SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 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.

(Name of Registrant as specified in its Charter)

Nevada	**87-0365673**

(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**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

(Issuer s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Exchange Act: None

Securities registered pursuant to Section 12(g) of the Exchange Act: Common Stock, $0.001 par value.

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 1b-2 of the Act). Yes ¨ No x

At June 30, 2004, the aggregate market value of the voting stock and non-voting common equity held by non-affiliates of the registrant was $44,278,393. The aggregate market value has been computed by reference to the last sales price of the common stock on June 30, 2004.

On March 18, 2005 the registrant had 50,159,312 shares of Common Stock outstanding.

PART I

ITEM 1. DESCRIPTION OF BUSINESS

This Report includes forward-looking statements. Statements other than statements of historical fact included in this Report, including the statements under the headings Management s Discussion and Analysis of Financial Condition and Results of Operations, Business and elsewhere in this Report regarding future events or prospects, are forward-looking statements. The words may, will, expect, anticipate, believ estimate, plan, intend, should or variations of these words, as well as other statements regarding matters that are not historical fact, constitute forward-looking statements. We have based these forward-looking statements on our current view with respect to future events and financial performance. These views involve a number of risks and uncertainties which could cause actual results to differ materially from those we predict in our forward-looking statements and from our past performance. Although we believe that the estimates and projections reflected in our forward-looking statements are reasonable, they may prove incorrect, and our actual results may differ, as a result of the following uncertainties and assumptions:

- *our business development, operating development and financial condition;*
- *our expectations of growth in demand for our products and services;*
- *our expansion and acquisition plans;*
- *the impact of expansion on our revenue potential, cost basis and margins;*
- *the effects of regulatory developments and legal proceedings on our business;*
- *the impact of exchange rate fluctuations; and*
- *our ability to obtain additional financing.*

We do not intend to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise except to the extent required by law. You should interpret all subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf as being expressly qualified by the cautionary statements in this Report. As a result, you should not place undue reliance on these forward-looking statements.

THE COMPANY

OVERVIEW

Private Media Group, Inc., a US incorporated company, and its subsidiaries (together referred to hereinafter as Private Media Group , we or us) is a leading international provider of high quality adult media content for a wide range of media platforms. Any references in this report to Milcap Media Group refers to Milcap Media Group S.L. (Spain), and Milcap Media Limited refers to Milcap Media Limited (Cyprus).

Private Media Group, Inc. is incorporated in the State of Nevada. In accordance with Nevada law we maintain a registered office at 3230 Flamingo Road, Suite 156, Las Vegas, Nevada. Our European headquarters are located at the offices of one of our principal operating subsidiaries, Milcap Media Group, S.L. ,whose address is Carretera de Rubí 22-26, 08190 Sant Cugat del Vallès, Barcelona, Spain, telephone + 34-93-590-7070.

We acquire worldwide rights to still photography and motion pictures tailored to our specifications from independent directors and process these images into products suitable for popular media formats such as print publications, videotapes , DVDs and electronic media content for Internet distribution. We distribute our adult media content directly, and through a network of local affiliates and independent distributors, through multiple channels, including (1) newsstands, video rental stores, travel retail and adult bookstores, (2) mail order catalogues, (3) cable, satellite and hotel television programming, (4) over the Internet via proprietary websites and broadband delivery services and (5) wireless telephony. In addition to media content, we also market and distribute branded leisure and novelty products oriented to the adult entertainment lifestyle and generate additional sales through the licensing of our *Private* trademark to third parties. In the fiscal year ended December 31, 2004, we had net sales of EUR 35.6 million and net income of EUR 0.2 million.

Our business was founded in 1965 and achieved initial success through our flagship publication, *Private*, the first full color, hard-core sex publication in the world. Today, we produce four X-rated periodical magazines: *Private, Pirate, Triple X* and *Private Sex*, as well as several special feature publications each year. As of December 31, 2004, we had compiled a digital archive of more than two million photographs and all of our 432 print publications. We expect to add two additional issues and hundreds of photographs each month to this archive. Approximately 300,000 copies of our print publications are distributed each month at an average retail price of approximately Euro 11.50. We distribute our publications through a network of approximately 250,000 points of sale in more than 40 countries, with strong market positions in Europe, Latin America, Australia and Canada. We believe that our distribution network has the potential to reach nearly 500,000 points of sale in our existing markets.

Since 1992, we have also acquired, processed and distributed adult motion picture entertainment. We acquire worldwide rights to motion pictures that meet our exacting standards for entertainment content and production value from independent directors, either under exclusive contracts or on a freelance basis. We then edit and process these motion pictures to ensure consistent image quality and prepare and customize them for distribution in several formats, including DVDs, videocassettes, broadcasting, which includes cable, satellite, broadband and hotel television programming, and the Internet. Our proprietary motion pictures and those produced by joint ventures in which we participate have received more than 100 industry awards since 1994, evidencing our success in setting high quality standards for our industry. As of December 31, 2004, our movie library contained close to 800 titles. We expect to add more than 100 titles in 2005.

