U.S. SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2004

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ___________ to ___________

Commission file number 000-25067

PRIVATE MEDIA GROUP, INC.

(Exact Name of Registrant as Specified in its Charter)

Nevada	**87-0365673**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

3230 Flamingo Road, Suite 156, Las Vegas, Nevada 89121

(Registered office)

Carretera de Rubí 22-26, 08190 Sant Cugat del Vallès, Barcelona, Spain

(European headquarters and address of principal executive offices)

34-93-590-7070

Registrant s telephone number

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act):

Yes ¨ No x

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date

Class	Outstanding at August 10, 2004
Common Stock, par value $.001	50,194,437

PART I.

Item 1. Financial Statements

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED BALANCE SHEETS

	December 31,	June 30, (Unaudited)	
	2003	2004	2004
	EUR	EUR (in thousands)	USD
ASSETS			
Cash and cash equivalents	856	700	854
Trade accounts receivable	9,768	10,950	13,354
Related party receivable	4,187	4,055	4,945
Inventories net (Note 3)	10,733	12,213	14,894
Deferred income tax asset	1,608	1,607	1,959
Prepaid expenses and other current assets	2,110	2,466	3,008
TOTAL CURRENT ASSETS	29,262	31,991	39,014
Library of photographs and videos net	16,807	15,362	18,734
Property, plant and equipment net	15,792	17,171	20,941
Other intangible assets	3,590	3,528	4,302
Goodwill	2,425	2,425	2,957
Other assets	273	263	321
TOTAL ASSETS	68,149	70,741	86,269
LIABILITIES AND SHAREHOLDERS EQUITY			
Short-term borrowings	4,094	3,804	4,639
Current portion of long-term borrowings	1,614	1,968	2,400
Accounts payable trade	7,486	7,271	8,867
Income taxes payable	981	814	993
Deferred income taxes	2	2	3
Accrued other liabilities	1,791	1,882	2,295
TOTAL CURRENT LIABILITIES	15,969	15,742	19,198
Long-term borrowings	4,451	5,771	7,038
Related party payable	2,237	2,237	2,728
Convertible notes	1,336	1,224	1,492
TOTAL LIABILITIES	23,993	24,974	30,456
SHAREHOLDERS EQUITY			

Common Stock, $.001 par value, 100,000,000 shares authorized, 49,955,057 and 50,167,271 issued and outstanding at December 31, 2003 and June 30, 2004, respectively	883	883	1,077
Additional paid-in capital	17,124	17,393	21,211
Retained earnings	27,976	29,919	36,486
Accumulated other comprehensive income	(1,826)	(2,428)	(2,961)
TOTAL SHAREHOLDERS EQUITY	44,157	45,767	55,814
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	68,149	70,741	86,269

See accompanying notes to consolidated statements

PRIVATE MEDIA GROUP, Inc.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

	Three-months ended June 30, (unaudited)		Six-months ended June 30, (unaudited)		
	2003	2004	2003	2004	2004
	EUR	EUR	EUR (in thousands)	EUR	USD
Net sales	10,078	9,267	19,669	19,218	23,437
Cost of sales	4,880	3,656	9,179	8,332	10,161
Gross profit	5,198	5,611	10,490	10,886	13,276
Selling, general and administrative expenses	4,907	4,452	9,966	8,984	10,956
Operating profit (loss)	291	1,160	524	1,902	2,320
Interest expense	204	191	406	365	445
Interest income	37	43	80	92	112
Income before income tax	124	1,011	198	1,629	1,986
Income taxes (benefit)	58	147	93	314	383
Net income	66	1,159	105	1,943	2,370
Other comprehensive income:					
Foreign currency adjustments	262	52	347	(602)	(734)
Comprehensive income	328	1,211	452	1,341	1,635
Income applicable to common shares	(6)	1,159	(43)	1,943	2,370
Net income per share:					
Basic	0.00	0.02	0.00	0.04	0.05
Diluted	0.00	0.02	0.00	0.04	0.05

