paragon®

Neue Kraft, bewegende Ideen

Quarterly Report
Third Quarter 2009

Highlights in the first nine months of 2009

- **Still impacted by the crisis in the automotive industry**
- **40 % drop in sales compared to the previous year**
- **Success with the cost reduction programme**
- **Operating earnings increase once again**

The first nine months at a glance

in EUR thousands	Q3 2009	Q3 2008	Change in %
Sales	54,114	90,234	- 40 %
EBITDA	1,528	16,357	- 92 %
Adjusted EBITDA*	2,940	17,720	- 83 %
EBIT	- 2,463	6,921	- 136 %
Net earnings for period	- 6,670	617	- 1,182 %
Earnings per share in EUR	- 1.62	0.15	- 1,180 %
Liquidity in millions	1,450	6,141	- 76 %
Employees	510	601	- 15 %

* EBITDA adjusted for restructuring costs (including scrapping, consultancy costs, severance pay)

Events after the Balance Sheet Date / Current Status

Since this quarterly report is only being published in August of 2010, we have elected to present it in a form that on the one hand traces the course of business from January 1 to September 30, 2009, and on the other takes into consideration the events in the subsequent period. As a result the outlook for the future refers to the years 2010 and 2011. More detailed comments in this respect and on the later insolvency, that lasted from January 1, 2010, to May 31, 2010, can be found in the Group management report of the 2009 annual report.

Overall Economic Conditions

The global economy sustained its upwards trend in the third quarter of 2009. The main reason for this turnaround was the stabilization of the financial markets due to intervention by central banks and the stimulus effect of government economic programmes. Production started up again as the prolonged depletion of inventories came to an end in many areas.

In the case of the automotive industry stabilization continued in foreign markets. At the same time order receipts from the domestic market declined less than expected.

Business Developments in the paragon Group

The sales collapse brought about by the financial and automotive industry crises, as well as the negotiations with banks, led to a difficult situation at paragon AG, resulting in the conscious initiation of insolvency proceedings on October 5, 2009. Consolidated sales nose-dived in the first nine months of the year by 40 % to EUR 54.1 million (prior year: EUR 90.2 million).

In the third quarter of 2009 paragon experienced noticeable growth rates as manifested by rising order levels, as did other suppliers. Against the backdrop of the strained liquidity situation, however, the Company was forced to curb material purchases. paragon was able to continue to service all customers, but built up higher backlogs in its order levels.

The Company's focus was on continuing the restructuring process. The goal of the restructuring measures is to adapt paragon to lower sales figures by reducing fixed costs. At the same time discussions with financiers secured valuable capacity in the financing arena. In the third quarter paragon eschewed expensive marketing measures as part of its cost-conscious approach and instead relied on personal dialogue with key customers and suppliers.

In addition to numerous other measures, the sale of activities in the US, as well as the closure of the subsidiary in Japan and foreign branches in Italy and France, contributed to cost reductions. Despite these efforts, discussions on the subject of financing were not always positive. Again and again individual banks torpedoed agreements which were almost within reach, so that finally the Managing Board initiated insolvency proceedings on October 5, 2009. This dashed paragon's hopes of restructuring without resorting to insolvency.

The two business segments – Automotive and Electronic Solutions – continued to develop in varied fashion. While the predominant Automotive segment was forced to deal with a steep decline in sales of 41.0 % compared to the previous year, the Electronic Solutions segment evidenced a drop of 35.3 %.

Financial Position and Net Assets

Total assets as at September 30, 2009, fell to EUR 49.1 million compared to EUR 53.5 million as at December 31, 2008.

The decrease in non-current assts to EUR 23.3 million (prior year: EUR 26.6 million) is based on customary asset wear and tear. Current assets in tandem dropped to EUR 25.8 million (prior year: EUR 27 million), despite the fact that trade receivables increased from EUR 4.4 million to EUR 8.3 million. Due to measures designed to increase liquidity, inventories were depleted by over EUR 4.2 million.

