paragon®

Neue Kraft, bewegende Ideen

Quarterly Report
Mid-Year Report 2009

Highlights in the First Half of 2009

- Industry crisis remains the dominating factor
- Sales decline of 40 % from 2008
- The downward trend in earnings values slows
- Operating earnings once again positive

The first six months at a glance

in EUR thousands	First half of 2009	First half of 2008	Change in %
Sales	36,480	60,460	- 40 %
EBITDA	186	11,156	- 98 %
Adjusted EBITDA*	1,223	12,031	- 90 %
EBIT	- 2,482	4,849	- 151 %
Net earnings for period	- 5,331	482	- 1,206 %
Earnings per share in EUR	- 1.30	0.12	- 1,183 %
Liquidity in millions	1,465	1,857	- 21 %
Employees	518	599	- 14 %

* 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 June 30, 2009, and on the other takes into consideration subsequent events. 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

After world production again dipped sharply in the first quarter of 2009, the global economy began to recuperate slowly into the summer of 2009. Given the continued existence of stress factors, however, the global economy is likely to recover only gradually. Production in the second quarter may have continued significantly lower than the previous year, but the decline was less steep than in the first quarter.

In the automotive sector there were increasing signs of stabilization during the second quarter, too. This bottoming out, which has been perceptible for several months, has been reinforced by global passenger car registration numbers. The positive effects of the government scrapping scheme have resulted in a flattening out of the decline in demand in many countries. In Western Europe new passenger car registrations were above the level of the previous year for the first time since spring of 2008, by 5 %. Market developments in China were especially gratifying; German manufacturers, too, benefited.

Business Developments in the paragon Group

Due to the continuing financial and automotive crisis sales at paragon AG were down 40 % compared to the previous year. Quarterly sales thus stabilized at a low level. In the first half of 2009 the Group achieved sales of EUR 36.5 million after sales of EUR 60.5 million as at June 30, 2008.

The market collapse continued to affect paragon's financial developments significantly. Release orders from carmakers, which suffered a steep decline, are slow in starting up again; a priority among customers is to deplete their own warehouse inventories in many cases. Against this backdrop production is still far from reaching the levels that were customary before the crisis. It is, however, apparent that the situation is bottoming out.

Generally speaking, paragon has focused above all on the optimization of internal processes as part of a broad-based restructuring programme during the second quarter. The goal of the restructuring measures is to adapt paragon to lower sales figures by reducing fixed costs. In order to reduce costs, paragon has foregone additional marketing measures other than regular visits and continuing servicing of existing customers. This extended to the cancellation of road shows already scheduled with new customers.

In the second quarter of 2009 as well, the situation in the business segments – Automotive and Electronic Solutions – differed. Sales in the predominant Automotive segment dropped in the first six months by 41.8 % compared to the previous year. The Electronic Solutions segment in contrast achieved sales only 28.9 % below the previous year's levels.

Financial Position and Net Assets

Total assets did not change significantly compared to the December 31, 2008, balance sheet date. They rose from EUR 53.5 million to EUR 54.8 million.

Non-current assets include virtually no capital expenditures; the decrease from EUR 26.6 million to EUR 24.7 million is due to customary wear and tear on fixed asset items. Current assets on the other hand rose by EUR 3.0 million to EUR 30.0 million (prior year: EUR 27.0 million), the result especially of an increase in trade receivables (EUR 11.2 million). Inventories on the other hand were decreased by almost EUR 2.8 million confirming the trend of the previous quarter.

Non-current liabilities fell considerably from EUR 52.6 million as at December 31, 2008, to a mere EUR 14.4 million. This reduction simply represents a reclassification of non-current to current financing elements. The reason for this is the now familiar 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. This process is taken into account retrospectively. Current liabilities in contrast have risen from EUR 55.1 million to EUR 99.8 million as at June 30, 2009.