We launched our first Internet website, *www.private.com*, in 1997. We now own a number of sites directed at specific customer bases, including www.privatespeed.com and www.private.com/shop. We also generate incremental sales by licensing our trademarks and proprietary adult media content for use on the websites of other companies.

Since 1997, we have expanded our presence in emerging electronic markets for adult media content, such as the Internet, broadcasting and are currently in the process of launching products developed for use on hand-held devices including both mobile phones and Personal Digital Assistants. We believe that these technologies represent a substantial growth opportunity for us in the future.

In addition, we license our content to cable and satellite television operators as well as to hotels. We have also launched three television channels, *Private Gold*, *Private Blue and Private Fantasy*, that broadcast our content. Consumers pay for these products either on a pay-per-view basis or by subscription.

We operate in a highly regulated industry. This requires us to be socially aware and sensitive to government strictures, including laws and regulations designed to protect minors and to prohibit the distribution of obscene material. We take great care to comply with all applicable governmental laws and regulations in each jurisdiction where we conduct business. Moreover, we do not knowingly engage the services of any business or individual that does not adhere to the same standards. Since 1965, we have never been held to have violated any laws or regulations regarding obscenity or the protection of minors.

Private, Private Media, our *Private* logo, *Pirate, Triple-X, Triple-X Files, Private Black Label, Private XXX, Gaia, Private Sex, Private Life, Private Style, www.privatespeed.com, Private Gold, Private Blue, www.private.com, www.prvt.com, www.privatelive.com, www.privatechannels.com, www.sex.se, www.privatepda.com*, www.privatenightclub.com, *www.privateathome.com*, www.privatestars.com, *www.private.com/shop*, and *www.privategold.com* are some of our trademarks and trade names. Other marks used in this Report are the property of their owners, which includes us in some instances. Information on these websites is not a part of this Report.

Market Opportunity

Demand for adult entertainment products has grown substantially in recent years. We believe that the total worldwide adult entertainment market exceeds $56 billion annually. Of this market, we believe that our target market, including print publications, videocassettes, DVDs, broadcasting and the Internet, comprises more than $40 billion. We believe that two principal factors are driving growth in our industry: the relaxation of social and legal restrictions on distribution of adult entertainment products and new technologies that facilitate the distribution of high quality adult media content to consumers in the privacy of their own homes. As a result of liberalized regulation of adult entertainment products, we now distribute our products in physical form in more than 40 countries worldwide with an aggregate current population of 1.1 billion, as compared to six European countries with a population of 144 million when the current management took over in 1991. We expect this liberalizing trend to continue, which should expand our potential markets further in the future.

The proliferation of easy to use electronic equipment, such as VCRs and DVD players, which allow consumers to view high quality video products in the privacy of their home, has boosted demand for adult media content compatible with these formats. For example, DVD players have been adopted by consumers faster than any other electronic device ever, including the cell phone and personal computer.

Also, the evolution of the Internet as a channel of commerce and content distribution has stimulated additional demand for adult media content. In addition, advances in cable, satellite and hotel communications systems furnish another relatively new channel for the delivery of media content, including adult entertainment, into private homes, hotels and businesses.

More recently, the telecommunications industry has shown considerable interest in the use of adult content on hand-held devices such as mobile telephones, PDAs and other wireless activated devices. This provides an additional and exciting new source of potential revenues for us as one of the principal providers of adult content.

We expect these regulatory and technological developments to fuel increasing demand worldwide for adult media content, including demand for our products. In addition, we believe that market demand for content to fill new media outlets will lead mainstream media content providers to seek still more adult media content in the future. We expect that the high quality standards of the mainstream media, technological demands of multiple delivery formats and global marketing and distribution costs will increase capital requirements for providers of adult media content. While the adult entertainment industry is currently characterized by a large number of relatively small producers and distributors, we believe that the factors discussed above will cause smaller, thinly capitalized producers to seek partners or exit the adult entertainment business, leading to a consolidation of the adult entertainment industry.

Our Competitive Strengths

We believe the following strengths, among others, will enable us to exploit the growing global market for adult entertainment:

Extensive library of high quality adult media content

We have an extensive library of high quality adult media content. As of December 31, 2004, our library included still photographs developed for more than 400 back-issues of magazines and close to 800 movies. We hold exclusive worldwide rights to this entire content archive. This has enabled us to enter into global distribution arrangements with a wide range of media content providers, including leading international companies. To facilitate electronic distribution of our products, we have converted our entire archive of print images into a digital format. We are currently digitizing our motion picture archive as well, and have now stored most of our existing motion pictures in digital form. We believe that this electronic archive constitutes one of the largest libraries of high quality adult media content in the world.

