

TUBACEX, S.A. AND SUBSIDIARY COMPANIES 2006 DIRECTORS' REPORT (Translation from the original in Spanish)

The worldwide economic boom which commenced in 2003 continued apace in 2006, with growth of around 5%, and was characterised in macroeconomic terms by upbeat performance in practically all areas and the increasing presence of emerging economies (in particular China and India).

The healthy situation of the worldwide economy has had a positive effect on the Group's business, with heightened end demand and growing orders for both tubes and stainless steel products (round and square products). Nevertheless, a number of highly relevant issues directly affect European export companies and continue to threaten the competitiveness of the iron and steel sector in general, such as the continuous rise in raw material prices and the depreciation of the US Dollar against the Euro. Of particular concern is the substantial jump in the price of oil. Although this acts as a catalyst for investment programmes in sectors which are end users of our products, it also creates considerable uncertainty over the sustainability of worldwide growth.

As regards the financial markets, the American Federal Reserve continued to raise interest rates in the first half of the year, which reached 5.25% in June and remained unchanged for the rest of the year due to the subsequent gradual downturn in the economy. The European Central Bank gradually increased interest rates in the second half of the year on account of the upsurge in activity to 3.5% at year end.

As in prior years, the currency markets had a serious negative effect on European export companies during 2005 with a Euro that has held its strength against the US Dollar (US\$1.26 on average in 2006) and has gained more than 7% against the Yen (11.4% in the last three years). This trend has been, and continues to be, particularly harmful to the competitiveness of European companies, as it directly jeopardises exports to the USA and indirectly favours emerging economies which have much lower labour costs and currencies that have not lost so much ground to the US Dollar.

For the fourth year running, the stock markets performed well and closed the year with important gains which, in the case of the Spanish stock market, stood at 32% in the IBEX35 and 35% in the IGBM. The gains recorded by the IBEX MEDIUM CAP, which comprises the twenty securities with the highest adjusted free-float capitalisation, excluding the thirty-five securities in the IBEX 35, and which included Tubacex in 2006, amounted to 42.1% during the year.

Trends in the price of basic raw materials used in our business (nickel and stainless steel scrap) continue to be of note, with an average price increase of 64.5% in 2006 based on average nickel quotations on the London Metal Exchange (LME). The rise in the price of nickel, which has risen fourfold in the last five years, means that this metal is now the main component of "raw and other materials" in the Group's income statement, and management of this material has taken on a new importance, particularly in light of the growth in the order book. A positive occurrence in 2006 has been the 25% reduction in the price of molybdenum, which is a reversal of recent years' trends. Various factors such as the strength of worldwide demand and the increasingly strong Chinese presence in global stainless steel production are behind this increase in prices. However, it should not be forgotten that these markets have been and are exposed to international hedge funds – at present extremely active in the main raw materials markets – and the value of the US Dollar.

The higher prices of certain raw materials in 2006, principally nickel, have been passed on to the end customer due to the healthy levels of demand, particularly in the projects market.

Oil prices continued to rise in 2006 as a result of factors such as the volatile situation in the Middle East, the weakness of the US Dollar, supply restrictions imposed by OPEC, heightened tensions in oil-producing countries and, above all, increased demand particularly in China and India. Nevertheless, the International Energy Agency (IEA) has issued repeated warnings of structural problems in matching supply to forecast demand and the need for significant investments at all stages of the production and processing of oil and by-products. In this context, the price of the Brent barrel rose to over US\$62 at the end of 2006. OPEC estimates that oil prices will rise at an average annual rate of 1.4% until 2030 and that oil will account for 40% of energy requirements for this period.

In terms of sectors, key end users of our products such as producers of electrical energy, oil and gas and the chemical and petrochemical industries have maintained high levels of activity throughout the year. 2006 has therefore been characterised by high demand from these sectors, which has translated into greater margins due to the enormous added value of the products, and by the gradual improvement in the distribution market, particularly in Europe and NAFTA countries, resulting in the largest order book ever. These favourable market trends in the European distribution market have enabled prices to rise, thus improving the Group's current and future performance.

