TELESTE

Annual Report 2006

Teleste

World class solutions for broadband and professional video surveillance networks

Values

» Customer Centricity

We will monitor our business environment, be open and operate proactively. We will understand the customer's overall needs and meet them together. We will be close to the customer – now and in the future. Customer centricity also involves the understanding and appreciation of internal customer relationships.

» Respect

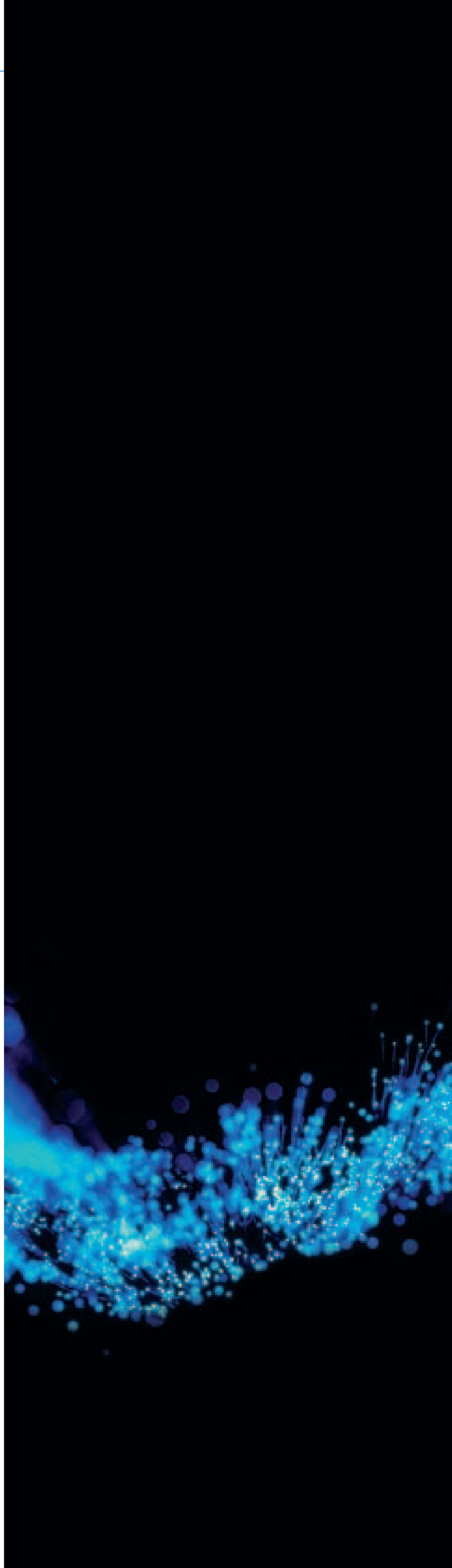
We will respect people and treat them with equal human dignity. We will give recognition, listen and be fair and just. We will communicate openly and give constructive feedback. We will encourage trust and an open, relaxed atmosphere.

» Reliability

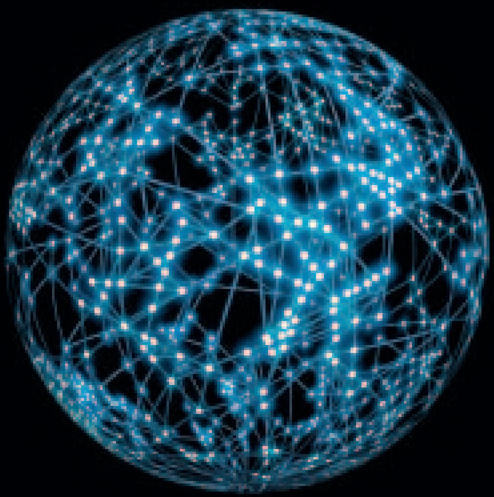
We will do what we promise and follow jointly established procedures and policies. We are all responsible for Teleste's success and each employee is entitled to good leadership. We will act responsibly and abide by laws and regulations.

» Result Orientation

We will make well-timed decisions, set challenging goals, communicate them clearly and complete tasks we set out to accomplish.
We will renew and develop ourselves in order to grow profitably.



The Vision and the Strategic Direction



›› Teleste's objective is to become the leading provider of Broadband Cable Access and Video Surveillance Networks in the world.

›› Even if we are now already the market leader in Europe, as far as both of our businesses are concerned, our aim is set on becoming one of the top three companies in the world.

›› In support of reaching our goals we are determined to provide our customers with continuously improving and increasingly high-quality product and service packages. Our approach is based on continuous improvement and high quality. Excellent customer satisfaction is one of our core targets. Thanks to our comprehensive network of sales offices we can keep a close contact with the customer.

›› We are driven by a continual need to develop our operations. As to production and soursing our core objectives include speed, world-class quality, cost-effectiveness and flexibility. Our production is based on Teleste's own organisation and a few carefully chosen partners.

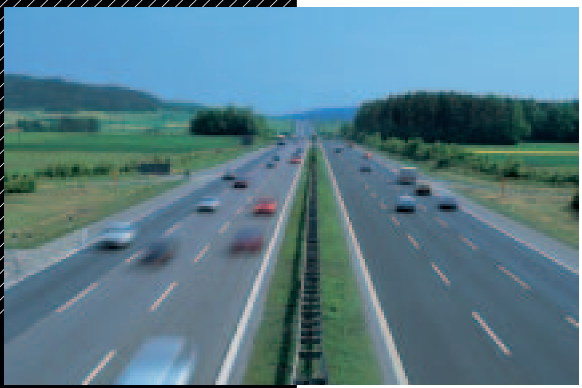
›› We are a high-tech company and our approach is characterised by products tailored precisely to the customer's needs. As to our own organisation or to that of our chosen partners, our product development is based on solid world-class R&D procedures.

›› Our strategy is based on organic growth in the promising business areas. To support this, we are also prepared to consider benefits provided by acquisitions and mergers.

›› Our strengths lie in proficient, innovative and dedicated personnel whose actions are guided by the desire to fulfil the vision shared by the entire company.

›› Our shareholders will be requited by tangible added value achieved through profitable growth. As to our staff, our wish is to create a challenging and inspiring working environment.

›› We encourage open and communicative corporate culture both internally and with our external stakeholders. The cornerstone of all our operation is dependability – we deliver on our promises.



CEO's Letter

With its two businesses Teleste is operational in two highly promising market areas. Broadband Cable Networks – our main business – provides network products and solutions mainly to cable operators, telecommunication operators and distributors. The operators put their networks into effective use by offering video, data and voice services to their subscribers. Video Networks – our second business – provides the public sector and selected industries with high-quality video surveillance solutions. Video surveillance applications are mainly related to management of safety and traffic control to ensure its smooth flow. In strategic terms Teleste is well positioned as both of our businesses are growing and characterised by favourable market trends. We should not, however, forget that when competing for orders in the international marketplace we are facing world-class players. Nevertheless, in 2006 market developed favourably for both of our businesses.

Continued Profitable Growth

In 2006 Teleste continued to grow profitably in line with its specified targets. Orders received grew by 26% amounting to EUR 107 million; net sales increased by 23% totalling EUR 102 million while the net profit grew by 16% to EUR 7 million. Return on capital employed was 24% while the equity ratio stood at 55%. In the year under review our share price went up by 56% and the Board proposed a dividend of 20 cents per share to be paid out.

All in all, figures like these give us reason for contentment, albeit we also faced challenges induced by the growth. Towards the end of the year our production capacity was in full use. Significant frame agreements and launching of the new EttH product range took up a large amount of our capacity. In Q4 relative profitability decreased compared with the same period of the previous year.

Nevertheless, the long-term frame agreements and the new technology for a new market are investments that will yield results in the current year. The EttH technology provides a good case in point as in December 2006 we received a significant new order from South Korea. Similarly, the situation involving our production capacity will be sorted out in Q1 of this year as our new SMT line will become operational. As a whole we can be satisfied with the year and bearing in mind that in terms of growth rate we performed better than the market on average. Moreover, through the significant frame agreements we have created favourable conditions for the present year.

Commercial Breakthroughs

In 2006 we concluded a number of commercially significant order contracts. One of the most important of these was the three-year and over EUR 10 million partnership agreement signed with British

Telecommunications plc on deliveries involving video surveillance technology. We also entered into a EUR 23 million contract with the French Altice on deep fibre supplies, which will cover most of the cable networks in France. Additionally, notable orders were received from Germany and other growing markets of the Central European countries. These projects involved upgrading of networks while expanding the bandwidth so as to enable the operators to provide their subscribers with new interactive services.

At the year-end we achieved an important breakthrough with our new EttH 100 Mb/s technology as the South Korean Hanaro Telecom chose Teleste as their supplier of the high speed broadband access solution for their existing HFC networks. What makes this order particularly significant is the fact that the South Korean market is the undisputed pioneer in broadband technology in the whole world. The customer is going to provide IPTV services (video service based on the Internet protocol) using our EttH technology. These and many other commercial projects kept our organisation effectively busy for the past year.

Special Focus Areas

Our vision is to be a global leader of Broadband Cable Access and professional Video Surveillance Networks in the world. We believe that the business of our main clientele, i.e. the cable operators, will continue to grow. The operators make available a widening range of service packages including video, voice and telecommunications. Especially the new video and TV services will promote demand for increased network capacity and ever faster connections. In addition, the operators want to focus on their core business, which is the development and renewal of their provided services. Our main market is Europe but we see potential for growth also in the Asian markets.

The market for our second business – Video Networks – also showed an increase. In an insecure world there is an increasing demand for investing in video surveillance combating crime and terrorism. CCTV systems are also used more and more widely in applications designed to control continually increasing volumes of traffic. These public sector markets constitute Teleste's main market areas but some special applications in certain industries are also included in our target markets. Geographically speaking the most promising areas include Europe, particularly France and the UK, as well as the United States.

In 2006 we divided our Broadband Cable Business into two separate business units. One of these units specialises in the HFC network business and the development of services for the cable operators. In this area we are the unmatched market leader in Europe. Our objective here is to strengthen our position through continuous development of our HFC products and by ensuring that our operation remains cost-effective. The ranges of amplifiers and the fibre-optic products we stand for will contain an increasing amount of smart functions and features. To be able to offer a truly comprehensive range of HFC products we also need to expand our product portfolio. Moreover, we will develop a whole range of services geared to our clientele with the intention of making it as easy as possible for them to maintain, operate and develop the relevant networks. We believe that outsourcing of and demand for services will increase significantly in the coming years.

The business unit of our other main business will focus on the provision and development of both fast broadband solutions for HFC networks and fibre-optic networks including video processing solutions. As the broadband market expands we intend to make a breakthrough with our own EttH 100 technology. This enables us as one of the first players in the world to provide a reliable bi-directional 100 Mb/s broadband access solution based on the existing cable infrastructure. We have already gained a significant foothold in this area and in 2007 we expect to see a clear upward swing. Besides, for fibre-optic networks we also provide fast FttH solutions. In this particular segment we strengthened our expertise by acquiring the share capital of the Swedish PromaCom AB in June 2006. Our solution to the video signal digitalisation and response to the growing IPTV market is the comprehensive range of IP based HeadEnd amplifiers. These markets are in for some tangible growth in the next few years.

Video Networks, the other business area of ours, will focus intensively on the development of their own product solutions, including primarily the development of software-based products. To complement our range of products we will complement our offerings by bringing in some third-party products. The crucial elements here include understanding customer requirements, efficiency of the operation and making use of a variety of distribution channels. Moreover, we produce integration solutions whereby we assume responsibility for the entire process all the way from the availability of the CCTV network including the solution design, any integration of the video surveillance network into a larger system and a range of maintenance services. The demand for integrated solutions is on the rise because instead of a number of separate standalone products customers now look for comprehensive video surveillance solutions. And here, Teleste's track record in deliveries of large-scale integration solutions is second to none. Referring to the video network management system delivered to the French National Railway Company SNCF should suffice. To address smaller integration solutions, the so-called mid-market segment, in June 2006 we acquired the share capital of the Finnish Suomen Turvakamera Oy. The idea here is to replicate Turvakamera's solutions for the international market through Teleste's international sales network.

Year 2006 in Brief

	2006	*2005*	*Change, %*
Orders received, Meur	*107.4*	*85.4*	*25.8*
Net sales, Meur	*101.8*	*82.6*	*23.3*
Operating profit, Meur	*9.8*	*8.6*	*14.2*
Profit for the financial period, Meur	*6.9*	*6.0*	*15.8*
Earnings per share, eur	*0.41*	*0.35*	*15.2*
Shareholder's equity per share, eur	*2.22*	*1.92*	*15.6*
Return on capital employed, %	*24.3*	*23.7*	*2.5*
Turnover, % of share capital	*81.4*	*62.3*	*30.7*

CEO's Letter

To ensure our customer-centric way of operation we establish a wide service network positioned close to the customer. Teleste runs 38 offices in all quarters of the world in no less than 17 countries. Typically, these offices provide sales and technical support service with some additional functions depending on the given location. Territorial organisations encompassing several countries seek to make the best of the available joint resources in a most efficient manner. Our network in Europe is, indeed, in a class of its own and this in turn enables us to offer the customers in our main market area a readily available service. To complement our own service network in selected market areas we have established ties with partners who are experts in the field.

To maintain our competitive edge we make our operative functions even more cost-efficient while shaping them increasingly flexible in all the relevant segments. Continuous efforts to improve on the processes and personnel enable us to respond faster to the customers' requirements. Enhancements made in our logistics and distribution chain, procurement of components by our plant in China with local manufacturing of volume products have all contributed to the improvement of our competitive edge. This is an on-going process so we are determined to continue on this path of improving our productivity.

Above all Teleste stands for technology with our core expertise being top-notch product development. As far as our lines of business are concerned, we are a world-class centre of expertise in the network technology. Our own R&D personnel are working to cover the most crucial technological key areas. As technologies develop rapidly we ensure the prompt commercialisation of our products by complementing our own product development by teaming up with some selected and competent technology partners. Since our product development departs from customer requirements, we prefer to maintain direct contacts with our key accounts also in issues involving R&D. Our work is conducted in compliance with systematically designed processes, which in combination with the selected development tools allow competitive products and systems to be launched in a fast and controlled manner.

Inspiring Working Environment

Our company operates based on values, which are customer-centricity, reliability, respect and result orientation. We want that our top professionals have a chance to work in a stimulating climate and be well motivated. And as to this, we have also succeeded in being an attractive employer. Personnel turnover has been insignificant and our growth has enabled us to take on new professionals in our organisation. In addition to our accumulated expertise Teleste also has state-of-the-art knowledge based on research about various segments of our business. Our management practices are based on open communication signalling clearly our strategy and targets. Together with the employees we carry out regular appraisal discussions, conduct climate surveys and – based on the received feedback – take developmental action with the object of furthering our areas of knowledge and methods of work. Motivation is ensured by seeing to it that the given work assignments provide sufficient challenge, by proceeding in line with our proven values and by having in place incentive bonus systems. Now as in future, profitable growth of our company is based on our proficient personnel.

Outlook

Teleste features an excellent growth potential. For the current year, signs of the world economy continue to be positive. In Teleste's business international competition is tough and the business environment combined with the involved technological dynamics bring in constant changes. In spite of all this, I believe that the positive market development of our business units will be sustained. The amount of video and the number of various video applications transmitted over networks will grow as the involved services continue to converge. This will push up data transmission rates and increase the number of subscribers to the new and more versatile services in our customer segments. Likewise, the demand for operator services and outsourcing of operations will keep gaining ground. Video surveillance is driven by the increased demand for safety, fear of terrorism and the need to control traffic. Our target is to grow organically but thanks to our strong balance we will also be able to make acquisitions in support with our strategy. Considering the aforementioned premises and bearing in mind our good market position and our customer relations, high-quality products and services, I believe that we will continue on our path of profitable growth in 2007.

Statements of Appreciation

Finally, I wish to thank all our employees for your excellent contribution and exquisite work in developing our company and for achieving the set objectives. I also want to express my heartfelt thanks to our customers, partners and our owners for the successful co-operation in 2006. We will continue to develop this company based on the same principles towards goals of profitable growth and our vision.

Jukka Rinnevaara

Industry Megatrends

Broadband Cable Networks	*Video Networks*
Broadband Internet as a strong growth driver, Triple Play coming	*General acceptance of video surveillance is increasing*
Video (HDTV, IPTV, WebTV, gaming…) is driving bandwidth demand	*Public security market is growing*
Existing cable networks will remain, new uses for the physical access	*The share of management software and storage capacity will increase*
FttH starting slowly, FttP going ahead in new build	*Systems require smarter intelligence and automation*
Broadcast content will become fully digital and networks will follow	
Operators consider outsourcing internal functions	

Shares and Shareholders

Annual General Meeting

Teleste Corporation's Annual General Meeting will be held on 3 April 2007, commencing at 3 p.m., at Finlandia Hall in Helsinki, Mannerheimintie 13 e. Registration begins at 2 p.m.

Shareholders wishing to attend the Annual General Meeting must be registered on the list of shareholders kept by the Finnish Central Securities Depository Ltd no later than Friday, 23 March 2007.

Shareholders wishing to attend the Annual General Meeting must inform the company (address information below) no later than Monday, 26 March 2007 by 4 p.m.

Registration

By telephone +358 (0)2 2605 611
By e-mail investor.relations@teleste.com
By mail Teleste Corporation, Tiina Vuorinen, P.O. Box 323, FI-20101 Turku, Finland

Proxies

Attendance information must be delivered before the deadline specified above. Please make reference to any proxies upon the registration procedure and the relevant document should be delivered to the company before the registration period expires.

Proposal for Distribution of Dividend 2006

The Board of Directors proposes that a dividend of EUR 0.20 per share for the financial year 2006 will be paid to free-floating shares. The dividend will be paid to shareholders who are registered on the record date of 10 April 2006 on the company's Shareholder List, which is kept by the Finnish Central Securities Depository Ltd.

Annual General Meeting	3.4.2007
Dividend ex date	4.4.2007
Dividend record date	10.4.2007
Dividend payment date	17.4.2007

Dividend History eur

1999	2000	2001	2002	2003	2004	2005	2006*
0.10	0.12	0.16	0.08	0.08	0.12	0.16	0.20

* Board proposal

For more information on Annual General Meeting see page 27.

Investor Relations

Teleste's communication objectives include openness and active support to business operations. Our key guidelines involve truthfulness, simultaneity, timeliness and balanced approach. CEO Jukka Rinnevaara is in charge of company communications. In addition to the CEO, the top management of the company is committed to serving various parties of the capital market. Matters related to communications, meetings and contact maintenance are handled by the Assistant to the CEO Tiina Vuorinen.

In the passed year investor activities abounded. In Finland there was a flurry of contacts with investors, analysts and financial correspondents. In addition, we participated in a range of investor and technology seminars set up by a number of different parties. Occasions like these provide an opportunity to meet with the company management and discuss issues related to the company strategy and development based on publicized information. Moreover, on roadshow tours taken in Nordic countries and in Europe in the context of publication of interim results the company has met representatives of foreign investors. Private investors and shareholders will have a chance to meet the management at the Annual General Meeting and, for the spring 2007, when the company takes part in the Investment Evening tour arranged by the Finnish Foundation for Share Promotion.

In line with our open information policy, these activities have been designed to raise awareness among the participants about the company in general, to promote interaction between the company and the participants as well as to provide an accurate and open view for the analysis of investment opportunities.

Publication Schedule for Financial Information in 2007

Annually, Teleste releases the Financial Statement bulletin, Annual Report and three Interim Reports. These publications including the stock exchange releases are available in Finnish and English on Teleste Website under Investors. You can also subscribe to the Interim Reports and the stock exchange releases on the company Website under Investors by accessing News Service under Stock Exchange Releases.

Interim Report January–March	24.4.2007
Interim Report January–June	17.7.2007
Interim Report January–September	23.10.2007
Financial Statements 2007	29.1.2008

Printed Annual Report will be delivered to all the shareholders registered with relevant contact information included in the Finnish Central Securities Depository.

Share Register

Shareholder mailings are conducted based on the information in the shareholder's register kept by the Finnish Central Securities Depository Ltd.

Shareholders are kindly requested to inform the custodian of their book-entry account of any changes in contact details.

In the event the account operator is the Finnish Central Securities Depository any changes should be addressed to:
Finnish Central Securities Depository, P.O. Box 1110, FI-00101 Helsinki, Finland.

Contact Information

In matters involving investor communications our aim is to provide a first-class and up-to-date service.

CEO, Mr. Jukka Rinnevaara is in charge of Teleste's investor relations. Please address any inquiries concerning the company to him as follows:
Phone +358 (0)2 2605 611
E-mail investor.relations@teleste.com

Investor Relations and Press Office:
Teleste Corporation
Tiina Vuorinen
P.O. Box 323
FI-20101 Turku, Finland
Phone +358 (0)2 2605 611
Fax +358 (0)2 2605 812
E-mail investor.relations@teleste.com

Analyst Coverage

According to our information the analysts listed below monitor Teleste's performance on their own volition (the list may be incomplete). Teleste takes no responsibility for the opinions expressed by analysts or for any evaluations presented by them.

CAI Cheuvreux Nordic Ab	Johan Eliason johan.eliason@cheuvreux.com

Shares and Shareholders

Carnegie Investment Bank Ab	Janne Rantanen janne.rantanen@carnegie.fi
Enskilda Securities	Sasu Ristimäki sasu.ristimaki@enskilda.fi
eQ Bank Ltd	Panu Laitinmäki panu.laitinmaki@eQ.fi
Evli Bank Plc	Ilkka Rauvola ilkka.rauvola@evli.com
FIM Securities	Raine Vammelvirta raine.vammelvirta@fim.com
Handelsbanken Capital Markets	Karri Rinta kari05@handelsbanken.se
Kaupthing Bank Oyj	Mika Metsälä mika.metsala@kaupthing.fi
Nordea Markets	Martti Larjo martti.larjo@nordea.com
OKO Pankki Plc	Antti Karessuo antti.karessuo@oko.fi

Share Basics

Teleste Corporation has been listed on the Helsinki Stock Exchange since 1999 and is included in the Mid Cap group on the Nordic list in the Information Technology sector (31.12.2006).

Due to abolition of property taxation no taxable values are specified for quoted shares for the year 2006.

Listed on	30.3.1999
ISIN code	FI0009007728
Trading code	TLT1V
Reuters ticker symbol	TLT1V.HE
Bloomberg ticker symbol	TLT1V FH
Nominal value	0.40
All time high (7 Sebtember 2000)	eur 39.00
All time low	eur 2.21

Liquidity Providing

The agreement entered in August 2005 between Teleste Corporation and Kaupthing Bank on the Liquidity Providing (LP) involving the Teleste Corporation's share has been extended. According to the agreement, Kaupthing Bank will provide Teleste Corporation's share with bids and offers so that the maximum difference between a bid and offer price is 2% of the bid. Bids or offers include at least 500 shares. Kaupthing Bank undertakes to submit bids and offers for Teleste Corporation in the trading system of the Helsinki Stock Exchange on each trading day for at least 85% of the time of continuous trading I and in the Exchange's opening and closing auction procedures applicable to Teleste Corporation.

Liquidity Providing is designed to increase liquidity of the share and reduce volatility in the relevant price stability and, by so means, facilitate trading by private investors.

Share Turnover on the Helsinki Exchange

In 2006 the share price and turnover of Teleste's share developed favourably with the share's price fluctuation remaining stable. In 2006 the turnover was 14.16 million shares whereas in the previous year the relevant figure was 10.79 million. In terms of percentage the growth for the period under review was 31.2%.

In 2006 the share price of the company share grew by 56%. As to share price in 2006 the low was EUR 6.46 (2005: 5.85) and the high EUR 12.75 (2005: 8.35). Closing price at the end of the year stood at EUR 11.63 (7.45).

Market capitalization at the year-end stood at EUR 202,237,582 (2005: 129,181,152).

Dividend Policy

Teleste intends to be an interesting investee corporation in which the investment's increase in value and the dividend yield form a competitive combination. The annual proposal for the dividend is validated by the Board in consideration of profitability, financial situation and needs for investment necessitated by profitable growth.

The Board of Directors proposes that a dividend of EUR 0.20 per share for the financial year 2006 will be paid to free-floating shares.

Share Capital and the Number of Shares

According to Articles of Association, the minimum share capital of Teleste Corporation is EUR 6,400,000, while the maximum authorised capital amounts to EUR 25,600,000. Thus, the company share capital may be increased or decreased within these limits without amending the Articles of Association.

On 31 December 2006 registered share capital of Teleste Corporation amounted to EUR 6,955,720.80, which is divided into 17,389,302 shares.

Increases in Share Capital in 2006

Date of registration	*Stock option*	*Number of new shares*	*New total number of shares*	*New share capital, euros*
10.5.2006	*2002A*	*4 000*		
	2002B	*10 000*	*17 353 752*	*6 941 500.80*
24.7.2006	*2002B*	*29 000*	*17 382 752*	*6 953 100.80*
14.9.2006	*2002A*	*4 000*		
	2002B	*100*	*17 386 852*	*6 954 740.80*
20.11.2006	*2002A*	*2 000*		
	2002B	*450*	*17 389 302*	*6 955 720.80*

Nominal value of the share is EUR 0.40. Teleste Corporation has one share class and in the Annual General Meeting each share has one vote.

The company shares are included in the book-entry securities system.

In 2006 the increases in share capital were attributed to share subscriptions made on the basis of 2002A and B options. In the period 10,000 own shares were subscribed using 2002A options and 39,550 using 2002B options.

Authorisations for the Board of Directors

The Annual General Meeting authorised the Board to acquire the maximum of 1,215,000 Teleste's own shares, convey at most 1,700,000 own shares and increase the share capital by a new issue of maximum 1,360,000 shares. These authorisations are valid for one year from the decision of the Annual General Meeting, i.e. they expire on 4 April 2007.

Own Shares

At the end of 2006 Teleste possessed 455,000 of the company's own shares.

In the financial period authorisations granted by the Annual General Meeting were used by conveying 30,000 own shares in the acquisition of Suomen Turvakamera Oy. Other authorisations were not used.

Redemption Obligation

Teleste Corporation's Articles of Association include a clause related to redemption obligation. This article stipulates that a shareholder whose proportional holding of all Company shares, either individually or jointly with other shareholders, as defined hereinafter, is or exceeds 33 1/3 per cent or 50 per cent (shareholder subject to redemption obligation) as defined hereinafter is obliged on demand by other shareholders (shareholders with rights of redemption) to redeem such shareholders' shares, and securities giving entitlement to them under the Companies Act, in the amount so demanded by the shareholders with rights of redemption and in the manner stipulated in the Article. This clause involving the redemption obligation has been specified in detail in the Articles of Association.