Recognized brand name

We believe that our target customers associate the *Private* brand name with high quality adult entertainment products and services. This name recognition attracts leading producers of adult media content, as well as distributors and prospective joint venture partners interested in working with Private Media Group. We believe that the strength of our brand name leads to more favorable economic terms than we could otherwise obtain in our processing and distribution contracts, and enables us to negotiate favorable revenue sharing arrangements and joint ventures from which we derive significant licensing fees and royalty income. We have entered into joint venture and co-branding agreements with leading participants in our industry and other related industries, including Playboy and Penthouse. We seek to strengthen awareness of our brand name by consistently featuring the *Private* label prominently in our product packaging, cross-promoting our own products, selectively sponsoring athletes and distributing under the *Private* label complementary or ancillary non-media products that are consistent with an adult entertainment lifestyle. We believe that these activities engender a loyal customer base which, in turn, enables us to grow even with relatively modest external advertising and marketing expenditures.

Established market position and distribution network

We have a well-established worldwide distribution network which has been built up over the past 40 years, including some 250,000 points of sale in over 40 countries as of December 31, 2004. In many markets, we believe that our established presence hinders our competitors ability to break into the market. In some cases, exclusive distribution agreements improve our market position further. This broad distribution network provides an effective channel to introduce new products and services and new formats for existing products and services. For example, we were able to utilize our existing video distribution channels to reach customers with our DVD-based products. In electronic media categories, we have entered into strategic alliances with a number of leading international service providers. In addition, we have assembled an internal team of Internet specialists to maintain and improve our Internet infrastructure and electronic products and services. We believe that our broad, multi-format distribution network affords our customers convenient access to high quality adult media content in the format of their choice.

Flexible operating structure and access to substantial capital

We acquire adult media content from third-party directors on a project basis. This approach gives us substantial flexibility in terms of production volume and delivery time, significantly reduces our fixed production overhead and largely eliminates the risk to us of cost overruns in production. Because of our multiple product and service formats and broad distribution network, we can afford to hire top directors in the industry, which we believe results in a higher quality product for our customers. Similarly, we reduce our fixed processing costs by outsourcing editing and duplication functions for most of our products, although we retain oversight of the overall production process for cost and quality control purposes. As a public company with access to the capital markets we believe that we will have sufficient financial resources to increase our production and grow through acquisitions without sacrificing our high quality standards. However, we cannot guarantee that funds will be available from the capital markets when needed.

Experienced professional management

Our management team has extensive experience in the production and distribution of adult media content and in general business administration. Berth H. Milton, our Chairman of the Board and Chief Executive Officer, has extensive knowledge of our industry and has successfully founded and developed other profitable businesses. Other members of our management team have broad expertise in content production, sales and marketing, technology and finance, and have contributed to our record of growth in our core business and in acquiring and integrating companies in related businesses.

Our Strategy

Our vision is to be the world s preferred content provider of adult entertainment to consumers anywhere, at any time and across all distribution platforms and devices. We have developed the strategies described below to increase sales and operating margins while maintaining the quality of our products and services and the integrity of our brand name.

Develop strategic alliances and joint ventures with businesses outside of the adult entertainment industry to broaden our distribution channels. We are entering into strategic alliances and joint ventures with leading media companies outside of the adult entertainment industry to distribute our adult media content for use on popular and newly developing media formats, including revenue sharing relationships with cable and satellite television operators and Internet service providers with significant market positions. We expect these initiatives to widen the scope of our distribution network, enabling us to reach new customers while supplying our partners and licensees with content.

To be at the forefront of the adult entertainment industry in adapting new technology and distribution channels such as broadband distribution of our motion pictures. By actively seeking out and utilizing advanced technologies to distribute our content such as, broadband, Internet ,cable and satellite television and wireless devices we expect to increase revenues with minimal incremental cost.

Increase market share through strategic acquisitions. The adult entertainment industry is currently fragmented and consolidating. We expect this trend to continue as small, privately owned companies seek to exit from the business. We plan to expand our market presence and increase our market share by acquiring local distributors in the markets in which we compete. In addition, we may seek to acquire existing business enterprises in other related businesses opportunistically. To finance future acquisitions, we expect to use a combination of debt and equity. As one of the few companies in our industry with publicly listed common stock, we believe that we will have a significant advantage over most of our competitors in financing such consolidating acquisitions.

To complete the digitalization of our entire movie and photograph library in order to prepare our library for distribution in new electronic media. We have developed an extensive library of motion pictures and other pictorial content. Until recently, this library was archived on a master print, which would allow duplication in traditional media. New forms of electronic distribution provide us with an opportunity to use this content by distributing it through new forms of media, such as, Internet ,broadband and wireless devices. To facilitate electronic distribution of our products, we have converted our entire archive of print images into a digital format. We are currently digitizing our motion picture archive as well, and have now stored most of our existing motion pictures in digital form.

Continue to increase and strengthen brand awareness. We have developed strong brand awareness within each of our magazines and videos targeted markets. We own the worldwide rights to all of our content. We seek to strengthen awareness of our brand name by consistently featuring the *Private* label prominently in our product packaging, cross-promoting our own products, selectively sponsoring sports and distributing under the *Private* label complementary or ancillary non-media products that are consistent with an adult entertainment lifestyle.

Our Principal Products and Markets

Magazine Publications

We are the publisher of *Private*, an international X-rated magazine. *Private* was founded in 1965, and was the first full color, hardcore sex publication in the world. Today, we produce four X-rated magazines which are released bi-monthly: *Private, Pirate*, *Triple X* and *Private Sex*. In addition, special editions are released monthly and a book, *The Best of Private*, is released annually. We distribute these magazines through newsstands and other retail outlets.