The Tubacex Group has therefore continued to implement its Competitiveness Plan and develop its Strategic Plan 2010 in order to fulfil its strategic objectives, the most distinguishing features of which are as follows:

- Creation of value and shareholder remuneration.
- Maximisation of structural profitability in all business units, with special emphasis on production units of seamless stainless steel tubes.
- Competitiveness in the manufacturing and marketing of our products.
- Clear commitment to added value in our products and leadership in customer service.
- Integration and development of synergies among the different units from a strategic group perspective, and on the basis of planning and a realistic adaptation of people, structures, processes and investment plans. Adaptation of the Group's management structure.
- Financial soundness and generation of cash flows as a guarantee of consistent shareholder remuneration over time and sufficient capacity to undertake the required investments to ensure the future competitiveness and profitability of the Group.
- Continuous improvement in corporate governance policies, including the most advanced principles based on international standards.
- Establishment of the principle of corporate social accountability as one of the Group's main values with a focus on total quality management, environmental policies and labour risk prevention in all the Group's units.

1. PERFORMANCE OF THE GROUP'S BUSINESS IN 2006

In order to carry out a detailed study of the main business variables during 2006, the variations in the main entries of the consolidated income statement will be analysed together with the most significant events deriving from the Group's financial, commercial and industrial activity.

- 1.1 Analytical analysis of the Group's income statement
- 1.2 Financial activity
- 1.3 Commercial activity
- 1.4 Industrial activity
- 1.5 Competitiveness Plan
- 1.6 Strategic Plan

1.1. Analytical analysis of the Group's income statement

For comparative purposes, the main captions of the consolidated income statements for 2006, 2005 and 2004 are as follows:

	(in millions of Euros)					
	2006	%	2005	%	2004	%
Revenue	539.07	100.00	430.50	100.00	347.45	100.00
Other income	1.11	0.21	4.13	0.96	1.63	0.47
Variation in stocks	6.95	1.29	28.89	6.71	17.72	5.10
Total operating income	547.13	101.50	463.52	107.67	366.80	105.57
Purchases and materials consumed	-321.65	-59.67	-264.60	-61.46	-198.74	-57.20
Personnel expenses	-85.36	-15.83	-82.55	-19.18	-70.73	-20.36
External and operating expenses	-76.09	-14.12	-63.72	-14.80	-57.19	-16.46
Gross operating profit	64.03	11.88	52.65	12.23	40.14	11.55
Amortisation, depreciation and impairment	-16.74	-3.11	-15.64	-3.63	-15.08	-4.34
Net operating profit	47.29	8.77	37.01	8.60	25.06	7.21
Financial income	6.69	1.24	6.61	1.54	3.71	1.07
Financial expenses	-12.76	-2.37	-10.37	-2.41	-8.79	-2.53
Profit on ordinary activities	41.22	7.65	33.25	7.72	19.98	5.75
Net extraordinary income/(expense)	-	-	-	-	-	-
Consolidated profit before income tax	41.22	7.65	33.25	7.72	19.98	5.75
Income tax	-10.27	-1.91	-7.83	-1.82	-4.60	-1.32
Net profit attributed to the parent company	30.95	5.74	25.42	5.90	15.38	4.43

The most significant trends in the consolidated income statement are as follows:

- Sales are up 25.2% on the prior year due to both the higher volume of tons sold and the price effect. The prices of our products rose significantly this year, which is improving and will continue to improve the Group's performance. However, also important is the fact that price increases in the main raw materials were able to be passed onto customers due to healthy demand. Evolution by geographical area is shown in section 1.3.

- As in prior years, the continued decline in value of the US Dollar against the Euro is a vital factor which has negatively affected sales. The drop in value of group sales made in US Dollars has been mitigated by the increase in prices in local currency, which has largely offset this effect.

- The cost of materials consumed, which amounted to 59.7% as a percentage of net sales, continues to remain high due to the price of raw materials – the cost of nickel has risen on average 64% in 2006 to historically high levels – and the growth in group activity, principally steel production.