Share-based Incentive Schemes

The Teleste reward programs include two share option programs for the management and key personnel. As of beginning of 2006 a share bonus scheme has been in place for the company Management Group making up a part of their target remuneration. On 4 April 2006 the Annual General Meeting confirmed the extension of conveyance of company's own shares enabling introduction of share-based incentive schemes.

Insider Register

As of 1 March 2000, the company has followed the insider regulations (revised on 1 January 2006) laid down by the Board of Directors of the Helsinki Exchanges. These regulations have been supplemented by company internal specifications. Membership in the Teleste permanent insider register is based on position. Thus, the group consists of members of the Board of Directors, the CEO and the auditors. Furthermore, the extended insider register includes members of the Management Group and the CEO's assistant.

Project-specific insider register includes personnel who, based on their position, have access to company-related information, which upon publication may affect the value formation of the company's share. The CEO will assess, on a case-by-case basis, whether an issue or arrangement under preparation will be defined as a project.

The permanent members of Teleste's insider register are obliged by the so-called Silent Period during which trading on company shares is banned completely for 14 days preceding publication of Interim Reports and the Financial Statements. During the specified period Teleste will not engage in any meetings with investors or analysts and Group representatives are not allowed to comment upon company results.

The company insider administration is included in the SIRE system of the Finnish Central Securities Depository.

Flagging Notifications

The largest single shareholder at the end of 2006 was the Sampo Life Insurance Company Ltd with a 9.34% holding.

In January 2006, Ilmarinen Mutual Pension Insurance Company reported its ownership having increased up to 5.42%. In August 2006, Schroder Investment Management Limited flagged their holding to have reached 5.01%.

Option Program

Date of Annual General Meeting	*Share option program*	*Number of shares*	*Subscription period*	*Subscription price 31.12.2006*	*Period of subscription price*
8.4.2002	*2002A*	*275 000*	*1.2.2005–1.10.2007*	*6.95*	*1.–30.4.2002*
	2002B	*275 000*	*1.2.2006–1.10.2008*	*2.29*	*1.–30.4.2003*
16.3.2004	*2004A1*	*150 000*	*1.4.2007–30.4.2009*	*5.70*	*1.–30.4.2004*
	*2004A2 **	*150 000*		*5.70*	*1.–30.4.2004*
	2004B1	*150 000*	*1.4.2008–30.4.2010*	*6.31*	*1.–30.4.2005*
	*2004B2 ***	*150 000*		*6.31*	*1.–30.4.2005*

** Options were released for subscription once certain financial goals determined in advance by the Board of Teleste Corporation were realized on 31 December 2006.*

*** Options are free for subscription only when certain financial goals determined in advance by the Board of Teleste Corporation are met on 31 December 2007.*

Shares and Shareholders

Public Insider Register and the Holdings on 31 December 2006

The Board of Directors	*Basis*	*Shares*	*Options*
Hintikka Tapio Jussi Anselmi	*Chairman of the Board*	*10 203*	*–*
Laaksonen Tero Mikael	*Member of the Board*	*20 643*	*–*
Raatikainen Kari Pertti	*Member of the Board*	*5 034*	*–*
Toivila Timo Tapio	*Member of the Board*	*51 784*	*–*
Vennamo Pekka Veikko	*Member of the Board*	*9 865*	*–*
Total		*97 529*	*–*
Management Group			
Rinnevaara Jukka Tapani	*President and CEO*	*11 800*	*135 000*
Bryssinck Reinaart Jozef Maria	*Other criteria for disclosure requirement*	*–*	*18 000*
Järvenreuna Juha Pekka	*Other criteria for disclosure requirement*	*2 000*	*40 000*
Kinnunen Esa	*Other criteria for disclosure requirement*	*–*	*–*
Myllylä Esko Olavi	*Other criteria for disclosure requirement*	*2 880*	*21 000*
Saarikoski Erja Pirkko Marjatta	*Other criteria for disclosure requirement*	*4 000*	*40 000*
Slotte Carl Johan Henrik	*Other criteria for disclosure requirement*	*1 900*	*50 900*
Vuorinen Tiina	*Other criteria for disclosure requirement*	*330*	*6 000*
Total		*20 910*	*300 700*
Auditors			
Nyman Sixten Ove	*Chief auditor*	*–*	*–*
Kailiala Esa	*Deputy auditor*	*–*	*–*
Total		*–*	*–*

For presentation of the Members of the Board of Directors see page 29. For presentation of the company Management Group see page 26.

Distribution of Ownership

At year-end 2006, the number of Teleste shareholders totalled 5,601, whereas the comparable figure for 2005 was 6,228. At the end of the year, foreign and nominee-register accounted for 20.53% (2005: 13.6%).

Sector Dispersion on 31 December 2006	*Shares*	*Percentage of shares*
Companies	*1 624 317*	*9.34*
Financial institutions	*5 128 736*	*29.49*
Public institutions	*2 713 131*	*15.60*
Non-profit organisations	*1 020 430*	*5.87*
Private individuals	*3 332 470*	*19.16*
Foreign and nominee registered	*3 570 218*	*20.53*
Total	*17 389 302*	*100.00*

Holding Dispersion	*Number of shareholders*	*Percentage of shares*	*Shares*	*Percentage of shares*
1–100	*1 357*	*24.23*	*98 493*	*0.57*
101–1 000	*3 426*	*61.17*	*1 389 733*	*7.99*
1 001–10 000	*742*	*13.25*	*2 153 301*	*12.38*
10 001–100 000	*56*	*1.00*	*1 616 307*	*9.29*
100 001–	*20*	*0.36*	*9 035 398*	*51.96*
Total	*5 601*	*100.00*	*14 293 232*	*82.20*
Nominee registered			*3 096 070*	*17.80*
Total			*17 389 302*	*100.00*

Largest Shareholders 31 December 2006

		Shares	Percentage of shares
1.	Sampo Life Insurance Company Ltd	1 624 200	9.34
2.	Ilmarinen Mutual Pension Insurance Company	1 284 931	7.39
3.	Kaleva Mutual Insurance Company	785 900	4.52
4.	Op-Suomi Pienyhtiöt	588 900	3.39
5.	FIM Fenno Mutual Fund	572 639	3.29
6.	Aktia Capital Mutual Fund	521 450	3.00
7.	Varma Mutual Pension Insurance Company	508 150	2.92
8.	The State Pension Fund	500 000	2.88
9.	Teleste Corporation	455 000	2.62
10.	Fondita Nordic Small Cap Placfond	360 000	2.07
11.	Nordea Nordic Small Cap Mutual Fund	305 350	1.76
12.	Odin Forvaltnings As	284 050	1.63
13.	Mutual Insurance Company Pension-Fennia	220 000	1.27
14.	FIM Forte Mutual Fund	203 350	1.17
15.	Pension Insurance Company Veritas	175 000	1.01
16.	Evli Bank Plc	152 718	0.88
17.	Aktia Secura Mutual Fund	146 150	0.84
18.	Sumato Oy	122 610	0.71
19.	Svenska Handelsbanken Ab (publ.), filial	114 000	0.66
20.	Svenska litteratursällskapet i Finland	111 000	0.64
21.	Renkkeli Oy	100 000	0.58
22.	Royal Skandia Life Assurance Ltd Eib	82 610	0.48
23.	Fondita 2000+ Mutual Fund	80 000	0.46
24.	Veikko Laine Oy	77 100	0.44
25.	Fondita Nordic Micro Cap Placeringsfond	75 000	0.43

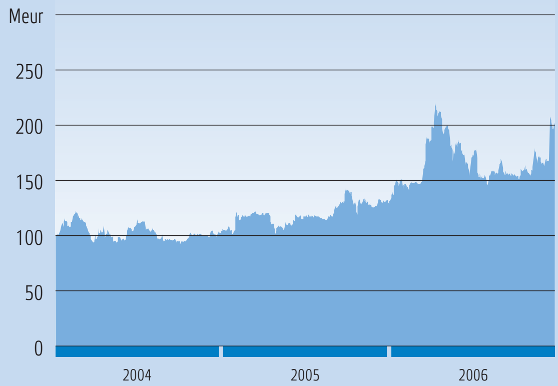
Provided data is based on the company shareholder's register kept by the Finnish Central Security Depository.

Key Figures by Share

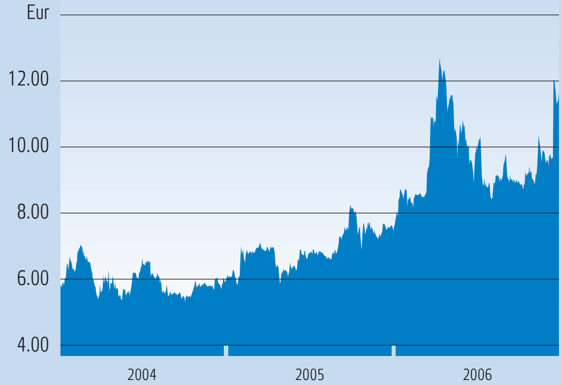
	2006	2005	2004
Earnings per share, eur	0.41	0.35	0.23
Earnings per share fully diluted, eur	0.38	0.33	0.22
Shareholders equity per share, eur	2.22	1.92	1.65
Dividend distribution, Meur	3.4	2.7	2.0
Dividend per share, eur	0.20*	0.16	0.12
Dividend per net result, %	49.5	45.7	52.2
Effective dividend yield, %	1.7	2.1	2.0
Closing price, eur	11.63	7.45	6.02
Price per earnings	28.6	21.0	25.8
Market capitalisation, Meur	202.2	129.2	101.4
Turnover, Meur	138.9	75.3	74.2
Turnover, number in millions	14.16	108	12.3
Turnover, % of share capital	81.4	62.3	70.9
Average number of shares	17 363 102	17 339 752	17 334 235
Number of shares at the year-end	17 389 302	17 339 752	17 339 752

** The Board's proposal to the Annual General Meeting*

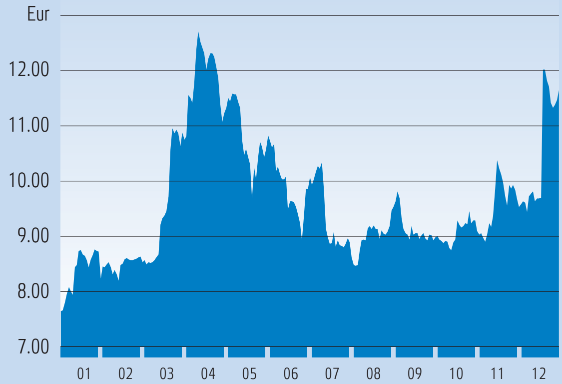
Market Value Development 2004–2006



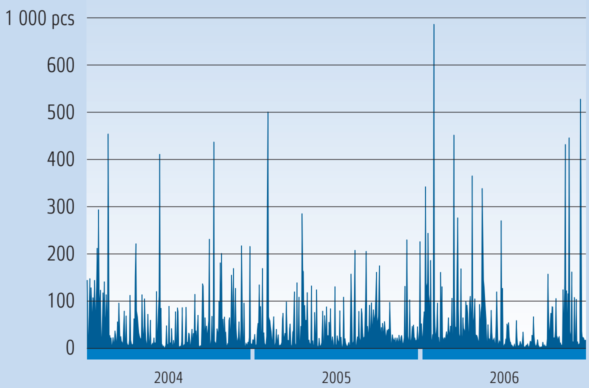
Share Price Development 2004–2006



Share Price Development 2006



Share Turnover 2004–2006



Stock Exchange Releases

In 2006 Teleste published a total of 33 stock exchange releases or announcements. See the highlights below.

12 January 2006:
Significant order from the Belgian Brutélé. Value of order is EUR 4 million.

18 January 2006:
Order from the German ImmoMediaNet GmbH. Value of the order is more than EUR 4 million.

21 March 2006:
Signing of letter of intent with the Dutch Essent Kabelcom on delivery of Teleste's high-speed (100 Mb/s) EttH solution.

3 April 2006:
Signing of frame agreement with British Telecom. Value of the contract exceeds EUR 10 million.

26 April 2006:
Teleste was chosen as the primary supplier of Elisa's broadband access networks. Value of the contract is EUR 2.5 million.

2 May 2006:
The Swedish cable operator chooses Teleste for their supplier of HFC products. Value of the three-year contract exceeds EUR 5 million.

2 June 2006:
Teleste acquires the Finnish Suomen Turvakamera Oy to strengthen the position of Video Networks business as a supplier of turnkey solutions.

19 June 2006:
Teleste acquires the Swedish system integrator PromaCom AB to strenghten its expertise in FttH solutions.

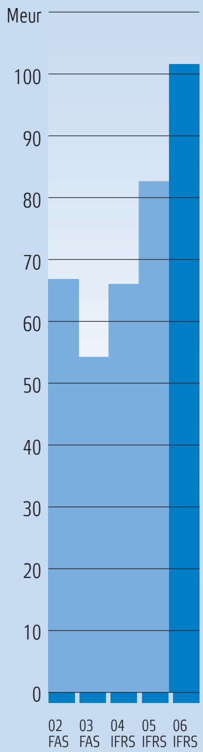
13 November 2006:
The existing frame agreement with the French Altice Group is extended. Value of the new extension agreement amounts to EUR 23 million.

15 December 2006:
The South Korean Hanaro Telecom chooses Teleste's EttH solution. Value of the first order placed in the project amounts to EUR 4.5 million.

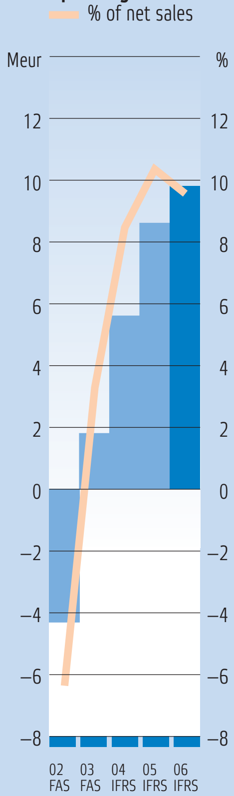
18 December 2006:
Teleste signs a frame agreement with a leading hospitality solutions provider. The order involves Teleste's Digital headend equipment together with Integration and support services. Value of the order is more than EUR 5 million.

See the company Website for a complete summary of the stock exchange releases and bulletins of 2006.

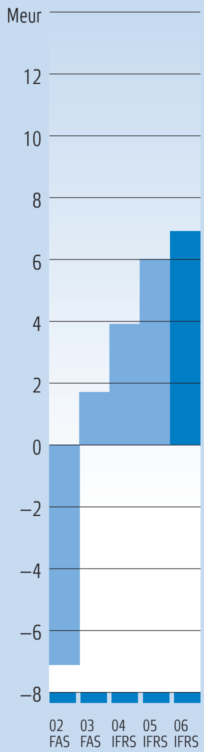
Net Sales



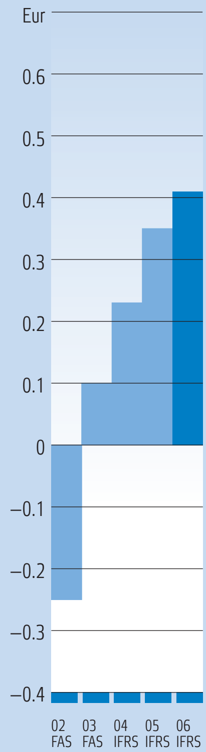
Operating Profit



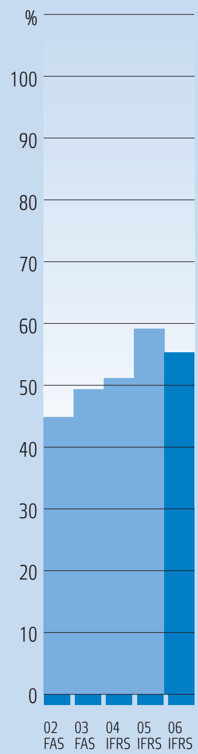
Profit for the Financial Period



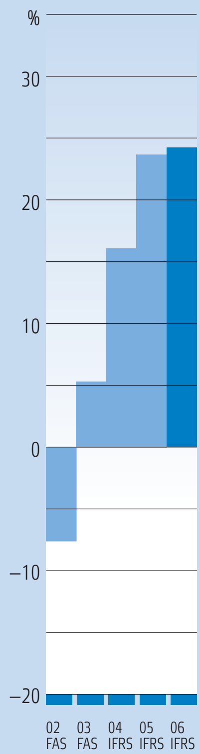
Earnings per Share



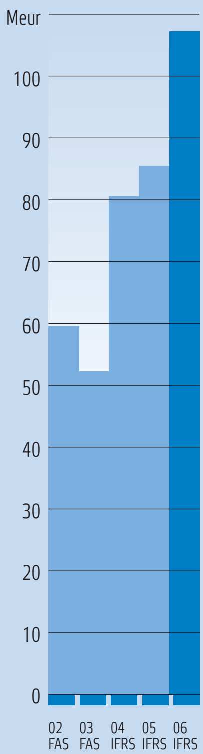
Equity Ratio



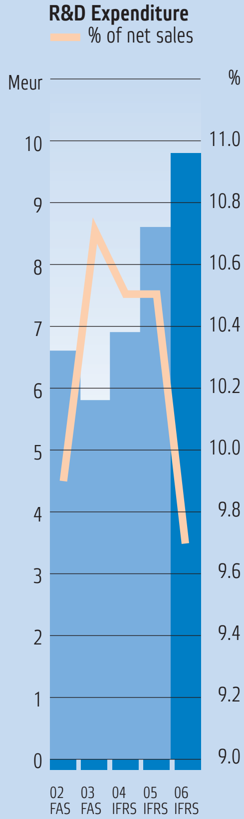
Return on Capital Employed



Orders Received



R&D Expenditure



Concern for the Environment

Concern for the Environment

We at Teleste act responsibly in environmental issues and wish to adopt an overall approach in support of sustainable development. Based on continuous improvement and in line with our environmental policy we are committed to reduce the environmental impacts of our own operations.

Product-driven environmental policies of the EU have shifted the focus of legislation from regulation of production to addressing the environmental impact of the product life-cycle as a whole. The involved changes have brought about substantial effects on the electrical and electronic industry and we at Teleste have adopted an active role in the related co-operation.

Statutory development is becoming increasingly product-driven across the board. We at Teleste keep a keen eye on developments in different markets and any implications thereof to our operations.

Operative Activities Cause of Minor Environmental Impact

At Teleste, environmental load caused by our production process is relatively low compared to the impact of the product life-cycle as a whole. Our production is based on assembly of printed circuit boards and electronic equipment giving no rise to significant discharges. The main causes of environmental aspects related to Teleste's operative activities include generation of waste, energy consumption and transport.

Most of the waste is recycled or used for energy production whereas only a fraction is disposed of in a landfill.

Items consuming energy include heating and power for production facilities, testing equipment and office equipment. In 2006 Teleste entered into an agreement with an electricity company concerning delivery of electricity produced by renewable sources of energy for our facilities in Finland.

Our logistics is designed to reduce the environmental impact to the minimum. By means of modern information technology, such as audio conferencing, we also pursue to do our bit in cutting down on business travel.

Similarly, we encourage our staff to select their means of transportation so as to be in line with our environmental policies. Thus, in summertime many of us commute riding a bike. In token of this, in summer 2006 we took part in the local inter-office 'go by bike' competition.

And when it comes to environmental issues and degree of commitment we apply the same standards to our suppliers by performing, for example, supplier assessments.

Environmentally Friendly Products

At Teleste, management of environmental issues is focussed on environmental impact control encompassing the product's life-cycle as a whole. This puts more emphasis on the significance of cooperation with our suppliers, sub-suppliers and customers. Product development provides a great tool for minimising the environmental impact of a given product.

Currently, our final products mainly consist of recyclable materials. In comparison with electronics in general, cable network equipment and video surveillance systems constitute relatively long-term investments. In addition, they are maintainable as well as upgradable meaning their life-cycle can be extended even more. This is to say that the single most significant environmental aspect related to our products is the power they consume.

The materials we use for packaging our final products are, for the most part, recyclable. These materials are mainly fibrous and, thus, easily recyclable.

And in the future, management of environmental issues related to products will only gain in importance. As to this, management of any product-specific information is about to become a key concern.

Teleste facilities in Finland received the first ISO 14001 Certification in 2006.

Objectives

To lessen the load we will specify a set of environmental objectives for our operation designed to be subject to an annual follow-up. In 2006 we launched systematic monitoring of environmental indicators, raising awareness among the staff in environmental issues through training while making further improvements in our sorting of waste and waste management practises.

A significant project having taken place in the period of 2005 to 2006 involved preparing for the European Union RoHS* directive banning the placing on the EU market of electrical and electronic equipment containing specified hazardous materials. Even before coming into force of the RoHS regulations Teleste has been breaking ground in the usage of lead-free soldering processes.

Our distinct objective for 2006 was to set up an environmental management system for our Finnish unit meeting the ISO 14001 requirements. As a result our environmental management system complying with ISO14001:2004 was certified in summer 2006.

**RoHS=Restriction of Hazardous Substances*

›› We understand environmental protection as a strategic choice that is in harmony with Teleste's economic and qualitative objectives.

›› We recognize the value of environmental responsibility and we are committed to sustainable development, prevention of pollution and reduction of resource consumption.

›› We comply with relevant environmental legislation, regulations and other requirements to which we subscribe.

Our Business Units

Our Business Areas

The Teleste way of making business is based on solid competence and innovative operation in two Business Areas characterised by vigorous growth and intense development. Our Business Areas are among the global leaders in supplying broadband cable networks and video surveillance networks and are recognised for their know-how and ability to produce technically cutting edge solutions year after year.

Our *Broadband Cable Networks* business consists organisationally of two Business Units that aim at promoting the business of cable operators as the primary clientele. We open the way to new versatile media world for the end users at home and businesses by offering the video quality and the data speeds of tomorrow, already today. This is achieved by making available advanced network solutions, which allow the operators to be prepared for the increasing expectations of the consumers whilst facing the challenges involved in the ever toughening market competition.

Our *Video Networks* business delivers world-class network solutions globally with official authorities as the primary clientele. We aim to improve the security and efficiency of society, by manufacturing and delivering professional video surveillance network solutions for the transmission of video, data and audio.

The core of our business can be defined with just one sentence: we combine understanding of technology and customer needs into enduring network solutions.

We are widely recognized in the industry for one of our strong success factors: we fill the gap between the standards and customer needs!

Broadband Cable Networks

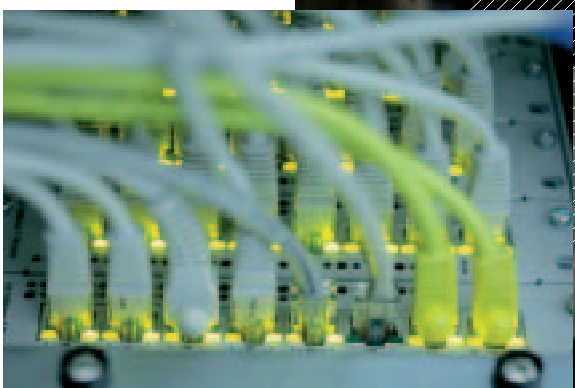
	2006	*2005*	*Growth*
Net Sales	*85.6 Meur*	*67.2 Meur*	*27%*
Order Intake	*92.8 Meur*	*72.9 Meur*	*27%*

			Export sales share	
Net Sales	*2006*	*2005*	*2006*	*2005*
Finland	*7.0 Meur*	*8.2 Meur*		
Export	*78.6 Meur*	*59.0 Meur*	*92%*	*88%*
Total	*85.6 Meur*	*67.2 Meur*		

Video Networks

	2006	*2005*	*Growth*
Net Sales	*16.2 Meur*	*15.4 Meur*	*5%*
Order Intake	*14.4 Meur*	*12.5 Meur*	*15%*

			Export sales share	
Net Sales	*2006*	*2005*	*2006*	*2005*
Finland	*2.6 Meur*	*0.6 Meur*		
Export	*13.6 Meur*	*14.8 Meur*	*84%*	*96%*
Total	*16.2 Meur*	*15.4 Meur*		



Business Unit HFC Networks and Services (HFCNS)

Business Description

The clientele of Teleste's Hybrid Fibre-Coaxial (HFC) Networks and Services Business Unit (HFCNS) consists of cable operators and cable network equipment distributors. The cable operators, in turn, provide end-users with three main basic services: video, telephone connections and broadband data services.

The HFCNS business unit provides cable operators with products and solutions for building hybrid fibre-coaxial (HFC) networks as well as services related to the construction and maintenance of the networks. These solutions contain both stand-alone applications and integrated network deliveries.

The transmission network covers solutions for signal transfer both in fibre-optic and copper cabling, the transmission technology itself being analogue.

Our main market area is Europe, where the business unit currently has 17 own offices and several channel sales partners.

Cable Operators Focus on Provision of a Variety of Telecommunication Services

Business of the European cable operators is shifting towards offering an ever widening range of telecommunication services for the benefit of end-users. In practice this means that the amount of data transferred over the HFC network infrastructure will increase pushing up demands set to its transfer capacity. On the other hand, the cable operators will focus increasingly on their core business – building up and running a whole host of services on their HFC networks.

Basically, there are two ways to increase the capacity of an HFC network. First, you can expand the available RF band and/or, second, segment the existing cable network structure into smaller cell areas. The first option requires network equipment covering a wider RF bandwidth whereas the latter one necessitates cost-effective fibre-optic and amplifier solutions adapted specifically to small cell areas. In most cases, the operators first increase the width of the used RF band after which they move over to segmentation of their fibre-optic network. This segmentation of cable networks and feeding the fibre closer to the end-users will drive the use of fibre optic technology. One of the key concepts here is the so-called deep fibre solution where the fibre-optic can be extended very close to the end-user with only the last leg of the access line being based on conventional coaxial cabling.

Nevertheless, we at Teleste do not take the view that pure fibre-optic networks would provide the operators with a commercially viable and cost-effective access solution. In such a case investments per end-user would get considerably higher compared to those using the copper-based coaxial network infrastructure.

The fact that the cable operators are increasingly paying attention on management of services in the cable network opens up new opportunities for the partners to provide network infrastructure related services. Some customers have started outsourcing of functions not considered as part of the operator's core business. This trend is expected to continue and strengthen in the years to come.

Small local companies involved in the construction, maintenance and distribution services will require larger international partnerships in order to continue the business within consolidated operator market. Clientele merge into ever larger groupings, a development clearly visible especially in Belgium, Netherlands, Sweden and UK.

