and cash equivalents | 20,613 | 18628 | 11,433 |
| *Cash ratio* | *0.28* | *0.29* | *0.06* |
| *Inventory cycle (days)* | *4.36* | *4.59* | *4.77* |
| Trade receivables | 9,481 | 13069 | 11,345 |
| *Average collection period (days)* | *7.48* | *8.46* | *9.65* |
| *Average operating cycle (days)* | *11.84* | *13.05* | *14.42* |
| Trade payables | 64,871 | 50958 | 57,985 |
| *Average payment period (days)* | *39.03* | *40.74* | *46.11* |
| *Cash conversion ratio (days)* | *(27.19)* | *(27.68)* | *(31.68)* |

*Definitions:*

- *Quick ratio: current assets less inventories to current liabilities;*
- *Current ratio: current assets to current liabilities;*
- *Cash ratio: cash and cash equivalents to current liabilities as at the end of the period;*
- *Inventory cycle (days) – average inventories to sales revenue, times the number of days in the period;*
- *Average collection period (days) – average trade receivables to sales revenue, times the number of days in the period;*
- *Average operating cycle (days) – sum of the inventory cycle and the average collection period;*
- *Average payment period (days) – average trade payables to sales revenue, times the number of days in the period;*
- *Cash conversion ratio – difference between the operating cycle and trade payables.*

Table: Debt (H1 2004–2006)

| PLN '000, unless stated otherwise | H1 2006 | H1 2005 | H1 2004 |
|---|---|---|---|
| Current assets | 46,295 | 42,255 | 36,716 |
| Non-current assets | 253,354 | 202,387 | 182,081 |
| Trade receivables | 9,481 | 13,069 | 11,345 |
| Liabilities | 160,176 | 136,732 | 209,031 |
| Non-current liabilities | 85,880 | 71,778 | 25,477 |
| *Inventories to current assets (%)* | *16.02%* | *13.34%* | *14.82%* |
| *Trade receivables to current assets (%)* | *20.48%* | *30.93%* | *30.90%* |
| *Cash and cash equivalents to current assets (%)* | *44.53%* | *44.08%* | *31.14%* |
| *Equity to non-current assets* | *0.55x* | *0.53x* | *0.05x* |
| *Debt ratio* | *0.53x* | *0.56x* | *0.96x* |
| *Long-term debt ratio* | *0.62x* | *0.67x* | *2.67x* |
| *Liabilities to equity* | *1.1x* | *1.3x* | *21.9x* |

*Definitions:*

- *Inventories, trade receivables, cash and cash equivalents to current assets: inventories, trade receivables, cash and cash equivalents, respectively, to current assets;*
- *Equity to non-current asset ratio: equity to non-current assets;*
- *Debt ratio: total liabilities and provisions for liabilities to assets;*
- *Long-term debt ratio: non-current liabilities to equity;*
- *Liabilities to equity: liabilities and provisions for liabilities as at the end of the period to equity.*

In H1 2006, AmRest Holdings N.V. reported sales of PLN 280,009 thousand, up by 22.9% compared with the corresponding period of 2005. The increase in sales was due to the opening of new restaurants and a consistent growth in sales at the existing restaurants. The increase in sales was not affected by the acquisition of restaurants in Hungary as the revenue generated by those restaurants will be included in the Group's results as of beginning of the third quarter of 2006.

The gross profit on sales increased by 17.4% in comparison with the corresponding period of 2005 and amounted to PLN 34,243 thousand. In the first half of 2006, the increase in restaurant costs was slightly higher than the growth in sales. Therefore, the gross margin on sales amounted to 12.2% (12.8% in the first quarter of 2005).

The overall performance was primarily affected by higher labour costs and depreciation and amortisation costs (relative to sales). The first factor, a relative increase in costs of salaries and wages and employee benefits is connected with general trends observed on the labour markets in Poland and the Czech Republic. The second factor, a relative increase in depreciation and amortisation costs, is primarily connected with a higher number of restaurants in operation. Depreciation and amortisation costs were also higher due to larger write-offs made in connection with planned refurbishment of several restaurants.

The operating profit rose to PLN 18,412 thousand (up by 114.2% on the H1 2005 figure) and EBITDA for the first half of 2006 amounted to PLN 39,359 thousand (increase by 50.2% on the corresponding period of 2005). The operating margin was 6.6% (3.8% in the corresponding period of 2005) and the EBITDA margin reached 14.1% (11.5% in H1 2005).