See accompanying notes to consolidated statements

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six-months ended June 30, (unaudited)		
	2003	**2004**	**2004**
	EUR	**EUR (in thousands)**	**USD**
Cash flows from operating activities:			
Net income	105	1,943	2,370
Adjustment to reconcile net income to net cash flows from operating activities:			
Depreciation	515	1,086	1,324
Bond Adjustment		123	150
Bad debt provision	150	712	868
Amortization of other intangible assets	25	62	76
Amortization of photographs and videos	3,474	3,247	3,960
Effects of changes in operating assets and liabilities:			
Trade accounts receivable	(926)	(1,894)	(2,310)
Related party receivable	(260)	132	161
Inventories	(1,889)	(1,480)	(1,805)
Prepaid expenses and other current assets	(993)	(356)	(434)
Accounts payable trade	3,043	(215)	(262)
Income taxes payable	64	(167)	(204)
Accrued other liabilities	155	91	111
Net cash provided by operating activities	3,462	3,284	4,005
Cash flows from investing activities:			
Investment in library of photographs and videos	4,227	1,802	2,198
Capital expenditures	1,060	2,441	2,977
Investments in (sale of) other assets	(2)	(10)	(12)
Net cash used in investing activities	5,285	4,233	5,163
Cash flow from financing activities:			
Conversion of warrants		10	12
Short-term borrowings repayments	(6,890)	(389)	(475)
Long-term loan repayments)		(901)	(1,099)
Related party note payable	(1,649)	0	0
Long-term loan additions	9,464	2,577	3,143
Short-term borrowings additions		99	121
Net cash (used in) provided by financing activities	925	1,396	1,702
Foreign currency translation adjustment	347	(602)	(734)
Net (decrease) increase in cash and cash equivalents	(551)	(156)	(190)
Cash and cash equivalents at beginning of the period	1,694	856	1,044
Cash and cash equivalents at end of the period	1,142	700	854

Cash paid for interest	219	210	256
Cash paid for taxes	320	17	21
Conversion of bond principal into common stock		236	288

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	Common stock		Preferred stock		Additional paid-in	Stock dividends to be	Retained	Accumulated other compre hensive	Total share holder s
	Shares	Amounts	Shares	Amounts	capital	distributed	earnings	income	equity
Balance at January 1, 2003	28,608,609	863	7,000,000		15,668	692	28,695	(2,467)	43,450
Issuance of warrants with and beneficial conversion feature for convertible debt					617				617
Translation Adjustment								642	642
Conversion of preferred stock to common stock	21,000,000	20	(7,000,000)						20
Stock dividends	346,448				840	(840)			
Stock dividends to be distributed						148	(148)		
Net income (loss)							(570)		(570)
Balance at December 31, 2003	49,955,057	883			17,124		27,976	(1,826)	44,157
Conversion of bond principal into common stock	153,438				236				236
Translation adjustment								(602)	(602)
Conversion of options	7,500				10				10
Cashless Conversion of series A warrants	38,987								
Conversion of bond interest into common stock	12,289				23				23
Net income (loss)							1,943		1,943
Balance at June 30, 2004	50,167,271	883			17,393		29,919	(2,428)	45,767

See accompanying notes to consolidated statements.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (U.S. GAAP) for interim financial information. Accordingly they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of financial position and results of operations have been included. Operating results for the six months period ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ended December 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s annual report on form 10-K for the year ended December 31, 2003.

Solely for the convenience of the reader, the accompanying consolidated financial statements as of June 30, 2004 and for the six months then ended have been translated into United States dollars (USD) at the rate of EUR 0.82 per USD 1.00 the interbank exchange rate on June 30, 2004. The translations should not be construed as a representation that the amounts shown could have been, or could be, converted into US dollars at that or any other rate.

2. Stock-Based Compensation

As permitted by Statement of Financial Accounting Standards No. 123 (SFAS No. 123), Accounting for Stock-Based Compensation, the Company has elected to continue following Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees, and related Interpretations for measurement and recognition of stock-based transactions with employees and adopted the disclosure-only provisions of SFAS No. 123. Under APB 25, generally no compensation expense is recognized because the exercise price of the options equals the fair value of the stock at the vesting date.

Had compensation cost for the Company s stock based compensation issued to employees been determined based upon the fair value at the grant date consistent with the methodology prescribed under SFAS 123, the Company s pro forma net income (loss) for 2003 and 2004 would have been as per the following table:

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

	Three-months ended June 30, (unaudited)		Six-months ended June 30, (unaudited)	
	2003	2004	2003	2004
	EUR (in thousands)	EUR	EUR (in thousands)	EUR
Net income, as reported	66	1,159	105	1,943
Deduct: Total stock based employee compensation expense determined under fair value based method for all awards net of related tax effects	(1,606)	(15)	(2,321)	(35)
Pro forma net income	(1,540)	(1,144)	(2,216)	(1,909)
Net income applicable to common shares, as reported	(6)	1,159	(43)	1,943
Deduct: Total stock based employee compensation expense determined under fair value based method for all awards net of related tax effects	(1,606)	(15)	(2,321)	(35)
Pro forma net income applicable to common shares	(1,612)	(1,144)	(2,364)	(1,909)
Earnings (loss) per share:				
Basic as reported	0.00	0.02	0.00	0.04
Basic pro forma	(0.04)	0.02	(0.06)	0.04
Diluted as reported	0.00	0.02	0.00	0.04
Diluted pro forma	(0.04)	0.02	(0.06)	0.04