Non-current liabilities fell considerably from EUR 52.6 million as at December 31, 2008, to a mere EUR 14.1 million. This reduction simply represents a reclassification of non-current to current financing elements. The reason for this is the acceptance of the insolvency plan on April 16, 2010, which establishes that this share will be serviced proportionally via the creditor table and, therefore, has a term of less than a year. Current liabilities in contrast have risen from EUR 55.1 million to EUR 95.8 million as at June 30, 2009.

Operating cash flow indicates the reversal in operating activity. It rose from EUR 0.5 million on June 30, 2009, to EUR 1.2 million at the end of the third quarter. Operating cash flow was EUR 11.2 million in the previous year.

Results of Operations

The most difficult automotive industry crisis in post-war history left deep traces in paragon's results of operations as well. Personnel expenses dipped in the first nine months of the current fiscal year by 20 % from EUR 21.6 million to EUR 17.3 million. This shows the effects of the cost reduction programme, especially since personnel expenses still showed a rise in the first quarter of 4 %. In relation to slumping sales the cost of materials ratio dropped disproportionately compared to the same quarter of the previous year by 8 %.

Due to the relative lack of liquidity the paragon Managing Board implemented a variety of measures in order to increase liquidity. In addition to shortening payment terms from customers and extending payment targets for suppliers, the Company endeavoured in particular to reduce inventory levels and transform them into liquidity. These measures are reflected in inventory changes. Write-offs were 58 % lower than in the previous year. The reason for this change relates to the write-offs that were undertaken in the Group as at December 31, 2008.

Even though financing expenses were significantly reduced due to the standstill agreement among the banks, paragon was still not able to show positive EBIT in the third quarter. The sales lost due to the financial and automotive industry crises could not be entirely offset by cost reductions. EBIT is currently at EUR -2.5 million (prior year: EUR 6.9 million).

Net income for the period at the end of the year under review according to IFRS amounted to EUR -6.7 million (prior year: EUR 0.6 million). Here, too, the percentage drop in relation to sales was reduced in comparison to the previous quarters of this year. EBITDA was EUR 1.5 million as at September 30, 2009. paragon also continued to increase its operating earnings – EBITDA adjusted for restructuring costs. The Company achieved a positive value of EUR 2.9 million in the first nine months, admittedly after a figure of EUR 16.4 million in the same period in the previous year.

Segment Report

The Automotive segment with its two divisions – Sensor/Actuator and Cockpit Systems – suffered considerable sales losses in the first nine months of 2009. Sales revenues plunged by 41.0 % to EUR 44.2 million (prior year: EUR 74.9 million). The share in total sales was 83.0 %. The Company had to deal with a sharp drop of 147.5 % in the first nine months of 2009 to EUR -2.8 million (prior year: EUR 5.9 million).

The Electronic Solutions segment, too, evidenced a sales slump due to the difficult overall economic conditions. Sales fell in the first nine months by 35.3 % to EUR 9.9 million (prior year: EUR 15.3 million). EBIT deteriorated by 70.0 % to EUR 0.3 million (prior year: EUR 1.0 million).

Research & Development

Research and development expenses were down from EUR 8.2 million to EUR 5.8 million against this backdrop of financial developments. In the Sensor/Actuator division the air quality improvement system, Air Quality Improver (AQI), was readied for its first use in series production. Another important step took place in development work on a novel start-stop sensor. Activities related to the belt microphone belt-mic, the Bluetooth hands-free system and on-board clocks continued in the Cockpit Systems division.

Employees

The paragon Group employed 510 people world-wide as at September 30, 2009. This reflects the personnel reductions planned for the current fiscal year. The work-force still numbered 639 people as at December 31, 2008. The current status does not, however, show the final figures, since work-force adjustments will continue. 67 employees were engaged at headquarters in Delbrück and 270 at the Suhl production site. As at September 30, 2009, paragon employed 10 temporary workers.

Investor Relations

Capital markets benefited from the economic recovery in broad portions of the global economy. The German Stock Index (Deutsche Aktien Index – DAX) rose significantly for instance. The leading index rose by almost 800 points to 5,675 in the third quarter.