The most notable competing network technologies include the IP-based data network solutions offered by the city carriers. Compared to the aforementioned networks the greatest benefit provided by the cable network technology is its ability to transfer large amount of analogue and digital video. All currently available telecommunication services can be supplied to households through this type of network.

In 2006 consolidation among the operators went on. The American-owned UPC sold their cable networks in Sweden and Norway to local cable operators, the merger between NTL and Telewest was sealed in the UK and the Dutch Essent Kabelcom was sold to an international investment company.

Direction and the Steps to be Taken

The strategy of the HFCNS business unit is based on both technology and service strategies, which complement each other by ways of support and synergy.

The significance of the technology strategy will be further emphasised becauce, as we see it, the number of standard solutions included in the HFC technology will increase markedly from the current situation. Regardless of this, customised amplifier solutions will continue to make a vital part of the business. The significance of software as an integral component of the product solution and network management will continue to increase in importance. Due to the technical backgrounds of the current HFC networks the large European operators will continue to have a need to be able technically to customise their systems with the help of their key supply partners.

The proper and correctly timed technical solutions will play a vital role in the future as the fibre-optic solution is extended closer to the end-user. Our deep fibre strategy is based on two models of evolution: the first being the traditional, bi-directional HFC network upgrade, which is gradually converging on the fibre-optic networks. On the other hand, the unidirectional HFC network will be used for a broad-casting video distribution while the data network will be built alongside it, completely separately.

HFCNS Business Unit

Vision	*To be the leading supplier of HFC solutions in the world*
Mission	*To enable enhanced entertainment content to households via innovative and reliable network solutions and services*
Solution	*Wide-ranging and innovative product portfolio supported with strong local services*
Key markets	*Europe*
Primary clientele	*Cable operators and of cable network equipment distributors*

Our product portfolio will be expanded and enhanced with regard to the needs of the HFC network. To support our currently available product offerings we provide an integrated HFC supply chain management concept as well as other technical and logistical service solutions needed when building and maintaining the operator's network. Network planning services as well as repair and upgrade services are good examples of this.

Geographically our main market remains Western Europe even if the rapidly developing areas in Eastern Europe are considered as a new and emerging strategic market. Moreover, our business based on the selected techno-commercial solutions will continue in the Asian market.

Year 2006

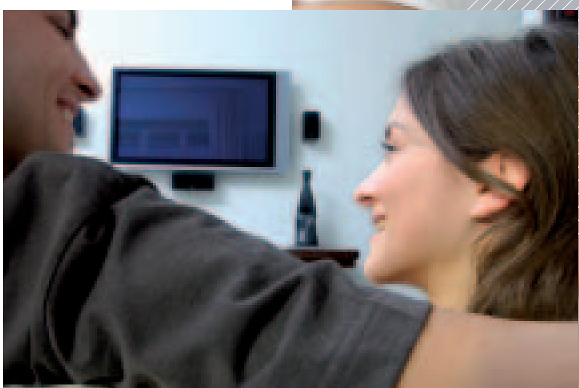
2006 was a year marked by supply projects of great volume, especially for the AC amplifier family. In terms of sheer numbers of manufactured amplifiers Teleste's previous records were broken and the production capacity was expanded from that of the previous year. As to manufacturing of parts and products we drove cost-effectiveness in China by increasing the number of employees in our Chinese plant assigned to the assembly of standard amplifiers. The number of employees assembling customised amplifier solutions at our plants in Finland was also increased. The most notable client projects included the Brutélé AC amplifier project in Belgium and yet another significant customised amplifier delivery project for a large West-European operator.

The deep fibre solution developed and delivered by Teleste was found to be an excellent and reliable solution in France, which paved the way to one of the biggest framework agreements in Teleste's history with Altice Group. This three-year agreement involves most of the deep fibre upgrading conducted by Altice in France.

Deliveries of the BK trunk line amplifiers for KDG in Germany were continued. Teleste ranks among one of the three key suppliers of BK technology for German cable networks. The relevant framework agreement was continued in spring to the end of the year and the volumes in terms of delivery remained on a high level.

Our sales organisation underwent some reforms as the regional structure was strengthened and the organisation was divided into five geographical areas. The aim here is further to increase our market share especially among the European cable operator base.

As to our product development the priority areas included three different product segments. First, the development of automatically controlled range of amplifiers was launched and the development continued actively throughout the year. Secondly, a cost-effective fibre-optic receiver was adapted for the deep fibre networks especially to support our strategy in Russia. And thirdly, in addition to the aforementioned development programmes and client customisations the first stage of the HDO fibre link system was completed.



Business Unit Digital Video and Broadband Solutions (DVBS)

Business Description

Teleste Digital Video and Broadband Solutions (DVBS) delivers solutions in the field of video signal processing and broadband access for cable and next generation networks. On the one hand, the business is focused on delivering advanced network solutions for high-speed broadband to cable operators and next generation network operators. This allows these operators to deliver 100 Mb/s speeds to their customers over existing coax infrastructures or new fiber rich networks.

On the other hand, DVBS uses its expertise in IP and video technologies to provide end-to-end solutions in video-processing to support these same customers in the roll-out of digital and interactive video services over these networks.

Additionally, DVBS offers value added services to assist the operators to commission, maintain and even run their networks and headends.

Typical customers include Cable Operators, Multi Service Operators (MSO), City Carriers, Utilities, Hospitality Integrators and smaller Telco's.

Through the combination of IP and video know-how, of service and network understanding, DVBS can offer its customers a wide and in depth solutions & services portfolio that enables them to build and run better networks, eventually giving them an economical advantage over their competitors. Teleste's long experience in creating enduring networks with a customized twist allows DVBS to offer perfect fit solutions in places where middle-of-the-road offerings fail to perform. DVBS activities are global and are supported by Teleste's network of sales and support offices and partners, which it shares with the HFCNS business unit.

Video Drives Broadband Growth

Although video processing and broadband access can be seen as two independent markets, there are many areas where the two worlds meet and influence each other. 2006 saw the revival of the video service, in many different fields. The revival of the Internet, commonly nick-named Web 2.0, was largely driven by video applications, which has loaded the broadband market with higher speed and capacity requirements. The roll-out of IPTV services by many Telco's has also created the realization that increased speed and capacity in access networks are needed. The de-facto interactive nature of IPTV services has driven traditional cable operators to increase the interactivity in their offering, which has created a wave of investments in headends around the world. In Europe, this is reinforced by the politically driven analogue switch-off that has started and should be completed by 2012.

The trends of 2006 are expected to continue over the next few years and will drive the DVBS business to further growth. We expect more operators to start deploying 100 Mb/s Ethernet to the Home (Etth) technology to support their high bandwidth applications, as the reuse of existing coax creates a strong economical and time-to-market advantage. For new built networks and network extensions, it can be expected that fibre to the building (FttB) and the home (FttH) will become more and more the technology of choice.

In the professional video field, we expect a strong demand among mid size operators for cost-effective headend solutions that offer an increased level of interactivity (Video and Music on Demand, Games etc.), to prepare the switch over to digital and to fight of the threat of IPTV roll-outs by incumbent telecom operators.

In the Satellite Master Antenna Television (SMATV) headend segment, an uptake of investments to renovate legacy analogue headends can be expected, but at the same time we can see the interest growing at telecom operators to take over these networks and run them through a deep fibre infrastructure. All in all, strong growth can be expected in the different DVBS business segments, and in most geographical areas. The recent successes in Korea (broadband) and India (Video) also offer great opportunities to establish a stronger presence in the APAC market.

Direction and the Steps to be taken

In the broadband space our primary aim is to support leading cable MSO's and other operators having access to cable infrastructure in their migration to next generation broadband networks. Through our Etth (Ethernet to the Home) portfolio we provide these operators with cost-effective network solutions to provide services that are normally only possible over FttH type of networks. At the same time we prepare the further migration to fiber rich networks, and we supply end to end solutions in FttH with a strong accent on maintaining the legacy TV services in these networks through radio frequency overlay solutions.

During 2007 we will further complete our Etth product portfolio and widen the adoption of the technology, either as a stand alone solution or as the extension of FttB architectures. This will be done through own channels as well as strategic partnerships with leading telecom equipment vendors and integrators that can benefit from Teleste's competence in cable.

DVBS Business Unit

Vision	*Being a global leader in the field of broadband and video solutions for cable networks and next generation access networks*
Mission	*To provide innovative solutions & services in the field of video and broadband over existing and next generation networks to enhance the competitiveness of cable and next generation network operators*
Solution	*Enduring next generation broadband networks & cost effective video headend solutions*
Key markets	*Europe and selected markets in Asia*
Key clientele	*Cable Operators, City Carries, Hospitality Integrators, Small Telco´s*

In the FttH domain, we will further complete our product portfolio and expand our geographical playing field within Scandinavia while keeping an interested eye on opportunities in the rest of Europe. Strong attention will be paid to the guiding of cable operators that want to make the move into FttH, without loosing the operational advantages of their existing cable plants.

In the domain of video processing, DVBS will focus on the professional mid sized headends, which in the coming years will have to be upgraded to digital. The aim is to offer cost-competitive interactive solutions through a combination of own core systems and complementary products from strategic business partners. In the field of SMATV Teleste will continue to provide top range mini headend solutions through a network of distributors and channel partners, which will be expanded throughout Europe.

Via its Project & Implementation team, the DVBS solutions are complemented by a range of value added services that support our customers either by the introduction (installation, commissioning, project management, consulting), maintenance (24/7 support, annual check up, maintenance agreement) or continuous operation (managed headends, remote Network Operating Centre) of the delivered solutions.

Highlights of 2006

Essent Kabelcom's confirms its support in Teleste's Etth solution and signs a new LoI to deploy Teleste's 100 Mb/s solution in the Netherlands.

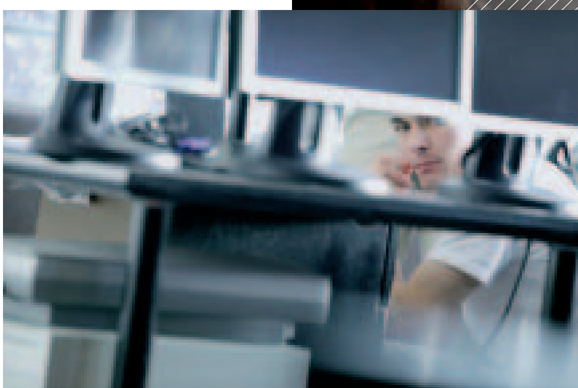
Teleste reorganizes and splits Broadband Cable Networks into two separate business units. Digital Video and Broadband Solutions is born.

Teleste acquires PromaCom AB and establishes a strong foothold in FttH network solutions in the Scandinavian market.

Teleste delivers multiple headends to various operators in India and positions itself strongly as a major headend supplier to Indian MSO's.

Hanaro Telecom, the major cable operator in the Republic of South Korea, selects Teleste's Etth technology for the roll-out of 100 Mb/s services in its networks.

Teleste signs a strategic frame agreement with a major hospitality integrator for the supply of 1,000 headends over the next 3 years.



Business Unit Video Networks

Business Description

Teleste Video Networks provides total CCTV solutions for video surveillance applications, specialising in areas such as high-quality real-time video, audio and data transmission, networking and recording.

The main end user group of Teleste Video Networks solutions are local authorities. Key applications are road and rail transportation, urban surveillance and other applications related to public safety such as border control for ports and airports as well as utilities and industrial processes.

Teleste Video Networks' aim is to address the client specific requirements with comprehensive solutions. The solutions are based on open architecture and international standards, which allow them to be used for standalone applications or as part of an integrated third-party network. Furthermore, Teleste solutions are modular and scalable and one of our main fields of special expertise is the integration of video surveillance networks consisting of several thousands of cameras into one unified system. Teleste Video Networks is one of those rare companies in the market with a proven track record in the delivery of large-scale CCTV networks.

Teleste Video Networks has presence in all the major geographical markets: Europe, America and Southeast Asia with our own local offices.

Smart Comprehensive Solutions

Concern for the environment, the general sense of insecurity and the heightened thread of terrorism strengthen the trends in CCTV market; the need for optimisation of traffic infrastructure and the increased need for protecting people and property with video surveillance.

Our end-customers are looking for comprehensive integrated solutions to an increasing degree. These developments can be in part attributed to technology developments, where the systems and solutions involved tend to become increasingly complex with a multitude of options available. Large companies such as GE and Cisco are entering the market with increased power, albeit to occupy market segments different from those of Teleste Video Networks. Price pressure on the market is considerable, but compensated by the fact that the overall market is growing. Simultaneously, networks are getting smarter with features such as the ability to identify and analyse video content automatically becoming a standard feature.

The core issue for video surveillance networks will be in their comprehensive management and recording software, an area where we at Teleste excel, providing our highly competitive solutions for video networking with other applications required for video transfer.

Our target market – advanced video surveillance systems requiring high-quality and real-time video, audio and data transmission, networking and recording – is a highly specialised segment distinct from the mainstream video surveillance market by the level of the technology excellence required.

In the coming years we expect to see growth in every Teleste Video Networks' target market segment. We expect this growth to spread out to all geographical markets and some regions such as the United States and France stand out by the more promising potential they provide. Another unfolding feature is that large-scale integrated network solutions will continue to gain in importance.

Direction and the Steps to be Taken

Teleste Video Networks focus on the following five priority areas: operational excellence, first class product solutions, high-end integration, mid-market integration and entering partnerships with our key clients.

Operational excellence is designed to strengthen our processes and eliminating any shortcomings in the way we operate. This is a paramount objective for which the entire Video Networks organisation has been engaged. Here, our scope of focus covers issues such as intensified follow-up and control of sales.

Product solutions encompass the whole range of requirements from the camera to the control room consisting of Teleste's own products in combination with third-party components. We use our extensive expertise of technology and the market supported by our insight in the clients' requirements, which effectively provides us with a competitive edge in the market. The focus in solutions development is shifting increasingly towards software applications and the related support services. We also aim better to identify any untapped market potential for our network solutions by establishing new channels.

Regarding integration functions, Teleste Video Networks has adopted a two-way approach which includes the areas of high-end and mid-market integration. Integration operations refer to the responsibility for the availability of the CCTV network including solution design, any integration of the video surveillance network into a larger system and a range of maintenance services. Demand for technical integration increases in step with the technology becoming more and more challenging to manage while the end-customers want turnkey deliveries. High-end integration focuses on large-scale network solutions carried out on a project-specific basis. Being one of the few players in the field having performed sizeable network solutions involving especially road and rail transport projects Teleste is very well positioned in this market segment. Mid-market integration involves solutions that can be replicated for a number of various customer requirements.

Concerning key accounts Teleste intends to create close partnerships with our key customers among which British Telecommunications plc is in a class of its own. Our goal is to promote mutual profitable

Video Networks Business Unit

Vision	*A leading global supplier of professional video surveillance network solutions*
Mission	*To apply the technology to enable reliable, real-time and high-quality video for security and*
	identification over transmission networks
Solution	*Comprehensive video surveillance solutions for the area between the camera and the control room*
Key markets	*The business focus is on high-quality video surveillance networks for traffic control systems (road and rail traffic),*
	urban surveillance system and security systems (including border, port and airport control) on a globe scale
Primary clientele	*The systems manufactured by Teleste are supplied mainly to the public sector*
	Teleste delivers its solutions to the end-clients mostly through system integrators

growth by getting to know the market and the partner's business. We also intends to enable our key customers to focus on their own core businesses by making available services such as network maintenance designed to support and sustain their business processes.

Year 2006

In 2006 Teleste continued its deliveries to the French National Railway Company SNCF. During the year the scope of the project was expanded and altered to ensure that the delivery will be completed in the first half of 2007. The project involves a comprehensive IP-based management system for integrating a number of existing local video surveillance networks into an organised infrastructure. Encompassing more than 120 railway stations in the Paris metropolitan area with over 3,000 cameras, this video surveillance network is one of the largest in the world. SNCF is planning to launch another project in the early 2007 for further stations in the Paris area and other French cities.

In 2006 Teleste concluded a framework agreement with BT redcare vision being part of British Telecommunications (BT Group) plc. This agreement ensures Teleste's position as the company's main supplier of CCTV equipment. The agreement spans three years and is worth more than EUR 10 million. An option is also included making it possible to extend the contract period by two more years. The agreement involves fibre modems and network products. To date Teleste has supplied BT just with fibre modem transmission equipment. Network product deliveries to BT were commenced in the year under review and in 2007 the volume is expected to increase.

In June 2006 Teleste acquired the entire share capital of the Finnish Suomen Turvakamera Oy. This transaction was a part of Teleste's Video Networks business area strategy designed to expand our current expertise in turnkey deliveries. Specialising in custom solutions that can be replicated this acquisition of Suomen Turvakamera marked Teleste's entry into the professional mid-market segment. In co-operation with Fingrid Oyj, the company running the Finnish National Power Grid, Suomen Turvakamera has developed a power station solution, which can be replicated overseas through our existing sales organisation.

Teleste Video Network continued to further the development of our MP-X network product platform. Additional priority areas included the family of MoRIS network management and storage solution platform and the range of products involving CFO fibre modems. Intensive development will continue in 2007 focussing primarily on the MP-X and MoRIS network product platforms.

Teleste Video Networks expects the market situation to continue to develop favourably in 2007.

Personnel

In line with its vision Teleste is an innovative organisation attractive for the best people in the industry. Our personnel policy is designed to meet the business units' requirements so that the number, availability, competence and motivation of our personnel are optimal from the viewpoint of achieving the set strategic objectives. Teleste personnel consist of experts of various fields led in compliance with the principle of open dialogue. Open dialogue promotes personal commitment and internalisation of goals in compliance with the company strategy. At the end of 2006, the number of Teleste's employees was at 621. The corresponding figure for the previous year was 557. Moreover, in 2006 Teleste hired, on average, 50 temporary employees assigned mainly to production. Acquisitions constitute an essential part of carrying out Teleste's strategy. In 2006 Teleste has got competences and personnel in line with the company strategy through acquisitions from Finland (Suomen Turvakamera Oy) and Sweden (PromaCom AB).

Personnel Recruitment and Development

In the period under review Teleste's number of personnel increased approximately by 70 to enable the current and future growth. As to required skills, geographic distribution and other criteria recruitment has been geared to meet the set strategic objectives. Recruitment and employment relationships are based on the company equality programme and are implemented accordingly. One of the cornerstones of Teleste's personnel policy is to provide the personnel with a possibility of job rotation. All vacant positions are always first made available for in-house application and, as far as possible, internal transfers constitute the preferred method of fulfilment.

Development of personnel competence has been observed in a number of areas. In 2006 the provided training focused primarily on furthering skills related to information technology and languages. Professional standards have been raised in technology and other areas by providing product and technical training as well as setting up courses in project management. In the past year key investments regarding personnel development included the tailor-made Leading Excellence management training programme carried out jointly with a couple of local high-tech companies and a course in superior training tailored exclusively to Teleste. The group, which started the Leading Excellence training programme (spanning one calendar year) in the autumn 2005 completed the course the following spring; a new group started in autumn 2006. The main objective with this training is to promote managerial skills and widen business thinking. The chosen participants in the programme include makers of Teleste's future. The programme is designed to support the company's future potential of success and the commitment of our key personnel segments.

Performance appraisal discussions conducted annually with each Teleste employee provide the essential tool for development of personnel and the entire community. Making use of the responses received from these development reviews the abovementioned superior training focused particularly on providing feedback, management of change and information flow. Teleste's management is intensively committed to personnel development and plays an active role in the planning and implementation thereof.

Incentives

Teleste's system of payroll and incentives is designed to support the corporate business strategy. Performance appraisal and target-setting discussions provide a setting for the definition of personal goals, which, in turn, are designed to promote performance while placing a special emphasis on personal development.

Incentive schemes are designed to promote performance within the company in general as well as individually. Teleste's personnel incentive schemes consist of a number of intangible and tangible inducements. Material incentives in place include systems of bonus pay and payment by results as well as those of share bonus scheme and options for key personnel. These schemes have been – and will continue to be – developed better to accommodate opportunities of participation by units, teams and individuals with the overall purpose of establishing a closer linkage between personal goals, performance outputs and the strategic goals of the company.

Well-being at Work

Teleste's process related to well-being at work, launched in 2003, was continued. At Teleste, job satisfaction and company climate are assessed by means of personnel questionnaires conducted once in two years. Next study is scheduled for the second half of 2007. Workplace ergonomics constitutes a part of this drive for well-being, which is subject to ongoing development, for instance, in forms of visits by physical therapist. We at Teleste believe that a good climate and work motivation strongly affect well-being at work and that in addition to signalling a positive image of the company and contributing to the willingness to stay of competent employees, a healthy work community is more productive both in terms of quality and quantity.

Our active free-time committee Vapari is elected annually from among Teleste personnel and it actively organizes e.g. different sports and culture events. Over and above, the company supports exercise opportunities for the personnel.

Personnel on December 31

	2006	*2005*	*2004*
Total	*621*	*557*	*513*
Research and Delvelopment	*146*	*127*	*130*
Operations	*282*	*286*	*256*
Sales and marketing	*159*	*114*	*101*
Finance + IT	*34*	*30*	*26*
Finland	*435*	*408*	*401*
Other countries	*186*	*149*	*112*
Female	*208*	*194*	*180*
Male	*413*	*363*	*333*

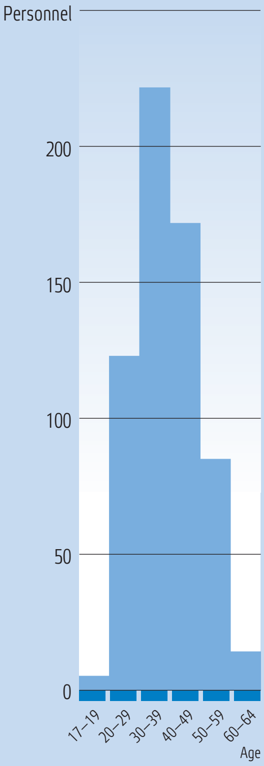
Co-operation

In 2006 market situation in the sector remained good. Continuous interaction and communication between the personnel and the company is ensured by way of monthly meetings between the representatives of the employer and the employees. Furthermore, the positive interaction between the management and the personnel is maintained by setting up joint meetings participated by the entire management group and the union representatives. This way we have succeeded in establishing a flexible mode of collaboration, which allows us quickly to adapt to both quiet spells and peaks in demand alike. Acceptable policies regarding use of hired labour in production have been subject of mutual understanding so that we have been able to respond to market fluctuations in a flexible manner. Application and development of various arrangement designed to increase flexibility in work will be continued in co-operation with the personnel.

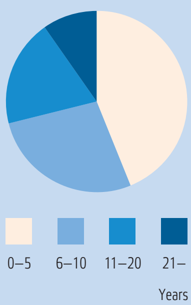
Co-operation with Universities and Third Parties

We have continued co-operation with universities and other educational establishments to promote the image of a positive workplace for future top professionals. This process has taken forms such as collaboration in the fields of testing and research, or Teleste's representation in various bodies of universities and educational institutes. This activity is designed to ensure that utilisation of top expertise of the scientific community and the company's strategic requirements will be taken into account in the drafting of curriculums of the respective institutes. Positive employer image has been promoted towards future top professionals by keeping in touch – through excursions, for instance – with student organisations of Universities of Technology.

Age Distribution 2006



Years of Service 2006



Management Group


Jukka Rinnevaara


Johan Slotte

Jukka Rinnevaara
M.Sc (Econ.), born in 1961
President and CEO
Joined Teleste in 2002

ABB Installaatiot, President 1999–2001
ABB Building Systems, Group Senior Vice President 2001–2002

Perlos Corporation, Member of the Board since 2006

Johan Slotte
LL.M, MBA, born in 1959
Senior Vice President, Video Networks
Business Development
Joined Teleste in 1999

Uponor Poland, Managing Director 1995–1999

Erja Saarikoski
Business school graduate, born in 1953
CFO
Joined Teleste in 1984

Juha Järvenreuna
M.Sc. (Eng.), born in 1964
Senior Vice President, HFC Networks and Services
Joined Teleste in 2004

Teleste Corporation, Product Operations, Director 1998–2003
Nokia Group, Nokia Networks, Quality Director 2003–2004

Reinaart Bryssinck
M.Sc. (Telecom), MBA, born in 1968
Senior Vice President, Digital Video and Broadband Solutions
Joined Teleste in 1995

Esa Kinnunen
M.Sc. (Econ.), B.Sc. (Eng.), born in 1967
Senior Vice President, Operations
Joined Teleste in September 4, 2006

Nokia Group, Nokia Networks, Director 1994–2005
Solectron Corporation, Vice President 2005–2006

Esko Myllylä
B.Sc. (Eng.), CBA, born in 1966
Research and Development, CTO
Joined Teleste in 1994


Erja Saarikoski


Juha Järvenreuna


Reinaart Bryssinck


Esa Kinnunen


Esko Myllylä

Corporate Governance

Teleste Corporation aims at organising its management in a consistent and functional manner. The governance is based on the Finnish Companies Act and Teleste Articles of Association. Teleste's shares are listed on the Helsinki Stock Exchanges. The company complies with the rules and regulations for listed companies as set by the Helsinki Stock Exchanges. As of 1 March, 2000, the company has followed the insider regulations drawn up by the Board of Directors of the Helsinki Stock Exchanges (revised 1 January, 2006). These regulations have been supplemented by the Company's internal guidelines. Teleste's corporate governance practices comply with the Corporate Governance Recommendation for Listed Companies approved by the Helsinki Stock Exchanges, the Central Chamber of Commerce of Finland and the Confederation of Finnish Industry and Employers in December 2003. The company has confirmed the set of applied key values.

Annual General Meeting

The Annual General Meeting (AGM) of Teleste Corporation is the highest decision-making body of the company. The Annual General Meeting is held at least once a year. The General Meeting shall be held annually by the end of June. The Annual General Meeting is held in Helsinki. The Annual General Meeting decides on any specified tasks in compliance with the Finnish Companies Act.

Issues decided by the AGM include:
- Approval of the financial statement
- The allocation of profit shown in the balance sheet
- The discharge from liability to the Board of Directors and the Managing Director
- The election of the members of the Board of Directors and the auditor.

Responsibilities of the AGM also include:
- Making amendments to the Articles of Association
- Deciding on share issues, granting of option and other special rights entitling to shares, repurchase and redemption of the company's own shares as well as decreasing the share capital.

Notice of the Annual General Meeting shall be announced in a newspaper as determined by the Board of Directors or verifiably delivered, in writing, to each shareholder using the address marked in the register of shareholders, no earlier than two months and no later than 17 days prior to the meeting.