3. Inventories

Inventories consist of the following:

	December 31,	June 30,

	2003	2004
	EUR	EUR
	(in thousands)	
Magazines for sale and resale	3,257	3,858
Video cassettes	2,838	2,545
DVDs	4,515	5,588
Other	123	221
	10,733	12,213

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

4. Earnings per share

The following table sets forth the computation of basic and diluted earnings per share:

	Three-months ended June 30,		Six-months ended June 30,	
	2003	2004	2003	2004
Numerator: (EUR in thousands)				
Net income (numerator diluted EPS)	66	1,159	105	1,943
Less: Dividends on preferred stock	72		148	
Income applicable to common shares (numerator basic EPS)	(6)	1,159	(43)	1,943
Denominator:				
Denominator for basic earnings per share Weighted average shares	44,983,761	50,163,938	38,153,326	50,105,600
Effect of dilutive securities:				
Convertible Note Weighted average outstanding	N/A	971,562	N/A	983,504
Common stock warrants and options	N/A	1,018,196	N/A	1,174,864
Denominator for diluted earnings per share weighted average shares and assumed conversions	N/A	52,153,695	N/A	52,263,968
Earnings per share (EUR)				
Basic	0.00	0.02	0.00	0.04
Diluted	0.00	0.02	0.00	0.04

For the three and six the month periods ended June 30, 2003 the impact of potentially dilutive securities (convertible preferred shares and outstanding options and warrants for common shares) is anti-dilutive therefore reported diluted and basic income (loss) per share are EUR 0.00.

For the three and six the month periods ended June 30, 2004, the equivalent of 1,860,326 and 1,802,576 common shares derived from dilutive securities such as options, warrants, convertible notes and convertible preferred shares are excluded from the diluted earnings per share calculation as they were not in-the-money in the respective periods.

PRIVATE MEDIA GROUP, INC.

NOTES TO THE CONSOLIDATED INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

5. Contingent Liability

In December 1999 the Company received final notification from the Swedish Tax Authority assessing its subsidiary in Cyprus for the tax years 1995-1998 for a total amount of SEK 42,000,000 (approx. EUR 4.5 million) plus fines amounting to SEK 16,800,000 (approx. EUR 1.8 million) plus interest. The Swedish Tax Authority has taken the position that the subsidiary carried on business in Sweden from a permanent establishment during the period in question and should therefore be taxed on the income attributable to the permanent establishment. The case is under litigation and the Company believes the circumstances supporting the Tax Authority s claim are without merit. However, the County Court has decided that a permanent establishment is at hand. The Court has only made a principle statement and the question how to calculate any eventual profit that can be allocated to the permanent establishment is not decided by the Court at this stage. The Company has appealed against the decision. The final outcome of this litigation will not be known for several years. Due to the early stages of this matter and the uncertainty regarding the ultimate decision, no amounts have been provided in the Company s financial statements for this dispute.

6. Other events

In April 2004, the Company signed an agreement for the sale of part of the Company s building in Barcelona, Spain. Under the agreement, the Company is selling the ground floor of its new office building, which represents approximately 14% of the sellable floor space. The consideration under the agreement is 1.8 million euro + VAT 16%. A 10% down-payment was received upon signature. The balance of the consideration will be received upon delivery of the property, which is expected to take place in August/September this year.

In June 2004, the Company signed an agreement for the sale of part of the Company s building in Barcelona, Spain. Under the agreement, the Company is selling the first floor of its new office building, which represents approximately 23% of the sellable floor space. The consideration under the agreement is 2.8 million euro + VAT 16%. A 10% down-payment was received upon signature. The balance of the consideration will be received upon delivery of the property, which is expected to take place in August/September this year.

Through the above agreements, the company has sold 37% of the sellable floor space for a total of 4.6 million euro + VAT 16%. Use of the proceeds includes investment in the Company s content library and repayments on costly financing not related to the property.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

You should read this section together with the consolidated financial statements and the notes and the other financial data in this Report. The matters that we discuss in this section, with the exception of historical information, are forward-looking statements within the meaning of the Private Securities Reform Act of 1995. Such forward-looking statements are subject to risks, uncertainties and other factors which could cause our actual results to differ materially from those expressed or implied by such forward-looking statements. Potential risks and uncertainties relate to factors such as (1) the timing of the introduction of new products and services and the extent of their acceptance in the market; (2) our expectations of growth in demand for our products and services; (3) our ability to successfully implement expansion and acquisition plans; (4) the impact of expansion on our revenue, cost basis and margins; (5) our ability to respond to changing technology and market conditions; (6) the effects of regulatory developments and legal proceedings with respect to our business; (7) the impact of exchange rate fluctuations; and (8) our ability to obtain additional financing.