- The above-mentioned factors, coupled with a competitiveness and cost-cutting programme and improved end demand, are the determining factors behind the rise in the Group's net profit for 2006.
- Personnel expenses have risen by 3.4%. In prior years provision was made to cover expected future liabilities deriving from an agreement to implement relief contracts during the periods 2003-2005 and 2006-2008 in Tubacex S.A., Tubacex Tubos Inoxidables, S.A. and Acería de Álava, S.A. These agreements are allowing the Group to improve competitiveness and profitability, streamline its workforce, enhance production structures and renew, train and improve the skills of its personnel.
- Other operating expenses increased by 19.4% on account of the following: an amount in excess of one million Euros was awarded as a shareholders' attendance allowance for the annual general meeting held on 25 May 2006 in order to attain the quorum necessary to lift the protection on the bye-laws; the current increase in group activity and the rise in energy bills (electricity and gas) has considerably affected this caption of the income statement; the Tubacex Group is developing specific projects aimed at curtailing the main expense items which have already shown results this year and will continue to do so in the future.
- The Group's financial situation is still sound - see point 1.2. of this report - due to the constant decline in long-term debt in recent years to around Euros 6.7 million at the end of 2006. However, the higher current asset financing requirements due to the rise in raw material prices and group production levels have resulted in more short-term credit facilities, thus leading to an increase in financial expenses of Euros 2.3 million in 2006.
- Income taxes remain in line with 2005 as tax credits were capitalised in prior years in accordance with prevailing legislation.

1.2 Financial activity

The Group generated its highest ever level of funds of Euros 47.69 million in 2006, an increase of 16.1% compared to the Euros 41.06 million generated in the prior year, which was also a record.

The Group's shareholders' equity amounted to Euros 225.2 million at the end of 2006, representing 41.7% of total liabilities (45.1% in 2005). Net debt as a percentage of shareholders' equity stood at 75.8% compared to 61.2% in 2005 due to the increase in the price of raw materials, which has substantially raised current assets. It is important to note that inventories, of which a significant portion comprises finished products pending dispatch, invoicing and collection, exceed interest-bearing loans and borrowings under current liabilities in the consolidated balance sheet.

Of the total amount of financing available from financial entities at the end of 2006, only 3% relates to long-term debt (8% and 13% in 2005 and 2004), with the remainder used for

financing companies' day-to-day operations and repayable in the short term. Had the rise in raw material prices and production levels not occurred, the Group's net debt in comparative terms would have fallen considerably.

The Group's working capital totals Euros 113.1 million for 2006, which is an increase of almost Euros 17 million on the prior year's amount of Euros 96.3 million. This reflects the soundness of the Group, which enhances its capacity to self-finance investment plans, including those set out in the Competitiveness and Strategic Plans.

As part of the financial activity analysis for 2006, attention should be drawn to the risk management policies currently in place to mitigate the Group's exposure to the principal risks associated with its line of activity, the most significant of which are the following:

- Mapping of top-level risks and controls for subsequent dynamic analysis by the Group's governing bodies.
- Hedging of credit risk through insurance policies.
- Hedging of foreign currency risk by means of exchange rate insurance.
- Hedging of interest rate risk using IRS (interest rate swaps).
- Hedging of raw material price risk through supply contracts guaranteeing sales at fixed prices.

This hedging of the Group's principal transactions are materialised through the following basic risk control objectives:

- Conservative policies that only seek to hedge industrial and commercial margins.
- Dynamic tools designed to analyse cash flows, exposure to credit risk and the impact of fluctuations in raw material prices.
- Independent advice on the design of financial hedging strategies.
- Contracting of financial operations in established, liquid markets with financial entities of renowned prestige and solvency.
- Proactive management on the part of sales, purchases and financial managers aimed at minimising risks in accordance with prudent policies.
- Independence in the fields of financial, sales and purchasing management.
- Levels of authority defined in accordance with operation type.
- Compliance with the hedging policies defined by the Audit Committee.

The value of the Group on the stock exchange rose by 38.0% in 2006. Shares increased from Euros 3.58 per share at the close of 2005 to Euros 4.94 at the close of this year. This is the sixth consecutive year that Tubacex, S.A. shares have risen, with values climbing from Euros 1.10 per share at the end of 2000 to the current price of Euros 4.94 (+349.1%). The maximum price quoted during the year was in May, when shares reached a high of Euros 5.77, whereas the minimum price of Euros 3.55 per share was quoted on 2 January.