The Board of Directors

Rules of Procedure

The Board of Directors of Teleste is responsible for managing the company in accordance with the law, official rulings, Articles of Association and the decisions as set out by the Annual General Meeting. The operating procedures and main duties of the Board of Directors have been specified in the Board's Rules of Procedure.

The Board shall resolve matters of great importance in terms of scope and magnitude to the group's operation. The Board oversees and assesses the operation of the CEO and the Management Group. The Board decides on the criteria of the company's compensation system and makes decisions on any other far-reaching issues related to personnel.

In line with the view adopted by the Board of Teleste Corporation, the proceedings of the Board will be carried out in an optimum way without formation of separate committees but by involving the entire Board in the so-called committee proceedings. The Board shall conduct an annual evaluation of its performance and working methods.

The Board of Teleste Corporation has laid down rules of procedure including the following fundamental issues:
- Provision for the company business strategy and its revision at regular intervals
- Approval of annual budgets and supervision of their implementation
- Decisions concerning major investments and divestments
- Handling and approval of annual financial statements and interim reports
- Appointment of the President and CEO and discharging him from his duties and specification of his responsibilities and conditions of work
- Decisions concerning incentive and bonus systems involving management as well as staff and presentation of any related proposals to the AGM as required
- Annual revision of any essential risks related to the company operation and management thereof
- Laying down the company values and policies.

Election and Term of Office of the Board of Directors

The Chairman and other members of the Board of Directors are elected by the Annual General Meeting. According to the Articles of Association the Board of Directors shall have a minimum of three and a maximum of eight members. In its meeting held on 4 April 2006, the Annual General Meeting elected five members to the Board of Directors of Teleste Corporation for a term of one year.

The Teleste Corporation Board of Directors:
Tapio Hintikka, Chairman of the Board
Tero Laaksonen, Member of the Board
Pertti Raatikainen, Member of the Board
Timo Toivila, Member of the Board
Pekka Vennamo, Member of the Board.

With the exception of Timo Toivila (CEO until 30 October, 2002) and Professor Pertti Raatikainen (expert member of the steering group in charge of the company technological development and convenes approximately five times a year) the Members of the Board are not employed by the company and can be considered independent in line with the Finnish recommendations.

In 2006 the Board of Directors of Teleste Corporation held 9 meetings one of which was set up as a telephone conference. The attendance of the Directors at the Board meetings was 95%. In addition to the Members of the Board the meetings were attended by the CEO, the CFO and persons invited separately as required.

Remuneration for the Members of the Board

The remuneration of the members of the Board is decided by the Annual General Meeting. On 4 April, 2006 the AGM decided that the Chairman of the Board be paid annually EUR 36,000 and each Member will receive EUR 20,000 a year. Attendance allowance, which is paid separately, stands at EUR 250 per meeting. Remuneration for the Members of the Board will be paid so that 40% of the specified amount will be company shares and the rest will be remitted in cash.

Salaries, remuneration and other benefits paid in 2006 to the Board of Directors were as follows:
- Tapio Hintikka EUR 38,250, of which were remitted in Teleste shares EUR 14,400 (1,500 pcs)
- Tero Laaksonen EUR 22,000, of which were remitted in Teleste shares EUR 8,160 (850 pcs)
- Pertti Raatikainen EUR 22,250, of which were remitted in Teleste shares EUR 8,160 (850 pcs)
- Timo Toivila EUR 22,250, of which were remitted in Teleste shares EUR 8,160 (850 pcs)
- Pekka Vennamo EUR 22,250, of which were remitted in Teleste shares EUR 8,160 (850 pcs).

President and CEO

The scope of duties of the Teleste Corporation CEO is determined by the law, the Articles of Association and instructions issued by the Board. Detailed terms of employment of the CEO are specified in a separate contract subject to the Board approval.

The CEO is not a member of the Board of Directors.

Corporate Governance

The current CEO of Teleste, Jukka Rinnevaara, assumed his present responsibilities on 1 November, 2002. The salary, fees and other benefits received by the CEO are determined by the Board of Directors. The aggregate amount of salary, remuneration and other benefits paid to the Managing Director of Teleste Corporation in 2006 was EUR 761,715. The aggregate compensation paid to the Managing Director included share bonus in the amount of EUR 132,000, which was based on the result targets of 2005. The aggregate compensation of the Managing Director included share bonus for the year 2006 in the amount of EUR 151,073.

The contractual age of retirement of CEO Jukka Rinnevaara is 60. The insurance premium of the voluntary retirement insurance policy of the Managing Director was EUR 47,114 which amount is not included in the paid salary and remuneration. As to the contract of Mr. Rinnevaara, his term of notice has been specified as six (6) months in case the President and CEO decides to withdraw, and eighteen (18) months should the contract be terminated by the company.

Management Group

The company Management Group is chaired by the CEO who reports to the Board of Directors. Members of the Management Group consist of the directors of Teleste Corporation business sectors and the group management. The Management Group handles the issues that concern managing the company, such as issues related to strategy, budget, interim reports and corporation deals, and prepares investments for approval by the Board of Directors.

The Management Group meets once a month or at other times, as required.

Salary for all Members of the Management Group consists of a fixed basic salary and a results-based bonus. The amount of results-based bonus is determined by the company performance, the business area in question and other key operative objectives. The Board is in charge of bonus systems applied to the Management Group. Page 9 of the Annual Report for 2006 contains more detailed information on the stock options of Teleste Corporation. See page 10 for the shareholdings and the stock options of the Managing Director and the members of the management group.

Auditing and Revisions

The term of office of the company auditor expires at the closing of the first Annual General Meeting following the election. On 4 April, 2006 the Teleste AGM selected KPMG Oy Ab as the company auditor and decided that the auditor's fee will be paid as invoiced. The company's chief auditor is Sixten Nyman.

In addition to their statutory duties the auditors report to the Teleste Corporation Board of Directors and attend the Board meetings at least once a year.

In 2006 the Group's auditing expenses totalled EUR 87,910 in which the share of KPMG was EUR 55,565. Moreover, auditing units of KPMG have supplied the Group companies with other consultation worth total EUR 73,023 and other than KPMG auditors for EUR 11,635.

Internal Auditing, Internal Supervision and Risk Management

The Teleste Board of Directors has laid down principles for the company's internal control, internal supervision and risk management.

Internal Auditing

Internal auditing in the Teleste Group is the responsibility of the company's director/legal affairs, who reports to a member of the Board appointed from within the same. The tasks connected with internal auditing are handled by means of control measures included in the company's operational processes. The internal assessors, controller function and chartered accountants report to the director/legal affairs on their observations.

Internal Supervision and Risk Management

The task of internal supervision is to ensure that the company's operations are effective and profitable, the information produced is reliable, and that the rules and operational principles are observed.

Risk management is an essential part of Teleste's internal supervision. By means of risk management, there is an attempt to ensure that Teleste achieves its operational goals and that the essential risks impacting business activity are recognised and followed up appropriately.

The risk management system is based on monthly reporting, by which the development of the orders received, turnover, order backlog, trade receivables and cash flow is monitored and, through the same, the profit development of the entire Group. Risk management supports the business activity and generates added value, assisting decision-making for the management in charge of business. The point of departure rests in Teleste's most pivotal business aims and processes. The reporting is dealt with in the monthly meetings of the Management Group.

In risk management, the regular evaluation of more significant risks and exercising control in a cost-effective manner are emphasised. The starting point for risk management is found in Teleste's business objectives. The risks threatening these objectives are identified, and they are monitored and assessed on a continuous basis.

Teleste's risk management system covers, for instance, the following classes of risk:

- Operational prerequisites
- Personnel risks
- Property and business interruption risks
- Interest groups
- Operational organisation
- Economic risks.

The risk management methods are specified and the implementation of risk prevention is carried out through the same. Similarly, all risks, which are reasonable to insure for economic or other reasons, are also covered.

Insider Register

As from 1 March, 2000 the company has complied with the insider regulations approved by Helsinki Exchanges' Board of Directors (revised on September 1, 2005). To support these regulations the company has introduced a set of internal guidelines.

Membership in the Teleste permanent inner circle is based on position. Thus, the group consists of members of the Board of Directors, the CEO and the auditors. Furthermore, the extended inner register includes members of the Management Group and the CEO's assistant.

Moreover, insider rules and regulations include provisions concerning temporary commercial activities. Project-specific insider register includes personnel who, based on their position, have access to company-related information, which upon publication may affect the value formation of the company's share. The CEO will assess, on a case-by-case basis, whether an issue or arrangement under preparation will be defined as a project.

It is recommendable for those included in the insider register to time any intended trading involving company shares and derivatives in such a manner that optimum information affecting the value of the shares is available in the market at the time. Permanent members of Teleste's insider register are obliged by the so-called Silent Period during which trading on company shares is banned completely for 14 days preceding publication of interim reports and the financial statements. During the specified period Teleste will not engage in any meetings with investors or analysts and Group representatives are not allowed to comment upon company results.

The company insider administration is included in the SIRE system of the Finnish Central Securities Depository.

The Board of Directors

Tapio Hintikka
M.Sc. (Eng.), born in 1942
Member of the Board since 2001
Vice Chairman of the Board 2001–2002
Chairman of the Board since 2003

Hackman Oyj Abp, CEO 1997–2002
Sonera Corporation, Chairman of the Board 2001–2002
TeliaSonera AB (Publ.), Chairman of the Board 2002–2004

CapMan Plc, Member of the Board since 2004
Evli Bank Plc, Member of the Board 2003–2004,
Vice Chairman since 2005
Aspocomp Group Plc, Member of the Board since 2007

Tero Laaksonen
M.Sc. (Math.), born in 1946
Member of the Board since 1999

Nokia Telecommunications Oy, Senior Vice President 1995–1998
Telia Finland Oy, CEO 1998–2001
Comptel Corporation CEO 2002–2004

Tieto-X Plc, Member of the Board 2004–2005
Chairman of the Board since 2005

Pertti Raatikainen
Dr. Sc. (Technology), born in 1956
Member of the Board since 2003

Helsinki University of Technology professor (fixed term) 1997
VTT Information Technology, Research professor, since 1998

University of Jyväskylä, Docent since 1998
Helsinki University of Technology, Docent since 2002

Timo Toivila
M.Sc. (Eng.), born in 1950
Member of the Board 1995–1997
Chairman of the Board 1996–1997
Member of the Board since 2003

Huurre Group Oy, Managing Director 1994–1995
Sponsor Oy, Director 1994–1997
Teleste Corporation CEO 1997 (1996)–2002

Tecnomen Corporation, Member of the Board since 2001

Pekka Vennamo
Student in technology, born in 1944
Chairman of the Board 2000–2001
Member of the Board since 2000

Suomen PT Oy, CEO 1994–1998
Sonera Corporation, CEO 1998–1999

Sijoitus Oy, Chairman of the Board and CEO since 1998
Soprano Group, Chairman of the Board since 2000
Aldata Solution Oyj, Chairman of the Board since 2002
Saunalahti Group Oyj, Chairman of the Board 2001–2003,
Member of the Board 2003–2005, Chairman of Board since 2005


Tapio Hintikka


Tero Laaksonen


Pertti Raatikainen


Timo Toivila


Pekka Vennamo

Report of the Board of Directors

Overview

Teleste continued to grow vigorously in its main market area. In the period under review long-term framework agreements were signed for value in excess of EUR 60 million. These framework agreements have allowed the company to improve its visibility in the key markets while providing good opportunities for implementing programs designed to increase profitability of product groups included in the framework agreements concerned. As to the EttH technology a significant breakthrough was achieved as the leading South Korean operator Hanaro Telecom chose Teleste's EttH solution for their high-speed (100 Mb/s) telecommunication technology. The placed order carries a significant reference value considering the pioneering position of the South Korean market and their advanced telecommunication infrastructure and requirements of high standards. In May Suomen Turvakamera Oy was acquired to broaden the range of solutions provided by Video Networks to an expanded clientele. In June the expertise in fibre technology (FttH) of Broadband Cable Networks was strengthened by acquisition of the Swedish PromaCom AB. In Q4 framework agreements constituted main part of deliveries by Broadband Cable Networks. In Q4 profitability was restrained by capacity constraints and accelerated production of the EttH product family.

Net Sales and Profitability

Teleste net sales totalled EUR 101.8 (82.6) million, an increase of 23.2% over the previous year. Net sales in Q4 amounted to EUR 28.4 (24.3) million.

Operating profit stood at EUR 9.8 (8.6) million making 9.6% (10.4%) of the net sales. Operating profit for Q4 stood at EUR 2.2 (3.1) million making 7.6% (12.6%) of the net sales. The operating profit for Q4 was encumbered by accelerated production of the new product versions and capacity constraints in the production.

Teleste's orders received improved by 25.6% standing at EUR 107.2 (85.4) million. Orders received in Q4 stood at EUR 33.9 (24.5) million. Teleste's order backlog grew by 23.9% amounting to EUR 28.1 (22.7) million at the year-end.

Profit after financial items totalled EUR 9.3 (8.3) million while the net profit equalled EUR 6.9 (6.0) million. Undiluted result per share for the Group stood at EUR 0.41 (EUR 0.35). Tax rate for the period was 25.9% (28.4%). Return on capital employed amounted to 24.3% (23.7%) and return on equity was 19.7% (19.8%).

R&D and Investments

The R&D expenditure for the period under review totalled EUR 9.8 (8.6) million making 9.7% (10.5%) of net sales. R&D efforts included further development of the Ethernet to the Home (EttH), Fiber to the Last Amplifier (FttLA), GigaHerz broadband solutions (Access), video surveillance transfer system (MP-X) and video surveillance management system (MoRIS) platforms as well as solutions tailored to client-specific requirements. Further development of Teleste's video headend technology was launched towards the end of the review period. Some 40% of the R&D expenses involved maintenance of solution platforms currently in production. The amount of activated product development expenses with the R&D grant included stood at EUR 1.4 (1.8) million. This capitalisation involved the broadband technology platforms of EttH, MP-X and GigaHerz. Depreciation on activated R&D expenses for the period under review amounted to EUR 0.9 (0.6) million. R&D expenditure in Q4 amounted to EUR 3.9 (2.6) million. This rise in expenses was mainly due to increased use of product development partners and accelerated finishing for production of the EttH client project. A number of Teleste's projects involved co-operation with Finnish universities and research institutes. Almost 22% of the Group personnel is assigned on R&D.

Investments for the period under review totalled EUR 6.2 (4.1) million making 6.1% of net sales. These investments include acquisitions of Suomen Turvakamera Oy and PromaCom AB as well as an additional purchase price on Teleste Video Networks (former S-Link AB) of EUR 0.2 million. Other investments included machinery and equipment for manufacturing, research and development as well as IT. As to investments made in the period EUR 0.5 (0.8) million was carried out by using financial leasing. In the financial period, the real estate in Norway was sold with inconsequential capital gain. A new circuit board production will be introduced in Q1 of 2007 improving capacity right in the first half of the year. The line will also speed up the R&D turnaround times. The investment is carried out by using financial leasing with the purchase price amounting to approximately EUR 1.4 million.

Finance

The Group liquidity remained good. Due to the growth working capital was tied to stocks, in particular, and the operating cash flow stayed at EUR 2.7 (5.5) million. Total cash flow equalled EUR –1.7 (–8.6) million. The company is prepared for strategic investments and increased need for working capital driven by growth by means of stand-by credits. The amount of unused stand-by credits at the end of the period amounted to EUR 23.0 (27.0) million. Credit limits remain valid till November 2008. The Group's equity ratio was 55.3% (59.1%) with gearing standing at 3.2% (–14.3%). Interest bearing debt on 31 December 2006 was EUR 8.0 (3.9) million.

Personnel and Organisation

During the year, the group employed an average of 608 people (546). At the year-end, the figure totalled 621 (557) people of which approximately 30% (27%) were stationed overseas. The stated number of staff does not include temporary labour averaging 50 persons in the financial period. At the year-end less than 10% of the Group's personnel was stationed outside Europe. In May the main business Broadband Cable Networks was split into two units named HFC Networks and Services and Digital Video and Broadband Solutions, respectively. The previous country-specific organisation in sales operations for the business was replaced by geographic sales territories serving both units. The organisation was designed to promote profitable growth by way of ensuring implementation of the business unit strategies so as to meet customer requirements and identify any new opportunities. The split does not affect the Group segment reporting. In the financial period the R&D operations were organised in centres of expertise replacing the previous division into product groups. Expenditure on employee benefits amounted to EUR 27.1 (24.1) million compared with that in 2004 having amounted to EUR 23.4 million.

Description of Business Areas and the Involved Key Risks

Founded in 1954, Teleste is a technology company currently running the business units of Broadband Cable Networks and Video Networks. In line with its strategy Teleste continues to focus on the chosen product and technology segments as well services and technical integration. Integrated deliveries of solutions create favourable conditions for growth even if the involved resource allocation and technical implementation pose a challenge involving, therefore, also reasonable risks. In addition, appropriate technological choices and their correct timing are instrumental for the success of the businesses not forgetting market dynamics such as the importance of consolidation of clients and competition. Strong euro against the US dollar may erode our price competitiveness with respect to the American competition. The company has covered risks involving any damage in operative functions of the businesses mainly by insurance policies. These insurances do not include credit loss risks. For Teleste in 2006 no such risks materialised and no such legal proceedings or juridicial procedures were pending that would have had any essential significance for the Group operation.

Broadband Cable Networks

Broadband Cable Networks provides its main clientele of cable operators with equipment and systems designed for the construction of transmission network and signal processing. Deliveries include individual pieces of equipment and turnkey networks alike. The business also makes available a number of services related to maintenance of network infrastructure. The main market area of Broadband Cable Networks is Europe, which business area involves 17 own sales offices supported by a number of retail and integration partners. Outside Europe, Broadband Cable Networks has own offices located in China and India. In the financial period Broadband Cable Networks entered into significant framework agreements with the largest European cable operators. Value of these framework agreements was nearly EUR 50 million including a three-year contract of EUR 23 million with the leading French cable operator Altice. As to the EttH technology, a significant customer order of approximately EUR 4.6 million was received from South Korea in December. Concerning our clientele in Europe 2006 continued to be characterised by mergers and changes in ownership relations. These developments may affect Teleste's position in view of the operators' choices of suppliers for products and services.

Broadband Cable Networks' growth in 2006 was ensured by our efforts designed to shorten the turnaround times in product development, strengthen the subcontractor network and logistics. Orders received by Broadband Cable Networks increased by 27.4% amounting to EUR 92.8 (72.9) million. Net sales grew by 27.3% amounting to EUR 85.6 (67.2) million. Operating profit grew by 22.9% equalling EUR 9.1 (7.4) million. At the year-end order backlog stood at EUR 26.7 (19.4) million. In Q4 orders received amounted to EUR 29.7 (21.0) million, net sales totalled EUR 23.8 (19.2) million while the operating profit stood at EUR 1.8 (2.5) million.

We expect the profitable growth of Broadband Cable Networks to continue in 2007 with improvements taking place in profitability. In our estimate this growth will be driven by the comprehensive Access network solutions, EttH deliveries and provided services. We expect profitability to improve through targeted cost control projects and growth.

Video Networks

Clientele of Video Networks consists mainly of public sector organisations and system integrators. In the financial period this clientele was expanded to include video surveillance solutions for industrial areas through acquisition of Suomen Turvakamera. The business area has focussed on high-quality video surveillance systems transferring real-time video, audio and data. In April Video Networks concluded a new three-year framework agreement with British Telecom with a value exceeding EUR 10 million. The business area provides solutions for traffic control and surveillance of city centres as well as industry-specific turnkey solutions. The technology involved in these applications is developing rapidly. In the financial period the delivery project for the French National Railroad Authority (SNCF) played a key role. Significance of technical integration in the unit's operations will increase in the future. The business has seven sales offices in Europe with offices outside Europe located in the United States, China and Thailand. R&D efforts involved mainly development of network systems.

Orders received by Video Networks increased by 15.5% amounting to EUR 14.4 (12.5) million. Net sales grew by 5.3% amounting to EUR 16.2 (15.4) million. Operating profit stood at EUR 0.7 (1.2) million. Decreased profitability was caused by investments made in resource allocation for video network management projects, product development and strengthening of sales organisation. At the year-end order backlog stood at EUR 1.5 (3.3) million.

In Q4 orders received amounted to EUR 4.2 (3.5) million with net sales equalling EUR 4.6 (5.1) million. Operating profit stood at EUR 0.3 (0.6) million.

In 2007 price competition will intensify especially in the area of network solutions. Large companies have entered the market. Based on the favourable development in sales pipeline we estimate the net sales for Video Networks to pick up in 2007 driven by factors like new network management projects. Profitability will improve along with the growth.

Report of the Board of Directors

Business Areas by Geography

In geographical terms, the Group's business areas are divided up into Scandinavia, rest of Europe and others.
Scandinavia:
Net sales in the Nordic countries amounted to EUR 32.2 (31.4) million.
Investments for the area totalled EUR 5.8 (3.3) million.
Rest of Europe:
Net sales for the rest of Europe stood at EUR 62.1 (45.7) million while the investments made in the area amounted to EUR 0.1 (0.2) million.
Others:
Net sales were up to EUR 7.4 (5.5) million. Investments totalled EUR 0.3 (0.6) million.

Group Structure

Acquisitions in the financial period include purchasing of share capital of the Finnish Suomen Turvakamera Oy and the Swedish PromaCom AB. The parent company of Teleste Group has branch offices in Belgium, China, Denmark, France, India, the Netherlands, Poland, Spain and Thailand with subsidiaries in 10 countries outside Finland.

General Meetings

The Annual General Meeting on 4 April 2006 confirmed the financial statements for 2005 and discharged the Board and the CEO from liability for the financial period. The Meeting confirmed the dividend of EUR 0.16 per share proposed by the Board. The dividend was paid out on 18 April 2006.

Moreover, the AGM elected Mr. Tapio Hintikka as Chairman of the Board of Directors while Mr. Tero Laaksonen, Mr. Pertti Raatikainen, Mr. Timo Toivila and Mr. Pekka Vennamo were elected as members of the Board of Directors.

The AGM authorised the Board to acquire the maximum of 1,215,000 of the company's own shares and to convey 1,700,000 company's own shares. The authorisation concerning own shares includes possibility of purchasing and conveying own shares to be used in stock-based incentives. The AGM authorised the company to increase the share capital by new issue of no more than EUR 1,360,000 being equal to 3.4 million shares. These authorisations expire on 4 April 2007. In the period the authorisations granted by the AGM were used by conveying 30,000 own shares in the acquisition of the capital stock of Suomen Turvakamera Oy; other authorisations were not used. At the balance sheet date, based on authorisations granted in 2001 and 2002, the company is in possession of 455,000 of its own shares.

Management and the Auditors

CEO of the company has been Mr. Jukka Rinnevaara. The AGM elected KPMG Oy Ab as the auditor.

Shares and Changes in Share Capital

The largest single shareholder at the end of 2006 was the Sampo Life Insurance Company Ltd with a 9.34% holding.

In January 2006, Ilmarinen Mutual Pension Insurance Company reported its ownership having increased up to 5.42%. In August 2006, Schroder Investment Management Limited flagged their holding to have reached 5.01%.

The share price low in 2006 was EUR 6.46 (5.85) and the high EUR 12.75 (8.35). Closing price at the end of the year stood at EUR 11.63 (7.45). During the year, 14.2 million (10.8 million) shares were traded on the Helsinki Exchanges; these shares represented 81.4% (62.3%) of the share capital.

Options allotted for Teleste key employees were listed on the Helsinki Exchanges on 1 February 2006. In the period 10,000 own shares were subscribed using 2002A options and 39,550 using 2002B options. At the balance sheet date the company's registered share capital amounted to EUR 6,955,720.80, divided up into 17,389,302 shares; out of these the company was holding 455,000 shares. At, the balance sheet date the shares in company possession, when put against the total amount of shares and votes, equalled 2.6%.

Other matters affecting the company governance will be stated in the annual report under Good Governance.

Outlook for 2007

New services provided by the cable operators such as HDTV, broadband Internet, VoIP and interactive digital services necessitate investments for the network upgrades and increased capacity. We believe the favourable market situation will continue for Broadband Cable Networks. In combination with cost control measures the wide range of products and services provided by the business area create conditions for continued profitable growth also in 2007. The increased need for security and more effective traffic infrastructure will promote demand in the Video Networks' market. We believe that deliveries of the high-quality network management systems provided by Video Networks will increase in 2007.

Teleste will continue to grow profitably in 2007 focussing on making the production process even more effective and speeding up the turnaround times in product development. The new circuit production line will increase the production capacity right in the first half of the year.

Board of Directors' Proposal for Dividends

As to the Annual General Meeting to be held on 3 April 2007, the Board proposes that a dividend of EUR 0.20 (EUR 0.16) per share be paid to the outstanding shares for the year 2006.