The following discussion should be read in conjunction with the consolidated financial statements and related notes included elsewhere in this Report.

Critical Accounting Policies

General

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amount of assets and liabilities revenues and expenses. On an ongoing basis, we evaluate our estimates, including those related to impairment of the library of photographs and videos and other long lived assets, allowances for bad debt, income taxes and contingencies and litigation. Accounts receivable and sales related to certain products are, in accordance with industry practice, subject to distributors right of return to unsold items. We base our estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily available from other sources. Management periodically reviews such estimates. Actual results may differ from these estimates.

We believe the following critical accounting policies are significantly affected by judgments and estimates used in the preparation of our consolidated financial statements.

Recognition of Revenue

Revenues from the sale of magazines, videocassettes, DVD s and other related products where distributors are not granted rights-of-return are recognized upon transfer of title, which generally occurs upon delivery. Revenues from the sale of magazines under agreements that grant distributors rights-of-return are recognized upon transfer of title, which generally occurs on delivery, net of an allowance for returned magazines. Revenues from the sale of videocassette and DVD products under consignment agreements with distributors are recognized based upon reported sales by the Company s distributors. Revenues from the sale of subscriptions to the Company s internet website are deferred and recognized ratably over the subscription period. Revenues from licensing of broadcasting rights to the Company s video and film library are recognized upon delivery when the following conditions have been met (i) license period of the arrangement has begun and the customer can begin its exploitation, exhibition, or sale (ii) the arrangement fee is fixed or determinable and (iii) collection of the arrangement fee is reasonably assured.

Inventories

Inventories are valued at the lower of cost or market, with cost principally determined on an average basis. Inventories principally consist of DVD s, videocassettes and magazines held for sale or resale. The inventory is written down to the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional write-downs may be required.

Impairment of Long-Lived Assets

The Company periodically evaluates the carrying value of long-lived assets including its library of photographs and videos for potential impairment. Upon indication of impairment, the company will record a loss on its long-lived assets if the undiscounted cash flows that are estimated to be generated by those assets are less than the related carrying value of the assets. An impairment loss is then measured as the amount by which the carrying value of the asset exceeds the estimated discounted future cash flows. Management s estimated future revenues are based upon assumptions about future demand and market conditions and additional write downs may be required if actual conditions are less favorable than those assumed.

Accounts receivable

We are required to estimate the collectibility of our trade receivables and notes receivable. A considerable amount of judgment is required in assessing the ultimate realization of these receivables including the current credit-worthiness of each customer. Significant changes in required reserves have been recorded in recent periods and may occur in the future due to the current market environment.

Results of Operations

Three months ended June 30, 2004 compared to the three months ended June 30, 2003

Net sales. For the three months ended June 30, 2004, we had net sales of EUR 9.3 million compared to net sales of EUR 10.1 million for the three months ended June 30, 2003, a decrease of EUR 0.8 million, or 8%.

DVD and Video sales decreased 24% to EUR 5.4 million. The change is primarily attributable to a decrease in Video sales of EUR 2.3 million which was not fully offset by DVD sales although DVD sales increased compared to 2003. The reason being a combination of the general industry decrease in Video sales and 40% less titles being released by the Company on Video in 2004 compared to 2003 as a result of fewer new movie productions available for sale. The reduction in new movie productions available for sale did also affect DVD sales. However, the Company has managed to offset a large part of the negative effect on Video and DVD sales in both the first and the second quarter of 2004 by opening additional distribution channels, thereby increasing sales on a per release basis. In 2003 and the first half of 2004, investment in new movie productions was temporarily cut back due to reduced cash-flow as a result of overspending in 2002 and 2003. Expected improvements in cash-flow during the remainder of 2004 will allow the Company to resume its normal investment activity in new movie productions. See also *Liquidity and Capital Resources Investing Activities.*

The decrease in Video sales of EUR 2.3 million was offset by increases in DVD, Broadcasting and Internet sales totaling EUR 1.5 million. Magazine sales remained stable at EUR 1.3 million. Internet sales increased 22% to EUR 1.3 million as a result of the Company s decision to move to a new IT solution provider in an effort to ensure down-time to be kept to a minimum in order to maximize revenues. Broadcasting sales increased 128% to EUR 1.3 million primarily as a result of the broadcasting launch of our own TV channel in the United States in February 2004.