Movie Productions

Since 1992, we have acquired and distributed adult motion picture entertainment. These productions generally feature men and women in a variety of erotic and sexual situations, generally in both hardcore and softcore versions. We distribute these movies primarily on videocassettes, DVDs, through cable, satellite and hotel television programming and over the Internet. We maintain the ownership and copyrights of every movie we finance and produce.

We expect to produce approximately 80 X-rated and 36 R-rated movies in 2005, with distribution through a worldwide network that covers approximately 60,000 points of sale, including primarily video shops and adult book stores. We believe we have the potential to reach more than 155,000 points of sale. We have also worked together on creating labels with other recognized brands, including, in 2000 the introduction of a the *Private Penthouse Video label* in conjunction with Penthouse.

As of December 31, 2004, our movie library contained close to 800 movie titles. All titles are available on videocassette and DVD. These products are sold by distributors, primarily to retail stores and wholesalers worldwide. Many of our original motion picture programs have also been re-edited and licensed to cable, satellite and hotel television operators.

Internet

We launched our first Internet website, *private.com*, in 1997. We now own a number of sites directed at specific customer bases, including *privatespeed.com* and *private.com/shop*. We also generate incremental sales by licensing our trademarks and proprietary adult media content for use on the websites of other companies.

The Internet team has combined Private Media Group s extensive media library with the most advanced technology to take advantage of the growth of Internet access and new distribution methods. Private has developed several key product offerings which include a subscription based service, broadband video on demand site, live sex chat service, adult personals, DVD rental service, and e-commerce shop.

In 2003, Private took the decision to outsource the Internet operations in order to lower operational expenses and increase its profit margin. This move will allow Private to focus solely on its strategic marketing and sales plan for the future growth of its catalogue of online products.

Other Markets

In April 1996, we launched our Private Collection International, Inc. line of adult pleasure products. We also license the Private name in connection with various lines of clothes, nutritional supplements, and energy soft drinks. Channels of distribution for licensed products include conventional distribution channels, e-commerce and television home shopping.

History

The parent company, Private Media Group, Inc., was originally incorporated in 1980 as a Utah corporation under the name Glacier Investment Company, Inc. for the purpose of acquiring or merging with an established company. In 1991, we changed our domicile to the State of Nevada. The parent company had no material business activity prior to its acquisition of Milcap Media Limited and Cine Craft Limited in June 1998.

On December 19, 1997 Private Media Group, Inc. entered into acquisition agreements with Milcap Media Limited and Cine Craft Limited to acquire all of their outstanding capital stock in exchange for 22,500,000 shares of Common Stock, 7,000,000 shares of the $4.00 Series A Preferred Stock, and 2,625,000 common stock purchase warrants. Private Media Group, Inc. completed these acquisitions on June 12, 1998. In connection with these acquisitions, in December 1997 the parent company changed its corporate name to Private Media Group, Inc. and declared a one for five reverse split of its Common Stock.

On January 28, 2000, we acquired all of the outstanding shares of Extasy Video B.V. for total consideration of Euro 3.2 million. The consideration consisted of 208,464 shares of common stock and warrants to purchase 208,464 shares of common stock. The warrants were exercisable during the period January 28, 2001 to January 28, 2004 at an exercise price of $9.63.

In May 2000, we authorized a three-for-one stock dividend on our common stock, which was distributed to holders of record of common stock on May 30, 2000.

As of January 1, 2001, we acquired Coldfair Holdings Ltd., a company incorporated and organized under the laws of the Republic of Cyprus, for a total consideration of Euro 1.5 million payable in 248,889 shares of common stock. Coldfair Holdings is a company engaged in the marketing and sale of adult entertainment products and services.

Effective April 1, 2001, we acquired the inventory and certain contracts of our U.S. distributor, Private USA, in exchange for Euro 1.0 million and the assumption of Private USA s obligations under some contracts.

On April 8, 2001, Peach Entertainment Distribution AB (Sweden), a subsidiary of Private Media Group, Inc., sold its interest in Private Circle, Inc., a company engaged in the design, production and marketing of trendy casual apparel, for an adjusted consideration of Euro 2.9 million as of May 2001.

On December 31, 2002, we acquired all of the outstanding shares of Barbuda B.V., a company owning a building, for total consideration of Euro 10.0 million. The consideration consisted of cash and a note payable in the amount of Euro 6.6 million. The purpose of this transaction was to acquire this property as its European headquarters. Since the acquisition, the Company has been reevaluating its need for additional space and as of February 2005, the Company no longer owns this property, see Note 22 subsequent events in the consolidated financial statements.

On May 30, 2003 the Company acquired certain assets, including governmental film board approvals and distribution rights from its former Canadian distributor, Software Entertainment Ltd. In exchange for Euro 0.7 million.