30 January 2007

TELESTE CORPORATION	Jukka Rinnevaara
Board of Directors	President and CEO

Teleste Group Financial Statement

Statement of Income

1 000 euros	Note	1.1.–31.12.2006	1.1.–31.12.2005	Change, %
Net sales	1	101 773	82 588	23.2
Other operating income	2	2 158	1 530	41.0
Changes in inventories of finished goods and work in progress		6 066	761	697.1
Raw material and consumables used		–54 743	–36 443	50.2
Employee benefits expense	3	–27 100	–24 124	12.3
Depreciation and amortisation expense	4	–2 393	–1 940	23.3
Other operating expenses	5	–16 006	–13 791	16.1
Operating profit		**9 755**	**8 582**	**13.7**
Financial income	6	194	280	-30.7
Financial expenses	7	–661	–541	22.2
Profit before tax		**9 288**	**8 321**	**11.6**
Income tax expense	8	–2 408	–2 363	1.9
Profit for the period		**6 879**	**5 956**	**15.5**
Attributable to:	9			
Equity holders of the parent		6 879	5 956	15.5
Earnings per share for profit of the year attributable to the equity holders of the parent (expressed in euros per share):				
Basic		0.41	0.35	15.2
Diluted		0.38	0.33	15.7

Balance Sheet

1 000 euros	Note	31.12.2006	31.12.2005	Change, %
Assets				
Non-current assets				
Property, plant and equipment	10	5 578	5 860	–4.8
Goodwill	11	12 127	9 205	31.7
Other intangible assets	11	3 614	2 589	39.6
Available-for-sale investments	12	1 116	1 116	0.0
		22 435	18 770	19.5
Current assets				
Inventories	14	16 604	9 623	72.5
Trade and other receivables	15	22 409	17 878	25.3
Financial assets at fair value through profit or loss	16	0	2 000	n/a
Cash and cash equivalents	16	6 789	6 524	4.1
		45 801	36 025	27.1
Total assets		**68 236**	**54 795**	**24.5**
Equity and liabilities				
Equity attributable to equity holders of the parent				
Share capital	17	6 955	6 935	0.3
Share premium	17	1 417	1 276	11.1
Translation differences	17	65	70	–7.1
Retained earnings	17	29 224	24 025	21.6
		37 661	32 306	16.6
Non-current liabilities				
Interest-bearing liabilities	18	742	706	5.1
Other liabilities		0	373	n/a
Deferred tax liabilities	13	368	60	513.3
Provisions	19	425	515	–17.5
		1 535	1 654	–7.2
Current liabilities				
Trade and other payables	20	20 045	15 022	33.4
Current tax payable	21	875	1 101	–20.5
Provisions	19	850	1 502	–43.4
Interest-bearing liabilities	18	7 270	3 210	126.5
		29 040	20 835	39.4
Total liabilities		**30 575**	**22 489**	**36.0**
Total equity and liabilities		**68 236**	**54 795**	**24.5**

Clash Flow Statement

1 000 euros	1.1.–31.12.2006	1.1.–31.12.2005	Change, %
Cash flows from operating activities			
Profit for the period	6 879	5 956	15.5
Adjustments for:			
Non-cash transactions	3 407	2 908	17.2
Interest and other financial expenses	661	541	22.2
Interest income	-188	-276	-31.9
Dividends	-6	-4	50.0
Taxes	2 100	1 955	7.4
Change in working capital			
Increase in trade and other receivables	-3 938	-5 450	-27.7
Increase in inventories	-6 651	-1 715	287.8
Increase in trade and other payables	3 392	3 026	12.1
Decrease in provisions	-742	-48	1 445.8
Paid interests and other financial expenses	-521	-781	-33.3
Received interests and dividends	194	280	-30.7
Paid taxes	-1 912	-855	123.6
Cash flow from operating activities	**2 675**	**5 537**	**-51.7**
Cash flow from investing activities			
Acquisition of subsidiary, net of cash acquired	-3 078	-1 854	66.0
Purchases of property, plant and equipment (PPE)	-699	-968	-27.8
Purchases of intangible assets	-1 734	-1 790	-3.1
Proceeds from sale of PPE	376	0	n/a
Net cash used in investing activities	**-5 136**	**-4 612**	**11.4**
Cash flow from financing activities			
Proceeds from borrowings	4 000	3 000	33.3
Payments of borrowings	-460	-10 386	-95.6
Payment of finance lease liabilities	-273	-137	99.3
Dividends paid	-2 697	-2 022	33.4
Proceeds from issuance of ordinary shares	161	0	n/a
Net cash used in financing activities	**731**	**-9 545**	**n/a**
Change in cash			
Cash and cash equivalents 1.1.	8 524	17 108	-50.2
Effect of currency changes	-5	36	n/a
Cash and cash equivalents 31.12.	6 789	8 524	-20.4

Statement of Changes in Equity

1 000 euros	Attributable to equity holders of the parent Share capital	Share premium	Translation differences	Retained earnings	Total equity
1.1.2005 (restated)	6 935	1 277	34	19 496	**27 742**
Exchange differences			36		**36**
Profit for the year				5 956	**5 956**
Total recognised income and expense for the year	0	0	36	5 956	**5 992**
Dividends				−2 022	**−2 022**
Equity-settled share-based payments		−1		594	**593**
	0	−1	0	−1 428	**−1 429**
31.12.2005	6 935	1 276	70	24 025	**32 306**
Profit for the year				6 879	**6 879**
Dividends				−2 697	**−2 697**
Equity-settled share-based payments				1 017	**1 017**
Issue of share capital	20	141			**161**
Exchange differences			−5		**−5**
	20	141	−5	− 1 680	**−1 524**
31.12.2006	**6 955**	**1 417**	**65**	**29 224**	**37 661**

Accounting Principles

Company profile

Teleste Corporation is a Finnish public limited liability company organised under the laws of Finland and domiciled in Turku in Finland. Its registered address is Seponkatu 1, 20660 Littoinen.

Founded in 1954 Teleste is a technology company running its two business units Broadband Cable Networks and Video Networks. Our Broadband Cable Networks business aims at promoting the business of cable operators making up our clientele. This is achieved by making available network solutions. Our Video Networks business manufactures and delivers high-quality video surveillance network solutions for the transmission of video, data and audio with official authorities and integrators as the primary clientele. The parent company of Teleste Group, Teleste Corporation, has operations in Belgium, China, Denmark, France, India, the Netherlands, Poland and Spain, and a subsidiary in ten countries outside Finland. Teleste Corporation has been listed on the Helsinki Stock Exchange since 1999.

A copy of the consolidated financial statements can be obtained either from Teleste's website (www.teleste.com) or from the parent company's head office, the address of which is mentioned above.

Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) in force as at 31 December 2006. International financial reporting standards, referred to in the Finnish Accounting Act and in ordinances issued based on the provisions of this Act, refer to the standards and their interpretations adopted in accordance with the procedure laid down in regulation (EC) No 1606/2002 of the EU. The notes to the consolidated financial statements also include additional information in accordance with the Finnish accounting and company legislation.

Teleste adopted IFRS as from 1 January 2005. Prior to IFRS Teleste's financial statements were based on Finnish accounting standards (FAS) applicable to listed companies in Finland. IFRS 1 First-time adoption of IFRS was applied in the transition. Teleste's date of transition to IFRS was 1 January 2004.

Basis of preparation

The consolidated financial statements are presented in thousands of euro (TEUR) and have been prepared under the historical cost convention, unless otherwise stated in the accounting principles.

Use of estimates

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the contents of the financial statements as well as use judgement when applying accounting principles. The estimates and assumptions are based on the management's current best knowledge reflecting historical experience and other reasonable assumptions. Actual results may differ from these estimates. Accounting estimates mainly relate to goodwill, obsolete inventories and warranty provisions. The chapter "Accounting policies requiring management's judgement and key sources of estimation uncertainty" discusses judgements made by management and those financial statement items on which judgements have a significant effect.

Subsidiaries

The consolidated financial statements include the accounts of the parent company Teleste Corporation and all those subsidiaries in which it holds, directly or indirectly, over 50 per cent of the voting rights or in which it otherwise has control (together referred to as "Group" or "Teleste"). Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The companies acquired during the financial periods presented have been consolidated from the date of acquisition, when control commenced. The companies disposed during a financial period are included in the consolidated financial statements up to the date of disposal.

Associates

Associates included in the consolidated financial statements are those entities in which Teleste Group holds voting rights over 20 per cent or in which it otherwise has significant influence, but not control, over the financial and operating policies. Holdings in associates are accounted for using the equity method from the date that significant influence commences until the date that significant influence ceases. The Group's proportionate share of associates' net income for the financial year is presented as a separate line item in the consolidated income statement. The unrealised profits between the Group and associates are eliminated in proportion to share ownership. The carrying amount of an investment in an associate includes the carrying amount of goodwill resulted from its acquisition. When Teleste's share in an associate's losses exceeds its interest in the associate, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate or made payments on behalf of the associate. As at 31 December 2006 the Group had no investments in associates.

Joint ventures

Joint ventures are those entities over whose activities the Group has joint control, established by contractual agreement. The consolidated financial statements include the Group's proportionate share of the joint ventures' assets, liabilities, revenue and expenses on a line by line basis, from the date that joint control commences until the date that joint control ceases. As at 31 December 2006 the Group had no interests in joint ventures.

Principles of consolidation

Acquisitions of companies are accounted for by using the purchase method. All intercompany income and expenses, receivables, liabilities and unrealised profits arising from intercompany transactions, as well as distribution of profits within the Group are eliminated as part of the consolidation process. The allocation of the profit for the period attributable to equity holders of the parent company and minority interest is presented on the face of the income statement and minority interest is also disclosed as a separate item within equity. Minority interest in the loss is recorded in the consolidated financial statements at the investment value at most.

Teleste has applied the exemption under IFRS 1 according to which the classification and accounting treatment of business combinations occurred prior to the IFRS transition date do not have to be restated but previous values under FAS are taken as a deemed cost.

Financial statements of foreign subsidiaries

The functional currency of the parent company is euro and the consolidated financial statements are presented in euro. The functional currency is the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity. In preparing the consolidated financial statements income statements and cash flows of those foreign subsidiaries whose functional and presentation currency are not the euro, are translated into euro at the average exchange rate during the financial period. Their balance sheets are translated at the closing rate at the balance sheet date. Goodwill and fair value adjustments to assets and liabilities that arose on the acquisition of a foreign entity occurred prior to 1 January

2004 are translated into euro using the rate that prevailed on the date of the acquisition. Goodwill and fair value adjustments arisen on the acquisitions after 1 January 2004 are treated as part of the assets and liabilities of the acquired entity and are translated at the closing rate.

All translation differences arising from consolidation of foreign shareholdings are recognised as a separate item to equity. In accordance with the exemption included in IFRS 1 those cumulative translation differences arisen until the transition date have been reclassified to retained earnings and consequently they will not be later released in the income statement. From the transition date onwards translation differences arising on the consolidation are presented as a separate component of equity. If an interest in a foreign entity is disposed of all, or part of, that entity, related cumulative translation differences deferred in equity are recognised in the income statement as part of the gain or loss on sale.

Foreign currency transactions

Transactions in foreign currencies are translated at the rates of exchange prevailing on the dates of the transactions. At the end of the accounting period, foreign currency monetary balances are translated at the closing rate at the balance sheet date. Non-monetary items stated at fair value in a foreign currency are translated at foreign exchange rates ruling at the dates the fair value was determined. Other non-monetary items are translated using the exchange rate at the date of the transaction. Gains and losses resulting from transactions in foreign currencies and translation of monetary items are recognised in the income statement. Foreign exchange gains and losses on trade receivables and payables are adjusted to revenues and operating expenses, respectively. Other foreign exchange gains and losses are presented as financial income and expenses.

Property, plant and equipment

Items of property, plant and equipment are stated at historical cost less cumulative depreciation and any impairment losses. Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment. Interest expenses are not capitalised as part of the cost of non-current assets. Ordinary maintenance, repairs and renewals are expensed during the financial period in which they are incurred. In Teleste there are no such significant inspection or maintenance costs that should be capitalised. The Group recognises in the carrying amount of an item of property, plant and equipment the subsequent costs when that cost is incurred if it is probable that future economic benefits in excess of the originally assessed standard of performance of the existing asset will flow to the Group and the cost of the item can be measured reliably. Such renewals and repairs are depreciated on a systematic basis over the remaining useful life of the related asset. Gains and losses on sales and disposals are calculated as a difference between the received proceeds and the carrying amount and are included in other operating income and expenses, respectively.

Depreciation is charged to the income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Expected useful lives and residual values of non-current assets are reassessed at each balance sheet date and where they differ from previous estimates, depreciation periods are changed accordingly. The estimated useful lives are as follows:

Buildings	25–33 years
Machinery and equipment	3–5 years
Computers	0–3 years
Software	3 years

Land is not depreciated.

Leases

Group as lessee

Leases of property, plant and equipment where substantially all the risks and rewards incidental to ownership have been transferred to the Group are classified as finance leases. These assets are capitalised and are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease less cumulative depreciation and any impairment losses. The associated lease liabilities are included in interest-bearing liabilities in accordance with their maturity.

These assets acquired under finance leases are depreciated as comparable owned assets over the shorter of the useful lives disclosed above for property, plant and equipment or lease period and are adjusted for impairment charges, if any. Lease payments are apportioned between the reduction of the outstanding lease liability and finance charge. In respect of finance leases, the depreciation on the leased assets and the financial charge on the lease liability are shown in the income statement. The financial charge is allocated to the income statement so as to achieve a constant interest rate on the outstanding liability during the lease term.

An operating lease is a lease of property, plant and equipment where the lessor retains significant risks and rewards incidental to ownership. Payments made thereunder are charged to the income statement as rental expense on a straight-line basis over the lease term.

Group as lessor

Those leases under which Teleste is a lessor are classified as operating leases. Leased assets are presented in the lessor's balance sheet under property, plant and equipment according to the nature of the asset. They are depreciated over their estimated useful lives in accordance with the depreciation policy used for comparable assets in own use. Lease income is recognised in the income statement on a straight-line basis over the lease term.

Intangible assets

An intangible asset is recognised only when it is probable that future economic benefits that are attributable to the asset will flow to the Group and if the cost of the asset can be measured reliably. All other expenditure is expensed as incurred.

Goodwill

After 1 January 2004 goodwill represents the Group's share of difference between the cost of the acquisition and the fair value measured at the acquisition date of the net identifiable assets, liabilities and contingent liabilities acquired. The difference is first allocated, where applicable, to the underlying assets. The rest of the excess is presented as goodwill as a separate item in the consolidated balance sheet. Goodwill has been allocated to segments and in respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment in the associate. Goodwill is stated at cost less any cumulative impairment losses. Goodwill (together with other intangible assets with indefinite lives) is not amortised but is tested annually for impairment. Consequently goodwill was amortised on a straight-line basis over the expected useful life until 31 December 2003, after which the amortisation was discontinued.

Research and development costs

Research and development costs are expensed as they are incurred, except for certain development costs, which are capitalised when certain criteria are met. Significant future product platforms for which the potential demand and future cash flows can be estimated with sufficient degree of accuracy have been capitalised as intangible assets. Amortisation of such capitalised development projects is

Accounting Principles

commenced after the completion of the subprojects related to the product platform concerned. They are amortised on a systematic basis over their expected useful life, which is three years.

Other intangible assets

Other intangible assets of the Group mainly consist of connection fees and these are not amortised.

Those intangible assets which have estimated useful lives are depreciated on a straight-line basis over their known or estimated useful lives.

The estimated useful lives are as follows:

Customer relationships	2–4 years
Trademarks	5–10 years
Technology	3–5 years

Non-current assets held for sale and discontinued operations

A non-current asset (or disposal group) is classified as held for sale when its carrying amount will be recovered principally through a sale transaction rather than through continuing use. It is measured at the lower of carrying amount and fair value less costs to sell. Such assets and associated liabilities are presented separately in the balance sheet. Assets held for sale are not depreciated (or amortised) after the classification as held for sale.

A discontinued operation is a component of the Group's business that represents a separate major line of business or a geographical area of operations or is a subsidiary acquired exclusively with a view to resale. The result of discontinued operations is presented separately on the face of the consolidated income statement.

Impairment

The carrying amounts of assets are assessed for potential impairment at each balance sheet date and whenever there is any indication that an asset may be impaired. For the purposes of assessing impairment, assets are grouped at the cash generating unit level, which is the lowest level for which there are separately identifiable, mainly independent, cash inflows and outflows. Goodwill, unfinished intangible assets and intangible assets with indefinite useful lives, if any, are in all cases tested annually. All goodwill items of the Group have been allocated to segments. If there is an indication of an impairment, the Group estimates the recoverable amount of the asset or cash generating unit. When the recoverable amount of the asset or cash generating unit is lower than the carrying amount, the difference is immediately recognised as an impairment loss in the income statement. If the impairment loss is to be allocated for a cash-generating unit, it is allocated first by writing down any goodwill and then on pro rata basis to other assets of the unit.

The recoverable amount is the higher of an asset's or cash generating unit's fair value less costs to sell or value in use. Teleste has applied value in use in its calculations in which case the estimated future net cash flows expected to be derived from the asset or cash generating unit are discounted to their present value. Expenditures to improve assets' performance, investments or future restructurings are excluded from the cash flow estimates.

An impairment loss relating to property, plant and equipment and other intangible assets excluding goodwill is reversed if there is an indication that the impairment loss may no longer exist and there has been a positive change in the estimates used to determine the recoverable amount of an asset or cash generating unit. An impairment loss is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised for the asset in prior years. However, an impairment loss in respect of goodwill is never reversed.

Inventories

Inventories are stated at the lower of cost or net realisable value. Cost is assigned by using the first-in, first-out (FIFO) method. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and the estimated costs necessary to make the sale. The cost of inventories comprises all direct costs incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of overheads based on normal operating capacity.

Financial assets and liabilities

In Teleste IAS 32 and IAS 39 have been applied since 1 January 2004, hedge accounting as defined under IAS 39 is not applied.

Since 1 January 2004 financial assets are classified into categories as follows: financial assets at fair value through profit or loss, held-to-maturity assets, loans or receivables (assets) and available-for-sale assets. Financial assets are classified when initially acquired based on their purpose of use. In the case of a financial asset not measured at fair value through profit or loss, transaction costs are included in the acquisition cost. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. All purchases or sales of financial assets are recognised or derecognised using trade date accounting.

A financial asset is derecognised when the Group has lost its contractual rights to the cash flows from the financial asset or when it has transferred substantially all the significant risks and rewards of ownership of the financial asset to an external party.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are either classified as held for trading, or they are designated by the Group as at fair value through profit or loss upon initial recognition. A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of short-term profittaking from changes in market prices or it is a derivative that does not qualify for hedge accounting. Currently Teleste does not apply hedge accounting as defined under IAS 39. Financial assets and liabilities at fair value through profit or loss are recognised on the balance sheet using trade date accounting. They are measured at their fair values, which is the bid price at the balance sheet date based on published price quotations in an active market. Both financial assets held for trading and other financial assets maturing in 12 months after the balance sheet date are included in the current assets. A gain or loss arising from a change in the fair value, realised or unrealised, is recognised in the income statement as incurred.

Derivatives

Derivatives, including embedded derivatives, are included in the financial assets at fair value through profit or loss. They are recognised on the balance sheet at cost, equivalent to the fair value, and are subsequently fair valued at each balance sheet date. The Group uses forward exchange agreements and the Group's hedging policy is to cover all material currency risks at least six months ahead. Since Teleste does not currently apply hedge accounting as defined under IAS 39, changes in fair value of instruments designated as hedging instruments are recognised in profit or loss. Gains and losses arising from changes in fair value are included in operating profit unless the hedged item relates to financing when fair value changes are recognised in financial income or expenses. Fair values are determined utilising public price quotations and rates as well as generally used valuation models. The data and assumptions used in the valuation model are based on verifiable market prices. Derivatives that mature within 12 months after the balance sheet date are included in current assets or liabilities. Derivatives are not used for speculative purposes.

Available-for-sale assets

This category comprises those non-derivative financial assets that are designated as available for sale or are not classified into other categories. In Teleste available-for-sale investments consist of holdings in listed and unlisted companies and they are normally measured at their fair value. Investments in listed companies are measured at the bid price at the balance sheet date based on published price quotations in an active market. Such unlisted shares whose fair value cannot be reliably determined, are measured at cost. Unrealised changes in value of available-for-sale investments, net of tax, are recognised in equity in fair value reserve. Cumulative fair value changes are released to the income statement when the investment is sold or disposed of. Such significant impairment losses for which there is objective evidence, are recognised in the income statement immediately. Normally available-for-sale investments are included in non-current assets unless the Group has the intention to hold them for less than 12 months after the balance sheet date.

Loans and receivables

Financial assets that belong to this category meet the following criteria: they are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Group does not hold them for trading purposes either. Loans and receivables arise when money, goods or services are delivered to a debtor. They are included in current or non-current assets in accordance with their maturity. Loans granted by the Group are measured at cost. An impairment loss is recognised on loan receivables if their carrying amount exceeds their recoverable amount.

Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity. They are stated at amortised cost less impairment losses and presented within non-current assets. As at 31 December 2006 the Group had no assets classified as held-to-maturity investments.

Financial liabilities

Since 1 January 2004 financial liabilities are classified either as financial liabilities at fair value through profit or loss or as other liabilities. Teleste only has liabilities classified to the latter category. On initial recognition a loan is measured at its fair value that is based on the consideration received. Subsequent to initial recognition, these liabilities are stated at amortised cost calculated using the effective interest method. Interest expenses are recognised in the income statement over the term of the loan using the effective interest method.

Trade receivables

Trade receivables are recognised at the original invoice amount to customers and stated at their cost less impairment losses, if any. The amount of doubtful receivables and assessment of a potential impairment is based on risk of individual receivables. Trade receivables are measured at their probable value at the highest. An impairment loss is recorded when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Bad debts recognised in the income statement are included in other operating expenses.

Cash and cash equivalents

Cash and cash equivalents comprises cash balances, call deposits and other short-term highly liquid investments with original maturities of three months or less from the date of acquisition. Bank overdrafts, if any, are included within current liabilities.

Treasury shares

Teleste Corporation's own shares acquired by the Group, including directly attributable costs, are presented as a deduction from total equity in the consolidated financial statements. Purchases or subsequent sales of treasury shares are presented as changes in equity.

Dividends

The dividend proposed by the Board of Directors is not recognised until approved by a general meeting of shareholders.

Provisions

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, a reliable estimate can be made of the amount of the obligation and it is probable that an outflow of economic benefits will be required to settle the obligation. The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the balance sheet date. If the effect of the time value of money on the amount of a provision is material, a provision is discounted. Provisions can arise from warranties, onerous contracts and restructurings. A warranty provision is recognised when the underlying products are sold. The provision is based on historical warranty data and an estimate. A provision for non-cancellable purchase commitments of the Group is recognised, if these commitments result in inventory in excess of forecasted requirements. A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. A reimbursement from a third party related to a provision is recognised as a receivable only when the reimbursement is virtually certain.

A provision for restructuring is recognised when the Group has a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly to those it concerns. The plan identifies at least the following: the business concerned, the principal locations affected, the location, function, and approximate number of employees who will be compensated for terminating their services, the expenditures that will be undertaken and when the plan will be implemented. Future operating costs are not provided for.

Revenue recognition and net sales

Revenue from the sale of goods is recognised in the income statement when all significant risks and rewards of ownership have been transferred to the buyer, which normally takes place when a commodity is delivered. Revenue from services is recognised when the service has been performed.

Revenue from construction contracts is recognised either on a percentage-of-completion basis, using units of delivery (based on predetermined milestones) or by applying the cost-to-cost method of accounting as the measurement basis. Estimated contract profits are recognised in earnings in proportion to recorded sales, when a certain predetermined milestone has been achieved. In the cost-to-cost method, revenue and profits are recognised after considering the ratio of cumulative costs incurred to estimated total costs to complete each contract (the stage of completion). Recognition of profit requires the outcome of a construction contract be estimated reliably. If this is not the case, revenue is recognised only to the

Accounting Principles

extent of contract costs incurred that it is probable will be recoverable; and contract costs are expensed in the period in which they are incurred. In the event that the Group can be held as the main contractor of a construction contract, various product expenses including raw materials and labour costs will be accounted for in the calculation of the stage of completion. Possible changes in the expected total expenses of a construction contract are expensed as incurred. The expected loss is charged to the income statement immediately.

Costs related to a construction contract for which revenue is not yet recognised are included in inventories under unfinished construction contracts. If costs incurred together with recognised profits exceed the amount billed, the difference is included in the balance sheet item "trade and other receivables". When costs incurred together with recognised profits are lower than the amount billed, the difference is shown under "trade and other payables".

Net sales include revenue from services rendered and goods sold, adjusted for discounts granted, sales-related taxes and effects of the translation differences.

Other operating income

Other operating income comprises income not generated from primary activities, such as rental income and gains from disposal of assets.

Government grants

Government grants that compensate the Group for expenses incurred are recognised as revenue in the income statement on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the Group for the cost of an asset are recognised by deducting the grant from the carrying amount of the asset.

Employee benefits

Pension arrangements

Pension plans are classified as either defined contribution plans or defined benefit plans. The plans the Group has currently are classified as defined contribution plans. Contributions to defined contribution pension plans are recognised as an expense in the income statement in the year to which they relate. The statutory pension plans of Finnish subsidiaries in the Group are funded through pension insurance. Subsidiaries outside Finland have various pension schemes in accordance with local requirements and practices.

Share-based payments

Teleste has applied IFRS 2 Share-based payments to granted share options to the extent that such share option plans are in the scope of this standard, i.e. to those share option arrangements in which share options have been granted after 7 November 2002 that had not yet vested until 1 January 2005. The options granted before this have not been expensed in the income statement. The granted share options are measured at their fair values using the Black-Scholes option pricing model at the grant date and are recognised as an employee expense during the vesting period with a corresponding increase in equity. When the options are exercised, the proceeds received, net of any transactions costs, are credited to share capital (nominal value) and the share premium reserve.

Operating profit

Operating profit is not defined under IAS 1 Presentation of Financial Statements. In Teleste it is defined as a net amount that is comprised of the following items:

net sales
+ other operating income
– raw material and consumables used adjusted for changes in inventories of finished goods and work in progress
– employee benefits expense
– depreciation and amortisation expense and impairment losses
– other operating expense

= operating profit / loss

All other items not mentioned above are presented under the operating profit. Translation differences relating to sales and purchases are treated as adjustments to these items. All other translation differences are included in financial income and expenses.

Borrowing costs

Borrowing costs are generally expensed in the period in which they are incurred. However, incremental transaction costs directly related to acquiring a loan are included in the initial cost and are amortised as an interest expense using the effective interest rate method. The Group had no such capitalised transaction costs in its balance sheet at 31 December 2006.

Interest and dividend income

Interest income is recognised using the effective interest method. Dividend income is recognised when the right to the dividend has established.

Income taxes

The income taxes in the consolidated income statement consist of current tax and the change in the deferred tax assets and liabilities. Current tax includes taxes of the Group companies calculated on the taxable profit for the period determined in accordance with local tax rules, as well as the tax adjustments related to previous years. Deferred tax relating to items charged or credited directly to equity is itself charged or credited directly to equity.

Deferred tax assets and liabilities are provided in the consolidated financial statements using the balance sheet liability method, providing for all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The main temporary differences arise from the treatment of development costs, the depreciation difference on property, plant and equipment and effects of consolidation and eliminations. Deferred taxes are not provided for impairment of goodwill, which is not deductible for tax purposes, nor for undistributed profits of subsidiaries to the extent that is it probable that the temporary difference will not reverse in the foreseeable future. Deferred tax liabilities are recognised at their full amounts in the balance sheet, and deferred tax assets are recognised at estimated realisable amounts. The enacted or substantially enacted tax rate at the balance sheet date is used as the tax rate.

Accounting policies requiring management's judgement and key sources of estimation uncertainty

Management's estimates regarding obsolete inventories, bad debts and warranties are based on approved financial models and case-specific judgments. Both historical experience and management's current view on the market situation have been employed when using the financial models. Management has used the best information available during the process of preparing the financial statements when making case-specific judgements. Impairment tests reflect assumptions made by management and underlying sensitivity analyses of the future cash flows.

