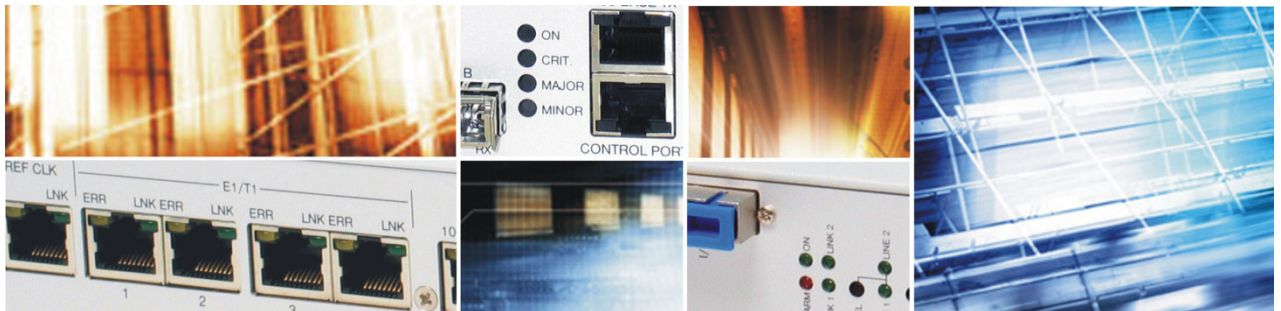




Updated Annual Report 2006

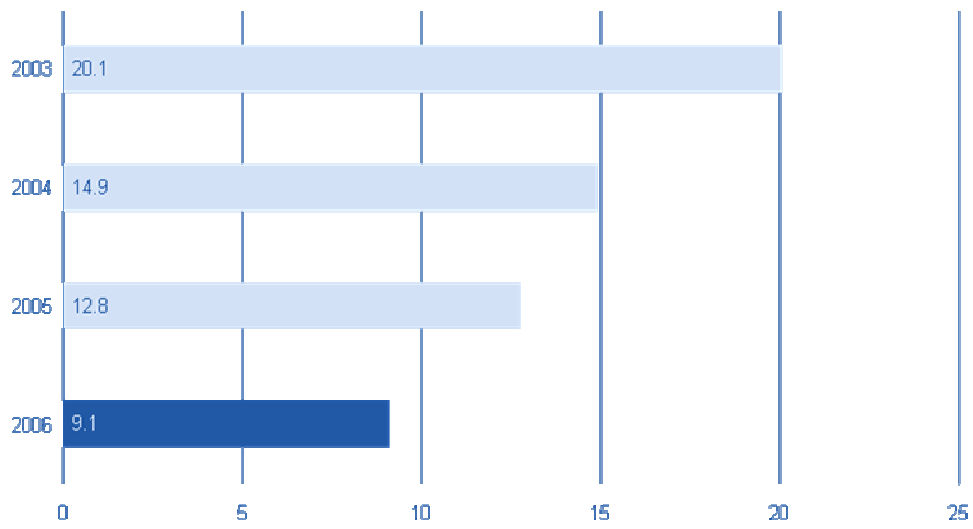


At a Glance

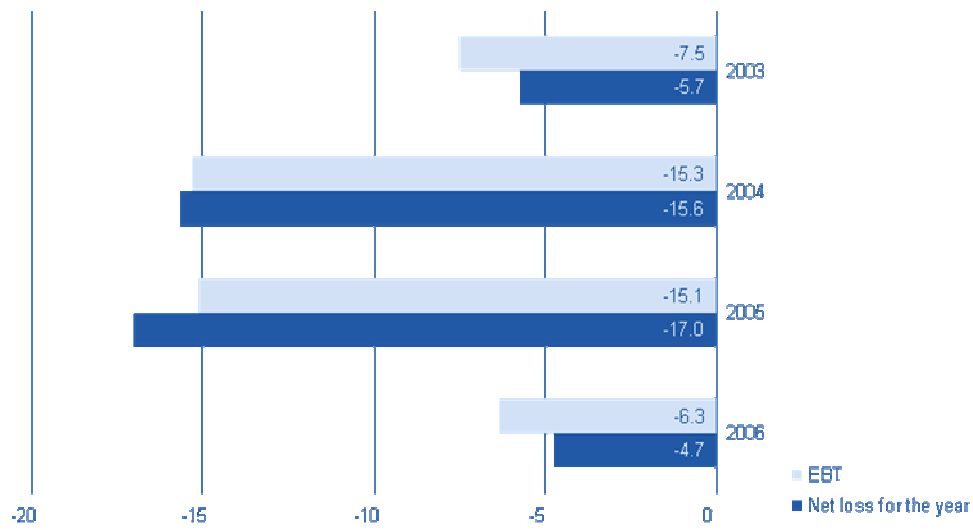
PANDATEL Group	US GAAP	US GAAP	US GAAP	US GAAP	US GAAP	IFRS	IFRS	IFRS
In €m	1999	2000	2001	2002	2003	2004	2005	2006
Balance sheet								
Balance sheet total	47.7	58.3	57.4	50.5	45.1	34.0	18.5	11.5
Shareholders' equity	44.0	50.2	50.3	47.9	42.5	29.6	13.1	8.5
Cash and cash equivalents	32.7	25.5	18.1	24.8	22.4	9.9	5.1	2.3
Statement of income								
Revenues	23.5	36.5	30.6	28.3	20.1	14.9	12.8	9.1
Capital expenditures*	0.2	1.8	1.9	1.2	1.3	7.1	0.2	0.7
EBIT	7.6	10.4	3.0	-3.8	-8.2	-15.6	-15.3	-6.2
Operating result	7.4	10.6	3.2	-2.4	-8.0	-15.3	-14.6	-6.2
Earnings before taxes	7.7	11.6	4.4	-2.8	-7.5	-15.3	-15.1	-6.3
Net income/loss for the year	3.5	5.6	2.3	-1.4	-5.7	-15.6	-17.0	-4.7
Statement of cash flow								
Cash flow	4.0	7.1	3.3	0.1	-3.9	-12.4	-8.9	-3.4
Other figures								
Earnings per share	0.59 €	0.78 €	0.32 €	-0.19 €	-0.78 €	-2.06 €	-2.15 €	-0.60
Employees (average)	106	141	162	172	178	184	120	71
Equity ratio	92.2 %	86.1 %	87.7 %	94.9 %	94.3 %	86.9 %	70.3 %	73.8 %
Share price at year-end	65.50 €	55.00 €	7.95 €	3.10 €	4.70 €	1.10 €	0.83 €	0.58 €

* Without financial assets

Revenues in €m



Earnings in €m



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Preface by the Management Board

Ladies and Gentlemen,
dear Shareholders,

Following our extraordinary shareholders' meeting on March 27, 2006, PANDATEL AG, was faced with its largest challenge so far. Several minority shareholders rejected the merger with Dowlake Microsystems, therewith, jeopardizing PANDATEL AG.

However, thanks to 100% support and cooperation from Dowlake Microsystems, the actuals are in line with the plan. With sales declining from €12.8m in 2005 to €9.1m in 2006 and EBT improving from €-15.1m to €-6.3m, the company seems to profit from the initiated restructuring measures. In this context, I would also like to mention that liquidity is now stable at about €2.3m and did not further decline thanks to the support and commitment of Dowlake.

At 2005's cash burning rate and with its business outlook 2005, PANDATEL was heading straight to bankruptcy within the next 12 months.

At that time, sole Director, Thomas Becker, presented the only two real options for PANDATEL AG in front of the Supervisory Board: Liquidation of the Company or investment by a strategic investor with a convincing corporate strategy.

Dowlake Venture invested at that critical moment to take over the majority from the previous majority shareholder AUGUSTA Technologie AG, and, in addition, Dr. Dan Yang became CEO effective the date of Dowlake Venture signing the purchase agreement on November 18, 2005.

Dowlake Venture was convinced of such risky investment, because of the understanding of PANDATEL business, and its structural problems. The new CEO introduced a series of restructuring measures put immediately into effect in order to stop cash burn and to ensure business continuation:

- a) Through merger with US-based Dowlake Microsystems, PANDATEL operations could be completely transferred to low cost operation locations in China.
- b) Consolidate PANDATEL's highly dispersed products and customers.
- c) Move headquarters to Hanover and position the company as "Ethernet Solution Provider" based on the existing PANDATEL Hanover R&D team.

With the support of both former and newly elected Supervisory Boards, the Management Board succeeded in a very short time in not only drawing up the strategy but also in implementing the change, including succeeding within 30 days after Dowlake takeover, the difficult negotiation with the Worker's Council. The new concept was obviously so convincing that the German Federal Office for Financial Services Supervision (BaFin), in its notice of January 17,

2006, announcing its decision to waive the obligatory tender requirement, insisted on the immediate implementation of the restructuring program and the merger of the two companies.

On March 27, 2006 we informed you of the decisions made by the newly elected Supervisory Board and the clear recommendations of the Management Board and received your predominant approval to the urgently required restructuring measures.

While we made huge progress, thanks to the unconditional support of Dowlake Microsystems, 14 plaintiffs, representing less than 2% of stockholding, made the merger fall off in December 2006!

We have slightly exceeded our revenue target of €8.5m, even though more than 80% of product models have been eliminated. We have succeeded in transferring hundreds of products to Dowlake Microsystems for production, which saw its inventory ballooned by four times, with less than 0.5 million in inventory on PANDATEL book. They had to put all the payment received from PANDATEL, at 15% plus cost slim margin into purchasing material. We have rescued and secured some customers who were turning away from PANDATEL. But we failed to execute our plan to merge PANDATEL and Dowlake.

In conclusion, here is some information on the development of the Company's sales and earnings in the business year 2006: Sales declined to €9.1 million in line with our expectation, and resulted in a loss of -€4.7 million mainly due to restructuring charges. At December 31, 2006, PANDATEL AG had funds at its disposal amounting to €2.3 million.

Dear Shareholders, PANDATEL AG has asked a great deal of you in the past in the way of patience and understanding. Now, however, we are faced with the challenge of having 10 R&D people and 10 sales and support staff to sustain a business that could grow at least 30% per year if it merges with Dowlake Microsystems.

The overall assessment of PANDATEL AG's risk potentials from the past financial year shows that its continued existence is still threatened as a result of

- a further drop in sales due to major sales still achieved with old products
 - excessively high return rate related to unnecessary costs
 - still little awareness for the new products due to low level of familiarity
 - some of the products are ahead of their time, and there are little early adopters and
 - cash reserves have continued to reduce,
- and PANDATEL AG cannot remedy this situation on its own.

We wish to thank you all for the trust you have placed in us.

Dr. Dan D. Yang CEO

Management Board



Dr. Dan D. Yang

Dr. Dan D. Yang graduated from University Paris-Orsay with a Doctorate degree in Optics and Photonics.

One of pioneers of intelligent optical networking, she was the founder of AFC Technologies in Ottawa Canada which was acquired by JDS Uniphase in 1999.

Holding nine United States patents on networking technology, she is also a renowned high tech entrepreneur in the Ottawa and Silicon Valley business communities.

In October 2000, she founded Dowlake Microsystems in the heart of Silicon Valley by investing her own money.

Since then Dowlake Microsystems has emerged as a leading OEM partner to major communications system makers, thanks to her vision, dedication, strategic investment in China operations, seamless execution, and her total commitment to customer satisfaction. Dr Yang became CEO of PANDATEL AG on November 18, 2005.

Supervisory Board



Manfred Wissmann

Mr. Manfred Wissmann has 30 years of professional experience as a lawyer. For app. 20 years, he has specialized in tax law. Mainly, he focuses on corporate law. In particular, he is consulting stock-listed corporations. He was senior partner in a supra-regional law firm in Mannheim, employing about 30 lawyers. Thereafter, in September 2006, he founded his own law firm "Wissmann & Partner" with several partners. Mr. Wissmann was already supervisory board member for several corporations. Presently too, he is member of various supervisory boards. Further he acts as management board member of the bar association Karlsruhe. As experienced lawyer, he has a university teaching position at the University of Heidelberg. Also, he has issued numerous publications covering his area of expertise.



Stefan Weidner

Stefan Weidner has comprehensive experience in corporate finance. This is mainly based on his occupation with Salomon Brothers Inc. in London and New York as well as with Price Waterhouse GmbH in Frankfurt/Main where he worked as Senior professional in the corporate finance department. His tasks mainly included M&A and IPO transactions, in particular in telecommunications, high tech as well as automotive. He studied business administration with focus banking, accounting/controlling at the University of Erlangen-Nuremberg and graduated with diploma in 1992. Presently, Mr. Weidner is independent consultant focusing on M&A, IPO, venture capital & private equity transactions (Europe/Asia).



Alex Fang

Since April 1994 Alex Fang has been Managing Director of CMT CHINA VALUE CAPITAL PARTNERS, a holding company focusing on investment opportunities in China. In 2001 he founded and became Director of eGARDEN VENTURES LIMITED, a holding company concentrating on start-ups in China and the USA. From 1998 to 2000 he was head of the business development division of GET MANUFACTURING, INC., a global supplier of EMS (electronics management services) with offices in Hong Kong, China, Mexico and the United States. From 1996 to 1997 he worked as Program Manager for the above corporation. In 1996 he was Assistant to the CFO of GENERAL ELECTRONICS (HK) LTD., a diversified corporation listed on the Hong Kong stock exchange. From 1994 to 1996 he worked as auditor for ERNST & YOUNG, Hong Kong. He holds an MBA degree in General Management at NORTHWESTERN UNIVERSITY, Kellogg School of Management, Evanston, Illinois, USA. He also attended the UNIVERSITY OF SOUTHERN CALIFORNIA, Levanthal School of Accounting, Los Angeles, California, USA, taking a B.Sc degree in Auditing. In June 1994 he completed his qualifications at the AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS.

The Year 2006 in Retrospect

January

At the beginning of the year, Dowlake Venture Ltd. acquires the remaining 20.98% of the shares in PANDATEL AG's share capital from AUGUSTA Technologie AG. AUGUSTA Technologie AG, therewith, terminating its PANDATEL AG holding so that Dowlake Venture Ltd.'s share increases to 49.98%.

According to the Management Board's application, BaFin exempts PANDATEL AG's new shareholder Dowlake Venture Ltd. and their owners Dr Dan Yang and Mr. Zibin Lu from their duty to publish their gaining control over PANDATEL AG, to transmit to the German regulatory authority BaFin a bidding document and to publish a mandatory offer.

BaFin grants the exemption subject to following conditions:

- a) BaFin is to be transmitted the notice of PANDATEL AG's general meeting.
- b) BaFin is to be notified of the resolution at the general meeting of PANDATEL AG.
- c) BaFin is to be provided with evidence of the registration with the Commercial Register about accomplishing the capital increase in cash.

Among others, BaFin mentions two essential reasons for granting the exemption:

- 1) In the absence of sufficing liquidity for restructuring, the only alternative to liquidating PANDATEL AG is the investment of a strategic investor.
- 2) The restructuring concept including the contribution of Dowlake Microsystems Corp. as combination partner provides the basis for a successful reorganization.

The Local Court Hamburg appoints Alex Fang and Dr. Axel Pfeifer members of the Supervisory Board to replace Axel Haas and Prof. Dr. Uwe Hannig.

They assume office the moment the company receives the court order and ends after conclusion of the next annual general meeting.

During its constituent meeting, the new Supervisory Board members elect from among them Dr. Axel Pfeifer chairman, Dr. Steffen Leistner deputy chairman and Mr. Alex Fang ordinary supervisory board member.

PANDATEL AG appoints a new management team. Andreas Hennig, head of R&D of PANDATEL's Hanover team, is appointed Vice President of R&D to lead PANDATEL's overall R&D effort. Munther Jadallah, Managing Director PANDATEL Asia Pacific, is now Vice President of Sales & Marketing.

February

Dr. Steffen Leistner resigns from his office as Vice Chairman of PANDATEL AG's Supervisory Board effective with the end of the extraordinary shareholders' meeting.

PANDATEL AG proposes to the extraordinary shareholders' meeting that Dr. Jozef Straus, former CEO of JDS Uniphase, to be elected member of the Supervisory Board.

March

In March 2006, PANDATEL presents itself on the CeBIT in Hanover. In this context, the company succeeds in establishing many interesting business contacts.

The company holds an extraordinary shareholders' meeting to approve the restructuring of PANDATEL AG. All items are passed with more than 95%.

April

Thomas Becker, member of the management board of PANDATEL AG, resigns from his office. Between October 2006 until the introduction of the new major shareholder, Becker led the company as sole board member.