The above results were primarily driven by a drop in general and administrative expenses (down by 7.6% on the corresponding period of 2005). Another factor with a significant impact on the results was the gain on disposal of non-financial non-current assets related to the sale of real property in Q2 2006. The H1 2005 results were affected by one-off costs of the IPO (PLN 1,937 thousand)

The net profit rose to PLN 18,951 thousand (up by 138.3% on the corresponding period of 2005), and the net margin increased from 3.5% to 6.8%.

A positive factor that contributed to the net profit recorded by the Company was the debt waiver described in the Report for Q2 2006, which increased the financial income by PLN 3,396 thousand. Another factor which boosted the Company's result on financing activities were translation differences on valuation of loans granted by AmRest Holdings N.V. to its subsidiary American Restaurants s.r.o. The translation differences disclosed in the profit and loss account for H1 2006 amounted to PLN 2,027 thousand.

In the first half of 2006, the financial liquidity of the AmRest Group remained similar to the H1 2005 figure. As at the end of the first quarter of 2006, the quick and current ratios were 0.52 and 0.62, respectively. The cash ratio amounted to 0.28 (vs. 0.29 as at the end of H1 2005).

Despite the rising sales and the growing number of restaurants, the Group managed – by optimising the supply chain management – to maintain its inventories approximately on par with the 2005 mid-year balance. The inventory cycle remained similar to that observed in H1 2005 and lasted 4.4 days. Due to a slight shortening of the average collection period and the average payment period (7.5 days and 39.0 days, respectively), AmRest is able to continue to finance much of its current operations with negative working capital. The further decrease in the average payment period (relative to the previous years) is a result of AmRest's better financial liquidity.

The AmRest Group's liquidity has remained at the same level. Given the nature of the restaurant business, the present liquidity ratios ensure the Group's disruption-free operations. The available free cash flow permits the Group to settle existing liabilities and to finance, in a balanced manner, its capex plans.

The debt of AmRest fell slightly in comparison with the 2005 mid-year figure – the debt to equity ratio fell to 1.1 (from 1.3), and the debt ratio decreased to 0.53 (from 0.56). The balance-sheet total as at the end of H1 2006 stood at PLN 299,649 thousand (up by 22.5% on the H1 2005 figure).

## 5.2. Loans Contracted within the Group

As at June 30th 2006, the following unused credit facilities were available to the AmRest Group:

a) ABN Amro Bank - PLN 29,342 thousand (PLN/CZK revolving loan)
b) ABN Amro Bank - PLN 1,502 thousand (CZK current account loan)
c) ABN Amro Bank - PLN 7,700 (PLN current account loan)
d) Bank BPH - PLN 142 thousand (PLN current account loan).

## 5.3. Key Domestic and Foreign Investments

The table below presents acquisitions of non-current assets in H1 2006 and comparable data for H1 2005.

Table: Acquisitions of non-current assets by AmRest Holdings N.V.

| thousand PLN | | Jun 30 2006 | Jun 30 2005 |
|---|---|---|---|
| Intangible assets, including: | | | |
| | Licences to use the Pizza Hut and KFC trademarks | 381 | 119 |
| | Trademark | - | 1,000 |
| | Favourable lease agreements | - | 1,731 |
| | Goodwill | 18,666 | - |
| | Other intangible assets | 817 | 261 |
| Property, plant and equipment, including: | | | |
| | Ground | - | - |
| | Buildings | 4,895 | 2,731 |
| | Restaurant equipment | 6,270 | 4,645 |
| | Vehicles | 113 | - |
| | Other, including: property, plant and equipment under construction | 14,191 | 14,314 |
| **Total** | | **45,333** | **24,801** |

Capital expenditure incurred by AmRest is primarily connected with the opening of new restaurants, and with reconstruction and replacement of assets in the existing restaurants. In the first half of 2006, capital expenditure was also affected by the acquisition of 100% of shares in Kentucky System Kft. The Company's capital expenditure depends primarily on the number and type of the newly-opened restaurants.