By the issuance of the consolidated financial statements Teleste is not aware of any significant uncertainties regarding estimates made at the balance sheet date, nor of such future key assumptions that might have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

New and amended standards and interpretations

Teleste will adopt the following new interpretations in 2007:

- IFRIC 8 Scope of IFRS 2
- IFRIC 9 Reassessment of Embedded Derivatives
- IFRIC 10 Interim Financial Reporting and Impairment

In 2007 the Group will adopt the new standard IFRS 7 Financial Instruments: Disclosures and the amendment of IAS 1 – Capital Disclosures. In addition, the Group will adopt IFRS 8 Operating Segments in 2009.

Teleste does not expect the adoption of the new and amended pronouncements will have a material impact on the Group's financial statements. The adoption of IFRS 7 will affect the extent of disclosures of financial assets and liabilities and IFRS 8 will affect the disclosures of segment reporting.

Segment Reporting

Teleste Group is organised in the primary reporting segments that are its business segments and secondary reporting segments that are geographical segments. These segments are based on the Group's organisational and internal reporting structure.

Business segments

The Group comprises two business segments that are Broadband Cable Networks and Video Networks.

Broadband Cable Networks segment's clientele consists almost exclusively of cable operators. Teleste supplies cable operators with equipment and systems designed to be used for building transmission networks and processing of video and data signals. Deliveries by Teleste include both individual pieces of equipment and comprehensive networks. Teleste also makes available a number of services related to the maintenance of network infrastructure.

Video Networks is in the business of manufacturing and supplying solutions for video surveillance networks between camera outputs and control rooms. The focus area is video surveillance applications requiring high-quality and real-time video, audio and data. With authorities as the main end-user group of Teleste systems, the most important applications are traffic control systems for both road and rail transport, urban surveillance systems and applications related to public safety in areas such as border control, ports and airports. One of Teleste's special know-how area is to integrate video surveillance network with hundreds cameras to one entirety.

Geographical segments

Secondary geographical segment is divided into three geographical areas:

- Nordic countries
- Other Europe
- Others (North America, Asia and Other countries)

The main market area of Broadband Cable Networks is Europe where the business unit is present with its 17 dedicated offices supported by several support and integration partners. Apart from Europe, offices have been established in China and India. Through its own offices Teleste Video Networks is present locally in all the major geographical markets: Europe, America and Southeast Asia.

Sales of geographical segments are shown based on customer location. Assets and investments are presented by geographical location of assets.

There are no inter-segment sales in the Group.

Segment assets and liabilities

Segment assets and liabilities include items directly attributable to the segment as well as those that can be allocated on a reasonable basis.

Unallocated items

Unallocated income statement items include costs and incomes which follow earnings after depreciations. Assets not allocated to the segments represent cash. Unallocated liabilities are intereste bearing liabilities and tax liabilities.

Business segments

2006	1 000 euros	Broadband Cable Networks	Video Networks	Group
External sales				
Services		2 813	195	3 008
Goods		82 738	16 027	98 765
Total external sales		85 551	16 222	101 773
Total revenue		85 551	16 222	101 773
Operating profit of segments		9 055	700	9 755
Operating profit				9 755
Unallocated expenses				–2 876
Profit for the period				6 879
Segment assets		46 927	14 520	61 447
Unallocated assets				6 789
Total assets				68 236
Segment liabilities		17 909	3 411	21 320
Unallocated liabilities				9 255
Total liabilities				30 575
Capital expenditure		2 032	4 143	6 175
Depreciation and amortisation		1 863	530	2 393

2005	1 000 euros	Broadband Cable Networks	Video Networks	Group
External sales				
Services		2 291	87	2 378
Goods		64 888	15 322	80 210
Total external sales		67 179	15 409	82 588
Total revenue		67 179	15 409	82 588
Operating profit of segments		7 374	1 208	8 582
Operating profit				8 582
Unallocated expenses				–2 626
Profit for the period				5 956
Segment assets		35 786	10 485	46 271
Unallocated assets				8 524
Total assets				54 795
Segment liabilities		13 648	3 757	17 405
Unallocated liabilities				5 084
Total liabilities				22 489
Capital expenditure		2 726	1 347	4 073
Depreciation and amortisation		1 607	333	1 940

Geographical segments

2006	1 000 euros	Nordic countries	Other Europe	Others	Group
Sales by origin		32 200	62 100	7 473	101 773
Assets		51 381	15 115	1 740	68 236
Capital expenditure		5 838	87	250	6 175

2005	1 000 euros	Nordic countries	Other Europe	Others	Group
Sales by origin		31 354	45 728	5 506	82 588
Assets		43 010	8 799	2 986	54 795
Capital expenditure		3 323	200	550	4 073

Business Combinations acquired during 2006 and 2005

The range of products and services of Video Networks for certain midmarket segments was strenghtened by the acquisition of the Suomen Turvakamera Ltd on May 2006. The purchase price of the share capital was EUR 3,067 thousand. The goodwill, amounted EUR 2,607 thousand, is mainly due to expected increase in demand of existing products of Video Networks business area. Treasury shares were conveyed as a part of the payment for the consideration EUR 311 thousand i.e. 30,000 numbers. The conveyance was based on the authorisation granted by the annual general meeting of Teleste Corporation at 4 April 2006. The shares conveyed were measured at the average trading share price quoted in the Helsinki Stock Exchange at 31 May 2006 being EUR 10.37 per share. The number of the shares then conveyed accounted for 0.17 per cent of the total number of the shares of Teleste Corporation.

The FttH knowledge of Broadband Cable Networks was strenghtened by the acquisition of the share capital of Swedish PromaCom AB on June 2006. The purchase price of the share capital was EUR 322 thousand. The goodwill, amounted EUR 305 thousand, is mainly due to expected increase in demand of existing products of Broadband Cable Networks business area.

The net profit of PromaCom AB for the period 16 June–31 December 2006 and Suomen Turvakamera Ltd for the period 1 June–31 December are included in the consolidated income statement for the year 2006. If the companies had been consolidated since 1 January 2006, the Group revenue would have been EUR 1.6 million higher and the Group profit would have decreased EUR 0.6 million.

During the third quarter of 2006 EUR 191 thousand were recognised as a probable additional consideration. A conditional supplementary contract price EUR 191 thousand related to the acquisition of S-Link AB in November 2003 was entered in the books in the third quarter of 2006. The conditional supplementary contract price in its entirety was booked in the goodwill.

During the last quarter of 2005 40% minority share of Teleste Electronics (SIP) Ltd was acquired. The purchase price was EUR 429 thousands, of which EUR 314 thousand was booked as goodwill. A conditional supplementary contract price EUR 369 thousand related to the acquisition of S-Link AB was entered in the books in the last quarter of 2005. S-Link AB's final acquisition price will be recognised at 31 December 2006 and it will be paid during spring 2007.

During the year 2005 the treasury shares were conveyed as a part of Flomatik AS's final acqusition price EUR 33 thousand i.e. 5,000 numbers. The conveyance was based on the authorisation granted by the annual general meeting of 5 April 2005. The shares conveyed were measured at the average trading share price quoted in the Helsinki Stock Exchange during the time period 1 June–30 June 2005 being EUR 6.60 per share. The number of the shares then conveyed accounted for 0.03 per cent of the total number of the shares of Teleste Oyj.

The fair values determined in the business combination are based on the following estimates:

- The fair value of acquired trade marks is determined to equate with the discounted royalties, which have been managed to be avoidable by owing the trademarks in question. A reasonable royalty per cent, that an external party would pay for a licensing agreement, has been estimated when determining the fair values.
- The fair value of acquired technology is determined to equate with the discounted product development costs, which have been managed to be avoidable by owing the technology in question.
- Determination of fair value of the customer relationships is based on the estimated life time of the customer relationships and the discounted cash flows to be derived from the existing customerships.

The following assets and liabilities were recognised in the acquisition Suomen Turvakamera Oy during the year 2006.

1 000 euros	Recognised fair values on acquisition
Fair values used in consolidation	
Trade marks (inc. in intangible assets)	65
Customer relationship (inc. in intangible assets)	223
Technology (inc. in intangible assets)	172
Book values used in consolidation	
Tangible assets	115
Inventories	279
Trade receivables	352
Cash and cash equivalents	0
Total assets	1 206
Book values used in consolidation	
Interest-bearing liabilities	256
Deferred tax liabilites	120
Other liabilities	368
Total liabilities	744
Net identifiable assets and liabilities	462
Total consideration	3 000
Transfer tax	48
Transfer tax shares	5
Other acquisition costs	16
Goodwill on acquisition	2 607
Consideration paid in cash	-2 758
Cash and cash equivalents in acquired subsidiary	0
Total net cash outflow on the acquisition	-2 758

The following assets and liabilities were recognised in the acquisition PromaCom AB during the year 2006.

1 000 euros	Recognised fair values on acquisition
Fair values used in consolidation	
Trade marks (inc. in intangible assets)	9
Customer relationship (inc. in intangible assets)	28
Technology (inc. in intangible assets)	131
Book values used in consolidation	
Tangible assets	3
Inventories	51
Deferred tax receivables	123
Trade receivables	240
Cash and cash equivalents	2
Total assets	586
Book values used in consolidation	
Interest-bearing liabilities	204
Deferred tax liabilites	44
Other liabilities	322
Total liabilities	569
Net identifiable assets and liabilities	17
Total consideration	300
Other acquisition costs	22
Goodwill on acquisition	305
Consideration paid in cash	-322
Cash and cash equivalents in acquired subsidiary	2
Total net cash outflow on the acquisition	-320

1 Construction contracts

Group revenue includes EUR 4,030 thousand in 2006 (2005: EUR 3,739 thousand) of income from construction contracts.

Revenue recognised in the consolidated income statement from construction contracts in progress amounted to EUR 4,030 thousand on 31 December 2006 (31 Dec. 2005: EUR 3,739 thousand). No advance payments included to balance sheet at the closing time.

1 000 euros	2006	2005

2 Other operating income

Government grants related to development costs	1 854	1 379
Rental income	106	151
Government grants	198	0
Total	**2 158**	**1 530**

3 Employee benefits

Wages and salaries	–21 068	–19 821
Pension expenses		
Defined contribution plans	–4 274	–3 086
Other post employment benefits	–2 055	–1 603
Activated R&D salaries and social costs	1 003	946
Equity-settled share-based transactions	–706	–560
Total	**–27 100**	**–24 124**

Information on the remuneration of (and loans to) the Group management is presented in the note Related party transactions.

The average number of employees in the Group during the financial year broken down by following categories

Research and Development	131	121
Production and Material Management	297	274
Sales and Marketing, Log. Services	148	124
Finance and IT	32	27
Total	**608**	**546**

4 Depreciation, amortisation and impairment

Depreciation and amortisation by asset type:

Tangible assets		
Buildings	–297	–306
Machinery and equipment	–761	–876
Other tangible assets	–316	–165
Total	**–1 374**	**–1 347**
Intangible assets		
Capitalised development expenses	–939	–593
Other intangible assets	–80	0
Total	**–1 019**	**–593**

No impairment test losses are booked to Profit and Loss Account during 2006 or 2005.

5 Other operating expenses

Rental expenses	–1 575	–1 246
External services	–1 198	–1 200
Impairment loss on trade receivables	–20	–130
Other cariable costs	–1 551	–1 740
Travel and IT costs	–4 440	–3 534
R&D costs	–2 564	–1 945
Other expenses	–4 658	–3 996
Total	**–16 006**	**–13 791**

Notes

1 000 euros	2006	2005

6 Financial income

Interest income	108	277
Dividend income	6	3
Other	80	0
Total	**194**	**280**

7 Financial expenses

Interest expenses	-381	-465
Exchange losses	-206	-29
Other financial expenses	-74	-47
Total	**-661**	**-541**

8 Income taxes

Recognised in the income statement		
Current tax expense		
Current year	-2 085	-2 016
Adjustments for prior years	-15	61
Deferred tax expense	-308	-408
Total	**-2 408**	**-2 363**

Reconciliation of the income tax expense in the income statement, EUR 2,408 thousand, and the income tax expense calculated using the Teleste Group's domestic corporation 26% tax rate.

Profit before tax	9 288	8 321
Income tax using the domestic corporation tax rate (26%/29%)	-2 415	-2 163
Effect of tax rates in foreign jurisdictions	161	25
Tax exempt revenues	12	7
Tax debt increase related to balance sheet items	-308	-263
Non-deductible expenses	-5	-46
Taxes from prevoius year	-15	61
Effect of tax losses utilised	161	19
Other items	0	-2
Income tax expense reported in the consolidated income statement	**-2 408**	**-2 363**

9 Earnings per share

The basic earnings per share is calculated as follows:

$$\frac{\text{Profit for the year attributable to equity holders of the parent}}{\text{Weighted average number of ordinary shares outstanding during the financial year}}$$

The number of ordinary shares outstanding excludes the treasury shares.

The diluted earnings per share is calculated as follows:

$$\frac{\text{Profit for the year attributable to equity holders of the parent (diluted)}}{\text{Weighted average number of ordinary shares outstanding during the financial year (diluted)}}$$

The changes in the number of the shares are presented in the note 17 Capital and reserves.

	2006	2005
Profit for the year attributable to equity holders of the parent, (1 000 euros)	6 879	5 956
Weighted average number of ordinary shares outstanding during the financial year (1 000 euros)	16 896	16 851
Basic earnings per share (euros)	0.41	0.35
Weighted average number of ordinary shares outstanding during the financial year (1 000 shares)	16 896	16 851
Effect of share options on issue (1 000 shares)	1 127	1 150
Weighted average number of ordinary shares outstanding during the financial year (diluted) (1 000 shares)	18 023	18 001
Diluted earnings per share (euros)	0.38	0.33

The share options granted by the Group have a dilutive effect, i.e. they increase the number of the ordinary shares when their subscription price is below the fair value of the share. The fair value is calculated based on the average share price during the period. The dilutive effect equals the number of the shares gratuitously issued; this difference arises when the Group can not issue the same number of shares at their fair value using the proceeds received on the exercise of the options.

10 Property, plant and equipment

1 000 euros	Land areas	Buildings	Machinery and equipment	Other tangible assets	Advance payments	**Total**
Balance 1.1.2006	108	5 523	13 421	2 684	59	**21 795**
Additions	0	59	917	196	37	**1 209**
Acquisitions through business combinations	0	0	118	0	0	**118**
Transfers between classes	0	0	0	59	–59	**0**
Disposals	0	–198	–37	0	0	**–235**
Balance 31.12.2006	108	5 384	14 419	2 939	37	**22 887**
Depreciation and impairment losses, balance 1.1.2006	0	–2 292	–11 564	–2 079	0	**–15 935**
Depreciation change for the year	0	–297	–761	–316	0	**–1 374**
Depreciation and impairment losses, balance 31.12.2006	0	–2 589	–12 325	–2 395	0	**–17 309**
Carrying amounts at 1.1.2006	108	3 231	1 857	605	59	**5 860**
Carrying amounts at 31.12.2006	108	2 795	2 094	544	37	**5 578**

1 000 euros	Land areas	Buildings	Machinery and equipment	Other tangible assets	Advance payments	**Total**
Balance at 1.1.2005	108	5 506	12 204	2 106	0	**19 924**
Additions	0	14	1 217	380	59	**1 670**
Transfers between classes	0	0	0	198	0	**198**
Effect of movements in foreign exchange	0	3	0	0	0	**3**
Balance 31.12.2005	108	5 523	13 421	2 684	59	**21 795**
Depreciation and impairment losses, balance 1.1.2005	0	–1 986	–10 688	–1 914	0	**–14 588**
Depreciation change for the year	0	–306	–876	–165	0	**–1 347**
Depreciation and impairment losses, balance 31.12.2005	0	–2 292	–11 564	–2 079	0	**–15 935**
Carrying amounts 1.1.2005	108	3 520	1 516	192	0	**5 336**
Carrying amounts 31.12.2005	108	3 231	1 857	605	59	**5 860**

Carrying amount of production machinery and equipment 31.12.2006	1 784
Carrying amount of production machinery and equipment 31.12.2005	1 603

Property, plant and equipment include assets leased under financial leases as follows:

1 000 euros	Machinery and equipment
31.12.2006	
Historical cost	1 383
Cumulative depreciation	–407
Carrying amount 31.12.2006	976
31.12.2005	
Historical cost	1046
Historical cost	–154
Carrying amount 31.12.2005	892

Notes

11 Intangible assets

1 000 euros	Goodwill	Development costs	Other intangible assets	Advance payments	Total
Balance 1.1.2006	9 205	3 763	75	0	**13 043**
Additions	194	1 344	72	0	**1 610**
Acquisitions through business combinations	2 728	0	628	0	**3 356**
Balance 31.12.2006	12 127	5 107	775	0	**18 009**
Amortisation and impairment losses, balance 1.1.2006	0	-1 249	0	0	**-1 249**
Amortisation for the year	0	-939	-80	0	**-1 019**
Amortisation and impairment losses, balance 31.12.2006	0	-2 188	-80	0	**-2 268**
Carrying amounts 1.1.2006	9 205	2 514	75	0	**11 794**
Carrying amounts 31.12.2006	12 127	2 919	695	0	**15 741**

1 000 euros	Goodwill	Development costs	Other intangible assets	Advance payments	Total
Balance 1.1.2005	8 526	1 982	59	205	**10 772**
Additions	679	1 781	16	0	**2 476**
Balance 31.12.2005	9 205	3 763	75	205	**13 248**
Amortisation and impairment losses, balance 1.1.2005	0	-656	0	0	**-656**
Amortisation for the year	0	-593	0	0	**-593**
Transfers between classes	0	0	0	-205	**-205**
Amortisation and impairment losses, balance 31.12.2005	0	-1 249	0	-205	**-1 454**
Carrying amounts 1.1.2005	8 526	1 326	59	205	**10 116**
Carrying amounts 31.12.2005	9 205	2 514	75	0	**11 794**

For the purposes of impairment testing goodwill items of the Group have been allocated to the segments, each of which represents a separate cash-generating unit. The aggregate goodwill amount totalled EUR 12.1 million at 31 December 2006. Goodwill has been allocated to the following cash-generating units: Teleste Broadband Cable Networks EUR 5.8 million (including Flomatik, PromaCom and Teleste Electronics (SIP) Co.), Teleste Video Networks EUR 6.3 million (including S-Link and Suomen Turvakamera).

The recoverable amount of the segments is based on value-in-use calculations. Those calculations use cash flow projections based on the strategy approved by the management. Calculations prepared cover 10 years' period and the expected growth rate during the first five years is 20 per cent. The expected future cash flows for a further 5 year period are extrapolated using a 5 per cent growth rate. Management's view on the cash flows after the first five years' period is cautious as the changes of the industry are difficult to foresee. 5 per cent growth rate has been used for all segments. A discount rate of 12,1 per cent (12 per cent) has been used in discounting the projected cash flows. The terminal value of the segments is calculated by discounting the future cash flows after the 10 year period, assumption is that cash flows are the same as at last year of the period. No terminal value was used in calculations in 2005.

Management is of the opinion that potential changes of any key parameters used in the calculations moderately assessed would not result the carrying amount of the segment to exceed the recoverable amount. Impairment losses would occur on Video Networks segment, if growth rate significantly less than 10 per cent and with a terminal value calculated as mentioned above.

The Group received a grant amounting to EUR 2.5 million from Tekes (National Technology Agency of Finland) towards development costs in 2006 (2005: EUR 1.61 million). From the grant received EUR 0.67 million (2005: EUR 0.232 million) has been recognised to deduct the carrying amount of the asset.

The grant has the condition, according to which 10% of the total costs of the project have to be incurred through subcontracting work in Finnish small and medium-sized companies.

12 Available-for-sale investment

1 000 euros	2006	2005
Unlisted shares	1 116	1 116
Total	1 116	1 116

The Group has not sold unlisted shares during the years 2006 and 2005.

13 Deferred tax assets and liabilities

1 000 euros	1.1.2006	Recognised in the income statement	31.12.2006
Movements in temporary differences during 2006:			
Deferred tax assets:			
Effects of consolidation and eliminations	200	192	392
Provisions	432	-126	306
Tax losses carried forward	25	-25	0
Cumulative depreciation difference	450	-101	349
Total	**1 107**	**-60**	**1 047**
Deferred tax liabilities:			
Capitalisation of intangible assets	-653	-248	-901
Cumulative depreciation difference	-514	-2	-516
Other taxable temporary differences	0	3	3
Total	**-1 167**	**-247**	**-1 414**

In the consolidated financial statements deferred tax receivables and liabilities have been offset.

1 000 euros	1.1.2005	Recognised in the income statement	31.12.2005
Movements in temporary differences during 2005:			
Deferred tax assets:			
Effects of consolidation and eliminations	9	191	200
Provisions	366	66	432
Tax losses carried forward	81	-56	25
Cumulative depreciation difference	487	-37	450
Total	**943**	**164**	**1 107**
Deferred tax liabilities:			
Capitalisation of intangible assets	-100	-553	-653
Cumulative depreciation difference	-495	-19	-514
Total	**-595**	**-572**	**-1 167**

In the consolidated financial statements deferred tax receivables and liabilities have been offset.

At 31 December 2006 the Group had unused tax losses in foreign subsidiaries amounting to EUR 574 thousand. No deferred tax asset has been recognised in respect of this because it is not probable that future taxable profit will be available against which the Group can utilise the benefit therefrom. This tax loss has no expiry date.

No deferred tax liability has been provided for the undistributed profits of the foreign subsidiaries amounting to EUR 4,994 thousand at 31 December 2006 (31 Dec. 2005: EUR 3,759 thousand). This is because dividend distribution in these countries is tax neutral or dividend distribution is unlikely.

14 Inventories

1 000 euros	2006	2005
Raw materials and consumables	3 846	3 084
Work in progress	5 839	1 979
Finished goods	6 919	4 559
Total	**16 604**	**9 623**

The amount of the impairment losses of inventories to the realisable value recognised as an expense durin the financial period is EUR 272 thousand. At the end of the financial year EUR 3,352 thousand was deducted from the inventory value to the net realisable value (31 December 2005: EUR 3,080 thousand).

Notes

1 000 euros	2006	2005

15 Trade and other current receivables

	2006	2005
Trade receivables	17 873	14 745
Receivables from associate(s)	(1 858)	(3 147)
Accrued income and prepayments	4 082	2 862
Other receivables	454	271
Total	**22 409**	**17 878**

During the financial year ended the Group has recognised impairment losses on trade receivables totalling EUR 34 thousand (2005: impairment losses amounting to EUR 399 thousand). Carrying amounts best represent the amount that is the maximum credit risk exposure, without taking account of the fair value of any collateral, in the event of other parties failing to perform their obligations. There are no significant concentrations of credit risk with respect to the current receivables of the Group.

The accrued income and prepayments include receivables of EUR 684 thousand from Tekes (National Technology Agency of Finland) and a receivable of EUR 840 thousand from construction contracts (31 Dec. 2005: EUR 1,520 thousand).

16 Cash and cash equivalents

	2006	2005
Cash at bank and in hand and call deposits	6 789	6 524
Liquid investments (maturity 1–3 months)	0	2 000
Total	**6 789**	**8 524**
Cash and cash equivalents in the statement of cash flows	6 789	8 524

17 Capital and reserves

1 000 euros	Number of shares, 1 000	Number of own shares, 1 000	Number of shares, total 1 000	Share capital, 1 000 euros	Reserve fund, 1 000 euros
1.1.2005	16 850	490	17 340	6 935	1 277
Own shares sold	5	-5	0	0	-1
31.1.2005	16 855	485	17 340	6 935	1 276
Share options exercised by employees	50	0	50	20	141
Own shares sold	30	-30	0	0	0
31.12.2006	16 934	455	17 389	6 955	1 417

The number of Teleste Oyj shares was 17,389,302 at 31 December 2006 (31 Dec. 2005: 17,339,752 shares). The nominal value of a share is EUR 0.40. The maximum share capital is EUR 25.6 million, i.e. 64 million shares (31 Dec. 2005: EUR 25.6 million and 64 million shares) and the minimum share capital is EUR 6.4 million (31 Dec. 2005: EUR 6.4 million) according to the parent company's articles of association. All shares issued have been fully paid.

The annual general meeting of Teleste Oyj held on 4 April 2006 authorised the Board to acquire the maximum of 1,215,000 Teleste's own shares, convey at most 1,700,000 own shares and increase the share capital by a new issue of no more than 3,400,000 shares. The authorisations given to the Board by the annual general meeting for acquisition of own shares and increasing the share capital were not used during 2006. The number of treasury shares conveyed for the purchase price of Suomen Turvakamera was 30,000 in 2006.

The annual general meeting of Teleste Oyj held on 5 April 2005 authorised the Board to acquire the maximum of 370,000 Teleste's own shares, convey at most 860,000 own shares and increase the share capital by a new issue of no more than 3,400,000 shares. The authorisations given to the Board by the annual general meeting for acquisition of own shares and increasing the share capital were not used during 2005. The number of treasury shares conveyed for the additional purchase price of Flomatik AS was 5,000 in 2005.

Shares subscribed for pursuant to the share option plans will entitle to dividend when the increase of the share capital is registered with the Finnish trade register. Voting and other shareholder rights will commence on the date on which the increase of the share capital is registered with the Finnish trade register.

Translation reserve

The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign subsidiaries.

Dividends

After the balance sheet date the dividend of EUR 0.20 per share (2005: EUR 0.16 per share) was proposed by the Board of Directors.

17 Share-based payments

The Group has had share option plans since the year 1997 as a part of a remuneration arrangement for the key management personnel. Teleste has applied IFRS 2 Share-based Payments to those option arrangements in which the options have been granted after 7 November 2002 that had not yet vested until 1 January 2005. During the financial period ended the Group has had 4 different option plans with the employees.

In April 2006 were granted 23,100 pcs of 2002A share options, 23,100 pcs of 2002B share options, 25,200 pcs of 2004A share options and 16,800 pcs of 2004B share options. These options were bounded to the following additional terms: orders for the year 2006 have to meet an amount of EUR 100 million at minimum (50% of the options are earned) and operating profit has to meet an amount of EUR 10 million at minimum (50% of the options are earned). At the moment the options were granted the probability for fulfilment of the terms was 25% and the actual fulfilment in the financial statements for 2006 was 50%. Due to this 11,550 pcs of 2002A share options, 11,550 pcs of 2002B share options, 12,600 pcs of 2004A share options and 8,400 pcs of 2004B share options were returned into possession of the company. In November 2006 2,500 pcs of 2004A share options and 2,500 pcs of 2004B share options were granted. During the financial year 31,000 pcs of 2004A share options and 20,000 pcs of 2004B share options were returned for the company due to termination of employment.