On November 26, 2003 the Company entered into an Asset Purchase Agreement to acquire certain intangible assets from International Film Production and Distribution Limited, including certain rights and distribution and licensing agreements. The transaction closed on November 28, 2003. The consideration for the transaction was Euro 2.5 million.

INDUSTRY OVERVIEW

The adult entertainment industry has evolved rapidly in recent years. In spite of often intense political campaigning, there has been a general trend towards wider acceptance of adult entertainment content among the general public and mainstream media channels. New technologies have lowered costs and changed the way in which adult content is produced, distributed and viewed. Lower costs, in particular, have lowered barriers to entry and increased competition in the adult entertainment industry. The trend toward wider acceptance of sexually-explicit material and ongoing technological developments has created a large and growing global market for adult content.

Historically, the adult entertainment industry has attracted a considerable level of government and regulatory attention primarily due to obscenity, which has led to limitations on either the explicitness of content or the availability. Traditionally, to view adult material, consumers were required to purchase movies in a public environment or to go to an adult movie theatre or peepshow.

Through a process of evolution rather than revolution the adult entertainment industry has become more acceptable over time, with a relaxation of the regulations and guidelines governing the industry. For example, in the United Kingdom, one of Europe s more restrictive countries with respect to adult entertainment, there has been a gradual relaxation of what is suitable for public viewing. The British Board of Film Classification, BBFC, has introduced the `R18 category, allowing distribution of hardcore adult videos through licensed sex shops for the first time. The approval from the BBFC, and subsequent theatrical release of movies such as The Idiots and Intimacy have also broadened what is regarded as acceptable adult content.

New technologies have helped to legitimize the industry and increase the size of the market. During the 1980s, the introduction of adult movies on videocassette and through broadcasting on cable and satellite television increased acceptance of adult media content by confining it to the privacy of the consumer s home. More recently, the Internet has become a primary distribution platform for both suppliers and consumers of adult media content providing low-cost delivery and increased privacy. Although currently under-exploited, third generation mobile and handheld devices are likely to increase the market even further in the future, making adult media content viewing mobile.

The production and distribution of adult media content is very competitive. Hundreds of companies are now producing and distributing movies to wholesalers and retailers, as well as directly to consumers. The low cost of high quality video cameras and equipment has significantly lowered the barrier to entry for production of adult media content. According to Adult Video News, annual worldwide release of movie titles peaked at 25,000 and is currently at 11,000 of which 4000 in US alone vs. 500 in Hollywood. The bulk of this production is represented by low quality, amateur productions, made for only a few thousand dollars, as opposed to the larger, professionally produced movies with high production values. Around 20 major producers, such as Private Media Group, Vivid, Video Company of America and Metro, release most high budget adult videos and DVDs. See Business-Competition. In addition, because it costs as little as $5,000 to establish an Internet presence, there is significant competition among distributors of adult media content over the Internet. The proliferation of websites distributing adult media content has itself fueled a greater and ongoing demand for the creation and licensing of new adult media content.

We believe that the global adult entertainment market exceeds $56 billion annually. This covers memberships and subscriptions, escort services, magazines, sex clubs, telephone sex lines, cable and satellite pay-per-view programming, adult videos and toys and other related products and services. In 1998, Forrester Research estimated the U.S. adult entertainment market at $10 billion annually. This compares to total U.S. cinema domestic box office receipts for mainstream motion pictures of over $9.3 billion in 2004, indicating the size and importance of the adult market within the entertainment industry.

Video and DVD Sales & Rental

Bringing adult movies into the privacy of the home through the introduction of videocassettes along with cable and satellite services all but eliminated the adult theatre business. The introduction of the DVD and its rapid acceptance by the public is gradually shifting the balance of home viewing from videos to DVDs. DVDs offer better picture and sound quality than videos, worldwide compatibility and other add-ons. The DVD format also benefits suppliers and retailers. Several languages can be combined onto one DVD, so only the DVD cover needs to be changed for different territories. Also, back catalogue sales should initially increase as consumers look to replace their videocassette library with the new format.

DVD players have been adopted by consumers faster than any other electronic device, including the cell phone and personal computer. 37 million DVD players were sold in the United states in 2004 and the installed base of DVD players reached 70 million households. The Digital Entertainment Group (US) estimates that more than 80% of US households will have at least one DVD player by the end of 2005. Consumers spent a record $21.2 billion renting and buying DVDs in 2004. DVD retail sales grew to $15.5 billion in 2004, an increase of 33 percent over last year.

In 2000, total sales and rentals of adult videos and DVDs in the United States were approximately $ 4.0 billion according to Adult Video News estimates, including sales through general interest retailers and dedicated adult stores. In 2001, PR Week reported that the Free Speech Coalition estimated that 20% of all U.S. households with either cable or satellite television or a VCR watch adult movies.

Broadcasting

Cable and satellite television has brought adult media content into the privacy of the home. Technological developments, in particular the evolution of digital broadcasting, has not only increased the number of channels that can be delivered directly to the home via satellite (DTH or DBS) and cable, but has also led to the development of on-demand technologies such as Video On Demand (VOD) and Near Vide On Demand (NVOD). The development of these services is benefiting the adult entertainment industry by providing a greater number of special interest channels allowing platform providers to target niche audience and also provide premium tier, Pay-Per-View (PPV) and subscription services.