By the end of April, PANDATEL publishes its annual report, which unmistakable displayed the disastrous situation of the company.

May

Several shareholders appeal against the company to nullify the resolutions taken at the extraordinary shareholders' meeting of PANDATEL AG on March 27, 2006, covering the following agenda items:

2. Resolution on share capital decrease for the purpose of restructuring and setting off losses and depreciations; amendments to the articles of association;
3. Resolution on approval of conclusion of business combination agreement between the company and the shareholders of Dowlake Microsystems Corp.;
4. Share capital increase of the company by contribution in kind and by excluding subscription rights for existing shareholders
6. Retroactive discharge of former director Norbert Wienck for fiscal year 2004
7. Supervisory board elections

The law suit is pending with the district court Hamburg.

The production transfer to Shanghai starts, including know-how and machinery. Production in Shanghai is at the state-of-the-art and available at much lower cost than in Germany.

June

The Hamburg headquarters as well as the Eisingen subsidiary are closed to streamline Germany operations in Hanover.

In this month, PANDATEL also announces a number of new products comprising three complementary PANDATEL Product Groups: Optical Networking, Ethernet and Multi-Service-over-PDH/-SDH/-Sonet, Last Mile/TDM-Access.

The company introduces latest developments on the GlobalComm in Chicago.

These products are also introduced on the company's annual press conference.

July

As part of the restructuring plan, PANDATEL consolidates its three German operational locations in Hanover to reduce operational costs. The company already runs its Ethernet products development center in Hanover. The company offers key engineers and developers to continue their work in Hanover as part of the R&D team. Lightmaze Solutions AG too, a subsidiary of PANDATEL in Eisingen, is integrated. The company continues the development and support of its YUMIX optical networking products.

The total number of PANDATEL employees in Germany decreases from 100 people to about 20. The layoff affects especially production, as well as sales and administration. Manufacturing is outsourced to Dowlake Microsystems.

Other details of the restructuring plan include product consolidation and a new management team. The total number of product platforms is decreased to less than 40.

August

For the first time in the company's history, the annual general meeting takes place at PANDATEL's new headquarters, Hanover. Due to the background of pending defensive actions, many shareholders appear and inquire about the outcome of this issue. Dan Yang presents her vision for the joint future of PANDATEL and Dowlake. All this depends on the court decision regarding those defensive actions.

The company publishes its semi-annual report.

November

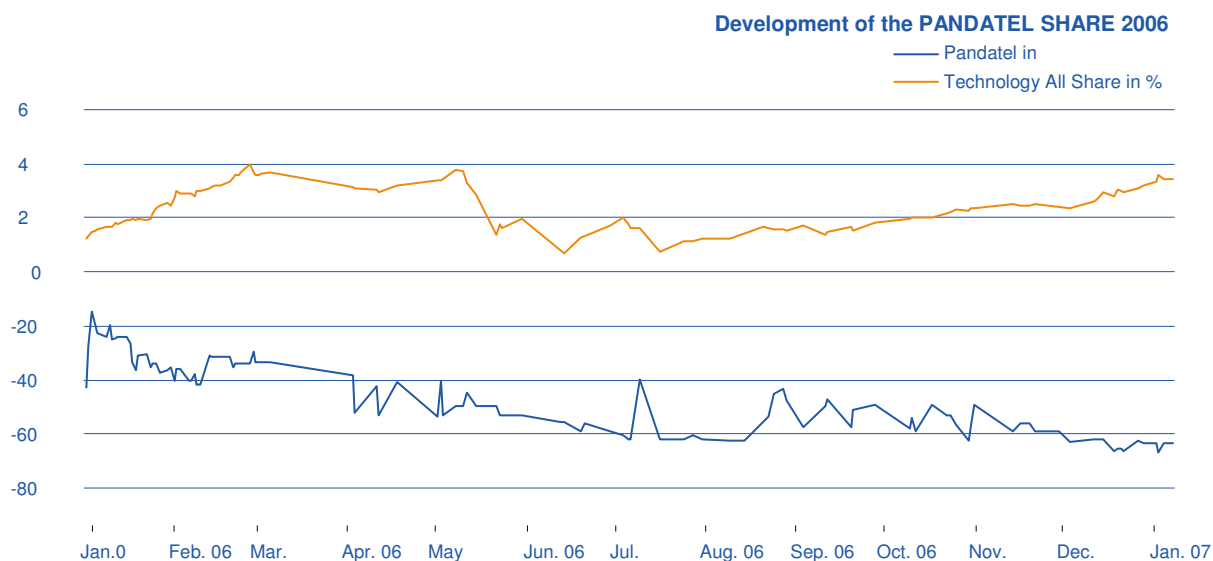
The company holds its annual analyst conference in Frankfurt/Main on November 28, 2006, within the German Equity forum. The presentation contains valuable information about the developments 2006, the present situation, and an outlook on the developments in 2007.

December

The Chairman of its Supervisory Board, Dr. Axel Pfeifer, Frankfurt/Main, and its Supervisory Board member Dr. Jozef Straus, Ottawa, Canada, resign from their positions after the foreseeable failure of the merger with Dowlake Microsystems Corp. effective 17 December 2006. The new members will be appointed by court decision shortly.

The Management Board files an application dated December 21, 2006, to appoint Manfred Wissmann and Stefan J. Weidner members of the Supervisory Board to replace the resigned board members.

The Share 2006 in Retrospect



The stock market

2006 was a good year for stock exchanges. The German stock index (DAX) experienced ups and downs. Last year, it finished at 5408.26 points. In this period, it passed the important 6000-points-barrier. At the end of 2006, it closed at a plus of 22 per cent.

Already before Christmas distinct economic improvements appeared. However, on January 1, 2007, the VAT increased from 16 to 19 percent so that many customers were faced with price increases.

The US business developed as expected. Rising oil prices and clearly increased real interest rate decelerated its dynamics. The skid marks are now quite visible.

The Dow Jones closed its last trading day 2006 with a negative result. However, for the year as a whole, the US key index grew considerably. It gained 16 per cent and almost 1746 points respectively.

The PANDATEL share

In fiscal year 2006, the PANDATEL AG share again was especially volatile. Over the year as a whole, the share closed at €0.58. This constitutes a decline of 36%. It reached its year-high on January 4, 2006, at €1.36. This increase was based on the publication of the new CEO's restructuring plan. In July and August, it recovered a little. This relates to the convening and holding the annual general meeting. In addition, half year figures improved somewhat boosting share performance.

Analysts and investors

In 2006, analysts were little aware of the PANDATEL AG share. This is mainly due to the uncertain outcome of the pending lawsuits.

The Share Key Data 2006

ISIN	DE 000 691 630 7
Number of shares	3,947,903
Closing price at year end 2005	€0.83
52-week high	€1.36
52-week low	€0.53
Closing price at year end 2006	€0.58
Market capitalization at year end	€2.3m
Market capitalization of free float at year end	€1.1m
Earnings per share	€-1.20
Shareholders' equity per share	€2.15

Corporate Governance

To ensure regular and open communication, PANDATEL AG is also implementing the recommendations and suggestions of the German Corporate Governance Codex. The code contains the regulations applicable in Germany for responsible leadership and for monitoring the company at the same time. The aim is to render these rules transparent for national and international investors and thereby strengthen confidence in the management of German companies. Most of the recommended rules have already been an integral part of corporate communications as practiced at PANDATEL AG for quite some time. Any deviations from these recommendations will most likely result from practical considerations based on circumstances within the Company, and will be explained in detail in the declaration of compliance. You can find a copy of the declaration published by the Executive and Supervisory Boards, including the exceptions, on the company's homepage www.PANDATEL.com and by clicking "Investor Relations".

The German Corporate Governance Codex recommends that the Executive and Supervisory Boards should include a report on corporate governance in the Company's Annual Report (3.10) and that this report should contain information on the emoluments paid to members of the Supervisory Board (5.4.7), on the purchase or sale of Company shares by members of the Boards or of the Company's management (6.6) and on share option programs or other incentive systems. PANDATEL AG has not so far produced such a corporate governance report, the information referred to above being included in the Notes to the Consolidated Financial Statements.

Declaration of compliance in accordance with Art. 161 of the Stock Corporation Act (AktG)

Declaration of conformity pursuant to Article 161 of the Stock Corporation Act (AktG) Declaration by the Management Board and Supervisory Board of PANDATEL AG, Hamburg, on the recommendations of the "Government Commission on the German Corporate Governance Codex" in accordance with Art. 161 of the Stock Corporation Act (AktG) According to the Management Board and the Supervisory Board, PANDATEL AG complies with all recommendations of the "Government Commission on the German Corporate Government Codex" as amended on 24 July 2006 published by the Federal Ministry of Justice in the official part of the Federal Gazette ("Bundesanzeiger") on 12 June 2006 excluding the following:

Sub-paragraph 2.2.2

The German Corporate Governance Codex recommends that shareholders are basically entitled to subscribe a number of shares representing their share in the share capital on the issue of new shares.

The company reserves itself to exclude subscription rights for capital increases against contribution in kind (e.g. in case of company or stock acquisitions).

Sub-paragraph 2.3.4

The German Corporate Government Codex recommends the company that it should make it possible for shareholders to follow the General Meeting using modern communication media (e.g. Internet).

At present, PANDATEL AG shareholders are not provided such media, for these measures would be far too expensive given the company's present situation.

Sub-paragraph 3.6

The German Corporate Governance Codex recommends that, in jointly run supervisory boards, the shareholders' und employees' representatives prepare the meetings of the supervisory board in each case separately and if necessary together with management board members.

Pandatel does not have a jointly run supervisory board, because it is not legally stipulated to have one considering the company's size.

Sub-paragraph 3.8

The German Corporate Government Codex recommends to agree upon an appropriate deductible when taking out a Directors & Officers Insurance.

The insurance policy taken out for the board members of PANDATEL AG does not provide for a deductible.

Sub-paragraph 4.2.1

The German Corporate Governance Codex recommends that the management board consists of several persons and shall have a chairman. Rules of procedure shall determine the allocation of duties and the co-operation within the management board.

The management board consists of one single person, because further management board members are not reasonable due to the company's size.

Sub-paragraph 4.2.3

The German Corporate Governance Codex recommends that monetary remuneration elements contain fixed and variable components. Further, the German Corporate Governance Codex recommends that variable remuneration elements contain non-recurring as well as annually recurring components with long-term incentive and risk character.

Basically, this recommendation is applied, however, the remuneration of the present management board forms an exception, because of the company's special restructuring situation.

The German Corporate Government Codex recommends that, in particular, company stocks with a multi-year blocking period, stock options or comparable instruments (e.g. phantom stocks) serve as variable compensation components with long-term incentive effect and risk elements. Stock options and comparable instruments shall be related to demanding, relevant comparison parameters.

Presently, the company does not have a stock option plan.

The German Corporate Government Codex recommends to report the compensation of the members of the Management Board as well as details of a stock option program or comparable instruments containing long-term incentive components and components with risk character on the company's internet page in a suitable form and to specify them in the annual report.

PANDATEL AG discloses neither the compensation system of the members of the Management Board on its internet page nor in its annual report. The compensation system does not comprise a stock option program or comparable components.

Sub-paragraph 4.2.4

The German Corporate Government Codex recommends to report the total compensation of the individual Management Board members, divided into non-profit-related and profit-related components with long-term incentive effect by indicating names as far as the shareholders' meeting did not resolve otherwise based on a majority of three quarters.

The CEO of PANDATEL AG receives a monthly fixed remuneration, which does not contain any further components.

Sub-paragraph 4.2.5

The German Corporate Governance Codex recommends to publish a compensation report containing the disclosure, which as part of the Corporate Governance Report shall as well explain the compensation system for the management board in a general comprehensible way.

The company does not publish a compensation report, because the relevant information is contained in the financial statements and annual report.

The German Corporate Governance Codex recommends that the description of the precise contents of a stock option plan or comparable structure for components with long-term incentive and risk character shall comprise their respective value. In case of pension promises, the addition to pension accruals or pension funds shall be published.

Such remuneration components are not intended.

The German Corporate Governance Codex recommends that the basic contents of promises, in case his work for the management board is terminated, have to be published if the promises concerning their legal relevance vary considerably from the promises made to employees. The compensation report shall also contain details on the kind of perquisite made by the company.

No such promises exist.

Sub-paragraph 4.3

Conflicts of interest

Sub-paragraph 4.3.1

The German Corporate Governance Codex recommends that management board members are subject to a comprehensive non-competition clause while they work for the company.

Dr. Dan D. Yang is exempted as regards her work for Dow-slake Microsystems Corp.

Sub-paragraph 5.1.2

The German Corporate Government Codex recommends that the Supervisory Board can delegate preparations for the appointment of members of the Management Board to a committee, which also determines the conditions of the employment contracts including compensation.

The Supervisory Board of PANDATEL AG comprises three members and does not set up committees because of its size.

Sub-paragraph 5.1.3

The German Corporate Government Codex recommends that the supervisory board shall draft rules of procedure for itself.

The supervisory board of Pandatel consists of no more than three members and has, therefore, not drafted rules of procedure.

Sub-paragraph 5.2

The German Corporate Government Codex recommends that the Chairman of the Supervisory Board shall also chair the committees that handle contracts with members of the Management Board and prepare the Supervisory Board meetings. He should not be Chairman of the Audit Committee.

The Supervisory Board of PANDATEL AG comprises three members and does not set up committees because of its size.

Sub-paragraph 5.3.1

The German Corporate Government Codex recommends the Supervisory Board to form committees with sufficient experience depending on the specifics of the enterprise and the number of its members.

The Supervisory Board of PANDATEL AG consists of three members and does not form any committees.

Sub-paragraph 5.3.2

The German Corporate Government Codex recommends that the Supervisory Board shall set up an Audit Committee.

The Supervisory Board of PANDATEL AG did not set up an Audit Committee.

Sub-paragraph 5.3.3

The German Corporate Government Codex recommends that the Supervisory Board can delegate other subjects to be handled by one or several committees. These subjects include the strategy of the enterprise, the compensation of the members of the Management Board, investments and financing.

The Supervisory Board of PANDATEL AG did not set up any committees for this is not necessary due to its size.

Sub-paragraph 5.3.4

The German Corporate Governance Codex recommends that the supervisory board can determine that committees prepare supervisory board meetings and are in addition entitled to decide instead of the supervisory board.

PANDATEL AG's supervisory board did not appoint any committee because this is not necessary due to its size.

Sub-paragraph 5.6

The German Corporate Government Codex recommends the Supervisory Board to review the efficiency of its activities on a regular basis.

In the past years, the Supervisory Board reviewed its efficiency on a yearly basis. However, it did not carry out an review in 2006, because the Supervisory Board Members changed near the examination.

Sub-paragraph 7.1.2

The German Corporate Government Codex recommends to make the Consolidated Financial Statements publicly accessible within 90 days of the end of the financial year; interim reports shall be publicly accessible within 45 days of the end of the reporting period.

Generally, PANDATEL AG complies with this recommendation. The only exception is its Nine Month Report 2006 owing to intra-corporate restructuring reasons.

PANDATEL AG Hanover, March 2007

Management Board Supervisory Board

Report of the Supervisory Board

In fiscal 2006, the Supervisory Board advised and regularly monitored the work of the Management Board and was kept constantly informed by the Management Board on the business situation at PANDATEL AG and its subsidiaries in the form of written and oral reports.

Matters which required the involvement of the Supervisory Board were notably and duly addressed in accordance with legislative regulations and the Articles of Association. The Supervisory Board comprehensively reviewed all the relevant business occurrences and, in the course of regular meetings with the Management Board, discussed the business development, strategy and the main business topics of the company. In the twelve months under review, the Supervisory Board convened at two ordinary meetings and passed seven resolutions in circulation procedure. At these meetings, among other items the business situation at PANDATEL AG and its associated companies was discussed as well as the future business strategy and issues relating to acquisitions and the strategic direction of the company. The Management Board provided detailed, up-to-date and in-depth reports on the development of business, the situation of the company as well as the strategy and plans. In addition to the scheduled meetings, the members of the Supervisory Board and the Management Board repeatedly met to exchange ideas and information. The Supervisory Board was therefore kept permanently informed on business developments.

In this way, the Supervisory Board was constantly supplied with detailed information on the current situation of the Company, so that it was able to recognize and react in a timely fashion to the risks that had arisen and were threatening PANDATEL AG's continued existence. In order to ensure that the necessary measures were taken, the Board involved itself at all stages and participated fully in the decision making process.