Going forward and as cash-flow strengthens, we believe will be able to attain optimum release frequency of new movie productions. We believe that the growth in DVD, Broadcasting and Internet sales compared to 2003 will continue through the remainder of 2004.

Net sales in general were affected by unfavorable changes in exchange rates.

Cost of Sales. Our cost of sales was EUR 3.7 million for the three months ended June 30, 2004 compared to EUR 4.9 million for the three months ended June 30, 2003, a decrease of EUR 1.2 million, or 25%. Cost of sales as a percentage of sales was 39% for the three months ended June 30, 2004, compared to 48% for the three months ended June 30, 2003. The decrease in cost of sales as a percentage of sales was primarily the result of sales mix, see *Gross Profit*.

Gross Profit. In the three months ended June 30, 2004, we realized a gross profit of EUR 5.6 million, or 61% of net sales compared to EUR 5.2 million, or 52% of net sales for the three months ended June 30, 2003, an increase of EUR 0.4 million, or 8%. The increase in gross profit was the result of sales mix, with lower sales volume in products generating cost of sales, such as Videos, Magazines and DVDs combined, and higher sales in products generating lower or no cost of sales, such as Broadcasting and Internet sales. Furthermore, the Company s group-wide review of restructuring its operations to focus on core business and reduce or abandon spending on activities not generating sufficient gross profits and/or operating profits has also contributed to an overall improved gross profit.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 4.5 million for the three months ended June 30, 2004 compared to EUR 4.9 million for the three months ended June 30, 2003, a decrease of EUR 0.4 million, or 9%. We attribute the decrease to an overall program started in late 2003, where the objective is to review and reduce all controllable selling, general and administrative expenses in low or non-profitable areas, which was offset by our expansion in Canada through our new subsidiary, Private Media Group Canada, which became fully operational during the second half of last year. We expect selling, general and administrative expenses in low or non-profitable areas to continue to decrease in 2004.

Operating profit. We reported an operating profit of EUR 1.2 million for the three months ended June 30, 2004 compared to an operating profit of EUR 0.3 million for the three months ended June 30, 2003, an increase of EUR 0.9 million, or 298%. The increase was primarily the result of higher gross profit and decreased selling, general and administrative expenses.

Interest expense. We reported interest expense of EUR 0.2 million for the three months ended June 30, 2004, compared to EUR 0.2 million for the three months ended June 30, 2003.

Income tax expense/benefit. We reported income tax benefit of EUR 0.1 million for the three months ended June 30, 2004, compared to income tax expense of EUR 0.1 million for the three months ended June 30, 2003.

Net income. We reported net income of EUR 1.2 million for the three months ended June 30, 2004, compared to net income of EUR 0.1 million for the three months ended June 30, 2003. We attribute the increase in net income in 2004 of EUR 1.1 million to higher operating profit.

Six months ended June 30, 2004 compared to the six months ended June 30, 2003

Net sales. For the six months ended June 30, 2004, we had net sales of EUR 19.2 million compared to net sales of EUR 19.7 million for the six months ended June 30, 2003, a decrease of EUR 0.5 million, or 2%.

DVD and Video sales decreased 17% to EUR 11.5 million. The change is primarily attributable to a decrease in Video sales of EUR 3.8 million which was not fully offset by DVD sales although DVD sales increased compared to 2003. The reason being a combination of the general industry decrease in Video sales and 40% less titles being released by the Company on Video in 2004 compared to 2003 as a result of fewer new movie productions available for sale. The reduction in new movie productions available for sale did also affect DVD sales. However, the Company has managed to offset a large part of the negative effect on Video and DVD sales in both the first and the second quarter of 2004 by opening additional distribution channels, thereby increasing sales on a per release basis. In 2003 and the first half of 2004, investment in new movie productions was temporarily cut back due to reduced cash-flow as a result of overspending in 2002 and 2003. Expected improvements in cash-flow during the remainder of 2004 will allow the Company to resume its normal investment activity in new movie productions. See also *Liquidity and Capital Resources Investing Activities.*

The decrease in Video sales of EUR 3.8 million was offset by increases in Magazine, DVD, Broadcasting and Internet sales totaling EUR 3.3 million. Magazine sales increased 20% to EUR 2.7 million. Internet sales increased 10% to EUR 2.6 million as a result the Company s decision to move to a new IT solution provider in an effort to ensure down-time to be kept to a minimum in order to maximize revenues. Broadcasting sales increased 93% to EUR 2.4 million primarily as a result of the broadcasting launch of our own TV channel in the United States in February 2004.