General growth in the PPV market in the US and Western Europe is expected to result in part from cable system digitization upgrades utilizing fiber-optic, digital compression technologies or other bandwidth expansion methods that provide cable operators additional channel capacity. Cable operators have begun the shift from analog to digital technology in order to upgrade their cable systems and to respond to competition from DBS (Digital Broadcast Satellite) providers who offer programming in a 100% digital environment. When implemented, digital compression technology increases channel capacity, improves audio and video quality, provides fully secure scrambled signals, allows advanced set-top boxes for increased interactivity, and provides for integrated electronic programming guides (EPG). Cable operators are also using their upgraded plants to provide their digital customers with VOD (Video-On-Demand) services. For the most part, the appeal of VOD to adult video consumers is no different than it is to consumers of other genres: VOD gives subscribers the opportunity to purchase movies impulsively, and the ability to watch movies exactly when, where and as often as they want. However, the ability to pause, rewind and fast-forward a VOD program - essentially mimicking the functionality of a DVD - may hold even more appeal for adult video consumers.

Adult services will serve as an important driver to cable systems in their efforts to convert analogue subscribers to digital services. Private Media Group expects that all of its future cable launches will be on a digital platform.

United States

According to the National Cable and Telecommunications Association (NCTA), Cable MSOs deliver service to approximately 72 million basic households in the United States as of September 2004 and approximately 24.3 million received digital cable service. The NCTA estimates that by 2006 there will be 48.6 million digital cable subscribers. NCTA reported in its 2004 Year-End Industry Overview that there were a total of 24 million DBS households as of September 2004 (DirecTV provides services to 13.5 million households and EchoStar Communications Corporation s DISH Network (DISH) provides services to 10.5 million households). During 2004, DirecTV and DISH gained 3 million net new subscribers. Kagan estimates that DBS will grow to 26 million subscribers by the year 2006. Based on the above sources, we estimate the number of digital cable and satellite subscribers for 2006 to be approximately 75 million households, a growth of 54%.

Turning to the adult entertainment segment, content distribution has evolved over the past twenty-five years from home video platforms (video cassette) to cable television systems and DBS providers via PPV, and more recently to VOD. In the early 1980 s, cable television operators began offering subscription and PPV adult programming from network providers such as Playboy Enterprises, Inc. Kagan estimates that adult PPV revenue generated by cable systems and DBS providers in 2002 was $609 million, representing an increase of 15% from revenues of $529 million generated by the category in 2001. Kagan projects revenues from the adult category to grow to $917 million by the year 2006.

VOD availability is becoming increasingly widespread and is now on its way to becoming a mainstream content-delivery platform. Kagan research (*Video-On-Demand 2005: A Strategic and Economic Analysis*) indicates that nearly 20 mil. homes had VOD by the end of 2004, a number that is on track to nearly double to 39.2 mil. by the end of 2008. Kagan estimate that VOD revenue and cable VOD revenue from movies and TV series more than doubled from $157 mil. in 2003 to $318 mil. in 2004. By 2006, VOD revenue will comprise the majority of the PPV/VOD revenue sector. In 2007, Kagan estimates that cable VOD revenue (from all sources, including adult and SVOD) will cross the $2 billion mark on its way to $6 billion in 2013.

Europe

According to a March 2005 report from Strategy Analytics, Inc. (*Digital TV in Western Europe: Market Outlook & Analysis*), approximately 25 million households received digital satellite service and 7.6 million households received digital cable service. The report estimates that by 2010 there will be 49.1 million digital satellite subscribers and 28.9 million digital cable subscribers. Based on the report, the total estimated number of digital cable and satellite subscribers in Europe for 2010 is approximately 78 million households, a growth of 139%.

Internet

The adult entertainment industry was among the first to commercially exploit the Internet as a distribution channel and is, together with gambling and online games, among the few industries which generate profit on the Internet. The Internet offers relative privacy for users, a seemingly endless selection of adult media content and can provide immediate delivery.

Pay sites contain most of the adult media content on the Internet, but free sites are also common and are primarily supported by advertising from pay sites. Free sites get a few cents for each viewer who clicks on an advertising banner. The banner then transports these viewers to a site that tries to entice the user into paying for content using their credit cards. However, the bulk of revenues comes from pay sites.

As of March 2005 the number of Internet users in the European Union and United States was 206 million and 201 million, respectively, which represent a growth over the past five years of 121% and 111%, respectively. The total number of Internet users in the world as of March 2005 was 889 million. Based on information from RHK Inc. the Company estimates global adult entertainment Internet revenues to have grown from nothing to more than US$3 billion in 2004, in less than ten years. Furthermore, RHK Inc. estimates global adult entertainment Internet revenues, exclusive of revenues from online Video-on-Demand (VOD), to grow to more than US$5 billion by 2007.