A total of 263.34 million shares were traded on the stock exchange during the year, which is 30.2% higher than the 202.33 million traded in 2005.

This figure signifies a rotation of 198% of the total number of the Company's shares, which comes to 132.98 million. Effective trading for the year amounted to Euros 1,214.27 million, 104.6% higher than the prior year when the value of shares traded reached Euros 593.62 million. The Company's market capitalisation at 31 December 2006 amounted to Euros 656.92 million, 38.0% up on the prior year-end figure of Euros 476.06 million.

On 1 July 2005 the Spanish Stock Exchanges, integrated within the BME Group, launched two new trading indices, IBEX MEDIUM CAP and IBEX SMALL CAP, which track the performance of small and medium capitalisation companies. Tubacex entered the IBEX SMALL CAP index at the beginning of 2006, which comprises the twenty securities with the highest adjusted free-float capitalisation, excluding the thirty-five securities in the IBEX 35. This index recorded gains of 42.1% in 2006.

At the end of 2006, the Technical Assessment Committee of the IBEX indices agreed that as of 2 January 2007 Tubacex would be withdrawn from the IBEX MEDIUM CAP index and placed in the IBEX SMALL CAP index, of which it already formed part in the second half of 2005. This latter index includes the thirty securities with the highest adjusted free-float capitalisation, excluding the thirty-five securities in the IBEX 35 and the twenty in the IBEX MEDIUM CAP index.

1.3 Commercial activity

Consolidated group sales reached Euros 539.07 million in 2006, a rise of 25.2% compared to the prior year. The volume and price effects of this variation are discussed in section 1.1 above. However, in order to take into account the geographical side of business performance for the year as commented previously, details of group sales by geographical market for the last three years are as follows:

	(in millions of Euros)			
	2006	2005	2004	2006/2005
Europe	368.33	283.26	236.59	+30.0%
USA	93.97	85.67	65.26	+9.7%
Other Countries	76.77	61.57	45.60	+24.7%
Total sales	539.07	430.50	347.45	+25.2%

68% of total sales in 2006 relate to the European market, 18% to the USA and 14% to other countries. In 2005 this distribution was 66%, 20% and 14%, respectively. The most significant factors behind this evolution are as follows:

The North American market, which had regained ground in 2005, maintained its position in 2006 through improved levels of end demand that made it possible to minimise the weakness of the US Dollar. This growth in demand resulted in turnover of Euros 93.97 million, 9.7% up on 2005, and is

attributable to the rise in exports to this market from group factories in Europe and, to a significant extent, the 23.5% increase in sales made by Salem Tube Inc. This company attained its highest profitability and turnover figures since it was integrated into Tubacex in 1995.

In 2006 the European market grew by 30.0% as a result of the strong demand in the European Union as a whole, which has enabled raw material cost increases to be passed on to the end customer, and base prices to be increased, thereby improving group performance. Group sales in Europe continue to account for over 65% of total sales, thus confirming the Company's solid commercial positioning in this market.

The consolidation of net sales to the rest of the world is directly attributable to the high rates of growth in Asia and the Group's commercial efforts to expand its presence in new markets. This resulted in commercial branches being opened in Shanghai (China) at the end of 2004 and in Sao Paulo (Brazil) in 2006. It has also taken the necessary steps to open a further commercial branch in Dubai (United Arab Emirates) in 2007 with a view to maintaining a much closer relationship with our end customers and markets.

1.4 Industrial activity

During 2006 the Tubacex Group continued the strategy initiated in prior years of maintaining a strict policy of prudent investment based on in-depth analyses of expected return on proposed investments (payback in under four years). As a result of the application of these criteria, investments in plant, machinery and equipment in 2006 amounted to approximately Euros 11.3 million compared to the Euros 12 million invested in 2005. This increase is largely attributable to the implementation of the Competitiveness Plan described in section 1.5 of this report.