Table: Number of restaurants of AmRest Holdings N.V. (2003–2006)

| As at | Sep 29 2006 | Dec 31 2005 | Dec 31 2004 | Dec 31 2003 |
|---|---|---|---|---|
| **Number of restaurants** | | | | |
| Pizza Hut in Poland | 52 | 52 | 55 | 57 |
| Pizza Hut in the Czech Republic | 0 | 0 | 1 | 1 |
| Pizza Hut in Hungary | 13 | 0 | 0 | 0 |
| KFC in Poland | 79 | 76 | 71 | 67 |
| KFC in the Czech Republic | 44 | 41 | 30 | 23 |
| KFC in Hungary | 4 | 0 | 0 | 0 |
| FreshPoint in Poland | 2 | 0 | 0 | 0 |
| Rodeo Drive in Poland | 1 | 0 | 0 | 0 |
| **Total** | **195** | **169** | **157** | **148** |
| Total opened restaurants | 29 | 25 | 13 | 9 |
| Total closed restaurants | 3 | 13 | 4 | 0 |
| **Net increase in the number of restaurants in the reporting period** | **26** | **12** | **9** | **9** |

Since the beginning of 2006, the total number of restaurants rose by 26, mainly as a result of the acquisition of restaurants in Hungary. In Poland, AmRest opened three new KFC restaurants and two new Pizza Hut restaurants, as well as the first restaurants of its new chains: two FreshPoint restaurants and one Rodeo Drive restaurant. In the same period, three KFC restaurants were opened in the Czech Republic. In Hungary, since the takeover, one KFC restaurant was opened and one Pizza Hut restaurant was closed. Since the beginning of the year, a total three restaurants have been closed.

## 5.4. Major Events With a Significant Bearing on the Company's Operations and Financial Results

a) In January 2006, the Management Board of Amrest Holding N.V. was notified of the completion of registration of Amrest Ukraina t.o.w. of Kiev, Ukraine. AmRest Holdings N.V. holds, through its subsidiary American Restaurants Sp. z o.o., 100% of shares in the newly-established company. Amrest Ukraina t.o.w.'s share capital amounts to UAH 252,500. The company was established in order to supervise investments and operate restaurants in Ukraine.

b) On March 23rd 2006, an annex was executed to the Distribution Agreement of April 2nd 2003 concluded between American Restaurants Sp. z o.o. and McLane Polska Sp. z o.o. of Błonie. The annex, effective as of August 1st 2006, extends the term of the Distribution Agreement and changes the amounts of the minimum guaranteed quantity of AmRest's purchases from the Distributor, the Distribution Fee (and frequency of its calculation) and the Distribution Fee for export sales (to external franchisees). Detailed terms of the Annex are presented in Regulatory Announcement No. 8/2006 of March 24th 2006.

c) In mid-March 2006, the first FreshPoint restaurant was opened in Warsaw. Currently, two FreshPoint restaurants are in operation (both situated in Warsaw).

d) In April 2006, the first Rodeo Drive (American Bar & Grill) restaurant was opened in Wrocław.

e) April 1st 2006 was the effective date of debt waiver, based on signed debt waiver agreements received on August 4th 2006 from the shareholder International Restaurants Investments, LLC ("IRI"). The agreements cover loans advanced in preceding years for a total of USD 818 thousand and EUR 38 thousand along with accrued interest. These amounts also include long-term loans granted by Yum!. As of April 1st 2006, Yum! transferred its receivables under these loans onto IRI. The debt waiver increased the Company's financial income, which had a positive effect on the net profit recorded by the Company in the second quarter of 2006 and the whole of the first half of 2006.

f) On April 19th 2006, AmRest Holdings N.V. and Talus Limited concluded a Partnership Agreement whereby the parties agreed to establish a company whose business objective would be to open and operate restaurants in Ukraine. Talus Limited is a subsidiary of Kazyrna Karta ("Royal Card"), the largest restaurant company in Ukraine, which has been in operation since 1988 and currently manages over 70 restaurants countrywide. AmRest Holdings N.V. will acquire 51% of shares and 51% of the total vote in the newly establish company, with Talus Limited holding the remaining 49%. The parties agreed to contribute to the company, in appropriate proportions, an initial share capital of USD 2m. The Partnership Agreement will become effective upon fulfilment of certain conditions, the most important of which is obtaining the approval of the Supervisory Board by AmRest Holdings N.V. and approval from YUM Restaurants International LLC, the franchisor of Pizza Hut and KFC brands, by Talus Limited.

g) The Annual General Shareholders Meeting of AmRest Holdings N.V. was held on May 22nd 2006. The only shareholder with 5% or more of the total vote at the general meeting was International Restaurant Investments LLC, with 5,338,000 votes, which represented 100.00% of votes at that meeting and which represent 39.54% of the total vote. The Annual General Shareholders Meeting considered all the items included in the agenda and adopted resolutions concerning *inter alia*: approval of the financial statements for the financial year 2005, allocation of the 2005 profit to cover retained deficit, and approval of performance of duties by Members of the Supervisory Board and the Management Board of AmRest. Moreover, the Annual General Shareholders Meeting approved the employee stock option plan and authorised the Management Board to increase AmRest's share capital. The text of all the resolutions adopted at the Meeting is presented in an Appendix to Regulatory Announcement No. 19/2006 of May 22nd 2006.