The options expire unless they have been redeemed within the subscription time. If the employee leaves the Group before the options ultimately vest, the options are forfeited. The options granted are fair valued at the grant date using the Black-Scholes (BS) option pricing model and are recognised as an employee expense during the vesting period. The fair value of the shares for the arrangements in which shares are granted was based on the quoted share price. The measurement of the options' fair value did not consider expected dividends.

The following tables illustrate the terms and conditions of the option plans.

Arrangement	Share options, granted to key management 2002A	Share options, granted to key management 2002B	Share options, granted to key management 2004A	Share options, granted to key management 2004B
Nature of the arrangement	Share options	Share options	Share options	Share options
Date of the Annual General Meeting	8.4.2002	8.4.2002	16.3.2004	16.3.2004
Grant Date	15.4.2003, 15.10.2004, 4.4.2006	15.4.2003, 15.10.2004, 4.4.2006	15.6.2004, 4.4.2006, 15.11.2006	15.6.2005, 4.4.2006, 15.11.2006
Total number of instruments granted	265 100	263 100	260 700	274 300
In the possession of the company 31.12.2006	21 450	23 450	51 900	34 100
Exercise price 31.12.2006	6.95	2.29	5.70	6.31
Share price at the grant date	2.57; 5.62; 11.50	2.78; 5.62; 11.50	6.19; 11.50	6.75; 11.50
Contractual life (years)	5.5	6.5	5	6
Vesting conditions	For the options granted in 2003: 2 year's service. For the options granted in October 2004: 5 month's service. For the options granted in April 2006: 9 month's service and additional condition: orders for the year 2006 have to meet at minimum an amount of EUR 100 million thus 50% of the options are earned and operating profit has to meet at minimum an amount of EUR 10 million thus 50% of the options are earned.	For the options granted in 2003: 3 year's service. For the options granted in October 2004: 17 month's service. For the options granted in April 2006: 9 month's service and an additional condition: orders for the year 2006 have to meet at minimum an amount of EUR 100 million thus 50% of the options are earned and operating profit has to meet at minimum an amount of EUR 10 million thus 50% of the options are earned.	For the options granted in June 2004: 3 year's service. For the options granted in March 2006: 1 year's service. 50% of the options are earned only if earnings/share is at minimum 0,30 and ROI is at minimum 20% at 31 December 2006. The options granted in April 2006 have an additional condition: orders for the year 2006 at minimum EUR 100 million (50%) and operating profit EUR 10 million (50%).	For the options granted in June 2005: 3 year's service. For the options granted in March 2006: 1 year's service. 50% of the options are earned only if earnings/share is at minimum 0,35 and ROI is at minimum 25% at 31 December 2007. The options granted in April 2006 have an additional condition: orders for the year 2006 at minimum EUR 100 million (50%) and operating profit EUR 10 million (50%).

Settlement	Shares, warrant sales	Shares, warrant sales	Shares, warrant sales	Shares, warrant sales
Expected volatility	40%/20%	40%/20%	35%/20%	30%/20%
Expected option life at grant date (years)	4.5	5.5	4.8	4.9
Risk-free interest rate	4%/2.5%	4%/2.5%	4%/2.5%	4%/2.5%
Expected dividend (dividend yield)	0%	0%	0%	0%
Expected departures (at the grant date)	0%	0%	0%	0%
Expected outcome of meeting performance criteria (at the grant date)	–, 25% for the options granted in April 2006	–, 25% for the options granted in April 2006	90%, 25% for the options granted in April 2006	90%, 25% for the options granted in April 2006
Fair value per granted instrument determined at the grant date	0.26–0.75/ April 2006 4.69	1.12–3.25/ April 2006 9.26	2.26/ April 2006 5.94	1.98/ April 2006 5.51
Valuation model	BS	BS	BS	BS

The expected volatility has been determined by using the historical volatility of the share price adjusted for any expected changes to future volatility due to publicly available information. The historical volatility is calculated based on the weight average remaining life of the share options.

Notes

The changes in the number of options and weighted average exercise price were as follows (options granted to key management):

	2006 Weighted average exercise price per share, euros	Number of options	2005 Weighted average exercise price per share, euros	Number of options
Outstanding at the beginning of the period	5.64	1 021 000	5.33	748 000
Granted during the period	5.29	93 200	6.47	275 000
Exercised during the period	–3.23	–49 550	0.00	0
Forfeited during the period	–5.94	–95 100	2.53	–2 000
Outstanding at the end of the period	6.41	969 550	5.64	1 021 000
Exercisable at the end of the period	4.76	500 450		

During 2006 10,000 pcs of 2002A share options were exercised at exercise price of EUR 6.95 and 39,550 pcs of 2002B share options at exercise price EUR 2.29. From the exercised options EUR 19,8 thousand were credited to the share capital and EUR 140,9 thousand to the share premium. No options were exercised during 2005.

Options outstanding at the end of the year granted to key management – exercise prices and remaining life:

Expire in	Exercise price, euros	2006 Number of options	2005 Number of options
2007	6.95	243 550	242 000
2008	2.29	212 000	240 000
2009	5.70	248 100	264 000
2010	6.31	265 900	275 000
Total	**5.44**	**969 550**	**1 021 000**

Management team and CEO are involved in a share-based remuneration arrangement. Additional information about this arrangement is presented in the Note Related Party Transactions.

18 Interest-bearing liabilities

1 000 euros	2006	2005
Non-current		
Finance lease liabilities	742	706
Total	**742**	**706**
Current		
Loans from financial institutions	7 000	3 000
Finance lease liabilities, current portion	270	210
Total	**7 270**	**3 210**

Interest-bearing loans from financial institutions are carried at amortised cost and finance lease liabilities are carried at fair value.

The long-term liabilities mature as follows:

1 000 euros 2006	2007	2008	2009	2010	2011	thereafter
Finance lease liabilities	274	278	268	161	28	0
Total	**274**	**278**	**268**	**161**	**28**	**0**

1 000 euros 2005	2006	2007	2008	2009	2010	thereafter
Finance lease liabilities	210	210	210	210	75	0
Total	**210**	**210**	**210**	**210**	**75**	**0**

1 000 euros	31.12.2006	31.12.2005
The currency mix of the Group long-term interest-bearing liabilities was as follows:		
EUR	742	706
	742	706
Group long-term interest-bearing liabilities – interest rates:		
Finance lease liabilities	3.9%–4.2%	3.7%–4.1%
The currency mix of the Group short-term interest-bearing liabilities:		
EUR	100%	100%
	100%	100%
Group short-term interest-bearing liabilities – interest rates are as follows:		
Bank loans	3.7%	3.0%
Finance lease liabilities	3.9%–4.2%	3.7%–4.1%
Finance lease liabilities of the Group are payable as follows:		
Minimum lease payments		
Less than one year	270	210
Between one and five years	813	770
Total	1 083	980
Present value of minimum lease payments		
Less than one year	274	210
Between one and five years	735	705
Total	1 009	915
Future finance charges	74	65
Total finance lease liabilities	1 083	980

Notes

19 Provisions

1 000 euros	Warranties	Restructuring	Onerous contracts	Other	**Total**
1.1.2006	1 444	107	298	168	**2 017**
Provisions made during the year	50	0	0	0	**50**
Provisions used during the year	–326	0	–298	–168	**–792**
31.12.2006	1 168	107	0	0	**1 275**

	2006	2005
Non-current	425	515
Current	850	1 502
Total	**1 275**	**2 017**

Warranties

The Group grants 12–36 months guarantees for its certain products. If defects are detected during the warranty period, the Group either repairs the product or delivers a comparable new product. The amount of the warranty provision is based on the past experience on defective products and an estimate of related expenses.

Restructuring

The provision is based on the restructuring of sales organisation carried out in 2002.

20 Trade and other current liabilities

1 000 euros	2006	2005
Current		
Trade payables	9 462	6 347
Liabilities due to associates	(4 109)	(7 189)
Personnel, social security and pensions	3 879	3 822
Accrued interest expenses and other financial items	140	8
Other accrued expenses and deferred income	3 608	2 485
Other liabilities	3 831	3 461
Total	**20 920**	**16 123**

Includes the income tax payable for the period.

21 Income tax payable for the period

The item other accrued expenses includes the income tax payable, EUR 875 thousand, on the profit for the period (31 Dec. 2005: EUR 1,101 thousand).

Financial Risk Management

The objective of the Group's financial risk management is to identify, evaluate and hedge financial risks to reduce the impacts of price fluctuations in financial markets and of other factors on earnings, balance sheet and cash flows as well as to guarantee cost-efficient funding for the Group at all times.

The Board has approved financial risk management guidelines and the allocation of responsibilities defined in the Group risk management policy and related operating policies covering specific areas. The Board oversees the Group's risk management framework. The Group's administration is responsible for the coordination and control of the Group's total financial risk position and external hedging transactions with banks in the name of the parent company. Teleste is risk averse in its treasury activities. The identification of the exposure is a common task of the business units and the Group administration.

Currently the hedge accounting principles as defined in IAS 39 are not applied in Teleste as the Group's volatility has not increased to a major extent.

Financial risks comprise market, credit, liquidity and cash flow interest rate risk, which are discussed more in detail below. The Group's exposure to price risk is low.

Market risk

Market risk includes three types of risk: currency risk, price risk and fair value interest rate risk. Fluctuations of foreign exchange rates, market prices or market interest rates may cause a change in the value of a financial instrument. These changes may have an effect on the consolidated earnings, balance sheet and cash flows.

Currency risk

The Group's currency position is divided into the transaction position and net investments in foreign operations. Foreign exchange exposures of the Group's units arise from receivables and accounts payables denominated in foreign currency, sales and purchase contracts and from forecast sales and purchases. Major part of the Group's sales is in Euro. The most significant non-euro sales currencies are US dollar (accounts for 10 per cent of the net sales), Swedish and Norwegian crowns (15 per cent) and UK pound sterling (9 per cent). Significant part of expenses, 60 per cent, arise in euro and in US dollar almost 30 per cent. The hedging decisions are based on the expected net cash flow for the following six months.

Since the Group's currency risk exposure regarding net investments in foreign operations is relatively low, the equity position, i.e. differences in the calculatory euro values of these amounts (translation risk) is not actively hedged. At 31 December 2006 the total non-euro-denominated equity of the Group's foreign subsidiaries amounted to EUR 5.6 million (31 Dec. 2005: EUR 4.2 million).

In principle Teleste hedges forecast and probable cash flows. The Group only uses forward exchange agreements. According to the Group's currency risk management policy all material currency risks are hedged at least six months ahead and the Group's transaction position shall at all times be hedged 80–100% by currency. The level of hedges is monitored on a monthly basis. Currency risk is also managed through, among others, operational planning, pricing and offer terms. Repricing varies between 3 to 24 months. At the year-end 2006 the fair value of currency derivatives amounted to EUR 10.1 million (31. Dec 2005: EUR 16.6 million).

Fair value interest rate risk and cash flow interest rate risk

Teleste's interest rate risk mainly comprises cash flow interest rate risk that arises from the interest-bearing liabilities. The loans have short-term interest rate as a reference rate. The interest period is of less than one year in all the Group's interest-bearing liabilities at the year-end 2006. All Group loans are denominated in euro. In 2006, the average interest rate of the loan portfolio was 3,7 per cent. All finance lease agreements are fixed-rate. The Group does not hedge the risk position resulting from the fair value interest rate risk as the position is small.

Credit risk

The Group's accounts receivables are dispersed to a number of customers worldwide. Thus the primary responsibility for commercial credit risks lies with the Group's geographical areas. Commercial credit risks are managed in accordance with the Group's credit policy and are reduced for example with collaterals. Credit risks are approved and monitored by the Group management team.

The credit risk related to financial instruments, i.e. counterparty risk is managed in the Group administration. Counterparty risk realises if a counterparty is unable to meet its obligations. In order to minimise counterparty risks, Teleste seeks to limit the counterparties, such as banks and other financial institutions, to those which have good credit rating. Liquid funds are invested in liquid instruments with low credit risk, e.g. in short-term bank deposits and commercial papers.

Liquidity risk

Liquidity risk is monitored through Group's cash flow forecasts. The Group seeks to reduce liquidity risk through sufficient cash reserves and credit facility arrangements as well as with balanced maturity profile of loans. Efficient cash and liquidity management also reduces liquidity risk. At the year-end 2006 the Group's cash reserves totaled EUR 6.8 million and its interest-bearing net debt EUR 8.0 million. The Group administration raises the Group's interest-bearing debt centrally. At 31 December 2006, Teleste had committed and available credit facilities as well as other agreed and undrawn loans amounting to EUR 23 million. Group's loan agreements and committed loan facilities include profitability and cash flow covenants.

The recognition and measurement principles applied to derivatives are described in the accounting principles for the consolidated financial statements. The nominal and fair values of derivatives at the balance sheet date are presented in the note Commitments and contingencies to the consolidated financial statements.

Notes

22 Fair values of financial assets and liabilities

All other financial assets and liabilities are measured at their fair values in the consolidated balance sheet except for the long-term bank loan, which is measured at amortised cost.

Derivative instruments

Teleste uses forward exchange contracts to hedge its balance sheet items against transaction risk. So far Teleste does not apply hedge accounting as defined under IAS 39 in its IFRS financial statements. Consequently the changes in the fair values of financial instruments designated as hedging instruments are fully recognised through profit and loss. The fair value changes of forward exchange contracts amounted to EUR –144 thousand in 2006 (2005: EUR 94 thousand) and they are recognised as adjustements to sales.

Available-for-sale financial assets

Available-for-sale financial assets comprise unlisted shares that are measured at cost. The fair value of these investments could not be determined reliably and the estimate fluctuates significantly or the probabilities within the range of different estimates are not reasonably determinable to be used to estimate the fair value.

Finance lease liabilities

The fair values of finance lease liabilities are based on the discounted future cash flows. The discount rate used is the market interest rates for homogeneous lease agreements.

Trade and other payables or receivables

For trade payables and other receivables than those arising from derivative instruments the notional amount equals their fair value as the discounting has no material effect considering the short maturity of these items.

Following discount rates were used for determining fair value:

	2006	2005
Finance lease liabilities	4.1%	3.9%

23 Adjustments to cash flows from operating activities

1 000 euros	2006	2005
Non-cash transactions:		
Depreciation and amortisation	2 393	1 940
Employee benefits	706	560
Deferred taxes	308	408
Total	**3 407**	**2 908**

24 Operating leases

Group as lessee

Minimum lease payments on non-cancellable operating leases are payable as follows:

1 000 euros	2006	2005
Less than one year	955	1 119
Between one and five years	1 910	660
Total	**2 865**	**1 779**

The Group leases factory and office facilities outside Finland under operating leases. The leases typically run for a period of 2–5 years, normally with an option to renew the lease after that date. According to the index clauses of the leases lease payments are increased every two years.

The Group has sublet part of its production and office property in Finland to an external company. The agreement is valid until further notice. In 2006 the lease payments in respect of this part of property amounted to EUR 106 thousand (2005: EUR 135 thousand).

25 Commitments and contingencies

1 000 euros	2006	2005
Collateral for own commitments		
Guarantees	819	340
Rental and leasing liabilities		
Rental liabilities	1 659	707
Lease liabilities	1 937	1 072
Currency derivatives		
Value of the underlying forward contracts	9 980	16 503
Market value of the forward contracts	10 124	16 597

26 Related party transactions

Identity of related parties

Teleste Group has related party relationships with its Board members and CEO.

Companies owned by the Group and parent company

	Group holding, %	Group voting, %
Parent company Teleste Oyj, Turku, Finland		
Flomatik A/S, Porsgrun, Norway	100	100
Kaavisio Oy, Turku, Finland	100	100
PromaCom AB, Stockholm, Sweden	100	100
PromaCom Intressenten AB, Stockholm, Sweden	100	100
S-Link ssp, Krakow, Poland	100	100
Suomen Turvakamera Oy, Vantaa, Finland	100	100
Suomen Yhteisantennit Oy, Turku, Finland	100	100
Teleste d.o.o., Ljutomer, Slovenia	100	100
Teleste Electronics (SIP), Shuzhou, China	100	100
Teleste France SAS, Paris, France	100	100
Teleste Försäljning AB, Malmö, Sweden	100	100
Teleste GmbH, Hannover, Germany	100	100
Teleste Kaurakatu Oy, Turku, Finland	100	100
Teleste LLC, Georgetown Texas, USA	100	100
Teleste s.r.o., Bratislava, Slovakia	100	100
Teleste Sweden AB (former Flomatik AB), Stockholm, Sweden	100	100
Teleste UK Ltd, Cambridge, UK	100	100
Teleste Video Networks AB (former S-Link AB), Täby , Sweden	100	100

The key management personnel compensations

1 000 euroa	2006	2005
CEO		
Salaries and other short-term benefits	417	391
Performance share arrangement	283	0
Share-based payments	62	62
Total	**762**	**453**

During 2006 no options were granted to the management of Teleste (2005: 40,000). The management's performance share arrangement at 2006 includes EUR 132 thousand performance share payments due to fulfilment of the performance targets in 2005. As to terms and conditions applicable to the Management Team stock options, the applied rules are similar to those of the key personnel options except for the 2004 options, which involve a share ownership plan. At 31 December 2006 management had 135,000 (2005: 140,000) options, of which 55,000 were exercisable (2005: 30,000). Management of the parent company has 0,69% of the parent company's shares equal to 120,439 shares.

Notes

1 000 euros	2006	2005
Remuneration to Board members and Managing Director:		
Chairman of the Board Tapio Hintikka	**38**	**32**
Members of the Board	**88**	**68**
Tero Laaksonen	22	17
Pertti Raatikainen	22	17
Timo Toivila	22	17
Pekka Vennamo	22	17
CEO Jukka Rinnevaara	**762**	**453**
Total	**888**	**553**

The contractual age of retirement of CEO of the parent company, Jukka Rinnevaara, is 60. As to the contract, his term of notice has been specified as six (6) months in case the President and CEO decides to withdraw, and eighteen (18) months should the contract be terminated by the company. A fixed remuneration for the Board is paid as shares of the company in accordance with the decision of the General Meeting.

No cash loans were granted to nor commitments assumed or collaterals given regarding CEO or the members of the Board of Directors in 2005 and 2006.

27 Subsequent events

The Group management is not aware of any significant events occurred after the balance sheet date, which would have had an impact on the financial statements.

Teleste Corporation Financial Statement

Statement of Income

1 000 euros	Note	2006	2005
Net sales	1	**87 217**	**66 030**
Change in inventories of finished goods		5 065	1 234
Other operating income	2	2 703	1 763
Materials, supplies and services	3	−49 509	−28 396
Wages, salaries and social expenses	4	−20 106	−19 691
Depreciation and amortisation	5	−1 735	−1 850
Other operating expenses		−17 953	−14 493
Operating profit		**5 683**	**4 597**
Financial income and expenses	6	4 481	1 515
Profit before taxes		**10 165**	**6 112**
Appropriations	7	162	44
Direct taxes	8	−1 475	−1 099
Profit for the financial period		**8 852**	**5 057**

Assets

1 000 euros	Note	2006	2005
Non-current assets			
Intangible assets	9	1 558	2 310
Property, plant and equipment	9	4 166	4 467
Investments	10	14 977	10 798
		20 701	**17 575**
Current assets			
Inventories	11	12 501	7 145
Trade and other receivables	12	19 009	16 503
Short-term investments	13	0	2 000
Cash and cash equivalents	13	4 080	3 402
		35 590	**29 050**
Total assets		**56 291**	**46 625**
Shareholders' equity			
Share capital	14	6 955	6 935
Share premium	14	1 417	1 276
Retained earnings	14	10 583	7 911
Profit for the financial period	14	8 852	5 057
		27 807	**21 180**
Appropriations	7	**1 122**	**1 284**
Provisions	15	**1 176**	**1 661**
Liabilities			
Long-term liabilities	16	0	373
Short-term liabilities	17	26 186	22 127
		26 186	**22 500**
Total equity and liabilities		**56 291**	**46 625**

Cash Flow Statement

1 000 euros	2006	2005
Cash flow from operations		
Operating profit	5 683	4 597
Adjustments to operating profit	1 250	1 674
Change in net working capital	-8 715	-5 854
Interest income	134	216
Interest expenses	-303	-294
Dividend income	4 806	1 755
Other financial items	-156	-162
Taxes paid	-1 085	-528
Cash flow from operations	**1 614**	**1 404**
Investments		
Other tangible assets	-723	-858
Investments in subsidiary shares	-3 677	-1 796
Cash flow from investments	**-4 400**	**-2 654**
Cash flow before financing	**-2 786**	**-1 250**
Financing		
Long-term liabilities	0	-8 571
Long-term assets	0	344
Short-term liabilities	4 000	1 571
Paid dividends	-2 697	-2 022
Share issue	161	0
Financing total	**1 464**	**-8 678**
Change in liquid funds	**-1 322**	**-9 928**
Liquid funds 1.1.	5 402	15 330
Liquid funds 31.12.	4 080	5 402

Accounting Principles

Accounting Principles of Teleste Corporation

Teleste Corporation is the parent company of the Teleste Group. Business ID of Teleste Corporation is 1102267-8 with registered office in Turku. The company registered address is Seponkatu 1, 20660 Littoinen.

Foreign Currency Transactions

Transactions in foreign currencies are recorded at the rates of exchange prevailing on the date of the transaction. At the end of the accounting period, unsettled foreign currency balances are translated into the accounting currency at the closing rate on the balance sheet date. Foreign exchange gains and losses on trade accounts receivable and payable are adjusted to revenues and operating expenses, respectively. Other foreign exchange gains and losses are recorded as financial income and expenses.

Currency Derivatives

The company has no other currency derivatives except for forward exchange agreements. Exchange agreements are designed to eliminate the effect of currency exposures on the company performance and financial standing.

Our corporate hedging policy is to cover all material currency risks at least six months ahead. The effect on company performance of the exchange rate agreements is recorded on their exercise day.

Valuation of Fixed Assets

The balance sheet values for fixed assets are stated as historical cost, less the accumulated depreciation and amortisation. Depreciation and amortisation is calculated on straight-line basis over the expected useful lives of the assets. Estimated useful lives for various assets are:

Intangible assets	3 years
Goodwill	10 years
Other capitalised expenditure	3 years
Buildings	25 to 33 years
Machinery	3 to 5 years
Computers	0 to 3 years

Write-downs on permanent impairment of the assets are recorded when it becomes evident that the carrying amount is not recoverable. Companies acquired or established during the financial period are included in the subsidiary shares as of date of acquisition or formation. Companies disposed of in the financial period have been included in the subsidiary shares up to the date of disposal.

Long-term investments and receivables include financial assets, which are intended to be held for over one year.

Leased Assets

Purchases made under operating leases and capital leases are entered into income statement as renting expenses.

Inventories

Inventories are stated at the lower of cost or net realisable value. Acquisition cost is determined using the first-in-first-out (FIFO) method. In addition to variable expenditure, value of inventory includes their share of the fixed expenditure under purchases and manufacturing.

Cash

Cash and cash equivalents include cash in hand and in bank. Short-term investments include other funds equivalent to cash, such as commercial papers.

Net Sales

Net sales include revenue from services rendered and goods sold, adjusted for discounts granted, sales-related taxes and effects of the translation differences. Revenue is recognised when services are rendered, or when the goods are delivered to the customer.

Percentage of completion method: sales and anticipated profits under significant long-term engineering and construction contracts are recorded on a percentage-of-completion basis, using units of delivery (based on predetermined milestones) or the cost-to-cost method of accounting as the measurement basis. Estimated contract profits are recorded in earnings in proportion to recorded sales. In the cost-to-cost method, sales and profits are recorded after considering the ratio of accumulated costs to estimated total costs to complete each contract. In the event that the company can be held as the main contractor of a long-term delivery contract, various product expenses, including raw materials and labour costs, will be accounted for in the calculation of the completion percentage. Possible changes in the anticipated total expenses or loss related to a long-term delivery contract are expensed as incurred.

Research and Development

R&D expenses are recorded as revenue expenditure.

Pension Arrangements

The statutory pension liabilities of Finnish subsidiaries in the company are funded through pension insurance.

Income Taxes

Income tax includes tax on profit for the current financial period and the accrual adjustment for the preceding financial period.

Treasury shares

Treasury shares acquired by the Group are not included in balance. As to this, final accounts for the year of comparison have been adjusted by eliminating the value of treasury shares from the company fixed assets and the equity. This adjustment is based on an amendment of the Finnish accounting legislation.

Notes

1 000 euros	2006	2005

1 Net sales

Net sales by segments

Broadband Cable Networks	73 934	52 472
Video Networks	13 283	13 558
Total	**87 217**	**66 030**

Net sales by market area

Finland	7 848	8 804
Scandinavia	14 136	12 957
Other Europe	58 733	37 549
Others	6 500	6 720
Total	**87 217**	**66 030**

2 Other operating income

R&D subvention and others	2 703	1 763
Total	**2 703**	**1 763**

3 Materials and services

Purchases	47 837	26 160
Change in inventories	-291	-1 041
	47 546	**25 119**
Purchases services	1 963	3 277
Total	**49 509**	**28 396**

4 Personnel expenses

Wages and salaries	16 578	15 969
Pension costs	2 401	2 626
Other personnel costs	1 127	1 097
Total	**20 106**	**19 691**
Remuneration to Board members and Managing Director	847	492

The aggregate compensation paid to the Managing Director included share bonus in the amount of EUR 132,000, which was based on the result targets of 2005.

Cash loans, securities or contingent liabilities were not granted to the President or to the members of the Board of Directors.