The use of the Internet for viewing adult media content is expected to increase significantly. Broadband Internet access is transforming the way that millions of consumers use and pay for news, entertainment, music and other media. Consumers will use their Internet high-speed, always-on broadband connections to access and pay for entertainment content, including adult content, and services. According to analysis and forecasts, global broadband subscriptions were estimated to have grown by 50% to 150 million[1] during 2004 and by 2009 the number of broadband subscribers is expected to grow to more than 287 million[2]. Although VOD online is still in its absolute infancy and VOD via cable is the default delivery pipe at the moment, it is interesting to note that forecasts[2] see global VOD online consumer spend going from US$ 70 million in 2003 to US$ 2.34 billion in 2007, representing a CAGR of 142%.

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1 Point Topic Ltd's (UK) World broadband market analysis of 16 December 2004.
2 Forecasted by RHK, Inc (USA)

The increased availability of adult media content on the Internet has attracted considerable attention. Concerns have arisen with respect to child protection and the distribution of illegal material. In response to the issue of child protection, a number of software packages have become available that control the content that can be accessed from a personal computer. Products such as Surfcontrol, NetNanny, Websense and others can be employed to filter sites for inappropriate material, blocking access for unauthorized users.

In-Room Entertainment

The provision of in-room entertainment services by major hotel chains throughout the world also serves as a distribution channel for adult media content. In addition to a selection of mainstream movies, hotel guests often will have a choice of softcore, and frequently hardcore, adult videos available on a pay-per-view basis. In the United States, these services are provided by companies such as On Command and Lodgenet, which supply approximately 750,000 and 810,000 hotel rooms, respectively. Estimates by analysts cited to by the Los Angeles Times in 2001 suggest that adult movies generate approximately half of total hotel pay-per-view revenue in the United States, approximately $ 250 million annually. Outside of the United States, excluding more restrictive countries such as the United Kingdom, hotel guests also have access to hardcore material on a pay-per-view basis.

MAGAZINE PUBLICATIONS

Our publishing operations include the publication of the adult magazines identified in the table below, special editions consisting of previously published material and occasional newsstand specials, calendars and paperback books. All of these magazines, together with local editions, are printed under various trade names and are distributed in over 40 countries. We publish several customized editions of our four principal magazines. Each edition contains the same editorial material but provides locally targeted content reflecting local governmental regulation regarding explicit adult publications. Most of our magazines feature pictures of men and women engaged in erotic and sexually explicit situations. We distribute approximately 200,000 copies of our print publications per month at an average retail price of approximately (Euro) 11.50. Our most popular publications are *Private, Pirate, Private Sex* and *Triple X*.

MAGAZINE LIBRARY

	As of December 31,	
	2004	**2003**
Title	**Nº of Issues**	**Nº of Issues**
Private	186	180
Pirate	88	82
Triple-X	62	56
Private Sex	53	47
Private Man	4	4
Mansize	4	4
Special Editions	19	14
Best of Private (Book)	15	14
Special Editions (Book)	1	1
Total	**432**	**402**

	Quantities of Magazines Produced (Printed, not sold)	
Title	**2004**	**2003**
Private	512,761	530,660
Pirate	390,531	380,905
Triple-X	340,901	365,465
Private Sex	298,221	318,825
Private Man		80,100
Mansize		154,125
Special Editions	317,451	309,190
Best of Private (Book)	42,420	
Total	**1,902,285**	**2,139,270**

Our publications offer a variety of features and have gained a loyal customer base. We believe we have earned a reputation for excellence by providing a high standard of quality to the adult entertainment industry, while we maintain circulation leadership as the leading hardcore magazine publisher. All of our publications have long been known for their graphic excellence and features, and publish the work of top artists and photographers in the field. They are also renowned for their pictorials of beautiful people. Our magazines command some of the highest prices in the industry.

All of our publications are printed by independent third parties. We have a longstanding relationship with several printers in Spain We believe that generally there is an adequate supply of printing services available to us at competitive prices, should the need for an alternative printer arise. All of our production and printing activities are coordinated through our operating facility maintained by our wholly owned subsidiary, Milcap Media Group.

Circulation

Our magazines have historically generated most of their revenues from firm sales distribution. However, now distributors with rights to return represent approximately 50% of our production. Single copy retail sales normally occur in adult book stores and similar establishments. Newsstand retail sales are permitted in most European countries, including France, Italy, Spain, Germany, Denmark, Sweden, Finland the Benelux countries and Portugal.

Our magazines are distributed to newsstands and other public retail outlets through a network of national distributors, who maintain a local network of several wholesale distributors and licensors. We have entered into national distribution agreements covering over 35 countries and generally deal with a magazine distributor for local distribution of our publications. We ship copies of each issue in bulk to our wholesalers, who distribute on to local retailers.

Independent distributors who distribute our magazines do so under individual distribution agreements. These agreements are normally subject to automatic yearly extensions unless either party terminates the arrangement.

For the past few years, we have sought to expand the use of our magazines content and other assets across different media formats. Our primary focus in recent years has been the re-editing and digitizing of every Private magazine for use on our websites. This content was initially available on our websites in May 1998, and we completed the digitization of our still photo archive in 2000.