The Supervisory Board regards the German Corporate Governance Code as an important step towards the further development of the practice of company management and control. For this reason, the implementation of the Code was repeatedly an issue at the Board's meetings. In the 2006 financial year the Supervisory Board did not heed the recommendation to regularly review the efficiency of its operations because two of its members resigned from the Board in December 2006 and their temporary replacements were not appointed by the Hamburg Local Court until February 2006. In March 2007 the Supervisory Board and Management Board jointly submitted a Declaration of Compliance pursuant to § 161 of German Company Law (AktG). This Declaration has been published on the Company's Internet homepage.

The following changes of the Boards of PANDATEL AG took place in 2006: In January 2006, two new members of the Supervisory Board were appointed by the Hamburg Local Court to serve on the Supervisory Board until the Supervisory Board election by the Extraordinary General Meeting. On February 10, 2006, Dr. Steffen Leistner resigned from his office as Vice Chairman of PANDATEL AG's Supervisory Board effective with the end of the extraordinary shareholders' meeting convened for March 27, 2006. On this shareholders' meeting a new Supervisory

Board was elected, consisting of Dr. Axel Pfeifer (chairman), Alex Fang (Vice Chairman) and Dr. Jozef Straus (ordinary board member). Dr. Axel Pfeifer and Dr. Jozef Straus resigned from their positions effective 17 December 2006 after the foreseeable failure of the merger with Dow-slake Microsystems Corp. On 8 February 2007, following the Management Board application dated December 20, 2006, attorney at law Manfred Wissmann, Mannheim, and Stefan J. Weidner, Frankfurt/Main were appointed members of the Supervisory Board to replace Dr. Axel Pfeifer and Dr. Jozef Straus who resigned effective December 17, 2006.

The financial statements and consolidated financial statements at December 31, 2006, and the management reports of the company and the group for financial 2006, all of which were prepared by the Management Board, have been reviewed by the auditors appointed at the Annual General Meeting, Dr. Ebner, Dr. Stolz und Partner GmbH Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft. The auditors found them to concur with the duly maintained accounts and statutory regulations. The auditors have issued an unqualified opinion on the financial statements and the consolidated financial statements. The auditors participated in the Supervisory Board meeting discussing the financial statements on 17 March 2007, commented on the findings of the audit and answered questions. The Supervisory Board has reviewed the financial statements and the consolidated financial statements as well as the management reports of the company and the group on the basis of the auditors' report and has no cause for objection. The Supervisory Board has formally by written resolution approved the financial statements and the consolidated financial statements drawn up by the Management Board on 27 March 2007. The financial statements for the year have thus been adopted.

In addition, the updated financial statements and updated consolidated financial statements at December 31, 2006, and the updated management reports of the company and the group for financial 2006, all of which were prepared by the Management Board, have been reviewed by the auditors appointed at the Annual General Meeting, Dr. Ebner, Dr. Stolz und Partner GmbH Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft. The auditors found them to concur with the duly maintained accounts and statutory regulations. The auditors have issued an unqualified opinion on the updated financial statements and the updated consolidated financial statements. The auditors participated in the Supervisory Board meeting discussing the updated financial statements on 15 June 2007, commented on the findings of the audit and answered questions. The Supervisory Board has reviewed the updated financial statements and the updated consolidated financial statements as well as the updated management reports of the company and the group on the basis of the auditors' report and has no cause for objection. The Supervisory Board has formally by written resolution approved the updated financial statements and the updated consolidated financial statements drawn up by the Management Board on 15 June 2007. The financial statements for the year have thus been adopted.

According to Art. 175 para 2 AktG, the management board of stock-listed companies is obliged to issue an explanatory report on the statements according to Art. 289 para 4 and Art. 315 para 4 HGB.

The group management report and the individual management report contain all components required according to Art. 289 para 4 and Art. 315 para 4 HGB. All statements comply with the company's articles of association and the contractual agreements with the management board of PANDATEL AG comprising the following:

"The share capital consists exclusively of common stocks. No preference shares or shares granting special rights or obligations exist. Neither any limits exist concerning voting rights or the transfer of shares.

Dr. Elke Jahn and Dr. Niraj Agrawal sold part of their shareholding to Dowlake Venture Ltd. on 28 April 2006 and the remaining shares to a private investor. Dowlake Venture Ltd. and their associated persons, Dr. Dan D. Yang and Mr. Zibin Lu, passed the 50% share-holding-threshold and now jointly hold 53.11% of the company's shares. Beyond this, the Management Board does not know of any shareholders holding more than 10% of the shares in Pandatel.

No share owners exist with special rights granting control rights. Also, no type of voting right control for employees exists who own shares in the company.

The Supervisory Board appoints and withdraws Management Board members. The Supervisory Board appoints the CEO. The maximum age for Management Board members is limited 68 years according to the articles of incorporation. Dr. Dan D. Yang is appointed Management Board member until 18 November 2007.

The Supervisory Board is entitled to decide on changes in the articles of association not affecting the version of the articles of association. Otherwise, legal regulations (Articles 133, 179 AktG) apply to changes of the articles of association.

The Management Board is entitled to one time or several times increase the share capital by up to €3,600,000.00 (authorized capital) until 26 May 2009 by issuing new bearer shares against contribution in kind or cash with the consent of the Supervisory Board. This right was exercised during the acquisition of Lightmaze Solutions AG amounting to €670,806.00 so that an authorized capital remains amounting to €2,929,194.00.

By resolution of the extraordinary shareholders' meeting of 22 September 1999 the share capital was contingently

increased by up to €350,000 by issuing up to 350,000 new common bearer shares as no-par shares. This capital increase is due to the granting of option rights to Management Board members, division managers and team leaders of Pandatel Aktiengesellschaft comprising several tranches. An option entitles to receive one common share of Pandatel Aktiengesellschaft according to the stock option plan approved by the general meeting. By resolution of the annual general meeting of 29 August 2006 the share capital was contingently increased by nominal €430,000. The contingent capital increase is carried out by issuing up to 430,000 new common bearer shares in the form of no-par shares. It is carried out only insofar as option owners exercise their subscription right issued within the stock option plan 2006 of Pandatel AG due to the authorization granted on 29 August and if the company does not grant own shares in fulfilling subscription rights.

Material special agreements of the company due to a potential change of control as a result of a take-over bid do not exist. Also, no compensation agreements exist with the members of the Management Board or employees in case of a take-over."

The auditors furnished the following opinion on the report of the Management Board on the relations to the affiliated companies in accordance with section 312 German Stock Corporation Act: "Having duly conducted our examination and assessment, we hereby confirm that

- the factual statements made in the report are correct,
- the company's performance in the legal transactions enumerated in the report was not inappropriately high."

The Supervisory Board concurs with the auditors' report. Following the final examination of the audit by the Supervisory Board, we raise no objections to the explanation by the Management Board at the end of the report regarding the relations to the associated companies.

The Supervisory Board would like to thank the Management Board for its activities and its commitment to the company. At the same time, the Supervisory Board would like to ex-tend its thanks to all the staff members of PANDATEL AG for their dedication in 2006.

Supervisory Board:

Manfred Wissmann Alex Fang Stefan J. Weidner

Hannover, 27 March 2007/15 June 2007

Updated Group Management Report PANDATEL AG

2006 is marked by two major events in PANDATEL's history: forceful execution of restructuring measures, from R&D to Operations to Sales and Product Management; and the discussion with 14 plaintiffs regarding the merger with Dowlake Microsystems Corp.

Consolidation of operating locations:

Based on the strategy set since the beginning of the year by the new Management Board, PANDATEL shutdown Hamburg and Eisingen (Lightmaze Solutions AG) locations. Lease contracts for two buildings in Hamburg (Fasanenweg and Bargkoppelstieg) were terminated after intensive negotiations. Lightmaze location in Eisingen was shutdown end of March.

Some assets and materials were disposed during shutdown. For Eisingen location, mostly office equipment and some production equipment were sold off on auction with a result of about €16,000 in cash. For Hamburg location, SMT machine, production machine, excess inventory were sold off on auctions, resulting in 160,000 Euro cash.

Newly rented 1,100 m² headquarters were installed in Hanover in June 2006.

New 280m² sales offices in Acton/U.S.A. were opened in October 2006.

Lightmaze Solutions AG subsidiary terminated its operational business in the first half 2006.

Layoff:

62 people from Hamburg and 25 people from Eisingen were laid off, with last group of people from Hamburg leaving the company end of June. Hamburg employees had Worker's Council negotiated layoff package, at a ratio of about 1 month per year of service. Eisingen employees received 0.5 months of layoff compensation. Compensation costs were accrued in the previous year.

Only two permanent employees responsible for East European Sales, and two contractors also responsible for Eastern European Sales, sued PANDATEL and these suits were settled with no major cost to PANDATEL.

Product Consolidation:

PANDATEL's new product portfolio was released after restructuring and consideration of Dowlake Microsystems products, which concentrates on Ethernet solutions. The solution portfolio covers the whole bandwidth from Optical to Last Mile.

We have put COP Series Circuit Emulation Over Packet, and ETC series Ethernet for Last Mile products at the focus of customers. Both products were developed by our R&D team in Hanover. However, the sales of these two product categories with total revenues of about €0.5m have not yet

met expectations. In case of COP series, it's mainly due to the market awareness of PANDATEL being capable of providing such products, because PANDATEL had never seriously promoted this technology in the past. For ETC series, 10/100M versions were too expensive for the market, while Gigabit versions were still too early for the market for mass deployment.

Other newer generations of converters like OMF for E1 extension, and CMG for G.SHDSL too, failed to represent significant revenue, with a total of about 0.5 M (or 6% of total revenue). Both these products were developed by outside companies thus using different materials and parts from PANDATEL regular products, posing operations a high degree of additional extra works.

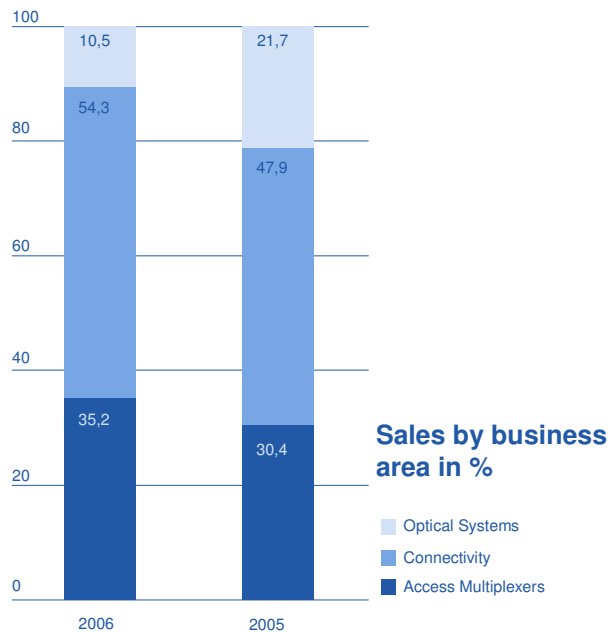
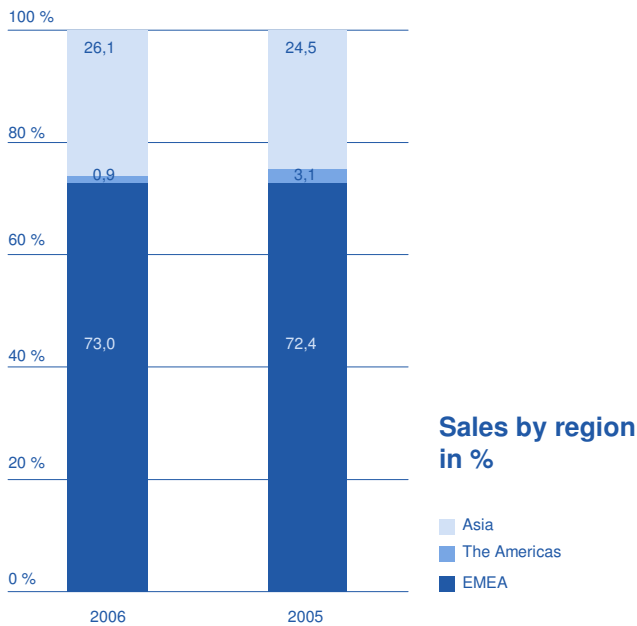
PANDATEL has been considered as a converter manufacturer for the last 20 years. Changing its image from a manufacturer to a solution provider requires marketing effort, complete marketable product portfolio, and the right sales strategy. It is obviously not reasonable to assume that such a switch in focus could be executed in that short time period with only 20 headcounts of PANDATEL. Thus the failure of the merger with Dowlake Microsystems caused that we could not completely leverage our R&D strength in Germany (PANDATEL), and US (Dowlake), with low cost operations in China (Dowlake) within a group of companies. And the failure of the merger also implies the major risk that PANDATEL new generations of products can't pick up fast enough.

Production Transfer:

PANDATEL AG and Dowlake Microsystems were planning to merge during the course of 2006. It was one of the conditions and reasons why Dowlake Venture invested in PANDATEL AG by acquiring >50% of PANDATEL AG from its original major shareholder AUGUSTA Technologie AG end of 2005.

Besides joint development, marketing and sales activities it was decided to transfer complete production of PANDATEL components to production location of Dowlake Microsystems in Shanghai. Both companies signed a respective agreement of co-operation. Production transfer linked with closing Hamburg production location and cost-effective production in China shall, in the medium term, sustainably improve margins.

a) Eisingen/Lightmaze production transfer: Dowlake Microsystems was manufacturing equipment similar to Lightmaze YUMIX products. Thus the transfer of production did not have much technical challenge except that Lightmaze has never integrated its products into PANDATEL operations system. Thus materials used by Lightmaze are not present in PANDATEL ERP system, posing major difficulty for inventory and production control. Dowlake engineering has spent four months inte-



grating Lightmaze production into PANDATEL systems, making it possible for customers to order directly to PANDATEL with production material requirement becoming immediately visible. Since Lightmaze shut-down, Dowlake Microsystems has supported YUMIX production shipment, with a total revenue of close to 0.5m.

- b) Hamburg production transfer: With about 4000 active parts for 157 types of circuit cards, no doubt to say it is a huge challenge to Dowlake operations. Most of materials needed to be bought via brokers due to old age of products and because they are often no longer part of distributor's portfolio. Bills of Materials needed to be entered into Dowlake MRP system for purchasing and production control. Often test instructions lack details what caused Dowlake additional personnel effort. However, total shipment exceeded 10,000 units from Dowlake Shanghai in 2006, representing more than 4 million Euro worth of revenue since.

Research and Development

10 R&D engineers are not enough to take care of 5 major series of products or 157 types of product types. In anticipation of the merger, 10 Dowlake Microsystems engineers have complimented PANDATEL R&D.

In 2006, PANDATEL has released new models of COP series COP-RS, ETC series ETC-B26 products. New fractional E1 converter CCF is also starting to be produced. Major software implementations include a web-based graphic user interface for MACS platform, and OAM features for ETC products.

General market situation

The economic growth did not just rise in Germany last year, but also gained considerable breadth. This balanced growth profile justifies a rather optimistic outlook on the coming quarters.

Therefore, the basic scenario forecasts continued upturn with a few fluctuations over the period. The reason is the increase in the value added tax rate at the beginning of this year, which according to our view will not interrupt the growth trend.¹

In the areas ITC and digital CE (digital consumer electronics – hardware), the TC infrastructure covers 3.2 % of the market. The German ITC-CE market 2007 develops slightly backwards compared to 2006. In 2006, TC booked sales of €66.4 bn with a growth in the ITC-CE market of 2.5%. Now, BITKOM (federal association for information, telecommunications and new media) forecasts sales of €66.3bn for telecommunications and a growth of 1.6% for the total ITC-CE market in 2007. In 2006, German telecommunications market grew by 0.5%. For 2007, BITKOM assumes a negative growth of -0.2%. Concerning telecommunications hardware, the situation is even more severe: In 2006, sales of €9.8bn were achieved with a decrease of -1.3%. For 2007 however, BITKOM expects slightly decreased sales of €9.7bn and a decrease -1.4%.²

Sales trends 2006

In fiscal 2006, sales continued to decline as expected to €9.1m. A major part of sales still come from PANDATEL old product ranges that are no more listed in the most recent

¹ Professor Dr. Axel A. Weber, president of Deutsche Bundesbank „the economy's prospects and challenges“ speech at the new year reception of Frankfurter Gesellschaft für Handel, Industrie und Wissenschaft e. V. – Casino-Gesellschaft von 1802 – in Frankfurt /Main on Friday January 19, 2007

² BITKOM press conference on economic development ITC market development 2006/2007, Berlin September 5, 2006, Willi Berchtold, BITKOM-president, management board member Informatics, finance and controlling ZF Friedrichshafen

product catalogue. Customers are buying mostly old products for existing network where PANDATEL has been supplying for long time converter type of products.