Operating cash flow, which dropped in the previous year from March 31, 2008, to June 30, 2008, increased in 2009 compared to the first quarter (EUR 0.3 million). Nevertheless, it was at a relatively low level at EUR 0.5 million.

Results of Operations

The comprehensive restructuring programme with which paragon responded to the drop in sales in the wake of the global economic and automotive crisis had a positive impact, also from a financial perspective, in the period under review. Measures initiated in the fourth quarter of 2008 and continued in the first quarter of 2009 contributed to the fact that paragon was able to again achieve a profit in operating earnings (EBITDA adjusted for restructuring costs) in the second quarter of 2009. At EUR 12.0 million personnel expenses were 18 % lower than the same cut-off date of the previous year (EUR 14.6 million). In the first quarter the Company's personnel expenses were up 4 %; at this stage it is clear that the cost reduction measures are already kicking in. In relation to slumping sales the cost of materials ratio dropped disproportionately compared to the same quarter of the previous year by 12 %.

Since there were no significant positive changes in terms of sales, the earnings indicators as at June 30, 2009, are still heavily influenced by the automotive crisis. 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.

Despite significantly reduced financing expenses due to the standstill agreement among the banks, paragon was still not able to show positive EBIT in the second quarter. The sales lost due to the financial and automotive crisis could not be entirely offset by cost reductions. EBIT is currently at EUR -2.5 million (prior year: EUR 4.8 million).

As at the end of the period under review, net earnings for the period were EUR -5.3 million according to IFRS (prior year: EUR 0.5 million), which is due to enormous losses in contribution margins resulting from lower sales. Operating earnings – EBITDA adjusted by restructuring costs – were positive again in the second quarter of 2009. paragon achieved an operating profit of EUR 1.2 million. Even taking into account restructuring costs, the Company earned EBITDA of EUR 0.2 million over the entire first half of the year, although this compares to EUR 11.2 million in the same period of the previous year.

Segment Report

The Automotive segment with its two divisions – Sensor/Actuator and Cockpit Systems – suffered considerable sales losses in the first half of 2009. Sales revenues plunged by 41.8 % to EUR 29.1 million (prior year: EUR 50.0 million). The share in total sales was 79.7 %. The Company had to deal with a sharp drop of 166.7 % in the first half of 2009 – to EUR -2.8 million (prior year: EUR 4.2 million).

The Electronic Solutions segment, too, evidenced a sales slump due to the difficult overall economic conditions. Sales fell in the first three months by 28.9 % to EUR 7.4 million (prior year: EUR 10.4 million). EBIT deteriorated by 57.1 % to EUR 0.3 million (prior year: EUR 0.7 million).

Capital Expenditure / Research & Development

As a consequence of lower sales and the considerable reduction in operational activities, paragon also perceptibly held back on capital expenditure in the first half of 2009. Capital expenditure amounted to EUR 0.9 million in the first six months. During the same interval in the previous year capital expenditure activities of EUR 4.6 million were undertaken.

paragon continued its important efforts for the future in the research and development area. In the period under review expenses for research and development totalled EUR 4.1 million (prior year: EUR 5.2 million). In the Sensor/Actuator division the focus was in particular on development of the air quality system, Air Quality Improver (AQI), to the point of production readiness, as well as further development of various multifunction sensors. In the Cockpit Systems division activities revolved around infotainment systems, the belt microphone belt-mic and a Bluetooth hands-free system.

Employees

The paragon Group employed 518 people world-wide as at June 30, 2009. The Company has thus reduced the number of employees compared to the previous year (June 30, 2008: 599 employees) in significantly greater measure than in the first three months. The end of the restructuring measures has not yet been reached, however; paragon plans to continue to reduce its work-force numbers during the course of 2009. 69 employees were engaged at headquarters in Delbrück and 272 at the Suhl production site. The reduction in the number of temporary workers supports the cost-cutting measures. Their numbers were strikingly decreased compared to the previous year – from

104 to 3. The personnel cost ratio of 32.5 % was greater than that of the same cut-off date on the previous year (21.3 %) despite the adjustments implemented. In the first quarter this ratio was 34.4 % in fact.

Investor Relations

The capital markets also benefited from the gradual recovery in the global economy. While, for instance the German Stock Index (Deutsche Aktien Index – DAX) slid downwards to just over 4,000 points at the end of the first quarter, it had rebounded by June 30, 2009, to a healthy 4,800 points.

The slight upwards trend in European and international financial markets failed to affect the paragon share in the period under review. The share was not quite able to maintain its starting price of EUR 2.70 on April 1, 2009, until the end of the quarter with rather slight movements in price. On June 29, 2009, the paragon share was quoted at EUR 2.52 (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.

Securities Identification Number:	555 869
ISIN:	DE 000 555 8696
Ticker symbol:	PGN
Trading segment:	Prime Standard
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 in the wake of the crisis had radical effects on all suppliers in the first half of 2009.

Due to the delayed preparation of this mid-year report, please refer to the risk report in the 2009 annual report at this stage. 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 initiated insolvency proceedings with the goal of implementing an insolvency plan. 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.

Capital Structure, Managing Board and Change of Control

Pursuant to the provisions of section 289, paragraph 4 and section 315, paragraph 4, of the German Civil Code, paragon AG provides the following comments:

Capital
paragon AG's capital stock at the end of the period under review consisted of 4,114,788 shares with a par value of Đ1.00. Subscribed capital amounted to EUR 4,114,788. As of January 1, 2009, these shares are entitled to dividend payments. As far as the Managing Board is aware no restrictions on transfer and voting rights exist.

There are no shares with special rights that grant control authorities. Klaus Dieter Frers has direct holdings in paragon AG in excess of 10 %. He holds circa 52 % of the shares.

Employees of the Company or the paragon Group do not participate in such a way in the Company's capital that they are in a position to exercise control rights directly.

Managing Board
paragon AG's Managing Board consisted of one member appointed by the Supervisory Board as at June 30, 2009: Mr. Klaus Dieter Frers, at the same time Chairman of the Board. In other respects, the provisions of sections 84 and 85 of the German Stock Corporation Act apply.

Furthermore, no member of the Managing Board occupied a position on a Supervisory Board. Subject to the condition of a change of control resulting from a takeover bid, agreements were included in paragon AG's Managing Board contracts that they be indemnified under certain conditions.

An authorization to repurchase treasury stock in amounts of up to 10 % of equity capital and to increase capital up to 2 million shares (authorized capital) was in force. Furthermore, capital was conditionally increased by up to 2,040,012 shares (conditional capital I, II and III).

Outlook

Given the context of the August 2010 publication period the outlook already 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 June 30, 2009

in **EUR** thousands	June 30, 2009	Dec. 31, 2008
Assets		
Non-current assets		
Intangible assets	5.355	6,061
Goodwill	0	0
Property, plant and equipment	18,804	19,898
Financial assets	180	180
Deferred taxes	395	447
Total non-current assets	**24,734**	**26,586**
Current assets		
Inventories	16,460	19,224
Trade receivables	11,162	4,375
Income tax assets	61	219
Other assets	883	849
Cash and cash equivalents	1,465	2,262
Total current assets	**30,031**	**26,929**
Total assets	**54,765**	**53,515**

in **EUR** thousands	June 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	- 5,331	- 71,836
Currency translation reserve	- 1,857	- 1,905
Total equity	**- 59,461**	**- 54,178**
Non-current provisions and liabilities		
Non-current finance lease obligations	762	947
Non-current borrowings	7,065	21,659
Profit-participation certificates	0	22,610
Special item for investment grants	5,690	6,432
Deferred taxes	294	359
Pension provisions	577	623
Total non-current provisions and liabilities	**14,388**	**52,630**
Current provisions and liabilities		
Current portion of finance lease obligations	395	470
Current borrowings and current portion of non-current borrowings	42,239	26,550
Profit-participation certificates	22,708	0
Trade payables	17,462	13,895
Other provisions	4,321	3,277
Income tax liabilities	1,014	1,778
Other current liabilities	11,699	9,093
Total current provisions and liabilities	**99,838**	**55,063**
Total equity and liabilities	**54,765**	**53,515**

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

in **EUR** thousands	Q-2 2009 01/04 – 30/06	Q-2 2008 01/04 – 30/06	First Half of 2009 01/01 – 30/06	First Half of 2008 01/01 – 30/06
Sales revenue	**17,900**	**31,057**	**36,480**	**60,460**
Other operating income	578	1,258	1,180	2,147
Increase or decrease in finished goods and work in progress	- 1,068	1,244	- 1,668	2,532
Other own work capitalized	20	1,076	149	2,937
Total operating performance	**17,430**	**34,635**	**36,142**	**68,076**
Cost of materials	- 8,461	- 17,810	- 18,032	- 35,375
Gross profit	**8,969**	**16,825**	**18,109**	**32,701**
Staff costs	- 5,577	- 7,429	- 12,004	- 14,529
Depreciation and amortization of property, plant and equipment and intangible assets	- 1,333	- 3,092	- 2,668	- 6,307
Impairment of property, plant and equipment and intangible assets	- 92	0	- 275	0
Other operating expenses	- 2,829	- 3,792	- 5,644	- 7,016
Earnings before interest and taxes (EBIT)	**- 862**	**2,512**	**- 2,482**	**4,849**
Financial income	40	51	41	121
Finance costs	- 1,374	- 2,152	- 2,865	- 4,046
Net financing costs	**- 1,334**	**- 2,101**	**- 2,824**	**- 3,925**
Earnings before taxes	**- 2,196**	**411**	**- 5,306**	**924**
Income taxes	- 18	- 170	- 25	- 442
Consolidated net income/loss	**- 2,214**	**241**	**- 5,331**	**482**
Earnings per share (basic)	- 0.54	0.06	- 1.30	0.12
Earnings per share (diluted)	- 0.54	0.06	- 1.30	0.12
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	4,124,294	4,114,788	4,124,983

Group Segment Reporting of paragon AG, Delbrück

in EUR thousands	**Sales**		**Earnings before interest and taxes (EBIT)**	
	First Half of 2009 01/01 – 30/06	First Half of 2008 01/01 – 30/06	First Half of 2009 01/01 – 30/06	First Half of 2008 01/01 – 30/06
Automotive	29,093	50,016	- 2,774	4,153
Electronic Solutions	7,387	10,444	292	669
Total	36,480	60,460	- 2,482	4,849

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

in EUR thousands	01/01 – 30/06/2009		01/01 – 30/06/2008	
Cash flow from operating activities				
Earnings before income taxes and deferred taxes	**- 5,306**		**924**	
Depreciation and write-ups of property, plant and equipment	2,668		6,307	
Net financing costs	2,824		3,926	
Gains (-), losses (+) from the disposal of property, plant and equipment and financial assets	0		- 36	
Increase (+), decrease (-) in other provisions and pension provisions	998		-159	
Income from the release of the special item or investment grants	- 742		- 1,007	
Other non-cash income and expense	- 99		0	
Increase (-), decrease (+) in trade receivables, other receivables	- 6,821		- 4,614	
Impairment of intangible asstes and PPE	275		0	
Increase (-), decrease (+) in inventories	2,764		- 3,697	
Decrease (+), Increase (-) in trade payables and other liabilities	5,079		4,721	
Interest paid	- 465		- 4,047	
Income taxes/deferred taxes paid	- 645		- 134	
Net cash provided by/used in operating activities	**531**		**2,184**	
Cash flow from investing activities				
Cash receipts from disposals of property, plant and equipment	0		70	
Cash payments to acquire property, plant and equipment	- 1,028		- 4,592	
Cash payments to acquire intangible assets	- 17		0	
Cash payments to acquire financial assets	0		- 1,900	
Interest received	41		121	
Net cash provided by/used in investing activities	**- 1,004**		**- 6,301**	
Cash flow from financing activities				
Dividends paid	0		- 411	
Cash repayments of borrowings	- 372		- 3,197	
Cash proceeds from issuing borrowings	0		6,494	
Net cash repayments of profit participation rights	0		- 3,000	
Net change in cash and cash equivalents		**- 372**		**- 114**
Cash-effective change in liquidity		- 845		- 4,231
Effects resulting from exchange differences, changes in the basis of consolidation and remeasurement		48		- 355
Cash and cash equivalents at beginning of period		2,262		6,443
Cash and cash equivalents at end of period		1,465		1,857