Going forward and as cash-flow strengthens, we believe will be able to attain optimum release frequency of new movie productions. We believe that the growth in DVD, Broadcasting and Internet sales compared to 2003 will continue through the remainder of 2004.

Net sales in general were affected by unfavorable changes in exchange rates.

Cost of Sales. Our cost of sales was EUR 8.3 million for the six months ended June 30, 2004 compared to EUR 9.2 million for the six months ended June 30, 2003, a decrease of EUR 0.8 million, or 9%. Cost of sales as a percentage of sales was 43% for the six months ended June 30, 2004, compared to 47% for the six months ended June 30, 2003. The decrease in cost of sales as a percentage of sales was primarily the result of sales mix, see *Gross Profit*.

Gross Profit. In the six months ended June 30, 2004, we realized a gross profit of EUR 10.9 million, or 57% of net sales compared to EUR 10.5 million, or 53% of net sales for the six months ended June 30, 2003, an increase of EUR 0.4 million, or 4%. The increase in gross profit was the result of sales mix, with lower sales volume in products generating cost of sales, such as Videos, Magazines and DVDs combined, and higher sales in products generating lower or no cost of sales, such as Broadcasting and Internet sales. Furthermore, the Company s group-wide review of restructuring its operations to focus on core business and reduce or abandon spending on activities not generating sufficient gross profits and/or operating profits has also contributed to an overall improved gross profit.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 9.0 million for the six months ended June 30, 2004 compared to EUR 10.0 million for the six months ended June 30, 2003, a decrease of EUR 1.0 million, or 10%. We attribute the decrease to an overall program started in late 2003, where the objective is to review and reduce all controllable selling, general and administrative expenses in low or non-profitable areas, which was offset by our expansion in Canada through our new subsidiary, Private Media Group Canada, which became fully operational during the second half of last year.

We expect selling, general and administrative expenses in low or non-profitable areas to continue to decrease in 2004 compared to 2003.

Operating profit. We reported an operating profit of EUR 1.9 million for the six months ended June 30, 2004 compared to an operating profit of EUR 0.5 million for the six months ended June 30, 2003, an increase of EUR 1.4 million, or 263%. The increase was primarily the result of higher gross profit and decreased selling, general and administrative expenses.

Interest expense. We reported interest expense of EUR 0.4 million for the six months ended June 30, 2004, compared to EUR 0.4 million for the six months ended June 30, 2003.

Income tax expense/benefit. We reported income tax benefit of EUR 0.3 million for the six months ended June 30, 2004, compared to income tax expense of EUR 0.1 million for the six months ended June 30, 2003.

Net income. We reported net income of EUR 1.9 million for the six months ended June 30, 2004, compared to net income of EUR 0.1 million for the six months ended June 30, 2003. We attribute the increase in net income in 2004 of EUR 1.8 million to higher operating profit.

Liquidity and Capital Resources

We reported a working capital surplus of EUR 16.2 million at June 30, 2004, an increase of EUR 3.0 million compared to the year ended December 31, 2003. The increase is principally attributable to increases in trade accounts receivable and inventories as a result of increased sales of Magazines and DVDs through high margin national newsstand network distributors with consignment agreements and long credit terms.

Operating Activities

Net cash provided by operating activities was EUR 3.3 million for the six months ended June 30, 2004, and was primarily the result of net income, as adjusted for non-cash transactions, offset by uses of cash related to changes in operating assets and liabilities. The net income of EUR 1.9 million was adjusted to reconcile net income to net cash flows from operating activities, representing depreciation of EUR 1.1 million, bond adjustment of EUR 0.1 million, bad debt provision of EUR 0.7 million, amortization of other intangible assets of EUR 0.06 million and amortization of photographs and videos of EUR 3.2 million provided a total of EUR 7.2 million. The total of EUR 7.2 million was then added to by changes in related party receivable and accrued other liabilities totaling EUR 0.2 million offset by EUR 4.1 million from trade accounts receivable, inventories, prepaid expenses and other current assets, trade accounts payable and income taxes payable. Net cash provided by operating activities was EUR 3.5 million for the six months ended June 30, 2003. The decrease in cash provided by operating activities for the six months ended June 30, 2004 compared to the same period last year is the result of changes in operating assets and liabilities offset by the increase in net income.