Germany marks the largest decline due to the pull out of old products, falling from €1.6m in 2006 to €1.3m in 2006. The largest contributors again came from the United Kingdom and France, with sales of €1.8m and €2m respectively. We have abandoned Eastern Europe in most cases due to competition and regularity requirement, as well as sales effort it needed. Same situation remains for Latin and South America. In Asia PAC, major drop is seen in China, as we abandoned supporting “customer” with bad payment habits. Overall Asia PAC sales is €2.2m flat in comparison to 2005 €3.1m.

The shares of total sales and the changes compared to 2005 accounted for by the different business divisions are included in the following table. The proportion of the total turnover for Access Multiplexers and Connectivity Products areas remained relatively stable whereas mainly Optical Systems did not meet expectations. Since the advanced but highly complex Yumix 4000 system produced by Lightmaze is employed in highly volatile project business. In addition in the first half of 2006, a one-time revenue was achieved from supply of raw materials and supplies to Dowlake Microsystems for fast setup of production process.

	2006		2005	
	€000	%	€000	%
Revenues				
Areas				
Access Multiplexers	3,019	33,2	3,889	30.4
Connectivity Products	4,665	51,4	6,122	47.9
Optical Systems	901	9,9	2,773	21.7
Spare Parts	498	5,5	0	0.0
	9.083	100,0	12.784	100.0

Earnings

Despite significantly improved earnings compared to 2005, in particular declining sales, high material usage together with extraordinary depreciations on Yumix patents due to failed revenue expectations and restructuring expenses led again to a negative result. A relatively high material usage ratio is in particular linked to high launching costs in connection with production transfer to Shanghai as well as to starting sales activities for third-party products initially connected with low margin for market introduction.

In fiscal 2006 PANDATEL AG recorded losses before interest and taxes (EBIT) amounting to -€6.2m, as compared to -€14.6 m in the previous year. The net loss for the year was -€4.7m (2005: -€17.0m), which corresponds to a loss per share of -€0.60 (2005: -€2.15).

Orders received in fiscal year 2006 fell only slightly to €10.9m as compared to €11.9 million in 2005. At December

31, 2006, PANDATEL AG's order books showed orders in hand amounting to €1.5 million, i.e. largely the same compared to the same date in 2005.

In 2006, restructuring costs amounted to a total of €1.4m (2005: €3.4m). These mainly result from the necessity to scrap no longer utilizable inventory due to elimination of stocks in Hamburg and Eisingen as well as to comprehensive streamlining the product portfolio, which was unpredictable in the previous year.

Financial position

Sales and earnings in 2006 were mainly in line with the forecast performed at the beginning of 2006; accordingly PANDATEL AG's assets continued to shrink. At December 31, 2006, the Company had an equity ratio of 73.8% and the balance sheet stated liquid funds of €2.3m (without securities). Due to the decline in sales, the balance sheet total fell from €18.6m in 2005 to €11.5m in 2006. This is primarily due to the reduction in inventory and liquid funds.

In 2006 PANDATEL AG invested a total of €0.7m in tangible and intangible assets, which corresponds to an investment ratio of 5% (2005: 2%).

Equity capital transactions and structure

The extraordinary shareholders' meeting on March 27, 2006, passed resolutions on reducing subscribed capital and the contribution of Dowlake Microsystems. It confirmed these items with a majority of more than 95% (of the voting shares present). However, a number of minority shareholders appealed against these resolutions. PANDATEL AG made a settlement proposal, which was declined by them. The court decision is still pending. The merger cannot be implemented according to the contribution agreement without taking a new resolution until 31 December 2006 due to time lapses. The resolved capital decrease was entered into the balance sheet despite accidental entry of capital decrease into commercial register.

The share capital consists exclusively of common stocks. No preference shares or shares granting special rights or obligations exist. Neither any limits exist concerning voting rights or the transfer of shares. No share owners exist with special rights granting control rights. Also, no type of voting right control for employees exists who own shares in the company.

Major technological areas

PANDATEL transferred its headquarters Hamburg and the Eisingen development center to its new headquarters in Hanover, which started operations on July 1, 2006. Israel and American subsidiaries were closed too.

In the course of its new corporate strategy, the Ethernet solution specialist PANDATEL merged its several thousand product versions into app. 40 platforms. The company continues to support and develop core technologies. In addition, the optical products of Dowlake expand the compatible product groups. The new concentration on

general and compatible product platforms forms the core measures of the company guidelines of new CEO Dan Yang.

Optical Networking: This category comprises all the Yumix products supplemented by Dowlake's transport products.

Ethernet and Multi-Service-over-PDD/-SDH/-Sonet: This category consists of the newer generation of the Ethernet over Sonet/SDH products. They offer the required variety for linking data networking to public backbone networks. This product line is complemented by Dowlake's high data-rate, small form-factor products.

Last Mile/TDM-Access: This category comprises various TDM devices: modems, converters as well as multiplexers are part of the third product scope. They are compatible with all other products. In June, the company introduced latest developments on the GlobalComm in Chicago.

The COP-FE combines multiple circuit lines such as T1/E1, together with up to 3 LAN interfaces, to be multiplexed and migrated to packet-switched network at 100Mbps speed, on up to 2 either copper or fiber WAN interfaces. The COP-RS is a solution to extend multi-protocol serial interfaces over packet-switched network.

The ETC-B26 combines Ethernet connectivity and service delivery using WDM technology, providing a simpler and lower CAPEX/OPEX solution than standard passive optical network equipment.

Main development focus is:

- The release of the ET-CB wideband Ethernet series. This piece of equipment is a centrally managed gigabit Ethernet converter with integrated switching function capability.
- The implementation of full ADM function capability, including in-band management and ring management, in the C-MUX-155.

Staff

In fiscal year 2006 PANDATEL AG employed an average of 71 staff, not counting the Management Board (2005: 120). On 31.12.2006 the number of employees reached 26 as scheduled (without Management Board).

Executive and Supervisory Board

In 2006, the Management Board consisted of Thomas Becker and Dr. Dan D. Yang. Becker who was with the company until 30 April 2006 received a fixed monthly salary. Dowlake Venture billed for Dr. Dan D. Yang a fixed monthly fee since 1 July 2006. Special allowances or emoluments are not planned.

Starting in business year 2006, the Supervisory Board receives fixed and variable compensation. The fixed compensation amounts to €5,000 annually for each member. The variable compensation for each Supervisory Board member increases by €500 per €0.05 dividend per share, which exceeds a dividend amount of €0.15 per common

stock. The afore mentioned variable compensation is capped at €5,000 for every Supervisory Board member. The Supervisory Board chairman receives one and a half time of the compensation. The compensation is due 10 days after adoption of financial statements. If a Supervisory Board member did not belong to the Supervisory Board for a full fiscal year it receives a pro rata fixed compensation. Further, the Supervisory Board members receive reimbursement for expenses and reimbursement of any value added tax, which does not form part of the compensation package.

The Supervisory Board appoints and withdraws Management Board members. The Supervisory Board appoints the CEO. The maximum age for Management Board members is limited 68 years according to the articles of incorporation. Dr. Dan D. Yang is appointed Management Board member until 18 November 2007.

The Supervisory Board is entitled to decide on changes in the articles of association not affecting the version of the articles of association. Otherwise, legal regulations (Articles 133, 179 AktG) apply to changes of the articles of association.

Material special agreements of the company due to a potential change of control as a result of a take-over bid do not exist. Also, no compensation agreements exist with the members of the Management Board or employees in case of a take-over.

The Management Board is entitled to one time or several times increase the share capital by up to €3,600,000.00 (authorized capital) until 26 May 2009 by issuing new bearer shares against contribution in kind or cash with the consent of the Supervisory Board. This right was exercised during the acquisition of Lightmaze Solutions AG amounting to €670,806.00 so that an authorized capital remains amounting to €2,929,194.00.

By resolution of the extraordinary shareholders' meeting of 22 September 1999 the share capital was contingently increased by up to €350,000 by issuing up to 350,000 new common bearer shares as no-par shares. This capital increase is due to the granting of option rights to Management Board members, division managers and team leaders of Pandatel Aktiengesellschaft comprising several tranches. An option entitles to receive one common share of Pandatel Aktiengesellschaft according to the stock option plan approved by the general meeting. By resolution of the annual general meeting of 29 August 2006 the share capital was contingently increased by nominal €430,000. The contingent capital increase is carried out by issuing up to 430,000 new common bearer shares in the form of no-par shares. It is carried out only insofar as option owners exercise their subscription right issued within the stock option plan 2006 of Pandatel AG due to the authorization granted on 29 August and if the company does not grant own shares in fulfilling subscription rights.

Changes in the Executive and Supervisory Boards

On January 24, 2006, the company received the court order of the Local Court Hamburg on the appointment of its Supervisory Board. Based on the Management Board application dated December 20, 2005, investment manager Alex Fang and attorney-at-law Dr. Axel Pfeifer were appointed members of the Supervisory Board to replace Axel Haas and Prof. Dr. Uwe Hannig who resigned in November 2005.

On February 10, 2006, Dr. Steffen Leistner resigned from his office as Vice Chairman of PANDATEL AG's Supervisory Board effective with the end of the extraordinary shareholders' meeting of March 27, 2006.

The Management Board of PANDATEL AG proposed to the extraordinary shareholders' meeting that Dr. Jozef Straus, former CEO of JDS Uniphase, the world-wide leading manufacturer of fiber optic components, be elected member of the Supervisory Board.

Mr. Thomas Becker, who joined the company in August 2005, ceased to be interim Management Board Member of the company effective as of April 30, 2006.

The Chairman of its Supervisory Board, Dr. Axel Pfeifer, Frankfurt/Main, and its Supervisory Board member Dr. Jozef Straus, Ottawa, Canada, resign from their positions effective 17 December 2006 after the foreseeable failure of the merger with Dowlake Microsystems Corp. The new members will be appointed by court decision shortly.

Major shareholdings

Dr. Elke Jahn and Dr. Niraj Agrawal sold their shares to Dowlake Venture Ltd. and a private investor. Dowlake Venture Ltd. and their associated persons, Dr. Dan D. Yang and Mr. Zibin Lu, passed the 50% shareholding-threshold and now jointly hold 53.11% of the company's shares. Beyond this, the Management Board does not know of any shareholders holding more than 10% of the shares in Pandatel.

Corporate governance

With the aim of ensuring regular and open communication, PANDATEL AG also implements the recommendations and suggestions of the German Corporate Governance Codex. This codex summarizes the rules applicable in Germany for responsible management and simultaneous company monitoring. The objective is to make these rules transparent for national and international investors and to reinforce confidence in the management of German companies. We largely follow the latest versions of the recommendations and implement them within the PANDATEL AG Group accordingly. Deviations from the recommendations – most of which derive from circumstances particular to the Company – are described in detail in PANDATEL AG's Statement of Compliance. PANDATEL AG has published the Statement of Compliance by the Management Board and

the Supervisory Board, together with its exceptions, in its homepage at www.PANDATEL.de > Investor Relations. The German Corporate Governance Code recommends that the Executive and Supervisory Boards should include a report on corporate governance in the Company's Annual Report (3.10) and that this report should contain information on the emoluments paid to members of the Supervisory Board (5.4.7), on the purchase or sale of Company shares by members of the Boards or of the Company's management (6.6) and on share option programs or other incentive systems.

PANDATEL AG has not so far produced such a corporate governance report.

Risk management

As a globally operating group, PANDATEL AG is exposed to a number of risks within the framework of its worldwide business dealings that are inseparably connected with its entrepreneurial activities. The Company has installed a comprehensive risk management system for the early detection, reporting and control of risks. An essential component of PANDATEL AG's risk management system is early risk detection: With the help of a matrix, individual risk factors are systematically identified and assessed at specified intervals. Any risks detected are recorded and documented with respect to their possible effects and the likelihood of their materialization.

Besides market- and economy-related risks, company-related risks in all areas of the Company that may have an adverse effect on business development, financial situation and net earnings are assessed. Incoming orders, economic data and the results of market studies by international research institutes contribute to the assessment of the forecasts and of the probability of their occurrence; wide-ranging projects, investments and restructuring measures are also taken into account in the assessment of risk.

The overall assessment of the risk potentials from the past financial year leads to the conclusion that even in 2007 the Company's continued existence is still considerably threatened as a result of

- the further drop in sales due to major sales still achieved with old products
- excessively high return rate related to unnecessary costs
- still little awareness for the new products due to low level of familiarity
- some of the products ahead of their time, little early adopters and
- low cash reserves,

and that PANDATEL AG cannot remedy this situation on its own.

Risks arising from changes in the market environment

Despite some consolidation in the communications industry and a noticeable revival of parts of the telecommunications

market (e.g. IP-Ethernet), the Company is continuing to lose sales and market share owing to lacking awareness for the new products.

Products liability risks are estimated to be small. No products liability claims have been filed against PANDATEL AG at any time in the past and the Company is insured against such claims. All measures taken with regard to quality control and security are constantly reviewed and improved.

Due to the high degree of transactions in foreign currency, in particular US Dollar, Pandatel is subject to foreign exchange risk. This risk is limited by the aim to largely compensate US Dollar in- and outflows.

Risks arising from loss of competitiveness

PANDATEL AG's traditional product portfolio is subject to increasing pricing pressure from low-wage Asian suppliers. Despite modernization and reorientation Pandatel needs to find out whether the measures taken are sufficient to positioning itself in the market as a reasonably priced, innovative manufacturer.

Due to the merger with the strategic partner Dowlake Microsystems with Pandatel cannot be implemented it remains uncertain whether with further reducing cash funds sufficient capital remains for carrying out necessary improvements on a stand-alone basis.

Dependence report

Owing to the existence of a majority shareholding and a majority of represented voting rights by Dowlake Venture Ltd., PANDATEL AG is obliged in accordance with § 312 AktG to issue a dependence report. This report is drawn up by the Company's Management Board and is reviewed and certified as part of the audit of the annual financial statements.

The concluding statement of the dependence report states as follows: "The Management Board of PANDATEL AG declares herewith that in all the legal transactions listed in this dependence report, according to the circumstances of which we were aware at the time these legal transactions were conducted, our Company and our dependent subsidiaries received fair consideration and were in no way prejudiced and that no measures were taken to the disadvantage of the Company."

Particular events following fiscal year end

On February 08, 2007, PANDATEL AG received court order of the Local Court Hanover on appointment of its

Supervisory Board. Based on its Management Board application dated December 21, 2006, Manfred Wissmann and Stefan J. Weidner were appointed Supervisory Board members to replace Dr. Axel Pfeifer and Dr. Jozef Straus who resigned effective December 17, 2006.

On 28 March 2007, PANDATEL AG received Dowlake Venture's application to, inter alia, resolve liquidation of the company during the next shareholders' meeting.

On the annual general meeting of May 11, 2007, which was, inter alia, to vote on the application of Dowlake Venture, a resolution was taken to adjourn the general meeting on motion of the shareholders present. None of the agenda items was voted on.

From May 2, 2007, until June 5, 2007, Juergen Schroeder held the position of CEO with PANDATEL AG. Since June 5, 2007, Dr. Dan D. Yang is again CEO.

Outlook

Now, that the merger of Dowlake Microsystems with Pandatel could not be implemented due to defensive actions cooperation is being continued based on a joint marketing, service and supply agreement with Dowlake Microsystems. It must be considered that this agreement was concluded in view of the merger of both companies. From today's point of view it is doubtful, whether this type of cooperation, in particular against the background of closing PANDATEL AG, fits into Dowlake Venture's strategic plans as investor in both companies.

Until resolution on the requested closure of PANDATEL, the chosen direction is being continued. Meaning, the future-oriented product portfolio based on IP technology will be extended.

The market in Western Europe with its good margin and the Asian market form the basis of revenue. On Asian markets Pandatel will more and more consider the payment behavior of customers.

For fiscal year 2007 we expect further declining sales.

Management and Supervisory Boards intend to increase subscribed capital to its former level of EUR 7,896.000 accidentally decreased by entry into the commercial register.