The most significant investments carried out during the year were those considered to be strategic and directly related to the Competitiveness Plan. These investments mainly focused on Tubacex Tubos Inoxidables, S.A., a European subsidiary involved in the production of seamless stainless steel tubes, and, to a lesser extent, in Salem Tube Inc, S.A., an American subsidiary, and amounted to approximately Euros 3 million. The main activities carried out during the year, some of which will continue in 2007, relate to improving the productivity of the extrusion press through increasing the heating capacity of the horizontal furnaces, the incorporation of a new cold tube laminator in the Amurrio plant and improving the efficiency of finishing lines.

These investments are ensuring improved performance and production capacity in the Group's key plants without significant increases in fixed costs through a limited volume of investments. The continual drive to cut costs and increase capacity and productivity means that our plants are among the most competitive of their kind in the world.

Also of note are investments totalling almost Euros 3 million in Acería de Alava, S.A. The main investments have been the improvement and expansion of raw material storage facilities,

thus allowing different types of scrap and steel alloys to be classified, and the expansion of the steel alloy storage capacity for additions in progress, both of which are vitally important for the increasing volume of special steels in our product mix. Other lesser important investments involved the modernisation of the AOD electronic control systems and the adaptation of the dump to meet with ever more stringent environmental standards and industrial safety standards.

Of the over Euros 5 million in investments remaining, in line with the amounts invested in recent years, special mention should be given to those aimed at improving the efficiency of the key installations of the Group's different industrial plants through the renovation and maintenance of equipment, tried and tested procedures for preventive installation maintenance, continuous improvement and reengineering of production processes, improvements in the quality and added value of our products and strict compliance with environmental legislation and industrial safety standards.

Investments for the coming years, which comprise maintenance of the Group's facilities, will amount to approximately Euros 10 million a year.

This policy of continually improving the Group's competitive position while always adhering to prudent investment criteria, together with the gradual reduction of financial debt, should be taken into consideration in any analysis of the Company's financial solvency and equity soundness.

From an industrial standpoint, the Group endeavours to seek solutions to the needs and problems of its customers, principally warehouse operators and engineers. It should be borne in mind that the sectors at which its products are aimed are constantly evolving, and therefore require constant updating of quality control, research and investment policies.

The average headcount of the Tubacex Group in 2006 was 1,771, an average increase of 143 on the prior year. This growth has improved the Group's production capacity in a highly favourable demand scenario.

1.5. Competitiveness Plan

A highly ambitious plan was drawn up in mid 2003 for the Tubacex Group's main production units with a view to improving operating margins and achieving a competitive edge in terms of productivity and costs. After an initial diagnostic phase of identifying areas requiring improvement, a series of projects were launched in 2004 which have been under development in recent years.

The implementation of some of these projects has resulted in a significant increase in profits in 2006 and has contributed to the buoyant outlook for the coming years.

The main projects carried out during 2006, and which are still under development, are as follows:

- Improvement in productivity in the Group's key installations
- Increased production in Acerálava for both the Group's tube producing plants and external clients

- Improvements to the supply mix from Acerálava to SBER
- Reduction in maintenance costs
- Management of centralised purchases of certain tools
- Monitoring of the main group installations in Spain

1.6. Strategic Plan

The Tubacex 2010 Strategic Plan launched at the end of 2004, which aims to convert the Tubacex Group into the world's leading producer of seamless stainless steel tubes, is showing good progress, aided in part by the aforementioned positive trends in demand. The cornerstones of this plan and the steps taken to achieve its objectives are as follows:

- Increase group profitability and volume of core business sales (seamless stainless steel tubes).

The positive evolution of demand has once again made it possible to increase prices and margins for almost all products and improve the product mix. This has led to sales and operating results which exceed the goals for 2010. Additionally, this increase is attributable to:

- Orientation towards the projects market with a more specialised product mix;
- Industrial improvements have been partially achieved during the year and will continue in the coming years, thereby ensuring growth in group productivity.

At the end of 2006, production improvements were incorporated, which should raise production in 2007 to levels approximating those outlined in the Strategic Plan.

- Maintain the Group's current competitive position in the European market in terms of market share and profitability.

As mentioned in section 1.3 – Commercial activity – the Group has improved its competitive position in the European market, basically on account of the growth in the projects market and the continued improvements in the distribution market, thus allowing it to implement successive price rises.

- Increase the Group's presence in the most rapidly expanding markets in our sector, namely North America and Asia.

Trends in these markets have differed. In North America both margins and the volume of tons sold rose while in Asia the volume of tons sold fell slightly. Asia is a geographical area which is being targeted through the opening of the commercial branch in Shanghai.

- Improve the Group's production possibilities through an optimum, specialised industrial structure adapted to production targets and unit costs per product, without relying on significant investments.

Investments made in 2006, which are described in section 1.4 - Industrial Activity - were primarily aimed at adapting facilities to produce a product mix of higher

added value and gradually increasing the Group's overall production capacity.

- A sound management and organisational structure adapted to objectives and action plans by geographical area. Organisation geared towards obtaining results.

- Broaden the product portfolio in areas of activity with higher added value and in which the Group is not yet present.

- Commercial excellence and customer service.

A customer loyalty policy has been actively followed throughout the year and close contact has been maintained with customers. In addition to the opening of a commercial branch in Sao Paulo, (Brazil) with a view to improving our positioning in the Latin American market, a commercial branch in Dubai (United Arab Emirates), the financial capital of the world's main oil-producing region and destination of a substantial portion of our production, is due to commence operations in the first quarter of 2007.

The Tubacex Group therefore has fifteen commercial branches in fourteen countries with sales agents in a further thirty countries across the globe. This is a result of the internationalisation process embarked upon in prior years which has converted the Group into the world's second largest producer of seamless stainless steel tubes.

2. GROUP SITUATION

The positive performance of the Group is a reflection of the significant improvement in demand during the year, particularly in the oil, gas, chemical, petrochemical and energy sectors and the gradual improvement in the tube distribution sector. Attention should also be drawn to the successful implementation of the industrial and commercial projects described previously, reflecting the Group's resolve in tackling increasingly difficult challenges, which it assumes with composure and flexibility.

The Tubacex Group is adequately structured in all areas of strategic, industrial, commercial, economic, financial and social activity. At present, the Group is focusing its efforts towards developing the Tubacex 2010 Strategic Plan, which is aimed at ensuring future growth and profitability. The Group relentlessly strives to achieve excellence when dealing with customers and suppliers, to ensure that all employees identify with a set of common values and goals, and to continually pursue ways to create value for our shareholders.

3. SIGNIFICANT SUBSEQUENT EVENTS

No significant subsequent events have occurred which require special mention.

4. OUTLOOK FOR THE GROUP'S BUSINESS

Having analysed 2006, a brief evaluation of what could be the main trends of economic activity for 2007 and subsequent years is as follows:

The worldwide economic climate is encouraging, with continued growth forecast for 2007, although at a slower rate than in 2006, despite the prevailing restrictions in the oil market, concerns over further rises in fuel prices, the possibility of interest rate hikes and inflated real estate prices.

A soft landing is predicted for the US economy, with forecast growth of less than 3% in 2007, on the back of positive corporate results and employment contrasted by uncertainties over consumer spending and investment in light of a potential slowdown in the property markets. There continue to be risks such as the high price of oil and its impact on inflation, a foreseeable rise in interest rates and, of course, the exorbitant external deficit.

Europe is forecast to grow in excess of the American market, thanks once again to the German economy. Inflation is expected to remain moderate, although there are risks such as the cost of energy, particularly oil, which in the past has been mitigated by the strength of the Euro.

Growth in Asia is expected to slow down somewhat, although it will remain vigorous, particularly in China and India, which will play an increasingly predominant role in the global economy. A point of interest to be followed is the Chinese government's desire to moderate its growth after figures in excess of 10% in recent years have placed this economy fourth in the global ranking, behind the United States, Japan and Germany and ahead of the United Kingdom and France.

The US Dollar, the Euro and the Yuan will once again figure strongly in the currencies market in 2007. Despite the introduction of higher interest rates by the American Federal Reserve in the first half of 2006, the US Dollar is still heavily depreciated. This has a negative knock-on effect on the Euro, as it acts as an alternative currency and its strength could be detrimental to exports, one of the main driving forces behind the European economy. Furthermore, since China's withdrawal from the fixed exchange rate against the US Dollar, its currency has devalued slightly against the Dollar.

The European Central Bank may continue to progressively raise interest rates, as it did in 2006, to around 4-4.5% at the end of the year to try to curb possible inflation risks. The American Federal Reserve, which maintained rates during the second half of 2006 at 5.25%, may even lower them during 2007.

During the initial months of 2007, oil prices dipped slightly to US\$50 a barrel but then rose again to top US\$60 a barrel due to the combination of factors described earlier. The tight margin of unused production capacity means prices are extremely sensitive to unexpected changes in the balance between supply and demand, which means prices will remain high and volatile.

The cost of other raw materials – nickel, stainless steel scrap, chrome and molybdenum – is expected to remain historically high for most of the year, although this market is likely to remain unstable throughout 2006, fuelled by increasing end demand and the speculative factors described previously.

The iron and steel sector will not be immune to these overall growth trends, and the influence of Chinese economic development will be a decisive factor in both production and the evolution of the raw material markets as it becomes the world's largest producer and consumer of steel. Points to follow closely will be the aforementioned control on growth exercised by the Chinese government, the probable closure of part of its steel production capacity concentrated in small manufactures as a result of the application of new environmental regulations, and, finally, possible mergers to create more powerful groups and thereby hinder the introduction of foreign capital.

Growth in the seamless stainless steel tube sector during the year is expected to continue in 2007 with an improved pricing structure, product mix and production capacity. Risks such as high raw material prices and the weakness of the Dollar against the Euro are expected to persist. It is against this background that the main objectives of the Tubacex Group's 2010 Strategic Plan, as described in the previous section, will be structured with a view to improving the competitiveness and profitability of the main business units.

Key aspects crucial to the development of action plans for 2007 and thereafter which are important strengths for the Group include the following:

- Development of and compliance with Corporate Governance and Social Accountability policies.
- Stable policy of shareholder remuneration through dividends, in the range of 30-40% of net consolidated profit for the year, which on occasion could vary.
- Continual improvements in productivity, competitiveness and production efficiency through specific investments that will enable the Group to reach a significant presence in products of high added value.
- Solid equity structure. Constant reduction in the Group's long-term financial borrowing.
- Maximum quality products and processes that respect the environment (ISO 9000 and ISO 14000).
- Excellence in customer service.

This series of strategic objectives and our commitment to productive and commercial excellence is the best way to increase value for our shareholders.

5. RESEARCH AND DEVELOPMENT ACTIVITIES

In view of the range of products on which the Tubacex Group focuses its activities, there are permanent policies in place to promote R&D activities.

In 2006 the Group continued its policy of investing in projects aimed at improving its manufacturing processes through higher quality, cost cutting, environmental improvements, consolidation of production processes through systematisation and the defining of values, thereby improving performance and minimising rejections.

The most relevant projects carried out were as follows:

- Development of more resistant steel and alloys for more critical uses.

The first steps have been taken in a multi-year programme for developing different grades of steel and nickel alloys.
- Research in cooperation with CEIT (Guipúzcoa Centre for Technical Studies and Research): in 2006, the programme initiated the prior year in conjunction with CEIT to improve the thermal treatments of Tubacex Tubos Inoxidables, S.A. (T.T.I.) and Acerálava products was concluded.

During the first few days of 2007, a new collaboration agreement was signed for a period of three years to continue research on materials for use in high temperature environments.
- Project for improving the titanium treatment of steel: with a view to optimising stainless grades stabilised with titanium, Acerálava has collaborated with Labein in the redesign of the casting process, which could improve steel products.

The projects described above are examples of the philosophy of improving the performance of our products and steels which are being incorporated into new manufacturing programmes, thus enabling us to maintain our ever increasing level of competitiveness and our leading-edge position as suppliers of products of higher added value in our market niche.