Production, Distribution and Fulfillment

Four independent printers in Spain currently print most of our magazines, books, brochures and video and DVD covers. Printing costs vary based upon the price of component raw materials. The principal raw materials necessary for publication of our magazines are coated and uncoated paper. Paper prices are affected by a variety of factors, including demand, capacity, pulp supply and by general economic conditions. Our printers have a number of paper supply arrangements and we believe that those arrangements provide an adequate supply of paper for our needs. In any event, we believe that alternative sources are available at competitive prices. With respect to color separation, pre-press and related services, we currently use our own scanning facilities and have the support of two independent suppliers for color separations. We are also using the latest technologies in this field, such as digital imposition and computer-to-plate process technology, or CTP. CTP eliminates the need for the production of film/color separations during the pre-printing process, saving time and money while improving quality. In simple terms, CTP allows printers to receive computer disks containing electronic files (both text and graphics) and output those files directly to a plate. The result is a top quality image which takes minutes instead of hours to produce.

We print and ship all of our proprietary magazines from Barcelona, Spain. We determine the amount of printed publications bi-monthly with input from each of our national distributors. Most of our products are packaged and delivered directly by the printer or supplier, while Milcap Media Group provides warehousing, customer service and payment processing.

Our full-time editorial and post-production staff consists of an editor-in-chief, six executive editors and approximately seven editors, associate editors and assistant editors who oversee the quality and consistency of the artwork and editorial copy and manage the production schedule of each issue. The production of each issue requires the editors to coordinate the activities of a writer, a pencil artist, an inker, a colorist and a printer over a two-month period. The majority of this work is performed on our premises in Barcelona, Spain. We have entered into agreements with some photographers and writers under which such people have agreed to provide their services to us on an exclusive basis, generally for a period of one to three years.

MOVIE PRODUCTIONS

In 1992, we began releasing movies under the *Private* label. Our adult movies are in genres similar to our magazines and books under the titles listed in the table below. Normally, we spend on average between $ 50,000 and $ 125,000 per movie. This amount excludes the computation of the post-production, master production, duplication and distribution costs. Generally, Milcap Media Group creates and designs all artwork for promotional items and packaging and contracts for printing services. Since 1997, independent laboratories have duplicated all of our videocassettes for us. Similarly, since 1999 all DVDs have been duplicated by independent laboratories as well. A number of our labels, including *Private Gold, Private Black Label, Private Movies, The Private Life of* and *Private Reality Video* are released on a monthly basis while others are released on a bimonthly or less frequent basis. As of December 31, 2004, our movie library contained close to 800 movie titles. By the end of 2005, we expect the total to increase to more than 900 titles. All titles are available on both videocassette and DVD. We sell approximately 270,000 DVDs per month. We continue to expand our video operations in international markets and presently market our video products in over 40 countries.

MOVIE LIBRARY

	As of December 31,	
	2004	**2003**
Label	**Nº of Titles**	**Nº of Titles**
Amanda s Private Diary	5	5
Best - End of Year	9	9
Gaia	6	6
H**** Housewives	9	9
Mansize	2	2
Peepshow Special	12	12
Pirate Fetish Machine	16	13
Pirate Video	12	12
Pirate Video de Luxe	16	16
Private Black Label	35	33
Private Castings	50	50
Private Fantasies	5	5
Private Films	28	28
Private Gold	68	62
Private Interactive	1	1
Private Lust Treasures	9	9
Private Man	6	6
Private Movies	12	10
Private Reality Video	26	22
Private Sports	6	5
Private Stories	27	27
Private Superf***ers	12	12
Private Tropical	14	9
Private Video Magazine	26	26
Private X-Treme	16	10
Private XXX	16	15

Private-Ninn	4	4
Private-Penthouse Movies	12	12
The Best by Private	63	52
The Matador Series	15	15
The Private Life of	22	17
The Private Story of	3	
Triple X Files	12	12
Triple X Video	32	32
Virtualia	6	6
When Pornstars Play	2	1
Erotica (soft titles)	164	137
Total	**779**	**702**

We finance all of our adult movies, and we contract with movie producers on a flat fee basis. We have entered into agreements with some movie directors under which they have agreed to provide their services to us on an exclusive basis, generally for a period of one to three years. All producers generally assume production costs and obligations, including among other things, the delivery of rights and model releases.

Video Duplication/Production Techniques

Masters are customized and duplicated by our subsidiary Peach Entertainment Distribution and from there they are sent to different distributors and DVD duplication centers. Some distributors receive a master directly and do their own duplication. All artwork to print the video covers is created at Milcap Media Group. Most countries receive their own pre-printed covers from Spain and some countries print their own covers from artwork provided in digital format.

Distribution

We distribute our productions worldwide via masters, videocassettes and DVD s that are sold or rented in video stores, sex shops, newsstands and other retail outlets, and where permitted, through direct mail. Our website has contributed to increasing video and DVD sales, and we expect this new medium to become a significant distribution channel in the future.

We have entered into distribution agreements in over 40 countries. Under these distribution agreements, and according to the territory, one of our subsidiaries, