Directors' report

The Board of Directors and the President of Bong AB (publ.), corporate ID no. 556034-1579, domiciled in Kristianstad, hereby submit their annual report for the financial year 1 January 2011 – 31 December 2011 for the Parent Company and the Group. Bong is the leading provider of specialised packaging and envelope products in Europe and offers solutions for distribution and packaging of information, advertising materials and lightweight goods. Important growth areas in the Group are the ProPac packaging concept and Russia. The Group has annual sales of approximately SEK 3.2 billion and about 2,300 employees in 15 countries. Bong has strong market positions, in most of the important markets in Europe, and the Group sees interesting possibilities for continued expansion and development. Bong is a public limited company and its shares are listed on NASDAQ OMX Stockholm, Small Cap.

MARKET

Economic uncertainty in Europe depressed demand in the second half of 2011. Following a modest decline early in the year, volume losses in the market accelerated in the autumn. According to statistics compiled by the European Envelope Manufacturers' Association (FEPE), envelope volumes fell in Western Europe by 6 per cent in the third quarter, with a projected decline of 9 per cent compared with 2010. On an annualised basis, the decline was approximately 4 per cent. Russia and Eastern Europe were also adversely affected, with growth in both markets limited to around 5 per cent compared with growth rates of around 10 per cent in previous years. Meanwhile, consolidation and capacity adjustments in the European envelope industry have accelerated.

The German Mayer Group acquired in autumn the French envelope manufacturer GPV, which has a European market share of around 10%, with operations in France, England, Romania and Bulgaria. Industry organisation FEPE reports that Mayer has taken over all factories except one in France, which has been shut down. Also according to FEPE, Mayer intends to retain 650 of GPV's 945 employees.

Following the merger with Hamelin, Bong transferred envelope production from its Belgian factory to other Group facilities and has adjusted staffing primarily in Germany, England and Scandinavia. Approximately 235 employees were made redundant as a result of these measures.

Early in 2012, the Spanish Tompla Group announced significant reductions in force in both France (57 jobs) and Spain (52 jobs). Moreover, Papyrus Kuvert, with production in Germany, initiated negotiations with the trade union to reduce staffing by 40 of a total of 120 positions. The Belgian company DeVroede went into reconstruction at the end of 2011. The main operations of DeVroede, the largest overprinting supplier in Europe, are in Belgium, but the company also has significant operations in the UK, the Netherlands, Germany and France.

DeVroede's sales amounted to about EUR 15 million on an annualised basis. The Mayer Group announced in early 2012 that it had bought the business.

Conprent, the largest independent envelope printer in Denmark, went into receivership in early 2012. Prior to the bankruptcy, Conprent had annual sales of around DKK 15 million. The business has been wound up and the machinery is being sold.

The packaging market, where Bong markets the ProPac range, is much bigger than the envelope market. The market is also much more multifaceted. Market statistics for the niches where Bong is active are lacking or difficult to obtain. In Bong's assessment, demand for packages used in sectors including e-commerce, mail order and retail is still growing and strong growth potential is expected over time.

SALES AND EARNINGS

Consolidated sales for the full year 2011 were SEK 3,203 million (2,326). The Hamelin merger had positive impact on consolidated sales, while the depreciation of the euro had negative impact. Recalculated at last year's exchange rate, consolidated sales would have amounted to SEK 3,371 million.

The volume trend for envelopes was negative during the period, which had a negative impact on earnings. ProPac delivered growth of 30%, driven primarily by the Hamelin deal (mainly expander bags) and the acquisition of Bong CSK in Poland. However, uncertainty in the retail trade during the autumn became evident in the weaker than expected sales of gift bags in the fourth quarter.

Operating profit improved to SEK 40 million (-91), driven primarily by lower non-recurring costs for the restructuring programme than in 2010. Figured at last year's exchange rate, operating profit would have amounted to SEK 46 million. The earnings figure reflects costs of SEK 23 million related to the Scandinavian restructuring programme (please refer to the section under Integration and restructuring programme below). Operating profit was also negatively impacted in the fourth quarter by accrual effects related to pensions amounting to approximately SEK 6 million.

Prices for uncoated fine paper, Bong's main production material, rose during the spring, which depressed the gross margin. Due to overcapacity in the European envelope market, Bong has not yet been able to fully pass on the price increases on uncoated fine paper.

Bong is reporting net financial items of SEK -63 million (-41), profit before tax of SEK -23 million (-132) and profit after tax of SEK -16 million (-97) for the year.

INTEGRATION AND RESTRUCTURING PROGRAMME

The integration process following the Hamelin merger and efforts to realise announced synergies progressed as planned during the year. Cost synergies had only a minor impact on earnings in 2011.

An agreement was reached in early July with the relevant trade unions concerning comprehensive restructuring of Bong's envelope production in Belgium. As a result of the agreement, the bulk of production in Bong's Belgian factory has been transferred to other Group facilities. In conjunction, about 60 people were made redundant.

The project is expected to result in an annual drawdown of costs of about SEK 40 million, taking successive effect beginning in the fourth quarter of 2011. An allocation was made for restructuring costs related to the project when the annual accounts for 2010 were prepared.

In response to lower demand, the company announced a programme to reduce fixed costs in Bong's Scandinavian operations. The measure includes a reduction in force of approximately 55 jobs (including both personnel involved directly in production and white-collar employees) in Sweden, Denmark and Norway. Programme costs of SEK 23 million were charged to fourth-quarter earnings. Annual savings of an estimated SEK 20 million will take successive effect beginning in 2012.

The merger with Hamelin's envelope division has enabled efficiency improvements in the Group's British production units. Towards that end, an efficiency improvement programme was implemented at the Milton Keynes factory, where about 30 people have left the company. An allocation for the costs of the measure was made in connection with preparation of the annual accounts for 2010. The estimated annual savings effect will be approximately SEK 7 million.

Production staff was also reduced in Germany during the year in connection with moving certain volumes to the Group's French factories. A total of about 235 people left Bong during the year.

CASH FLOW

There was a very strong upturn in cash flow after investment activities, which amounted during the year to SEK 137 million (-277).

The strong cash flow is primarily attributable to a reduction in working capital of SEK 142 million during the period. The success is mainly the product of industrious efforts to adjust inventories and achieve purchasing-related synergies in connection with the Hamelin acquisition.

FINANCIAL POSITION

Cash and cash equivalents at 31 December 2011 totalled SEK 151 million (SEK 149 million at 31 December 2010). The Group had unutilised credit facilities of SEK 290 million at 31 December 2011. This brought total available liquidity to SEK 441 million.

Consolidated equity at 31 December 2011 was SEK 496 million (SEK 531 million at 31 December 2010). Translation of the net asset value of foreign subsidiaries to Swedish crowns and changes in the fair value of derivative instruments reduced consolidated equity by SEK 35 million.

Interest-bearing net loan debt declined by SEK 115 million to SEK 947 million (1,062 at 31 December 2010) during the period. Translation of net debt in foreign currency to Swedish krona reduced consolidated net debt by SEK 4 million.

CAPITAL EXPENDITURE

Acquisitions affected cash flow by SEK –40 million and other investments by SEK +28 million, resulting in net impact of investment activities on cash flow during the year of SEK –12 million. Capital expenditures include investments in machinery to increase capacity within ProPac (gift bags), expansion of the Group's Russian property and investments in business systems for the new Group. Also included is the sale of a small property in Sucy, France, sales of machinery in connection with the restructuring of the Belgian company and the sale of a factory building in Wuppertal, Germany, which had positive impact on cash flow of EUR 9 million but had no effect on earnings.

EVENTS AFTER THE END OF THE FINANCIAL YEAR

Lober – from 70 to 100 per cent

In accordance with a 2006 agreement, Bong acquired the remaining 30% interest in the German company Lober Druck & Kuvert as of the first of January 2012. Domiciled outside Augsburg, Lober is one of the leading offprinting operations in southern Germany. As Lober has already been consolidated as a subsidiary, the acquisition of the outstanding equity interest had no effect on Bong's earnings.

Packaging first - from 45 to 100 per cent

On the first of February 2012, Bong exercised its option to acquire the remaining 55% stake in the British company Packaging First Ltd. Packaging First, with annual sales of approximately GBP 3 million, is a packaging wholesaler established northeast of London. Through the acquisition, Bong has strengthened its position in the British market and gained a wholly owned channel for sales of ProPac products. Packaging First Ltd will be consolidated as a subsidiary in the Group as of the first of February 2012. The transaction is expected to have immediate and positive impact on Bong's earnings.

EMPLOYEES

The average number of employees during the period was 2,431 (1,540). The number of employees at 31 December 2011 was 2,318 (2,497). The large change is attributable to the 2010 merger with Hamelin's envelope division and the restructuring measures taken during the year.

ENVIRONMENT

Bong's environmental work is aimed at minimising the environmental effects of both end products and processes. At present, Bong is working actively to improve production methods so that polluting emissions are minimised, to eco-label as large a portion of the range as possible, and to boost knowledge and awareness of environmental issues among its employees.

Besides imposing demands on its own operations, Bong is also trying to influence suppliers and customers to design their products so that ecocycle thinking and conservation of natural resources are prioritised.

In order to further rationalise environmental efforts, the company is working according to a plan for environmental certification with the objective that all plants in the Group will be certified to ISO 14 001. The plants in Wuppertal in Germany, Nybro and Kristianstad in Sweden, Tönsberg in Norway, Kavi in Finland, Milton Keynes and Derby in the UK, Sandweiler in Luxembourg and Angoulème in France are certified.

In 2009, Bong began efforts to obtain certification of its products according to the pan-European environmental certification standard Paper by Nature. The eco-label is applied to paper products such as envelopes, books and note pads. It takes into account the potential environmental impact of raw materials and manufacturing processes. Paper by Nature guarantees that the raw materials come from sustainably managed forests and that the products have been manufactured in certified facilities. Paper by Nature covers the environmental impact of manufacturing as well as energy aspects, emissions to water and air and environmentally harmful substances. The plants in Wuppertal and Aitrach in Germany, Kristianstad in Sweden, Milton Keynes, Washington and Darby in the UK, Evreux, Angoulême and Limoges in France and Venlop in the Netherlands are certified by the Paper by Nature Association.

There are many different eco-labels because they focus on different aspects of sustainability and environmental friendliness. Our products are certified under several schemes and since there is no single, overarching green standard, we apply for certification and labeling on as many fronts and in as many regions as possible. Sixteen of the Group's facilities are certified to produce FSC-labelled (Forest Steward ship Council) products. Our most recent green label is the "Carbon Reduction Label" from the Carbon Trust. The eco-label applies to our range of standard Tyvek envelopes.

During 2011, the Group conducted operations that required an environmental permit under the Environmental Code in Nybro through the subsidiary Bong Sverige AB. Net sales in the operation requiring an environmental permit in Nybro amounted to SEK 145 million, accounting for 4 per cent of consolidated net sales.

RESEARCH AND DEVELOPMENT

The Group does not conduct any research and development activities. However, active efforts are pursued to meet customer needs for different envelopes and packaging solutions.

PARENT COMPANY

The parent company's business extends to management of operating subsidiaries and Group management functions. Net sales were SEK 28 million (27) and earnings before tax for the period were SEK -19 million (24). Investments for 2011 amounted to SEK 6 million (17). The investments are IT-related and pertain to a common platform for administrative systems in the Group. Credits granted but not utilised amounted to SEK 290 million (319 at 31 December 2010).

THE BOARD'S PROPOSED 2012 GUIDELINES FOR REMUNERATION TO SENIOR EXECUTIVES

The Board of Directors of Bong AB proposes that the 2012 AGM resolve on remuneration to the President and other senior executives as described below. "Senior executives" here refers to executives included in the management group, which currently consists of the company's President/CEO, Chief Financial Officer (CFO), Managing Director Bong Scandinavia and Bong Packaging Solutions AB, Managing Director Bong Central Europe, Managing Director Bong UK and Managing Director France and Spain. Remuneration shall consist of fixed salary, variable remuneration, other benefits and pension. Total compensation must be at market rates and competitive to ensure that the Bong Group can attract and retain competent senior management. In addition to the above variable compensation, from time to time a long-term incentive scheme may be approved.

The variable portion of the salary shall have a predetermined ceiling, according to the basic principle that the variable salary portion can amount to no more than 60 per cent of the fixed annual salary. The variable portion is based on achievement of two or three of the following interim goals: 1) the Group's EBIT[1], 2) the Group's cash flow, 3) earnings in the business unit, and 4) individual/qualitative goals. The basic principle is that the variable remuneration is paid in accordance with the agreed-upon weighting between the interim goals if the interim goal has been achieved. The variable portion is based on a vesting period of one year. The goals for senior executives are established by the Board of Directors.

Pension benefits shall primarily be defined-contribution, but also occur for legal reasons as defined-benefit, although not at the Group Management level. Variable remuneration is not pensionable. Group Management is entitled to pensions under the ITP plan or the equivalent. The retirement age is 65 years. In addition to the ITP plan, some members of Group Management are also entitled to an increased occupational pension premium of up to 30 per cent of their fixed salary.

Group Management's employment contracts include provisions governing remuneration and termination of employment. According to these agreements, employment can ordinarily terminate at the request of the employee with a period of notice of 3–24 months and at the company's request with a period of notice of 6–24 months.

In the event of termination by the company, the period of notice and the period during which severance pay is payable shall not together exceed 24 months.

Remuneration to the President and other senior executives is prepared by the Board of Directors' remuneration committee and finalised by the Board based on the recommendation of the remuneration committee.

These guidelines apply to those persons who are included in the Group Management during the period the guidelines are in force. The guidelines apply to the employment contracts entered into after the AGM's resolution, and to any changes in existing contracts. The Board of Directors is entitled to disregard the above guidelines if it finds that special reasons exist to justify this in a particular case.

[1] Earnings Before Interest and Tax.

SUPPLEMENTARY INFORMATION

The cost of Group Management's variable remuneration – at maximum outcome, which assumes that all bonus-related goals are achieved – can be calculated to be about SEK 9 million (excluding social security contributions). The calculation is based on the current composition of the Group Management.

OWNERSHIP

Bong's principal owners, with stakes of more than ten per cent of the votes and capital, are the Hamelin family, with 25 per cent of the votes and capital, Melker Schörling (corporate ownership) and Alf Tönnesson (corporate ownership), both with about 22 per cent of the votes and capital. Skandia Liv and Fata Morgana AB each own about 4 per cent of the votes and capital in the company. The total number of ordinary shares was 17,480,995 on 31 December 2011. All shares carry the same rights.

There are no restrictions on the transferability of the shares due to legal regulations or rules in the Articles of Association.

Bong is not aware of any agreements between direct shareholders in Bong that entail restrictions in the right to transfer shares.

In the event of a public offer, no agreements are triggered that would have a material effect on Bongs earnings or position.

APPOINTMENT AND REMOVAL OF BOARD MEMBERS AND AMENDMENT OF THE ARTICLES OF ASSOCIATION

The company's Board of Directors shall consist of at least four and at most nine members. The members are elected at a General Meeting of Shareholders for the period until the end of the first Annual General Meeting (AGM) held after appointment of the member.

The Articles of Association can be amended at the AGM or a General Meeting of Shareholders.

OPPORTUNITIES AND RISKS

Like all business operations, Bong's operations are associated with risks and opportunities. The specific factors judged to have the greatest impact on Bong's operations are presented below.

OPERATING RISKS AND OPPORTUNITIES

Market development

Historically, the envelope market has followed the general economic trend. In Russia and Eastern Europe, a generally growing economy still drives envelope consumption. In Western Europe, the connection between general economic growth and envelope consumption is no longer as strong as it has been, given IT developments and associated digitisation.

Demand for envelopes for direct mail varies with the economy. With the aid of more sophisticated databases with personal information, a market is being created for highly sophisticated envelopes intended for personally addressed direct mail. Large promotional mailings in envelopes are declining in frequency and scope over time.

The administrative item as a whole has already declined with respect to account statements, order confirmations, etc. as part of digitisation and internet penetration. Other parts of the transaction-related item, such as invoices, still hold their own in the competition with the newer technology.

The strong demand for packaging in both e-commerce and traditional retail creates great opportunities for Bong to create growth in their speciality packaging line (ProPac). Packaging customers also present an opportunity for cross-selling of envelopes. Over time, growth in the packaging area is expected to compensate for the decline in envelopes. Bong is closely monitoring developments and is very active in speciality packaging to ensure sustained growth in ProPac.

Postage and charges

Changes in postage and charges can lead to changes in letter and mail volumes. Postage increases have a negative impact on volumes, while postage decreases have a positive impact. Postage is usually based on weight or size. More large markets are using weight-based postage. A transition from weight- to size-based postage could lead to changes in Bong's product mix and cause a shift towards smaller envelope sizes.

Industry structure and price competition

The European envelope market has undergone accelerating consolidation since 2009 as a result of the protracted financial crisis. The three largest envelope companies represent about 70 per cent of the total market. However, some of the major markets are still fairly fragmented. Bong believes that overcapacity in the industry has fallen slightly.

Paper prices

Uncoated fine paper is the single most important input material for Bong. The cost of fine paper is about 50 per cent of the total cost. Under normal conditions, Bong can compensate for price increases, with some time lag.

Dependence on individual suppliers and/or customers

Uncoated fine paper is Bong's most important input material and is mainly purchased from three major suppliers. Delivery disruptions from any of the three suppliers could affect Bong negatively in the short term. In a longer time perspective, Bong does not have any suppliers that are critical to its operations.

The Group's dependence on individual customers is limited. The biggest customer accounts for 6 per cent of annual sales, and the 25 biggest customers account for 36 per cent of total sales.

Capital needs and investments

All companies in the European envelope industry have roughly the same production equipment. The age of the machinery is of limited importance for production efficiency, but newer machines generally have higher capacity. Machine wear is low, and production control and automation are crucial for cost-effective production. In general, the long life of the machines inhibits scrapping and consolidation of the industry.

On the other hand, the low investment need leads to very good cash-generating capacity. At year-end, the Group's machinery consisted of about 250 envelope machines and 150 overprinting presses. During a period around the turn of the millennium, large investments were made in renewal and upgrading of the machinery to raise productivity. An important element has been increased robotisation. The investment need in existing structure is judged to be limited during the next few years and clearly less than the Group's depreciation costs.

Financial risk management

Information regarding goals and applied principles for financial risk management, use of financial instruments and exposure to currency risks, interest rate risks and liquidity risks is provided in Note 1.

EU commission investigation

In September 2010 the EU commission carried out inspections of several companies in the envelope and paper industry in Europe, including Bong in Sweden. The EC's investigation is currently underway. Against this background, Bong is not able to reasonably assess the outcome of the EC's judicial review.

Disputes

Bong is not currently involved in any legal disputes.

Environment

Bong complies with the environmental laws and rules that apply in each country to this type of industrial production. By means of measurements and regular inspections, Bong has ensured that emission limits are not exceeded, for example. There are no indications that the laws in this area will change in such a way that Bong would be affected to any significant extent or that Bong would be unable to comply with these requirements in the future.

Sensitivity analysis

Important factors that affect Bong's earnings and financial position are the volume trend for envelope sales, the price trend for envelopes, paper prices, payroll costs, currency rate fluctuations and interest rate levels. The table below shows how Bong's 2011 earnings would have been affected by a change in a number of business-critical parameters. Reported effects should be regarded merely as an indication of how profit after financial items would have been affected by an isolated change in the particular parameter.

Parameter	Change	Impact on earnings after financial items, SEK
Price	+/– 1%	32 +/–
Volume	+/– 1%	16 +/–
Paper prices	+/– 1%	16 –/+
Payroll costs	+/– 1%	9 –/+
Interest level borrowing	+/– 1% unit	6 –/+

CORPORATE GOVERNANCE REPORT

Effective and clear corporate governance helps secure the confidence of Bong's stakeholder groups while also increasing focus on business benefits and shareholder value in the company.

Bong's Board of Directors and management strive, by means of great transparency, to make it easier for the individual shareholder to follow the company's decision pathways and to clarify where in the organisation responsibilities and powers lie.

Corporate governance

Corporate governance within Bong AB ("Bong") is based on applicable legislation, the regulatory framework for NASDAQ OMX Stockholm and various internal guidelines. The most recent version of the Swedish Code of Corporate Governance ("the Code") was published in February 2010 and covers all listed companies as from 1 February 2010.

Bong applies the Code, and in those cases the company has chosen to disregard the rules of the Code, a reason is given in the appropriate section of the Corporate Governance Report.

Bong is a Swedish public limited liability company whose shares are traded on the OMX Nordic Exchange Stockholm in the Small Cap segment. Bong has around 1,200 shareholders.

Responsibility for management and control of Bong is divided between the shareholders at the General Meeting of Shareholders, the Board of Directors, its elected committees and the President/CEO, according to the Swedish Companies Act, other acts and ordinances, the Code and other applicable rules governing listed companies, the Articles of Association and the Board's internal policy instruments.

The purpose of corporate governance is to define a clear division of responsibilities and roles between owners, Board of Directors, executive management and appointed control bodies.

CORPORATE GOVERNANCE REPORT 2011

Owner influence

Governance of Bong is exercised via the General Meeting of Shareholders, the Board of Directors and the President. The highest decision-making body in Bong is the General Meeting of Shareholders.

The Annual General Meeting (AGM) elects the company's Board of Directors. The duties of the AGM also include adopting the company's financial statements, deciding how to distribute the earnings, and deciding whether or not to discharge the members of the Board and the CEO from liability. The AGM also elects Bong's auditors.

About 40 shareholders, representing 76 per cent of the total number of shares and votes in the company, participated in Bong's Annual General Meeting on 12 May 2011 in Malmö. All Board members and the company's auditors were present at the AGM.

Bong's principal shareholders can be seen under the heading Shareholders, page 13.