6. ENVIRONMENTAL ACTIVITIES

Having adapted the Group's plants to current environmental standards in recent years, and certified and consolidated its Environmental Management Systems, the basic projects for attaining Integrated Environmental Authorisation for the TTI (Amurrio and Llodio) centres, Acerálava and the Acerálava dump have been prepared and submitted. This new authorisation will involve a complete overview of the environmental aspects of the Group's activity and will demonstrate that Best Available Technologies from an environmental standpoint are being implemented.

A pickling bath regeneration facility has been set up in the IIT plant in Amurrio as a pilot project before subsequent implementation in other group production centres. This new facility will have a significantly effect on the environment due to the reduction in the use of raw materials and waste generation.

The Company has continued to carry out activities under the voluntary agreement signed in 2003 with the local government's Ministry of the Environment concerning the improvement of the environment in the sector. This voluntary agreement for the surface treatment sector affects two TTI centres (Amurrio and Llodio) which carry out tube pickling work.

This agreement, based on the strategic principle of commitment to sustainable development, endeavours to make manufacturing activities compatible with respecting the environment and improving peoples' quality of life.

The agreement represents a new challenge within the context of the demanding European Union legislation governing environmental activities. Acería de Alava, S.A. undertook to take early action and comply with the forthcoming legislation, cooperating with the local government and implementing appropriate monitoring tools.

In relation to this plan, Acería de Alava, S.A. installed a new emissions filter, thereby duplicating the extraction and filtering of fumes, reducing emissions and improving air quality.

Both TTI (2001) and Acería de Alava (2002) have implemented the Environmental Management System. This process has been validated by AENOR (Spanish Association of Normalisation and Certification) and has been awarded the environmental management certification in accordance with the requirements of ISO 14001 for all of the activities carried out at the related plants. Therefore, the whole of the production process carried out at the Group's Llodio and Amurrio plants, from the receipt of raw materials and the manufacture of stainless steel at Acería de Alava to the shipment of tubes produced at Tubacex Tubos Inoxidables (TTI), has obtained environmental management certification from an official organisation.

The Austrian subsidiary Schoeller-Bleckmann Edelstahlrohr has also been awarded the ISO 14001 certification for the production and sale of tubes at its installations in Ternitz (Austria).

We believe these recognitions to be a reflection of an effective, modern policy of quality management and environmental protection applicable to all of the Group's production units.

As one of its priority strategies, the Tubacex Group has undertaken to carry out environmental activities and, to this end, its policy is to establish at all the Group's business units a system to minimise the environmental impact caused by its industrial activity through the use of economically viable clean technologies and implementation of the measures necessary to prevent pollution in all operating situations, including emergencies.

Environmental management activities are systemised and included within the Group's Report on Corporate Social Accountability.

7. STATUTORY ACTIVITY

The Report on Corporate Social Accountability, attached to this Annual Report, details general policies and specific activities carried out by the Tubacex Group in 2006 in relation to key stakeholders such as the Company as a whole, the environment, employees and their representatives, shareholders, analysts and investors, the media, suppliers and contractors.

8. ACQUISITION OF OWN SHARES

No own shares have been acquired or sold during the year.

9. PROPOSED DISTRIBUTION OF PROFIT

The board of directors of Tubacex, S.A. will propose to the shareholders at their annual general meeting that the profit for the year be distributed as follows:

	Thousands of Euros
Legal reserve	466
Voluntary reserves	1,304
Ordinary dividend	12,379
Total	14,149

Dividends are employed to remunerate shareholders and 40% of net consolidated profit for 2006 will be distributed. This dividend will be the highest paid out to shareholders since this remuneration policy was agreed in 1996.

10. FINANCIAL INSTRUMENTS

Detailed information in relation to forward currency contracts and interest rate swaps held by the Tubacex Group at 31 December 2006 are shown in note 9 to the consolidated annual accounts.

11. OTHER

11.1. Audit fees

The audit fees for the professional services performed at the Spanish Tubacex Group companies in 2006 amounted to Euros 137 thousand. In accordance with the principles regarding the independence of auditors included in the report on compliance with the recommendations of the Company's Board of Directors' Code of Corporate Governance, the auditor did not receive any remuneration from the Tubacex Group for any items other than its audit work.