Due to paragon's special situation its share moved in the opposite direction. On July 14, 2009, the security slipped below the 2-Euro limit (EUR 1.97), but posted gains by the end of the quarter. On September 30, 2009, the paragon share was quoted at EUR 2.25 (information based on XETRA).

During fiscal 2009 communication with the financial markets was marked by special events. Due to the inability to predict paragon's continued operation as a going concern, the auditor was not able to provide an audit certification on the 2008 annual report prepared by the Company within the deadline. As a result of the absence of this certification, paragon was not in a position to inform financial markets in the manner that had been customary hitherto. The Managing Board had no guarantee at any time during 2009 that the financial data published did not reflect the final status at the time of publication.

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Sector:	Technology

Risk Report

paragon AG's Managing Board always assesses risks in close coordination with the Supervisory Board. The dramatic change in release orders from car manufacturers during the economic crisis had radical effects on all suppliers.

During the course of 2009 the situation – due to the failure of the banks to come to an agreement – came to a head to such an extent that the Managing Board on October 5 initiated insolvency proceedings with the goal of implementing an insolvency plan process. Given the positive outcome of these proceedings and the end of the insolvency as at June 1, 2010, as well as rising demand from automobile manufacturers and a clear drop in debt, the Managing Board believes there is a very good chance that the Company's history will take a positive turn after this most difficult crisis. At the time of publication of this report, no additional risks have been identified that might jeopardize the Company's continued existence.

Outlook

Given the context of the August 2010 publication period the outlook relates to the years 2010 and 2011. Interim findings are incorporated so as to provide an up-to-date and qualified forecast.

The Institut für Weltwirtschaft (ifw – Kiel Institute for the World Economy) forecasts recovery for the economy during 2010, but only at a moderate rate. The financial and economic crisis of the years 2008 and 2009 is gradually being overcome. The pace of expansion, however, differs greatly in individual regions around the world. While in some emerging markets there is even a risk of the economy overheating, the utilization of economic capacities on the whole in industrial countries continues to be low.

The Verband der Automobilindustrie (VDA – German Association of the Automotive Industry) presents a positive assessment of developments in the international markets and economy. The global automobile market is expected to increase by approximately 4 % to over 57 million passenger cars in 2010. China will initially play a decisive role, even though it is unlikely that the country can maintain the high growth rates of the first quarter – with a rise of more than three quarters to almost 2.8 million units – throughout the whole year. German manufacturers are superbly positioned in the growth markets of China and the US. The majority of automotive suppliers can anticipate double-digit growth rates this year according to VDA information.

The Managing Board of paragon AG envisions a future with excellent business prospects now that the insolvency has been suspended. These forecasts are bolstered not only by significantly lower debt, but also, in particular, by the gratifying operational developments in the Company. The Managing Board anticipates positive financial results for all of fiscal 2010. Sales of EUR 58 million and significantly positive free cash flow in the millions constitute paragon's goals. Operating earnings (EBITDA adjusted for the costs of restructuring and the insolvency) of EUR 7.5 million are anticipated. Even taking into account extraordinary expenses positive EBIT/EBT values for 2010 are anticipated according to information from the Managing Board.

paragon will concentrate fully on automotive electronics in future. paragon also sees opportunities in the area of New Drives in addition to its tried and true product portfolio. Electronic solutions for hybrid cars and, especially, for electric mobility play a key role in this domain. The departure from the divisional structure and the new breakdown into product groups minimizes complexity and creates additional clarity. This will create the conditions for paragon to optimally exploit the opportunities offered in the automotive industry.