Year-end personnel	435	433
Average personnel	436	428

Personnel by function at the year-end

Research and Development	119	109
Production and Materials Management	252	260
Sales and marketing	39	39
Finance and IT	25	25
Total	**435**	**433**

1 000 euros	2006	2005
5 Depreciation according to plan		
Other capitalized expenditure	305	161
Buildings	297	297
Machinery and equipment	381	640
Goodwill on consolidation	752	752
Total	**1 735**	**1 850**
Change in accumulated depreciation difference		
Buildings	170	162
Other capitalized expenses	-8	-118
Total	**162**	**44**
6 Financial income and expenses		
Interest income	92	178
Interest incom from Group companies	42	38
Interest expenses	-303	-294
Currency differences	-171	-6
Other financial income and expenses	15	-156
Dividend income from Group companies	4 800	1 752
Dividend income	6	3
Total	**4 481**	**1 515**
7 Appropriations and deferred tax assets and liabilities in the parent company		
Accumulated depreciation in excess of plan	1 122	1 284
8 Income taxes		
Direct taxes	1 490	1 160
Taxes from previous years	-15	-61
Total	**1 475**	**1 099**

9 Tangible and intangible assets

	Intangible assets	Tangible assets				
	Intangible rights	Land	Buildings	Machinery	Other capitalized expenditure	**Total**
Acquisition cost 1.1.	**7 579**	108	4 983	7 752	2 636	**15 479**
Increases	0	0	58	450	255	**763**
Decreases	0	0	0	-22	-58	**-80**
Acquisition cost 31.12.	**7 579**	108	5 041	8 180	2 833	**16 162**
Accumulated depreciation 1.1.	**5 268**	0	1 949	7 141	1 923	**11 013**
Depreciation	752	0	297	381	305	**983**
Accumulated depreciation 31.12.	**6 020**	0	2 246	7 522	2 228	**11 996**
Book value 31.12.2006	**1 558**	108	2 795	658	605	**4 166**
Book value of machinery and equipment 31.12.2006				492		
Book value of machinery and equipment 31.12.2005				536		

Notes

10 Investments

Parent company

	Shares in group companies	Shares others	**Total**
Acquisition cost 1.1.	10 367	1 116	11 483
Increase	4 179	0	4 179
Acquisition cost 31.12.	**14 546**	**1 116**	**15 662**
Accumulated depreciation 1.1.	-685	0	-685
Accumulated depreciation 31.12.	**-685**	**0**	**-685**
Book value 31.12.2006	**13 861**	**1 116**	**14 977**

1 000 euros	2006	2005
11 Inventories		
Raw materials and consumables	3 090	2 799
Work in progress	5 363	2 153
Finished goods	4 048	2 193
Total	**12 501**	**7 145**
12 Current assets		
Accounts receivables	14 540	11 795
Accounts receivables from Group companies	1 173	2 325
Other receivables from Group companies	685	822
Accrued income	2 611	1 560
Total	**19 009**	**16 503**
13 Liquid funds		
Short-term investments	0	2 000
Cash and cash equivalents	4 080	3 402
14 Changes in shareholders' equity		
Share capital 1.1.	6 935	6 935
Share issue	20	0
Share capital 31.12.	6 955	6 935
Share premium fund 1.1.	1 276	1 277
Share issues	141	0
Use of own shares	0	-1
Share premium fund 31.12.	1 417	1 276
Retained earnings 1.1.	12 968	9 898
Dividends	-2 697	-2 022
Transfer from treasury shares	311	34
Retained earnings 31.12.	10 583	7 911
Profit for the financial period	8 852	5 057
Accumulated profit 31.12.	19 435	12 968
Total	**27 807**	**21 180**

Company's registered share capital consists of one serie and is divided into 17,389,302 shares at 1 vote each.

	2006	2005
15 Obligatory provisions		
Provision for guarantees	1 069	1 096
Provisions for pension commitments	0	160
Provisions for restructuring	107	107
Others	0	298
Total	**1 176**	**1 661**

1 000 euros	2006	2005

16 Long-term liabilities

Other interestbearing liabilities	0	373
Total	**0**	**373**

17 Short-term liabilities

Bank loans	7 000	3 000
Advance payments received	95	112
Accounts payables	6 914	4 847
Accounts payables from Group companies	2 418	1 228
Other current liabilities	2 779	1 972
Other current liabilities from Group companies	1 691	5 961
Accrued liabilities	5 289	5 007
Total	**26 186**	**22 127**

18 Contingent liabilities and pledged assets

Leasing liabilities		
For next year	476	614
For later years	921	616
Total	**1 397**	**1 230**
Rental liabilities	257	365
Liabilities on own behalf		
Bank guarantees	819	320

19 Currency derivates

Value of underlying forward contracts	9 980	16 503
Market value of forward contracts	10 124	16 597

Forward contracts are used only for hedging currency exchange risks.

20 Companies owned by the Group and parent company

	Group's share, %	Parent company's share, %
Flomatik A/S, Porsgrun, Norway	100	100
Kaavisio Oy, Turku, Finland	100	100
PromaCom AB, Stockholm, Sweden	100	100
PromaCom Intressenten AB, Stockholm, Sweden	100	0
S-Link ssp, Krakow, Poland	100	100
Suomen Turvakamera Oy, Vantaa, Finland	100	100
Suomen Yhteisantennit Oy, Turku, Finland	100	100
Teleste d.o.o., Ljutomer, Slovenia	100	0
Teleste Electronics (SIP), Shuzhou, China	100	100
Teleste France SAS, Paris, France	100	100
Teleste Försäljning AB, Malmö, Sweden	100	100
Teleste GmbH, Hannover, Germany	100	100
Teleste Kaurakatu Oy, Turku, Finland	100	100
Teleste LLC, Georgetown Texas, USA	100	100
Teleste s.r.o., Bratislava, Slovakia	100	100
Teleste Sweden AB (former Flomatik AB), Stockholm, Sweden	100	0
Teleste UK Ltd, Cambridge, UK	100	100
Teleste Video Networks AB (former S-Link AB), Täby , Sweden	100	100

Notes

21 Own shares

	Number of shares	Nominal value, euros	Percentage of share capital and votes
Teleste Oyj owns own shares 31.12.2006	455 000	182 000	2.62

22 Major Shareholders 31.12.2006

	Number of shares	Percentage of share capital and votes
Sampo Life Insurance Company Ltd.	1 624 200	9.34
Ilmarinen Mutual Pension Insurance Company	1 284 931	7.39
Kaleva Mutual Insurance Company	785 900	4.52
Op-Suomi Pienyhtiöt	588 900	3.39
FIM Fenno Mutual Fund	572 639	3.29
Aktia Capital Mutual Fund	521 450	3.00
Varma Mutual Insurance Company	508 150	2.92
State Pension Fund	500 000	2.88
Teleste Corporation	455 000	2.62
Fondita Nordic Small Cap Fund	360 000	2.07
Nordea Nordic Small Cap Mutual Fund	305 350	1.76
Odin Forvaltnings As	284 050	1.63
Mutual Insurance Company Pension-Fennia	220 000	1.27
FIM Forte Mutual Fund	203 350	1.17
Veritas Pension Insurance Company	175 000	1.01
Evli Bank Plc.	152 718	0.88
Aktia Secura Mutual Fund	146 150	0.84
Sumato Oy	122 610	0.71
Svenska Handelsbanken Ab (publ.), filial	114 000	0.66
Svenska litteratursällskapet i Finland r.f.	111 000	0.64
Renkkeli Oy	100 000	0.58
Royal Skandia Life Assurance Ltd Eib 127	82 610	0.48
Fondita 2000+ Fund	80 000	0.46
Veikko Laine Oy	77 100	0.44
Fondita Nordic Micro Cap Fund	75 000	0.43
Foreign and nominee register accounts	3 570 218	20.53
Others	4 368 976	25.12
Total	**17 389 302**	**100.00**

Shareholder's by number of shares 31.12.2006

Shareholder's by segments	Number of shares	Percentage of share
Corporations	1 624 417	9.34
Financial and insurance institutions	5 128 736	29.49
Public organizations	2 713 131	15.60
Non-profit organizations	1 020 430	5.87
Households	3 332 370	19.16
Foreign and nominee register accounts	3 570 218	20.53
Total	**17 389 302**	**100.00**

Shares	Number of shareholders	Percentage of shares	Number of shares	Percentage of shares
1–100	1 357	24.23	98 493	0.57
101–1 000	3 426	61.17	1 389 733	7.99
1 001–10 000	742	13.25	2 153 301	12.38
10 001–100 000	56	1.00	1 616 307	9.29
100 001–	20	0.36	9 035 398	51.96
Total	5 601	100.00	14 293 232	82.20
Nominee register accounts			3 096 070	17.80
Total			**17 389 302**	**100.00**

Management interest

	Number of shares	Percentage of shares	Percentage of votes
CEO and Board Members	109 329	0.63	0.63

Option programs

Number of shares entitled to subscribe with options

	Number of shares	Percentage of shares and votes
CEO	135 000	0.7
Other option holders	834 550	4.5
2002 program warrants hold by the group	44 900	0.2
2004 program warrants hold by the group	86 000	0.5
Total	**1 100 450**	**6.0**

Proposal for the Distribution of Earnings

Board of Directors' Proposal for the Distribution of Earnings

As to the Annual General Meeting scheduled for 3 April 2007, the Board proposes that a dividend of EUR 0.20 (EUR 0.16) per share be paid for the outstanding shares for the year 2006.

Signatories to the Annual Report and Financial Statements

Helsinki 30 January 2007

TELESTE CORPORATION
Board of Directors

Tapio Hintikka

Tero Laaksonen

Pertti Raatikainen

Timo Toivila

Pekka Vennamo

Jukka Rinnevaara
President and CEO

The Auditors Note

The above financial statements and the report of Board of Directors have been prepared in accordance with generally accepted accounting principles in Finland. Our auditors report have been issued today.

Helsinki 30 January 2007

KPMG OY AB

Sixten Nyman
KHT

Auditors' Report

To the shareholders of Teleste Oyj

We have audited the accounting records, the report of the Board of Directors, the financial statements and the administration of Teleste Oyj for the period 1.1.–31.12.2006. The Board of Directors and the Managing Director have prepared the consolidated financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, containing the consolidated balance sheet, income statement, cash flow statement, statement on the changes in equity and notes to the financial statements, as well as the report of the Board of Directors and the parent company's financial statements, prepared in accordance with prevailing regulations in Finland, containing the parent company's balance sheet, income statement, cash flow statement and notes to the financial statements. Based on our audit, we express an opinion on the consolidated financial statements, as well as on the report of the Board of Directors, the parent company's financial statements and the administration.

We conducted our audit in accordance with Finnish Standards on Auditing. Those standards require that we perform the audit to obtain reasonable assurance about whether the report of the Board of Directors and the financial statements are free of material misstatement.

An audit includes examining on a test basis evidence supporting the amounts and disclosures in the report and in the financial statements, assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation. The purpose of our audit of the administration is to examine whether the members of the Board of Directors and the Managing Director of the parent company have complied with the rules of the Companies Act.

Consolidated financial statements

In our opinion the consolidated financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a true and fair view, as defined in those standards and in the Finnish Accounting Act, of the consolidated results of operations as well as of the financial position.

Parent company's financial statements, report of the Board of Directors and administration

In our opinion the parent company's financial statements have been prepared in accordance with the Finnish Accounting Act and other applicable Finnish rules and regulations. The parent company's financial statements give a true and fair view of the parent company's result of operations and of the financial position.

In our opinion the report of the Board of Directors has been prepared in accordance with the Finnish Accounting Act and other applicable Finnish rules and regulations. The report of the Board of Directors is consistent with the consolidated financial statements and the parent company's financial statements and gives a true and fair view, as defined in the Finnish Accounting Act, of the result of operations and of the financial position.

The consolidated financial statements and the parent company's financial statements can be adopted and the members of the Board of Directors and the Managing Director of the parent company can be discharged from liability for the period audited by us. The proposal by the Board of Directors regarding the disposal of distributable funds is in compliance with the Companies Act.

Helsinki January 30, 2007

KPMG OY AB

Sixten Nyman
Authorised Public Accountant

Financial Indicators 2002–2006

	FAS 2002	FAS 2003	IFRS 2004	IFRS 2005	IFRS 2006
Profit and loss account, balance sheet					
Net sales, Meur	66.8	54.2	66.0	82.6	101.8
Change, %	-34.9	-18.8	21.8	25.1	23.2
Sales outside Finland, %	82.6	81.9	85.1	89.3	90.6
Operating profit, Meur	-4.3	1.8	5.6	8.6	9.8
% of net sales	-6.4	3.3	8.5	10.4	9.6
Profit after financial items, Meur	-5.1	1.5	5.4	8.3	9.3
% of net sales	-7.6	2.8	8.2	10.1	9.1
Profit before taxes, Meur	-8.2	1.5	5.4	8.3	9.3
% of net sales	-12.3	2.8	8.2	10.1	9.1
Profit for the financial period, Meur	-7.1	1.7	3.9	6.0	6.9
% of net sales	-10.6	3.1	5.9	7.2	6.8
R&D expenditure, Meur	6.6	5.8	6.9	8.6	9.8
% of net sales	9.9	10.7	10.4	10.5	9.7
Gross investments, Meur	1.3	3.4	5.4	4.1	6.2
% of net sales	1.9	6.3	8.2	4.9	6.1
Interest bearing liabilities, Meur	15.0	10.0	10.8	3.9	8.0
Shareholder's equity, Meur	24.6	27.0	27.7	32.4	37.7
Total assets, Meur	52.0	48.1	54.4	54.8	68.2
Personnel and orders					
Average personnel	506	452	492	546	608
Order backlog at year end, Meur	9.7	6.6	20.7	22.7	28.1
Orders received, Meur	59.5	52.2	80.5	85.4	107.2
Key metrics					
Return on equity, %	-14.2	7.1	15.1	19.8	19.7
Return on capital employed, %	-7.6	5.3	16.1	23.7	24.3
Equity ratio, %	44.8	49.3	51.1	59.1	55.3
Gearing, %	5.8	-17.7	-22.9	-14.3	3.2
Earnings per share, euro	-0.25	0.10	0.23	0.35	0.41
Earnings per share fully diluted, euro	-0.25	n/a	0.22	0.33	0.38
Shareholders equity per share, euro	1.41	1.41	1.65	1.92	2.22
Teleste share					
Highest price, euro	14.00	6.49	7.06	8.35	12.75
Lowest price, euro	2.21	2.40	5.14	5.85	6.46
Closing price, euro	2.47	5.41	6.02	7.45	11.63
Average price, euro	5.52	4.41	6.03	6.97	9.83
Price per earnings	-10.0	53.7	25.8	21.0	28.6
Market capitalization, Meur	40.5	90.3	101.4	129.2	202.2
Stock turnover, Meur	82.7	43.7	74.2	75.3	138.9
Turnover, number in millions	15.0	9.9	12.3	10.8	14.2
Turnover, % of share capital	88.0	57.2	70.9	62.3	81.4
Average number of shares	16 974 287	17 094 910	17 334 235	17 339 752	17 363 102
Number of shares at the year-end	17 035 400	17 304 248	17 339 752	17 339 752	17 389 302
Number of shares subscribed, not registered 31.12.		23 304	0	0	0
Average number of shares, diluted w/o own shares	18 567 329	18 715 000	17 918 580	18 001 437	18 022 505
Number of shares at the year-end, diluted w/o own shares	18 715 000	18 715 000	17 999 752	18 004 752	18 034 752
Paid dividend, Meur	1.3	1.3	2.0	2.7	3.4
Dividend per share, euro	0.08	0.08	0.12	0.16	*0.20
Dividend per net result, %	-32.5	79.4	52.2	45.7	49.1
Effective dividend yield, %	3.2	1.5	2.0	2.1	1.7

* The Board's proposal to the AGM

Glossary

Calculation of Key Figures

Return on equity:

$$\frac{\text{Profit/loss for the financial period}}{\text{Shareholders' equity (average)}} * 100$$

Return on capital employed:

$$\frac{\text{Profit/loss for the period after financial items + financing charges}}{\text{Total assets – non-interest-bearing liabilities (average)}} * 100$$

Equity ratio:

$$\frac{\text{Shareholders' equity}}{\text{Total assets – advances received}} * 100$$

Gearing:

$$\frac{\text{Interest bearing liabilities – cash in hand and in bank – interest bearing assets}}{\text{Shareholders' equity}} * 100$$

Earnings per share:

$$\frac{\text{Profit/loss for the financial period} \pm \text{minority interest}}{\text{Average number of shares – own shares}}$$

Earnings per share, diluted:

$$\frac{\text{Profit/loss for the financial period} \pm \text{minority interest}}{\text{Average number of shares – own shares + number of options at the year-end}}$$

Equity per share:

$$\frac{\text{Shareholders' equity}}{\text{Number of shares – number of own shares at year-end}}$$

Price per earnings (P/E):

$$\frac{\text{Share price at year-end}}{\text{Earnings per share}}$$

Effective dividend yield:

$$\frac{\text{Dividend per share}}{\text{Share price at year-end}} * 100$$

AAL	ATM Adaptation Layer
ADSL	Asymmetric Digital Subscriber Line
ANGA	German Association of Private CATV Operators
ANSI	American National Standards Institute
ARPU	Average Revenue Per User
ASP	Advanced Simple Profile
ATM	Asynchronous Transfer Mode
AVC	Advanced Video Coding
BAT	Broadband Access Technology
CA	Conditional Access
CAPEX	Capital Expenditure
CATV	Cable Television
CCIR	Consultative Committee International Radio (see ITU-R)
CCITT	Consultative Committee International Telephone and Telegraph (see ITU-T)
CCM	City Center Monitoring
CCTV	Closed Circuit Television
CD	Compact Disk
CDM	Cable Data Modem
CDMA	Code Division Multiple Access
CD-ROM	Compact Disk Read-Only-Memory
CE	Consumer Electronics
CEC	European Committee for Standardisation
CENELEC	European Electrotechnical Standards Committee
CI	Common Interface (standard)
CIF	Common Image Format
CLI	Command Line (user) Interface
CMTS	Cable Modem Termination System
CPE	Customer Premises Equipment
CPU	Central Processing Unit
CVBS	Composite Video Baseband Signal
CWDM	Coarse Wavelength Division Multiplexing
DCN	Data Communications Network
DES	Data Encryption Standard (U.S.)
DOCSIS	Data Over Cable System Interface Standard
DTH	Direct To Home (satellite broadcasting)
DVB	Digital Video Broadcasting
DVB-C	DVB transmission standard for cable networks
DVB-S	DVB transmission standard for satellite networks
DVB-S2	DVB transmission standard for satellite networks – extended version
DVB-T	DVB transmission standard for terrestrial networks
DVD	Digital Versatile Disk
DVR	Digital Video Recorder
DWDM	Dense Wavelength Division Multiplexing
ECCA	European Cable Communication Association
EIA	Electronic Industries Association
EMC	Electromagnetic Compatibility
EMS	Element Management System
EPG	Electronic Program Guide
ESW	Embedded Software
ETSI	European Telecommunications Standards Institute
EttH	Ethernet to the Home
FE	Fast Ethernet
FCC	Federal Communications Commission
FTP	File Transfer Protocol
FttB	Fibre To The Building
FttH	Fibre To The Home
FttLA	Fibre To The Last Amplifier
FttP	Fibre To The Premises
GE	Gigabit Ethernet
GUI	Graphical User Interface
HD(TV)	High Definition Television
HE	Head End
HES	High End Security
HF	High Frequency
HFC	Hybrid Fiber Coax (network)
HMTS	Hybrid Management Termination System
HTML	Hyper Text Markup Language
HTTP	Hypertext Transfer Protocol
HW	Hardware
IANA	Internet Assigned Numbers Authority

Glossary

IEEE	Institute of Electrical and Electronic Engineers
IETF	Internet Engineering Task Force
IF	Intermediate Frequency
IFSEC	International Fire and Security Exhibition and Conference
IGMP	Internet Group Management Protocol (TCP/IP family)
IP	Internet Protocol
IPC	Industrial Personal Computer
IPR	Intellectual Property Rights
ISO	International Standards Organization
ISP	Internet Service Provider
ITS	Intelligent Transport (Traffic) System
ITU-R	ITU Radio communications Sector
ITU-T	ITU Telecommunications Sector
JPEG	Joint Photographics Expert Group
LAN	Local Area Network
LCD	Liquid Crystal Display
LMDS	Local Multi-point Distribution Service
MAC	Media Access Control
MDI	Medium Dependent Interface
MDIX	Medium Dependent Interface Crossover
MHEG	Multimedia and Hypermedia Experts Group
MIB	Management Information Base
MJPEG	Moving JPEG
MMDS	Multichannel Multipoint Distribution Service
MMF	Multimode Fibre
MOU	Memorandum of Understanding
MPEG	Motion Picture Experts Group
MPLS	Multi Protocol Label Switching
MSO	Multiple Systems Operator
NAT	Network Address Translation
NCTA	National Cable Television Association
NE	Network Element
NEMA	National Electrical Manufacturers Association
NMS	Network Management System
NTSC	National Television System Committee (TV standard)
NVOD	Near Video On Demand
NVR	Network Video Recorder
OA&M	Operations, Administration, and Maintenance
OEM	Original Equipment Manufacturer, After Market Manufacturers
OFDM	Orthogonal Frequency Division Multiplexing
OPEX	Operations Expenditure
OSI	Open System Interconnection
OSS	Operations Support System
PA	Public Address
PAL	Phase Alternating Line (TV standard)
PC	Personal Computer
PCMCIA	Personal Computer Memory Card International Association
PHY	Physical Layer Working Group of ATM Forum
PLC	Programmable Logic Controller
POTS	Plain Old Telephone Service
PSTN	Public Switched Telephone Network
PTZ	Pan Tilt Zoom
PVC	Permanent Virtual Channel
QAM	Quadrature Amplitude Modulation
QoS	Quality of Service
QPSK	Quadrature Phase Shift Keying
RAID	Redundant Array of Inexpensive (Independent) Disks
RF	Radio Frequency
RFC	Request for Comments
RFI	Radio Frequency Interference, Request For Information
RFP	Request For Proposal
RFQ	Request For Quotation
RSA	Public Key Cryptosystem invented by Rivest, Shamir and Adleman
RSTP	Rapid Spanning Tree Protocol
RTP	Real-Time Protocol (TCP/IP family)
RX	Receiver
SAP	Session Announcement Protocol
SCTE	Society of Cable Television Engineers
SDH	Synchronous Data Hierarchy
SD(TV)	Standard Definition Television
SECAM	Systeme Electronique Couleur Avec Memoire (TV standard)
SFN	Single Frequency Network
SIP	Session Initiation Protocol (see VoIP)
SLA	Service Level Agreement
SMF	Single Mode Fibre
SNMP	Simple Network Management Protocol (TCP/IP family)
SNR	Signal to Noise Ratio
SONET	Synchronous Optical Network
SQL	Structured Query Language
SSH	Secure Shell
SSL	Secure Socket Layer
STB	Set-Top Box
STM	Synchronous Transmission Mode
STP	Spanning Tree Protocol
SVC	Switched Virtual Channel
TCP/IP	Transmission Control Protocol/Internet Protocol
TDM	Time Division Multiplexing
TFTP	Trivial File Transfer Protocol
TMN	Telecommunications Management Network
TX	Transmitter
UDP	User Datagram Protocol (TCP/IP family)
UHF	Ultra High Frequency
UL	Underwriters Laboratory Inc.
UTP	Unshielded Twisted Pair
VCI	Virtual Channel Identifier
VF	Virtual Fibre
VHF	Very High Frequency
VIA	Video Image Analysis
VLAN	Virtual Local Area Network
VOD	Video on Demand
VoIP	Voice Over Internet Protocol
VPI	Virtual Path Identifier
VPN	Virtual Private Network
WAN	Wide Area Network
WDM	Wavelength Division Multiplexing
WLAN	Wireless Local Area Network
XML	eXtended Markup Language

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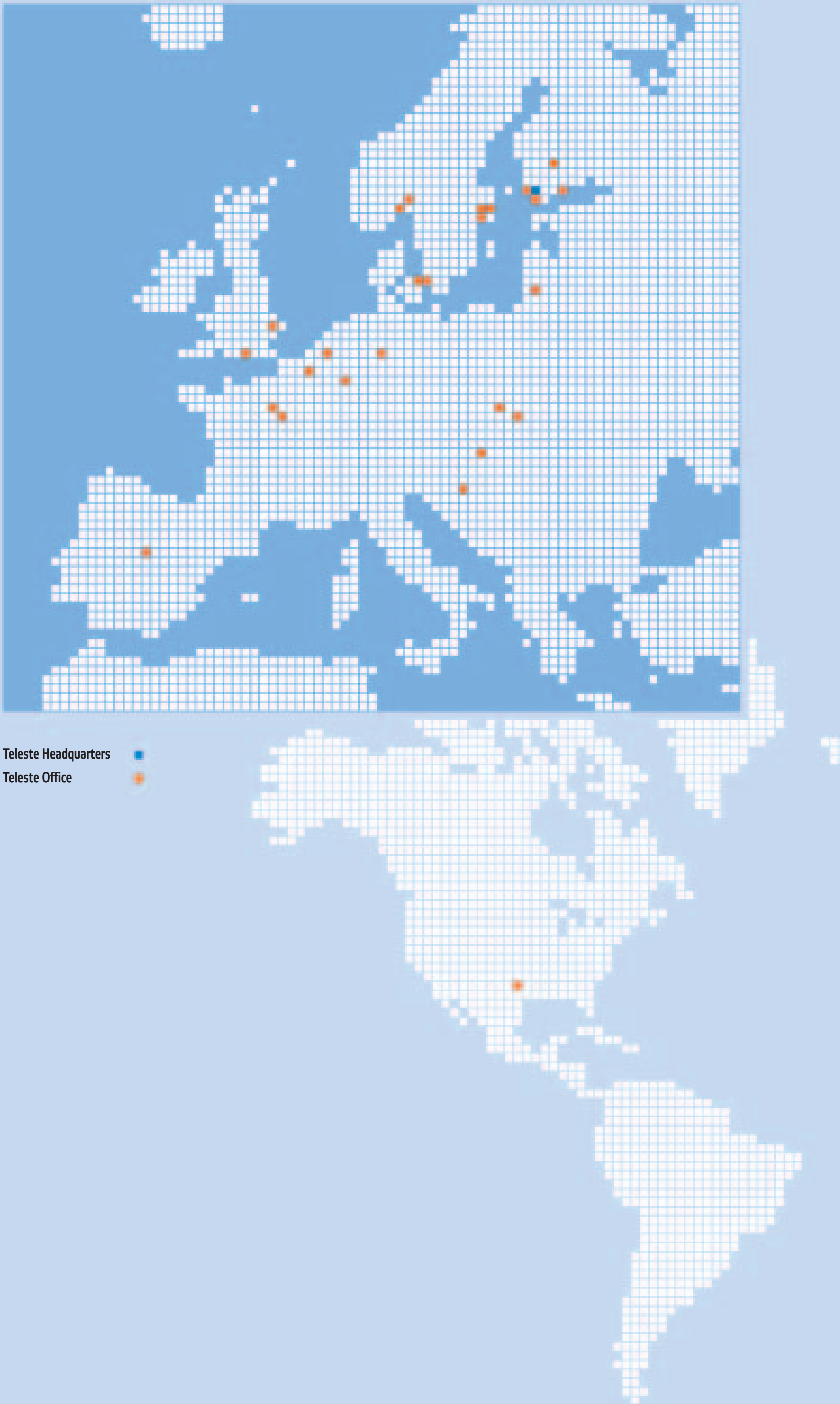

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