Hanover, 13 June 2007

Dr. Dan D. Yang (CEO)

<u>Updated Group Balance Sheet of PANDATEL Aktiengesellschaft, Hanover,</u>			<u>Annex 1</u>
<u>as of 31 December 2006</u>			
	Notes	31.12.2006 TEUR	31.12.2005 TEUR
ASSETS			
Non-Current Assets			
Intangible assets	(1)	903	1,030
Property, plant and equipment	(1)	580	1,361
Deferred taxes	(25)	0	300
Other non-current assets	(2)	1,081	0
Total non-current assets		2,564	2,691
Current Assets			
Inventory	(3)	753	3,644
Trade accounts receivable	(4)	2,246	3,422
Receivables from affiliated companies	(5)	7	0
Current financial assets	(6)	2,915	2,907
Tax receivable	(7)	117	162
Prepaid expenses and other current assets	(8)	570	701
Cash	(9)	2,319	5,093
Total Current Assets		8,927	15,929
Total Assets		11,491	18,620
LIABILITIES AND SHAREHOLDERS' EQUITY			
Shareholders' Equity			
Share capital	(10)	3,948	7,896
Additional paid-in capital	(10)	3,870	4,652
Changes in shareholders' equity from exchange rate	(10)	662	544
Revaluation reserve	(10)	9	4
Retained earnings/Accumulated deficit	(10)	0	0
Total Shareholders' Equity		8,489	13,096
Non-Current Liabilities			
Deferred taxes	(25)	30	541
Total Non-Current Liabilities		30	541
Current Liabilities			
Trade accounts payable	(11)	281	562
Liabilities against affiliated companies	(12)	1,693	0
Tax accruals	(13)	7	138
Other accruals	(14)	633	3,737
Other current liabilities	(15)	358	546
Total Current Liabilities		2,972	4,983
Total Liabilities and Shareholders' Equity		11,491	18,620

The attached notes form an integral part of these annual financial statements.

**Updated Group Statement of Income of PANDATEL Aktiengesellschaft, Hanover,
for the period from 1 January through 31 December 2006**

	Notes	2006 TEUR	2005 TEUR
Revenues			
Products		9,083	12,784
Services		0	0
	(16)	9,083	12,784
Cost of revenue			
Products		-7,368	-8,246
Services		0	-1
	(17)	-7,368	-8,247
Gross Profit/Loss		1,715	4,537
Selling and marketing expenses	(18)	-1,582	-3,938
Research and development expenses	(19)	-2,399	-4,454
General administrative expenses	(20)	-2,608	-2,961
Amortization (and impairment) of goodwill	(1)	0	-4,349
Restructuring expenses	(21)	-1,397	-3,449
Other income/expenses	(22)	96	2
Operating Income/Loss		-6,175	-14,612
Interest income/expenses	(23)	-110	229
Foreign currency exchange gains/losses	(24)	-17	-709
Financial Result		-127	-480
Result Before Income Taxes		-6,302	-15,092
Income tax	(25)	1,561	-1,920
Net Income/Loss for the Year		-4,741	-17,012
Withdrawal from capital reserve		793	17,012
Income from capital reduction		3,948	0
Net Profit/Loss		0	0
Earnings per share (diluted and undiluted) in EUR	(26)	-1.20	-4.31
Earnings per share before extraordinary expenditure (diluted and undiluted) in EUR	(26)	-1.20	-4.31
The attached notes form an integral part of these annual financial statements.			

**Group Cash Flow Statement of PANDATEL Aktiengesellschaft, Hanover,
For Fiscal Year 2006**

	2006 TEUR	2005 TEUR
Net loss for the year	-4,741	-17,012
Depreciation on tangible and intangible assets	1,175	5,787
Extraordinary depreciation on inventory	1,230	103
Personnel expenses for stock options	12	85
Profit/loss from sales of tangible assets	211	196
Other non-cash income expenses	-1,296	1,971
Cash flow	-3,409	-8,870
Changes in		
Trade accounts receivable	1,034	218
Inventory	1,662	857
Other assets, which cannot be classified as investing or financing activities	51	703
Changes in		
Trade accounts payable	-250	-36
Other liabilities, which cannot be classified as investing or financing activities	-1,730	1,782
Changes in cash and restricted cash equivalents	116	203
Cash flow from operating activities	-2,526	-5,143
Income from disposal of fixed assets	189	189
Income from disposal of intangible assets	0	0
Payments for investments in tangible assets	-6	-165
Payments for investments in intangible assets	-658	-61
Cash flow from investing activities	-475	-37
Payments to shareholders (dividends)	0	0
Cash flow from financing activities	0	0
Changes in cash and cash equivalents	-3,001	-5,180
Changes in cash balances due to exchange rates	227	395
Cash and cash equivalents at beginning of period	5,093	9,878
Cash and cash equivalents at end of period	2,319	5,093
Interest paid	0	2
Interest received	160	208
Tax paid (+)/received (-)	51	72

Updated Group Statement in Shareholders' Equity of PANDATEL Aktiengesellschaft, Hanover, In Fiscal Year 2006

	Subscribed capital		Changes in shareholders' equity			Revaluation reserve			Total shareholders' equity TEUR
	Shares	Amount	Capital reserve TEUR	Retained earnings TEUR	Net profit/loss TEUR	Currency translation TEUR	Currency TEUR	Financial instruments TEUR	
		TEUR							
At 31 December 2004	7,895,806	7,896	21,579	-	-	87	74	(42)	29,594
Stock option plan	-	-	85	-	-	-	-	-	85
Net loss for the year	-	-	-	-	(17,012)	-	-	-	(17,012)
Allocation of net loss for the year from retained earnings	-	-	-	-	-	-	-	-	-
Allocation of net loss for the year to capital reserve	-	-	(17,012)	-	17,012	-	-	-	-
Unrealized exchange and currency differences after deducting taxes €3,000	-	-	-	-	-	457	(74)	46	429
At 31 December 2005	7,895,806	7,896	4,652	-	-	544	-	4	13,096
Stock option plan	-	-	11	-	-	-	-	-	11
Net loss for the year	-	-	-	-	(4,741)	-	-	-	(4,741)
Allocation of net loss for the year to retained earnings	-	-	(793)	-	793	-	-	-	-
Capital decrease	(3,947,903)	(3,948)	-	-	3,948	-	-	-	-
Unrealized exchange and currency differences after deducting taxes €3,000	-	-	-	-	-	118	-	5	123
At 31 December 2006	3,947,903	3,948	3,870	-	-	662	-	9	8,489
								9	

The attached notes form an integral part of these annual financial statements.

Group Consolidated Fixed Assets of PANDATEL Aktiengesellschaft, Hanover,

For Fiscal Year 2006

	Cost of Acquisition and Products					Cumulated Depreciation					Book Values	
	1.1.2006	Currency differences	Additions	Disposals	31.12.2006	1.1.2006	Currency differences	Additions	Disposals	31.12.2006	31.12.2006	31.12.2005
	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR
I. Intangible Assets												
1. Licenses and software	3,341	0	658	494	3,505	2,431	0	715	483	2,663	842	910
2. Goodwill	4,349	0	0	0	4,349	4,349	0	0	0	4,349	0	0
3. Self-provided intangible assets	180	0	0	0	180	60	0	60	0	120	60	120
	7,870	0	658	494	8,034	6,840	0	775	483	7,132	902	1,030
II. Tangible Assets												
1. Land and buildings, incl. buildings on external premises	275	0	0	275	0	275	0	0	275	0	0	0
2. Technical plant and machinery	1,286	0	0	483	803	778	0	69	191	656	147	508
3. Other plant, factory and business equipment	4,315	0	6	2,109	2,212	3,462	-2	331	2,012	1,779	433	853
III. Financial Assets												
Other long-term financial assets	5,876	0	6	2,867	3,015	4,515	-2	400	2,478	2,435	580	1,361
	13,746	0	664	3,361	11,049	11,355	-2	1,175	2,961	9,567	1,482	2,391

The attached notes form an integral part of these annual financial statements.

PANDATEL Aktiengesellschaft Hanover Updated Notes to the Consolidated Financial Statements 2006

Preliminary Notes

On 27 March 2006, the Extraordinary Shareholders' meeting of PANDATEL AG resolved, inter alia, to decrease its subscribed corporate capital from EUR 7,895,806.00 by EUR 3,947,903.00 to EUR 3,947,903.00 according to the regulations on ordinary capital decreases pursuant to Articles 222ff AktG (German stock corporation law) by amalgamation of shares for the purpose of restructuring as well as loss and depreciation adjustments. Against the resolutions of the general meeting objections and subsequently law suits were filed.

Contrary to the intentions of Management and Supervisory Boards, the capital decrease was entered into the Commercial Register with the District Court Hanover on 27 October 2006. The company continues to assume that it is possible to retroactively adjust the entry due to its accidental entry. Because of uncertain time need, the annual financial statements as of 31 December 2006 are adapted to the commercial register in order to create a legally safe position.

Management and Supervisory Boards plan to increase its subscribed capital to its former level. The statement of changes in shareholders' equity as well as earnings per share (income statement) now matches the changes in shareholders' equity.

The notes were adjusted to match the changes in shareholders' equity as well as the result per share. In addition, the assumption of going concern was substantiated and the data under other financial liabilities was complemented by a possible payment to Dowlake Microsystems Corp. providing for a possible termination of the "Joint Marketing, Service and Supply Agreement" as well the current status of discussions regarding the "Joint Marketing, Service and Supply Agreement". The Management Report was adjusted to the current developments in sections „Capital Measures/Composition of Shareholders' Equity", "Particular Events following the End of the Fiscal Year" and "Outlook".

(A) The Company

PANDATEL AG, (formerly Hamburg, now Hanover) came into being from the transformation of Pan Dacom Telekommunikation GmbH, Hamburg, from a limited liability company into a joint stock corporation. The earlier company had commenced operations in 1987. The transformation into PANDATEL AG, Hanover, was resolved on March 30, 1999, and entered in the commercial register of the Hamburg District Court on May 14, 1999, under registration number HRB 71126.

On 28 August 2006, the relocation of company registered offices to Hanover, Garbsener Landstraße 10 was registered by entry into the Commercial Register with the local court Hanover under No. HRB 200825. The relocation of the company's registered offices is based on a resolution by the general meeting of 27 March 2006. The business of PANDATEL AG, Hanover, is to develop and trade in telecommunications systems and to engage in all activities directly or indirectly related to this.

PANDATEL develops and distributes active components for network access and network transmission. Its products include multiplexers, modems and the software for managing these systems. PANDATEL has its products mainly manufactured by Dowlake Microsystems Corp., Shanghai, after completing the company relocation by 30 June 2006 to Hanover.

The headquarters of PANDATEL are located in Hanover. It also has active representative offices in France, Spain and the U.S.A. The US subsidiary as well as the subsidiary Lightmaze Solutions AG, Eisingen, terminated their operations in 2006. However they have not yet been completely wound up. The Singapore subsidiary is dormant. The subsidiary in Israel terminated its operations already in fiscal year 2004.

The further development of the Company, its representation offices and subsidiaries are described in the Management Report in the section headed "Outlook".

(B) Summary of major accounting and valuation principles

Accounting principles

The consolidated financial statements have been prepared in line with the International Financial Reporting Standards (IFRS) and are denominated in Euros (€). All the rules laid down in the International Financial Reporting Standards (IFRS) that are applicable and legally binding in the countries of the EU as at December 31, 2006, have been complied with.

In the reporting year, new standards and interpretations were adopted, which are not yet effective. They affect IFRS 7 and IFRS 8 as well as IFRIC 7 to 12. As soon as these new standards and interpretations become effective PANDATEL will apply them. Significant effects on balance sheet as well as on profit loss statement are not expected. The individual financial statements of PANDATEL AG drawn up in accordance with the HGB (German Commercial Code) and the consolidated financial statements of the PANDATEL Group drawn up in accordance with the IFRS are published.

Pursuant to § 315a HGB in combination with Art. 4 of the EU IAS regulations, capital-market oriented parent companies in Germany that are obliged to render annual accounts must draw up the consolidated financial statements that they have so far prepared in accordance with § 290 HGB in accordance with the rules of the IAS/IFRS. Compliance with the requirement to render consolidated accounts in accordance with the IFRS as specified in § 315a HGB is a condition for the admittance of shares of the parent company to the regular stock market. PANDATEL AG meets this requirement and draws up the consolidated financial statements for its Group with binding effect in accordance with IAS/IFRS.

Assumption of Going Concern

Despite current developments described in the Management Report, the Management Board of PANDATEL further assumes the employment of the going concern principle for preparing group financial statements, because present business activities will continue at least until late 2008 despite upcoming liquidation. PANDATEL received Dowslake Venture's application on 28 March 2007. No shareholders' meeting has so far voted on the application.

Scope of consolidation

The consolidated financial statements include PANDATEL AG and the following companies in which PANDATEL AG has a controlling financial interest (100% of the voting rights):

- PANDATEL Inc., USA
- PANDATEL Asia Pacific Pte Ltd., Singapore
- PANDATEL Ltd., Israel
- Lightmaze Solutions AG, Eisingen

The headquarters of PANDATEL are located in Hanover. It also has active representative offices in France, Spain and the U.S.A. The US subsidiary as well as the subsidiary Lightmaze Solutions AG, Eisingen, terminated their operations in 2006. However they have not yet been completely wound up. The Singapore subsidiary is dormant. The subsidiary in Israel terminated its operations already in fiscal year 2004.

Consolidation principles

The statements of the individual companies have been drawn up in line with uniform accounting and valuation principles in order to facilitate their inclusion in the consolidated financial statements. All consolidated companies have the same balance sheet date.

The capital consolidation has been undertaken in accordance with the so-called revaluation method. The attributable values or current values of all the tangible assets and liabilities are first calculated and this portion of the equity capital is then set off against the acquisition costs. Any positive difference is declared as goodwill. Loans and other accounts receivable or payable between the consolidated companies are offset against each other. Income from intra-group sales as well as other intra-group income is offset against the corresponding expenses. Interim earnings or losses have been eliminated.

Translation of financial statements in foreign currency

Assets and liabilities carried by the foreign subsidiaries whose functional currency is the local currency of the country in which they are domiciled are translated into Euros at the exchange rate ruling on the recording date. The equity capital is translated at the exchange rate ruling on the date of the transaction concerned. For the purposes of the consolidated financial statements, the income statement and cash flow statement of these foreign subsidiaries are translated into Euros at the average exchange rate of the fiscal year.

Estimates used in preparing the financial statements

In order to prepare the financial statements, the Management Board must perform estimates and assumptions on matters that affect the amounts of the assets and liabilities in the balance sheet and items in the income statement and cash flow statement, as well as on the statements in the explanatory notes. These estimates and assumptions can deviate from the actual circumstances.

Currency translation

Receivables, cash and cash equivalents and liabilities in foreign currencies are translated at the exchange rate ruling on the date of acquisition. Short-term receivables and liabilities are shown at the rate applicable on the balance sheet date.

Intangible assets

The intangible assets comprise software, licenses and similar rights. Intangible assets with a short useful life are written off by the straight-line method over their probable useful life (3 years). There are, however, also intangible assets whose useful life is unlimited. These include the goodwill of the firm of Lightmaze Solutions AG, Eisingen, which was acquired in 2005. This goodwill was written off completely in 2006 by way of extraordinary depreciation.

Tangible assets

The tangible assets are valued at their acquisition or production costs and are written off over their useful life by the straight-line method. The useful life of the various tangible assets is taken to be as follows:

	Years
Technical plant and machinery	5 - 13
Operating and business equipment	3 - 14
Office equipment	3 - 13
Tools	5
Low-value goods	1

In view of the amalgamation of the operating facilities in Germany, some tangible assets (e.g. leasehold fixtures) had to be written off in full.

Impairment of values of durable goods and intangible assets

Durable and intangible assets are examined for value impairment if events or changes have occurred that indicate that the net book value of the assets could no longer be obtained through their sale. Should facts or circumstances lead us to conclude that values have indeed been impaired, the net book value of the assets in question is compared with the future estimated income from their sale. If necessary, the resulting figure is written down to the lower value.

Other long-term assets

Long-term interest free liabilities are discounted at an interest rate of 4.5%.

Inventories

Raw materials and supplies, products as well as merchandise are shown at cost of acquisition or at cost of production, whichever is the lower. Cost of production encompasses the cost of materials and wages entailed in production, as well as the material and production overheads which have to be declared as assets according to tax law. Interest on borrowed capital is not shown as an asset. Where inventories are exposed to risks, such as that of reduced usability after lengthy warehousing, appropriate deductions for storage are made. Except in the case of customary retentions of title, inventories are unencumbered by third party rights.