Consolidated Balance Sheet of paragon AG, Delbrück, as of September 30, 2009

in **EUR** thousands	**Sep. 30, 2009**	**Dec. 31, 2008**
Assets		
Non-current assets		
Intangible assets	5,076	6,061
Goodwill	0	0
Property, plant and equipment	17,710	19,898
Financial assets	180	180
Deferred taxes	368	447
Total non-current assets	**23,334**	**26,586**
Current assets		
Inventories	14,979	19,224
Trade receivables	8,277	4,375
Income tax assets	25	219
Other assets	1,046	849
Cash and cash equivalents	1,450	2,262
Total current assets	**25,777**	**26,929**
Total assets	**49,111**	**53,515**

in **EUR** thousands	**Sep. 30, 2009**	**Dec. 31, 2008**
Liabilities		
Equity		
Subscribed capital	4,115	4,115
Capital reserve	7,753	7,753
Profit carried forward	- 64,141	7,695
Consolidated net income/loss	- 6,670	- 71,836
Currency translation reserve	- 1,790	- 1,905
Total equity	**- 60,733**	**- 54,178**
Non-current provisions and liabilities		
Non-current finance lease obligations	669	947
Non-current borrowings	7,222	21,659
Profit-participation certificates	0	22,610
Special item for investment grants	5,351	6,432
Deferred taxes	255	359
Pension provisions	554	623
Other non-current liabilities	0	0
Total non-current provisions and liabilities	**14,051**	**52,630**
Current provisions and liabilities		
Current portion of finance lease obligations	383	470
Current borrowings and current portion of non-current borrowings	41,697	26,550
Profit-participation certificates	22,762	0
Trade payables	14,072	13,895
Other provisions	4,189	3,277
Income tax liabilities	804	1,778
Other current liabilities	11,886	9,093
Total current provisions and liabilities	**95,793**	**55,063**
Total equity and liabilities	**49,111**	**53,515**

Consolidated Income Statement of paragon AG, Delbrück, for the period from January 1 to June 30, 2009

in EUR thousands	Q-3 2009 01/07 – 30/09	Q-3 2008 01/07 – 30/09	2009 01/01 – 30/09	2008 01/01 – 30/09
Sales revenue	**17,634**	**29,774**	**54,114**	**90,234**
Other operating income	520	1,106	1,699	3,253
Increase or decrease in finished goods and work in progress	- 518	241	- 2,186	2,773
Other own work capitalized	77	1,074	226	4,012
Total operating performance	**17,713**	**32,195**	**53,855**	**100,272**
Cost of materials	- 8,811	- 17,060	- 26,843	- 52,435
Gross profit	**8,902**	**15,135**	**27,012**	**47,837**
Staff costs	- 5,298	- 7,098	- 17,303	- 21,627
Depreciation and amortization of property, plant and equipment and intangible assets	- 1,323	- 3,129	- 3,991	- 9,436
Impairment of property, plant and equipment and intangible assets	- 63	0	- 337	0
Other operating expenses	- 2,199	- 2,837	- 7,842	- 9,853
Earnings before interest and taxes (EBIT)	**19**	**2,071**	**- 2,463**	**6,921**
Financial income	0	67	41	188
Finance costs	- 1,369	- 2,116	- 4,234	- 6,163
Net financing costs	**- 1,369**	**- 2,049**	**- 4,193**	**- 5,975**
Earnings before taxes	**- 1,350**	**22**	**- 6,656**	**946**
Income taxes	10	113	- 15	- 329
Consolidated net income/loss	**- 1,340**	**135**	**- 6,670**	**617**
Earnings per share (basic)	- 0.33	0.03	- 1.62	0.15
Earnings per share (diluted)	- 0.33	0.03	- 1.62	0.15
Average number of shares outstanding (basic)	4,114,788	4,114,788	4,114,788	4,114,788
Average number of shares outstanding (diluted)	4,114,788	4,124,983	4,114,788	4,124,983

Group Segment Reporting of paragon AG, Delbrück

in EUR thousands	Sales		Earnings before interest and taxes (EBIT)	
	01/01 – 30/09/09	01/01 – 30/09/08	01/01 – 30/09/09	01/01 – 30/09/08
Automotive	44,206	74,936	- 2,782	5,897
Electronic Solutions	9,908	15,298	319	1,024
Total	54,117	90,234	- 2,463	6,921