h) On June 30th 2006, American Restaurants Sp. z o.o. (the Buyer), wholly-owned subsidiary of AmRest, and Central European Franchise Group, Ltd (the seller) concluded an agreement whereby American Restaurants acquired 100% of shares in Kentucky System Kft. of Budapest (in September 2006, the company's name was changed to American Restaurants, Kft). The selling price was USD 6.5m. Following the purchase of all shares in Kentucky System, AmRest came to own 13 Pizza Hut restaurants and four KFC restaurants in Hungary. The execution of the agreement represents an important step towards the implementation of the AmRest Group's strategy aimed at strengthening its market position in Central and Eastern Europe. The acquisition of restaurants in Hungary provides an opportunity for further expansion through the development of existing and new restaurant chains on the Hungarian market.

i) Three cases brought against IFFP by DOMONT Stefan Pastryk Anna Pastryk spółka jawna are pending before the Regional Court of Warsaw, XVI Commercial Division. The claims concern the payment of amounts due under notes issued by IFFP to DOMONT Stefan Pastryk Anna Pastryk spółka jawna for a total amount of PLN 3,867,000.

DOMONT's claims concern the payment for construction works that had been performed by DOMONT for IFFP before November 2000, i.e. before American Restaurants Sp. z o.o. acquired shares in IFFP. According to the Management Board of IFFP, the claims are groundless, as they are not justified by the balance of settlements between IFFP and DOMONT. According to the documents disclosed, DOMONT does not have the right to claim the payment of the disputed amount. The Court has not commenced examination of the facts of the case yet.

It should be noted that IFFP does not carry out operating activities and is not an entity material for the operations of the Company and its Group.

### 5.5. Other Factors and Extraordinary Events with a Material Impact on the Group's Performance

a) The financial results of AmRest's Czech operations expressed in the Polish złoty are affected by changes in the currency exchange rates used for currency translations. The appreciation of the Czech crown against the złoty, which took place in the first half of 2006, had a positive effect on the results of the Czech operations disclosed in the financial statements.

b) As at the end of the first half of 2006, the CZK/PLN exchange rate was higher by 5.7% as compared with the end of the corresponding period of 2005, while the H1 2006 average exchange rate increased by 0.6% on the H1 2005 average rate.

### 5.6. Assessment of the Feasibility of Investment Plans, Including Equity Investments

AmRest will focus on the development of existing restaurant chains on the existing markets. The Company also considers further development through introduction of new brands and expansion on new markets. By the end of the year, AmRest intends to finish the integration process of its Hungarian business, preparing the foundations to develop on this market in the years to come.

AmRest continues to carry out the plan of modernisation of selected Pizza Hut and KFC restaurants and is opening new restaurants. The Management Board of AmRest is planning to open additionally a total of approximately 15 new restaurants by the end of 2006. This number includes 7-8 FreshPoint restaurants and 1-2 Rodeo Drive restaurants.

The Management Board of AmRest is further assessing the potential of the Ukrainian market. The Company does not plan any restaurant launch on this market by the end of 2006.

It should be added that the plan of opening new restaurants will be adjusted on an on-going basis to reflect prevailing market conditions and the possibilities of finding new attractive locations in specific countries.

The Management Board predicts that the growth (investments) will be financed with the Company's own funds (operating cash flows) and debt financing.

# 6. AMREST HOLDINGS N.V. IN THE SECOND HALF OF 2006

## 6.1. Internal and External Factors Material to the Development of the Company's Business in H2 2006

In the opinion of the Management Board of AmRest, the following factors will have a material impact on the Company's development and performance in the future:

**a) External factors:**

- competitiveness in terms of prices, service and food quality, as well as location;
- demographic changes, tendencies concerning the number and profile of the restaurants' customers as well as the number and location of the competition's restaurants;
- amendments to laws and regulations, directly affecting the functioning of the restaurants and their employees;
- changes in the occupancy costs (lease of property) and related costs;
- changes in prices of the ingredients used in preparing meals and changes in prices of packaging materials;
- changes in the overall economic conditions in Poland, the Czech Republic and Hungary as well as consumers' confidence, the level of disposable incomes and individual spending patterns.