Receivables

Receivables are stated at their nominal value, less value adjustments for expected defaults.

Securities

PANDATEL holds a portfolio of available-for-sale securities. These are available to the Company as required and are evaluated at their market value at the end of the financial year. Unrealized profits and losses, less any deferred taxes payable on them, are shown as components of the revaluation reserve forming part of the equity capital and have no effect on the operating result. They are removed from the reserve when the securities in question are sold, the profits or losses concerned then being stated in the income statement. Unrealized losses that are not only of a temporary nature necessitate a write-down on the securities that is also shown in the income statement. PANDATEL does not hold any securities for trading purposes.

Financial derivatives

PANDATEL AG applies IAS 39 in the version currently valid. This accounting standard requires that all financial derivatives are shown at market value, regardless of the purpose or intention underlying their purchase or sale. Changes in the market value of the financial derivatives are recorded on an accrual basis either in the operating result or in the equity capital (as part of the other changes in equity capital which do not affect the operating result), depending on whether the transaction concerned is a fair value hedge or a cash flow hedge. PANDATEL AG has so far used derivative financial instruments only to a minor extent.

Cash and cash equivalents

Cash and cash equivalents include cash balances, current balances with banks and time deposits with original terms of up to three months.

Cash and cash equivalents which serve as collateral and to which the Company has no access are not contained in the cash and cash equivalents. They are shown under other short-term assets. For the purposes of the cash flow statement, cash and cash equivalents to which the Company has limited access are not included in the cash and cash equivalents.

Reserves and liabilities

Reserves are formed for uncertain liabilities and impending losses if there is a likelihood that an obligation exists and the amount of the claim or loss can be estimated with sufficient accuracy.

Liabilities are stated at the amounts repayable. Short-term liabilities in foreign currency are valued at the exchange rate ruling at the close of the financial year.

Realization of sales

As a general principle, sales are realized with the rendering of services in accordance with the conditions agreed upon. Sales revenues take rebates, customer bonuses and cash discounts into account.

Product-related expenses

Expenses relating to unit sales are entered in the income statement at the time they are incurred. Reserves for guarantee payments are formed at the time of the sale of the products.

Sales costs

Advertising costs and other sales expenses are entered immediately in the income statement.

Research and development expenses

Costs for the development of new products are stated as assets together with the production costs insofar as they can be allocated to a particular category and insofar as it is certain that the newly developed products are technically feasible and also marketable (IAS 38). The development activities must, moreover, be sufficiently likely to be profitable for the Company in the future. In this context the production costs comprise all the costs directly or indirectly attributable to the development process. Scheduled depreciation is based on the planned useful technical life of the products. Useful life is generally taken to be 3 years. According to IAS 38 research costs may not be declared as assets and are therefore entered immediately in the income statement as expenses. In PANDATEL AG's case no research costs have as yet been incurred.

For purposes of the annual financial statements, all assets are subjected to a value impairment test in which the variable gross margins, less unaccrued interest, are compared with the asset values and adjusted as necessary.

Remuneration in the form of stock options

The Company declares its stock options in accordance with the market value method. Accordingly, personnel expenditure is calculated on the basis of the market value of the options at their subscription date, taking the average option period in each case. The expenditure calculated in this way is therefore not necessarily indicative of the amounts actually debited in future reporting periods.

Income taxes

Taxes on income and earnings are calculated according to the so-called liability method. Deferred taxes are calculated for the expected future tax bill from differences in the valuation of assets and liabilities for tax purposes and the values shown in the financial statements. The valuation of these deferred taxes is based on the tax rates applicable at the time of reporting. The impact of changes in the tax rates is factored into the income statement in the year in which the changes take effect. The deferred tax values are adjusted, if necessary, depending on their realizability.

Earnings and diluted earnings per share

Earnings per share are calculated from the weighted number of outstanding ordinary shares, including equity-like securities. Equity-like securities for remuneration in the form of stock options are not included in the calculation if they have the effect of reducing the diluting effect on earnings.

(C) Explanatory notes

(1) Tangible and intangible assets, financial assets

The structure and development of the fixed assets are presented in the consolidated statement of fixed assets appended to this report.

The additions to the intangible assets result from the purchase of software.

It is expected that write-downs on intangible assets in the next few years will be as follows:

	T€
2007	351
2008	290
2009	201
2010	0
After 2010	0

The goodwill from the acquisition of Lightmaze Solutions AG in 2004 was written off completely in the course of the year 2006 due to a continuously negative development of the business.

Intangible assets booked total additions of €658,000. They mainly comprise production set-up, production tooling as well as component sourcing and product re-design.

The additions to the tangible assets are mainly due to the purchase of other operating and business equipment.

Depreciations of the year under review can be broken down as follows:

€ 000 Depreciation	2006		2005	
	Scheduled	Unscheduled	Scheduled	Unscheduled
Intangible assets	345	430	513	0
Tangible assets	400	0	717	208
Tangible assets	0	0	0	4,349
	745	430	1,230	4,557

Extraordinary depreciations concern YUMIX products' patents. These depreciations were not predictable in the previous year, because the sales generated with YUMIX products in 2006 were much lower than originally planned and future sales will probably not reach the volume initially intended. Extraordinary depreciations on patents are shown under restructuring expenses.

In the year under review an inflow of € 189,000 (previous year € 27,000) and disposals at book value of € 400,000 (previous year € 223,000) resulted from the disposal of fixed assets.

(2) Other long-term assets

The other long-term assets contain only the entitlement to corporation tax deposits, which is discounted at a rate of 4.5%. Due to the changes in law published in late 2006, an entitlement exists on distribution of corporation tax deposits from the change from corporate tax credit method definitive taxation starting in 2008. For PANDATEL AG it amounts to €1,412,000 per 31.12.2006. The discount amount of €331,000 is booked as interest cost.

(3) Inventories

The inventories are composed of the following:

€ 000	31.12.2006	31.12.2005
Raw materials and supplies	195	1,333
Unfinished goods and work in progress	0	464
Finished goods and services	558	1,028
Merchandise	0	331
Deposits paid	0	488
	753	3,644

Write down on inventory stocks amounts to € 1,483,000 (previous year € 4,979,000). Of this €1,229,000 account for scrapings, which were necessary for various corrective activities, the amount of which was not foreseeable in the previous year. This applies in particular to the termination of Hamburg and Eisingen locations as well to streamlining the product portfolio. €654,000 belong to raw materials and supply, €464,000 to unfinished goods and €111,000 to finished goods. Of €1,229,000 €967,000 belong to restructuring expenses and €262,000 are stated as usage of restructuring reserves.

(4) Trade accounts receivable

€ 000	31.12.2006	31.12.2005
Gross receivables	2,877	4,205
less value adjustments	631	783
	2,246	3,422

(5) Receivables from associated companies

Receivables from associated companies exist only for Dowslake Microsystems Corp. and result from ordinary business transactions.

(6) Short-term investments / marketable securities

The Company has no speculative intentions as regards the securities held at the balance sheet date, nor does it intend to retain these until maturity. These securities are therefore classified as available for sale and can be disposed of as required.

€ 000	Acquisition cost	Stock exchange or market value	Unrealized profits	Unrealized losses
Papers securitizing outside capital	2,900	2,915	15	0

The marketable securities available at the balance sheet date consist only of euro-floaters (maturing 2009). The unrealized profits, less deferred taxes, are stated as part of the revaluation reserve. Interest income amounts to €94,000 (previous year €97,000) in the fiscal year regarding to Euro Floater.

(7) Tax claims

The tax claims amounting to € 117,000 (previous year € 162,000) relate mainly to taxes on investment income.

(8) Prepaid expenses and other short-term assets

€ 000	31.12.2006	31.12.2005
Interest receivable	0	17
Prepaid expenses	37	38
VAT	296	338
Restricted funds	115	231
Other short-term assets	122	77
	570	701

Restricted funds comprise rental agreements (deposits). Since these agreements may be terminated at short notice, the funds involved are stated as short-term assets.

(9) Cash and cash equivalents

€ 000	31.12.2006	31.12.2005
Current account	316	1,385
Overnight money Euros	1,625	208
Time deposits	378	3,500
	2,319	5,093

No unrealized exchange-rate losses arose either at the balance sheet date or in the previous year. Restricted funds at the amount of € 115,000 (previous year € 231,000) are stated as other short-term assets.

(10) Equity capital

Subscribed capital

The subscribed capital amounts to € 3,947,903.00 (previous year € 7,895,806.00), divided into 3,947,903.00 (previous year 7,895,806) no-par value shares with an arithmetical share in the capital stock of € 1.00 each. The extraordinary shareholders' meeting of 27 March 2006 resolved the capital decrease, which was entered into the Commercial Register with the District Court Hanover on 10 October 2006. The gain from the capital decrease was partly used to cover the net loss for the year 2006. The remaining balance was withdrawn from the additional paid-in capital after offsetting with the net loss for the year. The Commercial Register entered the resolution on increasing the subscribed capital to EUR 11,470,974.00 on 27 October 2006. The capital increase will take effect only after entering execution of capital decrease. No intention exists to execute this capital increase.

Authorized capital

The Management Board is authorized, subject to the consent of the Supervisory Board, to increase the capital stock in one or several steps until May 26, 2009, by issuing new bearer shares against cash or non-cash contributions, by a maximum amount of € 3,600,000.00. Advantage was taken of this authorization in connection with the acquisition of Lightmaze Solutions AG to the amount of € 670,806.00 so that authorized capital at the amount of € 2,929,194.00 remains. Subject to the consent of the Supervisory Board, the Management Board is empowered to exclude the statutory subscription rights of the existing shareholders for newly issued bearer shares to a total of up to 720,000 new bearer shares, should the issue amount of the shares not be substantially lower than the share price on the stock market.

Contingent capital

The extraordinary General Meeting of September 22, 1999, resolved a conditional increase in the equity capital of up to € 350,000.00 by issuing up to 350,000 new ordinary bearer shares in the form of unit shares. This capital increase is connected with the granting of option rights in several tranches to members of the Management Board, department heads and managers. Each option entitles the holder to subscribe to one ordinary share in PANDATEL AG in accordance with the stock option plan resolved by the General Meeting.

By resolution of the annual general meeting of 29 August 2006, share capital was contingently increased by nominal €430,000. The contingent capital increase is carried out by issuing up to 430,000 new common bearer shares in the form of no-par shares. It is carried out only insofar as option owners exercise their subscription right issued within the stock option plan 2006 of Pandatel AG due to authorization granted on 29 August and if the company does not grant own shares in fulfilling subscription rights.

Allocation of retained earnings

Net loss for the year (€ 4,741,000) was offset against gains from the capital decrease. The remaining amount (€ 793,000) was withdrawn from the capital reserve. No balance sheet gain/loss was disclosed as of 31 December 2006. The company has not yet applied for entering the resolution into the Commercial Register.

Stock options

At December 31, 2003, stock options were granted in five tranches. The first tranche (of 1999) covered 54,163 stock options, of which 24,999 were held by Management Board members. These options could not be exercised until December 1, 2001. The second tranche (of 2000) covered 55,199 stock options, of which 24,999 were held by Management Board members. The options of the second tranche were returned without exception and without claim to compensation on January 31, 2001. The third tranche (of 2001) covered 60,199 stock options, of which 24,999 were held by Management Board members. The options of the third tranche could not be exercised until after the Annual General Meeting in May 2003. The fourth tranche (of 2002) covered 56,999 stock options, of which 24,999 were again held by Management Board members. The options of the fourth tranche cannot be exercised until after the Annual General Meeting in May 2004. The fifth tranche (of 2003) covered 123,150 stock options, of which 75,000 were held by Management Board members. The options of the fifth tranche could not be exercised until after the Annual General Meeting in May 2005.

The stock options from the first, third, fourth and fifth tranches can only be exercised if the price of the PANDATEL ordinary share exceeds either the issue price (€ 22.00 for the first tranche) by 20% or the reference price (€ 36.10 for the third tranche, € 12.41 for the fourth tranche and € 2.96 for the fifth tranche), and if the price of the PANDATEL ordinary share has at least kept pace during the period between issue and exercise of the option rights with the trend of a combination of the Neuer Markt index (All Share Index) with a one-third weighting, and the weighted sector index comprising Adva AG, AUGUSTA Technologie AG, BinTec AG, CeoTronics AG, euromicron AG, teles AG and transtec AG with a two-third weighting. The maximum maturity of the options is 7 years, the expected maturity 4.5 years. From the fourth tranche onwards, an annual fluctuation of 5% was taken into account, owing to the fact that some option holders left the Company before the stock option plan came to an end.

In the report prepared by the Institut für Wirtschaftsmathematik und betriebliche Altersversorgung GmbH, the fair value was calculated by way of simulation (the Monte-Carlo Method). The trends underlying both the prices of the PANDATEL shares and of the comparison portfolio, which were assumed to correlate positively, were calculated using the Black-Scholes Model.

	1 st tranche	3 rd tranche	4 th tranche	5 th tranche
Fair Value in €	14.25	10.01	4.29	1.29
based on the following assumptions:				
Average maturity in years:	4.5	4.5	4.5	4.5
Fluctuation rate	0 %	0 %	5 %	5 %
Dividend	keine	keine	keine	keine
Risk-free interest	5.575 %	4.76 %	4.90 %	5.4 %
Volatility	37.79 %	42.39 %	46.45 %	78.79 %

Options' value is spread across the conversion period as expenses and booked as counter-position to the capital reserves. The second tranche was returned to the Company in 2001. The expenses incurred by the option holders who left the Company before the blocking period of the issued options had expired were reversed in the years of their departure.

	1 st tranche	3 rd tranche	4 th tranche	5 th tranche	1 st tranche	Total units
Outstanding options at January 1, 2006	34,581	0	18,953	14,333	5,850	73,717
Weighted average remaining maturity at January 1, 2006, in months	0	0	0	8	20	11
Weighted average exercise price at January 1, 2006, in €	22.00	0.00	36.10	12.41	2.96	22.25
Outstanding options at December 31, 2006	0	0	18,953	14,333	5,850	39,136
Exercisable options at December 31, 2006	0	0	18,953	14,333	5,850	39,136
Options issued in 2006	0	0	0	0	0	0
Options exercised in 2006	0	0	0	0	0	0
Lapsed/returned options in 2006	0	0	0	0	0	0
Expired options in 2006	34,581	0	0	0	0	34,581
Weighted average remaining maturity at December 31, 2006 in months	0	0	0	0	8	8
Weighted average exercise price at December 31, 2006, in months	0.00	0.00	36.10	12.41	2.96	22.47

In the years 1999 to 2006 a total of 284,326 stock options were returned. These were not awarded again. In 2006, no further stock options were returned. Option rights from the first tranche expired in 2006. Due to reducing subscribed capital by amalgamation of shares without capital repayment by half, the number of shares reduced to one half share, for which one option right each may be purchased at exercise price. Because at 31 December 2006 all entitled employees left the company expenses were also booked for the remaining duration due to the stock option plan (concerns tranche no. 5 only). The expenses in connection with the stock option plan relate to the various functional areas as follows:

€ 000	2006	2005
Costs of goods sold	0	0
Sales costs	11	45
Research and development costs	0	7
General administrative costs	0	33
	11	85

(11) Trade accounts payable

€ 000	31.12.2006	31.12.2005
Trade accounts payable	281	498
Liabilities from deposits received	0	64
	281	562

(12) Liabilities towards associated companies

Liabilities amounting to €1,693 concern Dowlake Microsystems.

(13) Tax reserves

€ 000	Position at 01.01.2006	Used	Dissolved	Allocated	Position at 31.12.2006
Reserve for pre-tax costs of floatation	138	0	138	0	0
Other reserves	0	0	0	7	7
	138	0	138	7	7

In view of current case law the reserve for advanced taxes (VAT) on account of the cost for IPO were dissolved.

(14) Other reserves

€ 000	Position at 01.01.2006	Used	Dissolved	Allocated	Position at 31.12.2006
Sales reserves	137	84	53	25	25
Outstanding staff remuneration	161	66	85	189	199
Miscellaneous reserves	378	352	6	324	344
Restructuring reserve	3,061	2,958	38	0	65
	3,737	3,460	182	538	633

The sales reserves comprise mainly guarantee reserves. Personnel reserves contain primarily Management Board salaries (€117,000), national insurance contributions claimed by Deutschen Rentenversicherung Bund (€47,000) as well as expenses for employers' liability insurance association (€12,000). The miscellaneous reserves include mainly provisions for outstanding bills (€ 264,000), for costs of drawing up the annual financial statements (€ 86,000) and for costs of publishing the Annual Report (€ 20,000) and cost of litigation (€114,000). The restructuring reserve includes mainly expenses for the closure of PANDATEL Israel (€42,000) as well as legal fees (€21,000).