Consolidated Cash Flow Statement of paragon AG, Delbrück, in accordance with IFRS

in EUR thousands	01/01 – 30/09/2009		01/01 – 30/09/2008	
Cash flow from operating activities				
Earnings before income taxes and deferred taxes	**- 6,656**		**946**	
Depreciation and write-ups of property, plant and equipment	3,992		9,436	
Net financing costs	4,193		5,975	
Gains (-), losses (+) from the disposal of property, plant and equipment and financial assets	0		- 93	
Increase (+), decrease (-) in other provisions and pension provisions	843		- 207	
Income from the release of the special item or investment grants	- 1,081		- 1,550	
Other non-cash income and expense	620		0	
Increase (-), decrease (+) in trade receivables, other receivables	- 4,099		- 2,160	
Impairment of intangible asstes and PPE	338		0	
Increase (-), decrease (+) in inventories	4,245		- 2,869	
Decrease (+), Increase (-) in trade payables and other liabilities	134		8,448	
Interest paid	- 474		- 6,163	
Income taxes/deferred taxes paid	- 821		- 605	
Net cash provided by/used in operating activities		**1,231**		**11,158**
Cash flow from investing activities				
Cash receipts from disposals of property, plant and equipment	0		336	
Cash payments to acquire property, plant and equipment	- 1,677		- 6,791	
Cash payments to acquire intangible assets	- 99		0	
Cash payments to acquire financial assets	0		- 1,900	
Interest received	41		188	
Net cash provided by/used in investing activities		**- 1,735**		**- 8,167**
Cash flow from financing activities				
Dividends paid	0		- 411	
Cash repayments of borrowings	- 424		- 4,482	
Cash proceeds from issuing borrowings	0		4,691	
Net cash repayments of profit participation rights	0		- 3,000	
Net change in cash and cash equivalents		**- 423**		**- 3,202**
Cash-effective change in liquidity		- 928		- 211
Effects resulting from exchange differences, changes in the basis of consolidation and remeasurement		115		- 91
Cash and cash equivalents at beginning of period		2,262		6,443
Cash and cash equivalents at end of period		1,450		6,141

Consolidated Statement of Changes in Equity of paragon AG, Delbrück

in EUR thousands	Subscribed capital	Currency translation differences	Capital reserve	Profit/ loss carried forward	Consolidated net income/loss	Total
Balance as of Jan. 1, 2008	**4,115**	**- 1,824**	**7,753**	**5,642**	**2,464**	**18,150**
Earnings after tax					617	617
Profit/loss carried forward				2,464	- 2,464	0
Dividends				- 411		- 411
Capital increase (exercise of options)						0
Currency translation differences		- 91				- 91
Balance as of Sep. 30, 2008	**4,115**	**- 1,915**	**7,753**	**7,695**	**617**	**18,265**
Balance as of Jan. 1, 2009	**4,115**	**- 1,905**	**7,753**	**7,695**	**- 71,836**	**- 54,178**
Earnings after tax					- 6,670	- 6,670
Profit/loss carried forward				- 71,836	71,836	0
Dividends						0
Capital increase (exercise of options)						0
Currency translation differences		115				115
Balance as of Sep. 30, 2009	**4,115**	**- 1,790**	**7,753**	**- 64,141**	**- 6,670**	**- 60,733**

Shares held by members of the Executive and the Supervisory Board as at September 30, 2009

Capital stock: 4,114,788 shares	Shares 30/09/2009
Management Board, total	**2,111,730**
Supervisory Board, total	**6,000**
Boards, total	**2,117,730**
as % of share capital	**51.47**

Additional Comments

The third-quarter report has been prepared using the uniform accounting principles of the International Financial Reporting Standards (IFRS), which were also used for the 2008 annual report. The standards of the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) apply. The form and content of the report comply with the reporting requirements of the German stock exchange. The third-quarter report represents an update of the annual report. Its emphasis is on the current reporting period and it should be read in conjunction with the annual report and the additional information contained therein.

The scope of consolidation has not changed in the first nine months of 2009 compared to the 2008 annual financial statements.

The risk situation of paragon AG was covered in detail in the report on risks and opportunities in the 2008 annual report. Statements made in the report regarding the delayed date of publication and overall risk continue to apply.

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