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**	**2,465**	**18,851**
Earnings after tax					482	482
Profit/loss carried forward				2,465	- 2,465	0
Dividends				- 411		- 411
Capital increase (exercise of options)						0
Currency translation differences		- 356				- 356
Balance as of June 30, 2008	**4,115**	**- 2,180**	**7,753**	**7,696**	**482**	**17,866**
Balance as of Jan. 1, 2009	**4,115**	**- 1,905**	**7,753**	**7,695**	**- 71,836**	**- 54,178**
Earnings after tax					- 5,331	- 5,331
Profit/loss carried forward				- 71,836	71,836	0
Dividends						0
Capital increase (exercise of options)						0
Currency translation differences		48				48
Balance as of June 30, 2009	**4,115**	**- 1,857**	**7,753**	**- 64,141**	**- 5,331**	**- 59,461**

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

Capital stock: 4,114,788 shares	Shares 30/06/2009
Management Board, total	**2,111,730**
Supervisory Board, total	**6,000**
Boards, total	**2,117,730**
as % of share capital	**51.47**

Abbreviated Notes to the Consolidated Financial Statements of paragon AG for the period January 1 to June 30, 2009

Basis of Presentation
The interim paragon AG consolidated financial statements as of June 30, 2009, have been prepared according to the uniform accounting principles of the International Financial Reporting Standards (IFRS). Furthermore, the standards of the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) apply. The provisions of IAS 34, "Interim Financial Reporting", were also taken into account.

The form and content of the report on the first half of the year comply with the reporting requirements of the German stock exchange. This report represents an update of the 2008 annual report, which should be referenced for explanation and additional information while reading this report. It can be found at www.paragon-online.de.

Scope of Consolidation
The scope of consolidation did not change in the first half of 2009 vis-à-vis the 2008 financial statements.

Income Statement, Balance Sheet, Cash Flow Statement, Segment Report
The sections on "Net assets, financial position and results of operations" provide a detailed overview and specific explanations regarding paragon AG's income statement, balance sheet and cash flow statement.

Financial Obligations after the Mid-year Cut-off Date
As a consequence of the automotive crisis and the failed negotiations with the banks, the Managing Board of paragon initiated insolvency proceedings on October 5, 2009. These proceedings were commenced on January 1, 2010, and, once the creditors' meeting had approved the insolvency plan submitted by the Company on April 16, 2010, suspended as at June 1, 2010, by the Paderborn district court.

Notes on the Preparation of the Mid-year Report
An audit or audit review of the interim consolidated financial statements was not performed.

Future-oriented statements entail risks. The present report on the first half of the year contains statements that relate to paragon AG's future development. These statements are based on assumptions and estimates. While the Managing Board is convinced that statements regarding the future are realistic, there can be no guarantees in this respect. The assumptions harbour risks and uncertainties that may result in actual events diverging from expected events.

Responsibility Statement

To the best of my knowledge, and in accordance with the applicable reporting principles for interim financial reporting, the interim consolidated financial statements give a true and fair view of the assets, liabilities, financial position, and profit or loss of the Group, and the interim management report of the Group includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group for the remaining months of the fiscal year.

Delbrück, August 12, 2010

Klaus Dieter Frers

Neue Kraft, bewegende Ideen

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