(15) Other short-term liabilities

€ 000	31.12.2006	31.12.2005
Social insurance contributions	12	142
Other	346	404
	358	546

(16) Sales

Sales of € 9,083,000 (previous year € 12,784,000) declined by 29% compared to previous year, which was in line with the forecast announced in the semi-annual report. This decline is based on major reduction of product variants, elimination of products with low sales volumes and concentration on key customers. In the reporting year 2006 portion of foreign sales improved to 87.3.0% after 79.0% in the previous year. EMEA (Europe, Middle East, Africa) was again the strongest region with 69.0% (previous year 72.4%) supported by domestic sales, France and Great Britain. Asia Pacific performed similarly

strong as in 2005 (24.5%) achieving 24.7%. With a share of 0.8%, the Americas (North and South America) again were last after 3.1% in the previous year.

(17) Cost of goods sold

€ 000	2006	2005
Raw materials and supplies	6,620	5,676
Goods and services purchased	515	1,145
Personnel costs	233	1,426
Other attributable costs	7,368	8,247

The expenses regarding goods and services purchased decreased in the year under review not in line with the decline in sales. A relatively high material usage ratio is particularly attributable to set-up cost associated with production transfer to Shanghai as well as with starting marketing third-party products associated with initially low margins for market development. In addition in the course of starting production in Shanghai, it was necessary to compensate unexpected scrap with material provision free of charge. This resulted in a gross margin unexpectedly deteriorating from 35% in 2006 to 19% in 2006. For 2007, the gross margin is expected to improve significantly due to removing double procedures.

(18) Sales costs

The sales costs totaling € 1,582,000 (previous year € 3,938,000) consist mainly of personnel costs at the amount of € 831,000 (previous year € 1,320,000), losses on receivables and adjustments of value of € 237,000 (previous year € 441,000) and advertising and marketing costs of € 387,000 (previous year € 843,000).

(19) Research and development costs

The research and development costs include development costs for the new product YUMIX and costs for the further development of existing products. Since the volume of sales realized through the newly developed products was far lower than expected, no additional development costs were stated in 2006 as assets in the balance sheet.

(20) General and administrative expenses

The general administrative expenses contain costs in connection with the Company's stock exchange listing of € 273,000 (previous year € 261,000). These relate to investor relations services, the admittance fees payable to Deutsche Börse AG, the costs for the Annual General Meeting and the costs for the semi-annual report and the consolidated financial statements.

(21) Restructuring expenses

€ 000	2006	2005
Personnel expenses	0	2,370
Provisions for rents	0	593
Depreciations on intangible assets	430	0
Depreciations on leasehold fixtures	0	208
Other	0	278
Inventory scrapping	967	0
	1,397	3,449

Regarding the background of restructuring expenses in fiscal year 2006, please refer to the statements und (1) tangible assets, intangible assets, financial assets and (3) inventory.

(22) Other income / other expenses

€ 000	2006	2005
profits from disposals of fixed assets	188	27
Non-cash remunerations	0	36
Income from the release of reserves		
Accruals	320	59
Other income	5	119
Less:	513	241
Accounting losses from disposals of fixed assets	-417	-223
Other taxes	0	0
Other operating expenses	0	-16
	-417	-239
	96	2

(23) Interest income/expenses

€ 000	2006	2005
Income from securities and lendings carried as financial assets	0	7
Other interest and similar income	61	24
Interest income from fixed-term deposits	162	202
Total interest income	223	233
Interest expenses from short-term liabilities	-333	-1
Guarantees	0	-3
Total interest expenses	0	-4
	-110	229

Interest paid basically results from discounting corporate income taxation (€331,000) stated as other long-term assets.

(24) Currency gains/losses

€ 000	2006	2005
Currency gains from foreign investments loans and deposits	779	117
Currency gains from open foreign-currency accounts receivable and payable	0	106
Currency losses from open foreign-currency accounts receivable and payable	0	0
Currency losses from debtors/creditors	-796	-932
	-17	-709

(25) Income taxes

The results before income tax of all the companies included in the consolidated financial statements for 2006 are -€ 6,302,000 (previous year -€ 15,092,000). These results are subject to taxation in Germany, Singapore, the USA and Israel. PANDATEL AG and its subsidiary in Singapore recorded a loss in 2006, while Lightmaze Solutions AG and the U.S. subsidiary reached a small profit. The Israel subsidiary was no longer operational in the reporting period and reported a result of zero. The income tax income/expenses contain current and deferred taxes:

€ 000	2006	2005
Current taxes	1,405	-11
Deferred taxes	156	-1,909
	1,561	-1,920

In 2006 the Company was subject to corporation tax at a rate of 25% of taxable income plus the German solidarity surcharge of 5.5% of the tax bill. This results in a combined tax rate of 26.375% for 2006 (previous year also 26.375%). Moreover, the Company is subject to trade tax which is deducted when calculating the profit for corporation tax purposes. Thus the effective trade tax for 2006 was 18.699% (previous year 19.028%). The combined tax rates for 2006 were therefore 40.14% (previous year 40.38%), taking into account the deductibility of the trade tax. The change in trade tax is due to the relocation from Hamburg to Hanover. The following table explains the most important differences between the expected tax bill for corporation tax plus the German solidarity surcharge for the years 2006 and 2005, and the actual tax bill incurred:

€ 000	2006	2005
Expected tax yield/expenses	-2,530	-6,095
Non-deductible expenses		
Stock option plan	5	34
Other	5	13
Value adjustments pursuant to Art. 60 EStDV		
investments in securities of affiliates	415	2,005
loans to subsidiaries	0	-545
Accruals	-755	0
Value adjustment for deferred tax losses carried forward	2,834	6,326
Adjustment for deferred taxes previous years	-196	183
Activation of corporate income tax deposit	-1,412	0
Deviating tax rate abroad	59	66
Other	14	-67
	-1,561	1,920
Effective tax rate	-24.8%	12.7%

At the balance sheet date PANDATEL AG had corporation tax loss carry forward of € 38,015,000 (previous year € 32,456,000) and trade tax loss carryovers of € 38,526,000 (previous year € 32,967,000). These can be carried forward in full. Accumulated deficits of PANDATEL were adjusted to the full amount due to its persistent loss situation.

In addition, the accumulated deficits of PANDATEL are at risk because of the transmission of more than 50% of its shares to Dowlake Venture. In the USA, loss carry forward exists of € 4,792,000 (previous year € 4,792,000). These have been fully value-adjusted in each case, since it appears uncertain whether the tax authorities will recognize them. These loss carry forwards expire in the years 2011 to 2024.

The subsidiary in Singapore reported a loss for 2006 of € 362,000 (previous year a loss of € 354,000). For 2006 a tax loss carry forward of € 1,298,000 (previous year € 972,000) remains, use of which is not subject to any limitation. In this context too, value adjustment was made to the full amount due to uncertain future expectations.

Deferred taxes carried as assets and liabilities result from the following items:

€ 000	31.12.2006	31.12.2005
Deferred taxes carried as assets:		
Inventories	0	19
Provisions	0	279
Loss carried forward AG	15.356	13.204
Loss carried forward USA	1.916	1.917
Loss carried forward Singapore	268	214
Corporation tax credit balance pursuant to § 37 KStG	0	1.412
Receivables	0	2
	17.540	17.047
Value adjustments	-17.540	-16.747
	0	300
Deferred taxes carried as liabilities:		
Securities	5	0
Accounts receivable	0	61
Provisions	0	29
Development costs declared as assets	25	49
Tangible fixed assets	0	140
Intangible fixed assets	0	262
	30	541
Deferred taxes (net)	-30	-241
	(liabilities)	(liabilities)

Due to the changes in law published in late 2006, an entitlement exists on distribution of corporation tax deposits from the change from corporate tax credit method definitive taxation starting in 2008. For PANDATEL AG it amounts to €1,412,00 at the balance sheet date. The disclosure of discounted distribution claims is stated under other long-term assets.

(26) Earnings per share

The following table shows the calculation of the undiluted and diluted earnings per no-par value share:

€ 000	2006	2005
Numerator		
Group net loss/profit for the year	-4.741	-17.012
	-4.741	-17.012
Denominator		
Weighted average of outstanding no-par value shares in units	3.947.903	3.947.903
Diluting shares in accordance with the stock option plan	0	0
	3.947.903	3.947.903
Loss/profit per no-par value share in €/unit	-1,20	-4,31
Diluted loss/profit per no-par value share in €/unit	-1,20	-4,31

Options are not included if their issue price is higher than their average stock market price. If the number of shares outstanding decreases as a result of share capital amalgamation, the number of shares has to be accounted for all periods presented retroactively pursuant to IAS 33.64. A maximum of 39,136 options can have a diluting effect up to the year 2010.

(D) Other information

Cost of materials

€ 000	2006	2005
Expenses for raw materials and supplies	7,306	5,372
Expenses for services rendered	324	256
	7,630	5,628

Personnel expenses

€ 000	2006	2005
Wages and salaries	2,252	5,376
Social insurance contributions	406	958
Pension payments	0	1
	2,658	6,335

Rents and other financial obligations

Other financial obligations arise from rental and leasing contracts in the following amounts:

	€000
2007	38
2008	9
2009	9
2010	9
2011	2
After 2011	0

In 2007 and thereafter, PANDATEL could be faced with a potential obligation by a contingent takeover of Dowlake Microsystem's stock for production. This stock had a value of app. €2.1m by the end of 2006 and PANDATEL is obliged to buy it in case of termination of the joint marketing, service and supply agreements. Beyond, PANDATEL AG would have to pay a certain amount (to be negotiated) to shut off production, to lay off people, and to sell off production equipment. Dowlake Microsystems has an option to terminate this agreement if PANDATEL orders products worth less than €400,000 per months over a period of three months. For the months October to December, the monthly orders fell below €400,000 for each month. At presents, conditions are being discussed of terminating the „Joint Marketing, Service and Supply Agreements“ as well as royalty payments to PANDATEL if Dowlake sells products to PANDATEL on its own account. Presently, the amount of possible royalty payments depends on the amount of margin related to products.

Information on the business areas

The Company's reports are divided between primary and secondary segments. The primary segment reports break the Company's business down by geographical region, the secondary segment reports by product. In the primary segment reports that are broken down by region PANDATEL differentiates between the following reporting areas to which our customers are allocated according to their place of domicile:

- EMEA (Europe, Middle East and Africa)
- The Americas
- Asia Pacific

Results according to primary segments 2006

		EMEA	The Americas	Asia	Other	Total	Conversion	Group financials
Segment sales external	31.12.2006	6271	73	2241	498	9083	0	9083
	31.12.2005	9250	397	3137	0	12784	0	12784
Segment sales internal	31.12.2006	0	4	146	0	150	-150	0
	31.12.2005	4084	0	0	0	4084	-4084	0
Segment operating result	31.12.2006	-4206	-81	-325	0	-4612	-1563	-6175
	31.12.2005	-9633	-104	-170	0	-9907	-4705	-14612
Segment assets	31.12.2006	9099	0	105	0	9204	2288	11491
	31.12.2005	17685	138	1593	0	19416	-796	18620
Segment liabilities	31.12.2006	3073	0	43	0	3116	-114	3002
	31.12.2005	5487	3856	2507	0	11850	-6326	5524
Segment investments	31.12.2006	664	0	0	0	664	-	664
	31.12.2005	213	2	11	0	226	-	226
Segment depreciation (scheduled)	31.12.2006	514	6	184	41	745	-	745
	31.12.2005	1158	5	67	0	1230	-	1230
Segment depreciation (unscheduled)	31.12.2006	297	3	106	24	430	-	430
	31.12.2005	4557	0	0	0	4557	-	4557
Major non-cash expenses	31.12.2006	-886	-10	-317	-70	-1283	0	-1283
	31.12.2005	2355	0	0	0	2355	0	2355

Segment revenues under "others" refer to the supply of raw materials and supply to Dowlake Microsystems.

Due to the fact that the company's subsidiaries in the U.S.A., Israel and Singapore terminated their operational business it was not possible, compared to the previous year, to allocate all items of primary segment reporting of these companies directly. The categorizations "segment depreciation" and "major non-cash expenses" comply with the respective segments' sales shares. Pricing for intercompany transactions bear comparison with prices from non-related external parties. In addition, for the secondary classification PANDATEL breaks down its reporting into the following product segments:

- Connectivity
- Access Multiplexers
- Optical Systems.

The Connectivity Segment encompasses products for converting data or for linking companies. For example, it employs rack systems including management for modems and converters. The Access Multiplexers segment makes products for data bundling and accessing metro networks, e.g. SDH over IP or IP over SDH multiplexers. Complex wWDM systems for SAN applications belong in the Optical Systems segment. These include YUMIX, FOMUX, DWDM and CWDM systems as well as TDMs. The following table shows the secondary segmentation by business areas:

		Access Multiplexers	Connectivity	Optical Systems	Other	Total	Conversion	Group financials
Segment sales	31.12.2006	3019	4665	901	498	9083	0	9083
	31.12.2005	3889	6122	2773	0	12784	0	12784
Segment assets	31.12.2006	3907	6038	1166	645	11756	-265	11491
	31.12.2005	5883	9412	4314	0	19609	-989	18620
Segment Investments	31.12.2006	221	341	66	36	664	0	664
	31.12.2005	69	108	49	0	226	0	226

The segment assets and segment investments are calculated on the basis of the percentage contributions of the different business segments to the segment earnings. The share of total sales accounted for by the different business segments changed only slightly. It was mainly in the area of optical systems, which failed to meet earnings expectations, since the advanced but highly complex Yumix 4000 system produced by Lightmaze is employed in project business. The segment with the largest proportion of sales was again Connectivity Products, with 51.4% of total turnover. The contributions of Access Multiplexers and Optical Systems were 33.2% and 9.9% respectively.

Business relations with affiliated companies

Dowslake Venture Ltd. owns 53.11% of the Company's shares. PANDATEL AG and its direct subsidiaries (PANDATEL Inc., PANDATEL Asia Pacific Pte Ltd., PANDATEL Ltd. and Lightmaze Solutions AG) are therefore controlled by Dowslake Venture Ltd. PANDATEL AG has business ties with Dowslake Microsystems Corp., a subsidiary of Dowslake Venture Ltd., as defined in the joint marketing, service and supply agreement. Besides joint sales, marketing and development activities, this agreement also provides for any production and product support matters resulting from the production transfer from Hamburg to Shanghai. This means: In addition to the production of PANDATEL products at agreed prices, procurement, redesign, troubleshooting, etc. are also defined. All conditions and terms are at arm's length and appropriate services supplies have been received. All transactions between PANDATEL and Dowslake Microsystems are laid down in the following table:

Transactions Dowslake Venture – PANDATEL AG	€000
Management fee CEO Dr. Dan D. Yang	117
Transactions Dowslake Microsystems – PANDATEL AG	
Services of Dowslake Microsystems to PANDATEL	€000
Engineering support from Dowslake	231
Production set-up for Pandatel production	338
Production tooling for Pandatel production	90
Product development	229
Freight for material supply Dowslake	36
Material supply to PANDATEL	2,923
Travelling expenses (for engineers)	13
Compensation for increased scrap ratio	498
Total	4,358
Services PANDATEL to Dowslake Microsystems	€000
Supply of raw materials and supplies to Dowslake	498
Withdrawal of inventory from PDT stock Shanghai by Dowslake	98
Sales of finished products to Dowslake	7
Total volume	603

In addition, certain equipment was shipped to Shanghai and facilitates production of PANDATEL products. At 30 June 2006, the book value of this equipment amounted to app. €90,000. Equipment will be depreciated over the next 2.5 years. PANDA-

TEL does not charge a fee. The amount of open orders to Dowslake amounts to app. €1,532,000 at 31 December 2006. Dr. Axel Pfeifer supplied legal services to the company in the reporting period. For his advisory services 2006, Dr. Pfeifer charged app. €113,000.

Information on financial instruments

PANDATEL did not apply any foreign exchange transactions or other derivative financial instruments.