**b) Internal factors:**

- recruiting and training employees needed to develop the existing and new restaurant chains;
- acquiring attractive locations;
- success in launching new restaurant chains and new products;
- developing an integrated IT system.

## 6.2. Key Risk and Threats to the Company

### a) Factors Outside of the Company's Control

There are a number of factors outside of the Company's control which affect AmRest's development strategy, based on launching new restaurants. These factors include: the ability to identify and secure suitable restaurant locations which the Company is able to acquire, the ability to obtain the required authorisations in due time, and possible delays in launching new restaurants.

### b) Dependence on the Franchisor

AmRest manages KFC and Pizza Hut restaurants as a franchisee. Therefore, numerous factors and decisions made in connection with AmRest's operations are determined by the limitations and specifications imposed by the franchisor and depend on its approval.

The term of each Franchise Agreement (the first of which commenced in 2000) is ten years. AmRest has an option to extend the term by another ten years, provided that it complies with the terms and conditions of the agreement and other requirements, including the requirement to pay an extension fee. Notwithstanding the fulfilment of the above-mentioned conditions, there can be no assurance that after the first two terms have expired a given Franchise Agreement is prolonged for another term.

### c) Lack of Exclusivity Rights

The Franchise Agreements do not provide AmRest with any exclusivity rights in a given territory, protection or any other rights in the territory, region or market where the AmRest restaurants operate.

According to previous arrangements, the Development Agreement of September 25th 2003 concluded between the franchisor and YUM!'s subsidiaries, KFC International Holdings ("KFCIH") and Pizza Hut International, LLC ("PHILLC"), expired on December 31st 2005. Under the Agreement, the Company was granted the right and was obliged to construct and develop new KFC and Pizza Hut restaurants in Poland and the Czech Republic. Subject to compliance with the Agreement's terms and conditions, the Company had the right of first refusal in relation to any new KFC or Pizza Hut restaurant in Poland and the Czech Republic proposed to be developed by the franchisor or in respect of which the franchisor proposed to grant franchise rights.

In line with the current YUM!'s policy, which does not envisage concluding such agreements in relation to stable markets such as Poland and the Czech Republic, the parties agreed that it is not necessary to execute a new agreement. YUM! undertook to inform the Company of concluding an agreement with another franchisee no later than six months before launching the franchisee's first KFC or Pizza Hut restaurant in Poland or the Czech Republic. During this period, the Company has the right to express its opinion on the matter. YUM! has stated that presently it has no intention to conclude agreements with other potential franchisees in Poland or the Czech Republic or to launch new restaurants itself.

### d) Lease Agreements and Their Extension

Nearly all AmRest restaurants use leased premises. The majority of lease agreements are long-term agreements, concluded for at least a ten-year period beginning on the lease commencement date (assuming that all extension options are exercised on specified terms, and excluding those agreements which are renewed periodically unless terminated, and agreements concluded for an indefinite term). Under a number of lease agreements, AmRest holds the right to extend the term of the agreement, providing that the Company complies with the terms and conditions of the lease. Notwithstanding the fulfilment of such terms and conditions, there can be no assurance that AmRest will be able to extend the lease agreements on commercially reasonable terms. If there is no such possibility, the potential loss of key restaurant locations may have an adverse effect on AmRest's performance and operations.

Furthermore, under certain circumstances, AmRest may decide to close down a given restaurant, and the termination of the respective lease agreement on cost-effective terms may prove impossible. Such a situation may adversely affect the Company's performance and operations. Closing down of any restaurant requires the franchisor's approval, and there can be no assurance that such an approval will be obtained.

## e) AmRest's Status of a Foreign Entity

The Company is a joint-stock company incorporated under the Dutch laws, therefore its internal relations are also subject to these laws. Polish investors should be aware that rights of shareholders attached to the Company shares are subject to Dutch laws and that there are numerous differences between the provisions of Dutch companies law and the Polish Companies Act. Lack of knowledge of Dutch regulations may impede exercising of rights attached to shares by Polish investors. Additionally, given the location of the Company's registered office, investors intending to lodge claims against AmRest may encounter difficulties relating to service of process and settling the dispute.