Investing Activities

Net cash used in investing activities for the six months ended June 30, 2004 was EUR 4.2 million. The investing activities were principally capital expenditures of EUR 2.4 million of which EUR 2.1 million was related to the construction of a building and investment in library of photographs and videos of EUR 1.8 million. The decrease over the comparable six-month 2003 period is principally due to decreased investments in library of photographs and videos offset by capital expenditures. In 2003 and the first half of 2004, investment in new movie productions was temporarily cut back due to cash-flow restrictions as a result of overspending in 2002 and 2003, which in turn has affected the release frequency of new productions on both Video and DVD. During the second half of 2004 the Company is expecting the cash-flow to recover as a result of its overall program started in late 2003, where the objective is to review and reduce all controllable selling, general and administrative expenses in low or non-profitable areas. In addition the Company is expecting to receive EUR 4.6 million + VAT 16%, less repayment of a proportionate part of the mortgage, in August/September 2004 from the sale of part of its building. Use of the net proceeds from the sale include investment in the Company s content library. Going forward and as cash-flow strengthens, we believe will be able start acquiring movie productions at a normal rate and attain optimum release frequency of new movie productions.

Financing Activities

Net cash provided by financing activities for the six-month period ended June 30, 2004 was EUR 1.4 million, represented primarily by EUR 2.7 million in cash provided by short- and long-term borrowings offset by EUR 1.3 million in repayments on short- and long-term borrowings. We attribute the increase of EUR 0.5 million in net cash provided by financing activities over the comparable six-month 2003 period to higher additional borrowings. The main movements during the six-month period ended June 30, 2004 are described as follows:

In March 2003, the Company was granted a loan from an institutional lender in the principal amount of EUR 4.2 million of which EUR 1.75 million was received. The loan bears interest at the rate of EURIBOR + 1.5%, repayable over 12 years, including an initial period of 18 months during which only interest is payable. The loan was obtained for the purpose of financing the construction of an office building and is secured by a mortgage on the building. During the first six months in 2004, an additional EUR 2.45 million was received in order to pay for the completion of the construction of the building.

During the period, the remaining balance on the Note in the original principal amount of $4.0 million held by Consipio Holding b.v. was increased by EUR 0.1 million as a result of exchange rate changes. As of June 30, 2004 the remaining balance on the Note was EUR 2.7 million. As previously reported in the Company s Form 10-K for the year ended December 31, 2003, in December 2003 Consipio notified Private that Private was in default under the Note, and demanded immediate payment of the outstanding principal under the Note. The Company continues to make all regularly scheduled interest payments on the Note and believes that it has valid defenses to the demand for immediate repayment of the Note, should Consipio seek to enforce immediate repayment. In any event, the Company does not believe that the acceleration of the Note by Consipio, if not rescinded, will have a material adverse effect on the Company, as the Note is fully collateralized by 4,950,000 shares of Private Media Group, Inc. Common Stock pursuant to a guaranty agreement from Slingsby Enterprises Limited, an affiliate of the Company s principal shareholder, to Consipio.

During the six months ended June 30, 2004, the remaining balance of EUR 0.4 million on the $2.0 million loan from Beate Uhse AG was repaid and remaining balance on the $3.0 million loan from Beate Uhse AG was reduced by EUR 0.8 million. As of June 30, 2004 the remaining balance on this loan was EUR 1.8 million. As previously reported in the Company s Form 10-K for the year ended December 31, 2003, In December 2003, Beate Uhse AG notified Private Media Group, Inc. that the full loan amount was due and payable and offered to extend the loan maturity, subject to receipt of adequate collateral. Subsequently, Beate Uhse AG proposed an agreement whereby, so long as Private and Beate Uhse continued to maintain a business relationship, no action would be taken to enforce repayment of the $ 3 Million Beate Uhse Loan, and that loan payments would be made from credits based upon orders by specified Beate Uhse companies to specified Private Media Group companies, as was done with the $ 2 million Beate Uhse loan. Beate Uhse offered that this arrangement would be acceptable until December 31, 2005 and that any outstanding balance on the loan would have to be paid by then. Although no formal agreement has been reached with Beate Uhse AG regarding the restructuring of the $ 3 Million Beate Uhse Loan, and there are no assurances that an agreement will be reached, the Company expects that an agreement satisfactory to the Company will be reached.

Pursuant to securities purchase agreements entered into in 2003 separately with four accredited institutional investors we agreed to issue and sell to each of these investors convertible notes in the aggregate principal amount of $2.25 million. Effective January 2004, one investor converted $0.3 million (EUR 0.2 million) of principal into common stock. As of June 30, 2004 the remaining balance on the convertible notes was $1.95 million (EUR 1.6 million).

In May 2003 Euro 1.65 million of the related party note payable was re-financed by an institutional lender at the same interest rate as on the note payable, EURIBOR + 1%. The loan is repayable in equal monthly installments over a four year period starting June 29, 2004. The loan is guaranteed by the Company s principal shareholder and affiliates of the Company s principal shareholder. During the six months ended June 30, 2004, the Company repaid Euro 0.1 million and subsequently the remaining balance was Euro 1.55 million.