Key accounts

With the Company's two largest customers, sales were generated in the financial year of €1.6m (previous year € 2.0m), € 1.4m (previous year € 1.5m).

The sales to these customers related to the segments Connectivity Products at € 1.55m (previous year € 2.05m) and Access Multiplexers at € 1.45m (previous year € 1.48m).

Payroll

The average number of persons employed by the Company in the year under review changed compared with the previous year as follows:

	2006	2005
Salaried staff	67	88
Wage earners	4	32
	71	120

Company Boards

The Management Board is composed of the following: Dr. Dan D. Yang, Shanghai, Chairman & Mr. Thomas Becker, Calw (until April 30, 2006)

In 2006 the emoluments of the Management Board totaled € 230,000 (previous year € 600,000). Of this €117,000 account for Dr. Dan D. Yang and €113,000 for Mr. Becker. Both salaries are fixed and they did not receive any other form of compensation. As in the previous year, no stock options were awarded. Mr. Becker left the company as scheduled without receiving any compensation payments.

The Supervisory Board consists of the following persons:

Dr. Axel Pfeifer, Chairman of the Supervisory Board (until December 17, 2006),

Dr. Ing. Steffen Leistner (until March 27, 2006)

Mr. Alex Fang (since January 19, 2006, vice chairman since February 22, 2007)

Dr. Jozef Straus (until December 17, 2006)

Mr. Manfred Wissmann (since February 8, 2007, chairman since February 22, 2007)

Mr. Stefan J. Weidner (since February 8, 2007)

Dr. Axel Pfeifer is also Supervisory Board chairman of PROUT Aktiengesellschaft, Darmstadt.

Mr. Fang is also Supervisory Board Member of Osram Lighting Center Systems Ltd., Hongkong, China and Diyician.com Ltd., Hongkong, China.

By decision of the Hamburg District Court on January 19, 2006, Dr. Axel Pfeifer, a lawyer, and Mr. Alex Fang, an investment banker, were appointed to the Supervisory Board. At the Supervisory Board meeting on January 30, 2006 Dr. Axel Pfeifer was elected Chairman of the Supervisory Board. Dr. Axel Pfeifer held this position until resignation from his office as Supervisory Board member on December 17, 2006.

Mr. Leistner resigned effective March 27, 2006.

Dr. Jozef Straus was also appointed Supervisory Board Member during the extraordinary shareholders' meeting of the company on March 27, 2006. He held his position until resignation from his office on December 17, 2006.

The local court Hanover appointed Mr. Manfred Wissmann and Stefan J. Weidner members of the Supervisory Board. On its constituent meeting on February 22, 2007, Mr. Manfred Wissmann was elected Supervisory Board chairman and Mr. Alex Fang Vice Supervisory Board chairman.

Mr. Manfred Wissmann is also Supervisory Board member of Exept AG, Reilingen, as well as of TEC Consult Holding AG, Mörlenbach.

The emoluments of the Supervisory Board amounted to € 17,500 (previous year € 33,000). Of this, € 7,500 were paid to Dr. Pfeifer, € 5,000 to Mr. Alex Fang and € 5,000 to Dr. Jozef Straus.

The members of the Supervisory Board are elected until the close of the Annual General meeting that approves its actions for the fourth year following the commencement of its term of office.

	Number of shares = amount of nominal capital			Number of stock options	
	31.12.2006	31.12.2005	Percentage of nominal capital	31.12.2006	31.12.2005
Management Board					
Thomas Becker	0	0	0.00	0	0
Dr. Dan Dan Yang *	0	0	0.00	0	0
Supervisory Board					
Dr. Axel Pfeifer	0	0	0.00	0	0
Dr. Steffen Leistner	0	0	0.00	0	0
Alex Fang	0	0	0.00	0	0
Dr. Jozef Straus	0	0	0.00	0	0
Total board members	0	0	0.00	0	0

Dr. Dan D. Yang holds 50% in Dowlake Venture Ltd.

Particular events following the end of the financial year

Detailed information on the events following the end of the financial year is contained in the Management Report.

Disclosure in accordance with § 25 para. 1 WpHG (German Securities Trading Act)

The company received the following disclosures: The following reports have been submitted concerning ownership of more than 5% of the shares of PANDATEL AG:

	Shares at 31.12.2006
Shareholder	in %
Dowlake Venture Ltd.	53.11

The following notifications were received by the Company:

January 2006

AUGUSTA Technologie AG, Wilhelm-Leuschner-Str. 9-11, Frankfurt am Main, informed the Management Board in accordance with § 21 para. 1 WpHG that its share of the voting rights in PANDATEL AG, Hamburg, had fallen below the statutory notification levels of 10% and 50% with effect from December 30, 2005, and was now 0.0% (0 shares).

April 2006

Dr. Elke Jahn, Höchberg informed the Management Board in accordance with § 21 para 1 WpHG that her voting rights in PANDATEL AG, Hamburg had fallen below the statutory notification level of 5% and was now 3.13% on April 6, 2006. Of this 0.30% of voting rights are attributable to Dr. Jahn in accordance with § 22 para. 2 WpHG.

Dr. Niraj Agrawal, Höchberg informed the Management Board in accordance with § 21 para 1 WpHG that her voting rights in PANDATEL AG, Hamburg had fallen below the statutory notification level of 5% and was now 3.13% on April 6, 2006. Of this 2.83% of voting rights are attributable to Dr. Agrawal in accordance with § 22 para. 2 WpHG.

May 2006

Dowlake Venture Ltd., a company registered in the British Virgin Islands (Reg. Office Offshore Incorporation Ltd., PO Box 957, Roadtown, Tortola, BVI, with the postal address 3206 Scott Boulevard, Santa Clara, CA 95054, United States of America) ("Dowlake"), informed the Management Board in accordance with § 21 para. 1 WpHG that its share of the voting rights in PANDATEL AG, Hamburg, had risen above the statutory notification level of 50% with effect from April 28, 2006, and was now 53.11% (4,193,784 no-par value shares).

In addition, Dr. Dan Yang and Mr. Zibin Lu, both resident at 2388 Hong Qiao Road, C-37 Dynasty Villa, Shanghai 100335, People's Republic of China, informed the Management Board in accordance with § 21 para. 1 WpHG that their respective joint share of the voting rights in PANDATEL AG, Hamburg, had risen above the statutory notification level of 50% also with effect from April 26, 2006, and was now 53.11% (4,193,784 no-par value shares).

Ownership by the two above-named persons of 4,193,784 no-par value shares of PANDATEL AG of each 53.11% of the voting rights of PANDATEL AG via their jointly owned company Dowlake Venture Ltd. is confirmed in accordance with § 22 para. 1 no. 1 WpHG and, in view of their mutual agreement to act in unison, also in accordance with § 22 para. 2 WpHG.

Information on the auditing company

The auditing company Dr. Ebner, Dr. Stolz und Partner GmbH, Hanover, was entrusted with the task of auditing the Group's annual financial statements. Its total fees for 2006 were as follows:

Audit of financial statements	€76.681,15
Other certifications and evaluations	€31.161,78
Tax advice	€11.142,59
Other services	€2.799,49
Total	€121.785,01

The other services consisted mainly of examining the semi-annual report, support in connection with an inspection of Deutsche Prüfstelle für Rechnungslegung (DPR – German Inspection Authority for Accounting) as well as various economic advisory services.

Declaration regarding the Corporate Governance Code

In March 2007 the Executive and Supervisory Boards submitted the Declaration of Compliance as required by § 161 AktG and made it available to shareholders on the PANDATEL AG Internet homepage under www.PANDATEL.de.

Hanover, 13 June 2007

Dr. Dan Dan Yang
Chairman of the Management Board

Thomas Becker
Member of the Management Board

Auditors Report

We have audited the consolidated financial statements prepared by PANDATEL AG, Hanover, comprising the balance sheet, the income statement, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year

from January 1 to December 31 2006. The preparation of the consolidated financial statements and the group management report in accordance with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315a Abs. [paragraph] 1 HGB are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations. In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of

operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Without restricting our evaluation, we would like to refer to the management group report. The sections risk management and outlook contain risks that could jeopardize the company's continuation. Among these risks are in particular a high sales percentage of older products, a not yet achieved market acceptance of new products and the further reduction liquidity reserves. In addition, Dowlake Venture Ltd., St. Clara, U.S.A. demanded to include into the agenda of the next general meeting among other things a resolution on liquidation of the company.

Our report is based on our dutiful annual audit finished on 23 March 2007 and our re-audit relating to changes in balance sheet items "Subscribed Capital" and "Capital Reserve", to changes in items "Withdrawal from Capital Reserve" and "Revenues from Capital Decrease", to earnings per share, to statement of changes in shareholders' equity, to going concern, to shareholders' equity, granted stock options and earnings per share and other financial obligations in the notes as well as data on capital measures/structure of shareholders' equity, results after balance sheet date and outlook in the management report. We refer to the reasons of changes by the company in the updated notes in paragraph "Preliminary Notes". The re-audit did not lead to any objections.

Hanover, March 23, 2007/June 14, 2007

Dr. Ebner, Dr. Stolz und Partner GmbH

Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft

Wilfried Steinke Hans-Peter Möller

Wirtschaftsprüfer Wirtschaftsprüfer

[German Public Auditor]

[German Public Auditor]

Glossary

Backbone	Powerful supra-regional main data line that links up many sub-networks
Bandwidth	Transmission capacity of communication systems, measured in data per second
Broadband technology	Transmission method in which the bandwidth of the transmission medium is broken down into several frequency bands that specific tasks (sending/receiving) or types of communication are allocated to
Carrier	Network operator that provides transport services to other companies for a fee
CESoP	Circuit Emulation Services over Package – technology for transporting TDM data streams via packet-based networks
C-MUX-155	Optical multiplexer which transmits voice and data information via SDH/SONET networks in very fine speed gradations with the help of >Virtual Concatenation Technology
Connectivity	Ability of systems to communicate with each other via a network
Converter	System that converts data set in a particular format into another format
COP-FE	TDM multiplexer for the >CESoP standard, which transmits voice and data information via IP/Ethernet networks
Cross-connect	Optoelectronic component which switches between two optical channels depending on individually definable parameters
CWDM	Coarse WDM – Method that uses broader channels and is therefore more cost-efficient than >WDM or >DWDM
DSL	Digital Subscriber Line – Transmission technology for broadband Internet access via the telephone network
DWDM	Dense Wavelength Division Multiplexing – Special form of >>WDM where the individual wavelengths are positioned very close to one another and thus ensure even more efficient use of the fiber optic cable
Ethernet	Transmission protocol for local area networks (>LANs)
First mile access	>Last mile access
G.SHDSL	>SHDSL; the “G ” stands for a standardization series of the International Telecommunication Union
Gigabit Ethernet	Ethernet variant with a maximum transmission rate of 1000 Mbit/s, corresponding to 1 Gbit/s
GSM	Global System for Mobile Communications – European mobile radio telephone standard
Integrated Access Device	Integrated device for network access – multifunctional device
Interface converter	>Converter for the copper area; converts electronic signals from one interface to another
Internet Protocol (IP)	Non-manufacturer-specific >transmission protocol for cross-network communication
Internet Service Provider	>Service provider for Internet access, abbreviated ISP
Inverse multiplexer	>Multiplexer that splits a high-speed channel into several independent channels with low transmission speed or combines several independent data streams to form one broadband channel

LAN	Local Area Network – Computer network that is installed at the user 's end and is geographically limited
Last-mile access	The last mile is the connection range between the network exchange and the home exchange; frequently what is meant is the copper line between telephone company and end customer
MACS4000	Management system for PANDATEL products with which all local and remote components in a network can be centrally operated, monitored and configured
Mbit/s	Megabit per second – Data transmission speed in million bits per second
Meshed network	Meshed networks – In a meshed network, the nodes of a network can be linked to each other at random; the data can reach their destination using any routes, and these routes can be individually defined
Metro Ethernet	Metro networks equipped with >Ethernet-based services; virtual >LANs, for example, can be established by means of Ethernet connections, allowing several company locations to be integrated into a homogeneous network
Metro network	Metropolitan Area Network – Telecommunication network that covers a city or region
Modem	Modulator/Demodulator – Device that converts digital data into suitable signals for transmission over analog lines and at the other end converts the signals back into digital data
Multiplexer	System that enables the simultaneous transmission of several mutually-independent data streams down one and the same physical channel (copper cable, fiber optic line)
Multi-services	Merging of different solutions in convergent networks
Network management	System for managing a network as well as its resources and components
Network nodes	Connecting point between more than two transmission routes in a computer network, for example a >multiplexer or >router
Network operator	Organization or company which operates and maintains a network and which places it at the disposal of third parties for use – usually for a charge
OEM	Original Equipment Manufacturer – Manufacturer that buys products from other manufacturers and integrates them into its own products; sometimes the original manufacturer is termed OEM
OEM product	Product from an external manufacturer that a company includes into its own product portfolio and sells under its own label
Optical systems	Instruments and systems that enable the >optical transmission of data
Optical transmission	Data transmission via fiber optic line or synthetic fiber with light as the signal carrier
Packet-based networks	Networks for the fast and reasonably priced transport of large quantities of data. In packet-based networks, >Ethernet technologies and the >IP protocol are mainly used today
PSN	The abbreviation for "Packet Switched Network"
QoS	Quality of Service in communication networks
Redundancy	This designates the additional presence of the functionally identical or comparable resources of a technical system which are not required in normal operation and are only used in the event of a fault
Routing	In telecommunications: a method of conveying news between networks; routers convey data packages in the best possible way from one network to another

SAN	Storage Area Network – Centrally-managed high-speed storage network which provides several servers with simultaneous storage access and increases error tolerance thanks to its structure
SDH	Synchronous Digital Hierarchy – Standard for the high-speed transmission of data via fiber optic networks
SDSL	Symmetric Digital Subscriber Line – >>DSL with symmetric transmission speed, i.e. upload and download speed are identical
Service provider	Company that provides communication or storage services with network access, e.g. Internet service provider
SHDSL	Single Pair High Bit Rate Digital Subscriber Line – Symmetric >>DSL method for copper double cores
SONET	Synchronous Optical Network – international standard for single-level multiplexing of high-speed networks with transmission rates of 44 Mbit/s and higher; basis of the SDH standard
Storage Area Network	>SAN
Switching	Means by which a transmission path is switched between sender and receiver
TDM	Time Division Multiplexing – Technology in which signals for different messages are transmitted in a time—interleaved pattern down a single channel
Topology	In a computer network, the topology represents the structure of the connections between the individual >network nodes
Transceiver	Acronym derived from Transmitter/Receiver – a combined transmitter and receiver
Transmission protocol	Definition of the way in which information is to be exchanged between two systems
Value added reseller	Reseller with additional service
Virtual concatenation	Technology that allows the efficient transport of large data bandwidths via >SDH
VoIP	Voice over IP – Abbreviation for IP telephony; designation for telephony using a computer network on the basis of the >Internet Protocol (IP)
WDM	Wavelength Division Multiplexing – Technology which uses laser light of different wavelengths ((colors) to simultaneously transmit several communication channels down a single fiber optic line
xWDM	Collective term for the multiplexing technologies >WDM, >CWDM and >DWDM
YUMIX	Product platform for intelligent optical networks, by the PANDATEL subsidiary Lightmaze Solutions

PANDATEL

86 countries, 800+ customers, 100,000+ units of communications products deployed in today's worldwide networks.

Our History

- 1987: Pandatel formed as Pan Dacom Telekommunikation GmbH
- 1999: Pandatel went public, listed at the Prime Standard of Frankfurt Stock Exchange
- 2004: Pandatel acquired Lightmaze Solutions AG, a specialist in optical metro WDM transport systems
- 2005: Dowslake Venture Ltd., a major shareholder of Dowslake Microsystems, acquired 49.98% stake in Pandatel AG
- 2006: Pandatel is in the process of merging with Dowslake Microsystems, headquartered in Santa Clara, California. Dowslake has a fully owned operations center in Shanghai, China.

Up to 2006: Pandatel deployed more than 100,000 units of communications products, with 800 satisfied customers in over 86 countries.

Our Focus

Leveraging on our technology and know-how, working with hundreds of customers worldwide, we focus on providing cost-effective network solutions to network operators and service providers in following areas: enterprise, security, military, home and local access.

Our Commitment

We commit to make continuous improvement on our products, operations process and our support networks. We commit to work on issues and problems to reach our goal – to meet and exceed customers' expectations.

The German version of this annual report is legally binding.

Ethernet Solutions – from Optical to Last Mile



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