## f) Health Concerns Relating to the Consumption of Food Products

Health concerns relating to chicken meat, which is the main ingredient of the KFC meals, may affect consumers' preferences. Consumers' preferences may also change as a result of dissemination by mass media of any adverse information about the quality of products, diseases caused by them and any other types of damage suffered because of dining at AmRest's or other KFC and Pizza Hut franchisees' restaurants, or publication by the government or market segment analysts of unfavourable reports on products offered in these restaurants, on health issues and the manner of functioning of any one or more restaurants operated either by AmRest or its competitors. The Company mitigates this risk by using at the AmRest restaurants ingredients of the highest quality, sourced from proven and reputed suppliers, by complying with strict quality control and hygiene standards, and by applying the most advanced equipment and processes ensuring absolute safety of the meals.

## g) Higher Food Prices

A significant portion of food products supplied to AmRest restaurants is grown in Poland. Therefore the extremely dry weather which affected Poland in 2006 may have a negative impact on the costs of food products. This in turn may have a direct influence on the Company's profitability. However, the risk is to a large extent mitigated by entering into long-term agreements with suppliers.

## h) Restrictions Imposed by Lenders

On April 4th 2005, AmRest Holdings N.V., American Restaurants Sp. z o.o. and American Restaurants s.r.o. (the Obligors) entered into a credit facility agreement of PLN 110m.

Under the credit facility agreement, each of the Obligors has covenanted to observe certain restrictions on their ability to borrow money, incur capital expenditure, grant security and dispose of assets, and has also covenanted to comply with certain financial ratio tests. It is possible that these covenants could materially impair AmRest's ability to run its business in the future and any failure to comply with the covenants could cause an acceleration of loans granted under the facility, which in turn could have a material adverse affect on the financial condition and results of operations of AmRest.

### i) Risks Related to the Launch of New Brands

In line with its development plan, in 2006 AmRest launched two new dining concepts, Rodeo Drive and FreshPoint. Because these dining concepts are completely new to the Company, there is a risk related to the level of demand and the reception of the products by consumers.

### j) Risk Related to the Opening of a Restaurant in Ukraine

It will be the first restaurant in a new geographical and geopolitical region. The investment entails the risks that the consumer preferences in Ukraine may be different and that the Company may lack adequate knowledge of the market. The Company is also exposed to the regulatory risk related to local regulations.

## 6.3. The Company's Development Directions and Strategy

AmRest's strategy assumes developing and operating large-scale branded restaurant concepts with the projected rate of return exceeding 20% (IRR). The Company's objective is to become the leading restaurant operator in Central and Eastern Europe.

AmRest intends to expand its activities in two restaurant market segments (Quick Service Restaurants and Casual Dining) in Poland, the Czech Republic and Hungary. The Company intends to continue its expansion in other countries and expects that the markets of Central and Eastern Europe will remain its principal region of investments.

In the near future, AmRest will focus on the development of the Hungarian market, boosting sales at existing restaurants, extension of existing restaurant chains, and introduction of new restaurant brands in the abovementioned segments on the market.

AmRest intends to continue to improve profitability at the restaurant level and increase the Company's operational efficiency. Concurrently, the Company expects that the introduction of new restaurant concepts will entail considerable costs related to their launch and the creation of organisational structure necessary for their development. AmRest expects that those factors may negatively affect the Group's profitability in a short term. An important contribution to the Group's development will be the integration and upgrading of IT systems, to be completed by the end of 2008.

AmRest is committed to continuing the efforts aimed at increasing the customer value. Through further improvement of the customer service, serving tasty dishes made with fresh ingredients, and introducing new products, the Company intends to raise its customers' awareness of the excellent value for money offered by the AmRest restaurants.

# 7. STATEMENT OF THE MANAGEMENT BOARD

## 7.1. True and Fair View Presented in the Financial Statements

To the best knowledge of the Management Board of AmRest Holdings N.V., the semi-annual financial statements and the comparable data presented in the semi-annual financial statements of the AmRest Group were prepared in accordance with the applicable accounting standards and give a true and fair view of the assets, financial standing and financial results of the AmRest Group. This semi-annual Directors' Report gives a true view of the developments, achievements and the situation of the AmRest Group, including the description of key risks and threats.

## 7.2. Appointment of the Entity Qualified to Audit Financial Statements

PricewaterhouseCoopers Sp. z o.o., the entity qualified to audit financial statements which has reviewed the semi-annual consolidated financial statements of the AmRest Group, was appointed in accordance with the applicable laws. The entity and the auditors performing the review met the conditions necessary to issue an impartial and independent opinion on the review in accordance with the applicable laws.

Wrocław, September 22nd 2006

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|---|---|
| Henry McGovern | Wojciech Mroczyński |
| AmRest Holdings N.V. | AmRest Holdings N.V. |
| Member of the Management Board | Member of the Management Board |