Contractual obligations

During the six-month period ended June 30, 2004, we have not experienced any material changes in our contractual obligations compared to what was reported in our Form 10-K for the year ended December 31, 2003.

Outlook

We expect growth in 2004, particularly in the broadcasting, DVD and Internet segments. As a result of expected improvements in cash-flow, the Company will start acquiring productions at a normal rate during the fall of 2004 and resume its normal release frequency of new movies in the near future.

In July 2004 the construction of our building was completed and we expect to formally receive the building from the contractor in August. As a result of our change in strategy, the Company has been reevaluating its need for additional space and presently we expect to be selling all, or a substantial part, of the building in parts during 2004 and 2005. We expect the net proceeds from sale of the building to cover additional investments in our content library and repayments on short-term and long-term debt during the same period.

We expect that our available cash resources and cash generated from operations and the sale of real estate will be sufficient to meet our presently anticipated working capital and capital expenditure requirements for at least the next 12 months. However, we may need to raise additional funds to support more rapid expansion or respond to unanticipated requirements.

If additional funds are raised through the issuance of equity securities, our shareholders percentage ownership will be reduced, they may experience additional dilution, or these newly issued equity securities may have rights, preferences, or privileges senior to those of our current shareholders. Additional financing may not be available when needed on terms favorable to us, or at all. If adequate funds are not available or are not available on acceptable terms, we may be unable to develop or enhance our products and services, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements, which could harm our business.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

We do not use derivative financial instruments for trading purposes and were never a party to any derivative, swap or option contracts. We do not hedge our interest rate or foreign currency exchange rate exposures.

As our cash and cash equivalent and short-term investments consist principally of money market securities and investments in short-term debt or equity securities and our borrowings are primarily at fixed rates of interest our market risk related to fluctuations in interest rates is limited. Accordingly, a one percentage change in market interest rates would not have a material impact on our results of operations.

We transact our business in various currencies, principally the Euro and the U.S dollar and certain other European Union currencies. We generally attempt to limit exposure to currency rate fluctuations by matching transaction currencies (revenues/expenses) to the functional currency of its operating subsidiaries. Our exposure to market risk for fluctuations in foreign currency exchange rates relates primarily to fluctuations in the Euro versus the U.S dollar. We translate our consolidated subsidiaries whose functional currency is not the euro into the euro for reporting purposes. Income statement amounts are translated into euros using the average exchange rate for the fiscal year. The balance sheet is translated at the year-end exchange rate. Due to the significance of the results reported in dollars the impact of the euro/dollar exchange rate on our major categories of revenue and expense can be material.

Item 4. Controls and Procedures

The Company maintains disclosure controls and procedures designed to ensure that information required to be disclosed in reports filed under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the specified time periods. As of the end of the period covered by this report, the Company s Chief Executive Officer and Chief Financial Officer evaluated, with the participation of the Company s management, the effectiveness of the Company s disclosure controls and procedures. Based on the evaluation, which disclosed no significant deficiencies or material weaknesses, the Company s Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures are effective. There were no changes in the Company s internal control over financial reporting that occurred during the Company s most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 2. Changes in Securities and Use of Proceeds

In the fall of 2003 we sold convertible notes to four accredited institutional investors in the aggregate principal amount of $2.25 million. Interest on the convertible notes accrues at the rate of 7%, and is payable quarterly in cash or common stock, at the election of the Company, based upon a weighted average market price during the 15 trading days preceding payment. The notes are convertible at the option of the holder at a fixed conversion price of $2.00.

In 2004 we issued an aggregate of 39,455 shares of common stock in payment of $88,512 of accrued interest under the notes. The issuance of the common stock is deemed to be exempt from the registration requirement of the Securities Act of 1933, as amended, in reliance on Section 4(2) of the Securities Act and Regulation D promulgated thereunder, as it was sold to institutional investors believed to be accredited investors and was made without general solicitation or advertising.

Item 6. Exhibits and Reports on Form 8-K

a. Exhibits:

31.1 Certifications pursuant to Rule 13a-14 under the Securities Exchange Act of 1934.

31.2 Certifications pursuant to Rule 13a-14 under the Securities Exchange Act of 1934.

32.1 Certification of CEO and CFO Pursuant to 18 U.S.C. § 1350, as Adopted Pursuant to § 906 of the Sarbanes-Oxley Act of 2002.

b. Reports on Form 8-K:

None

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

PRIVATE MEDIA GROUP, INC.
(Registrant)

Date: August 16, 2004

/s/ Johan Gillborg

Johan Gillborg, Chief Financial Officer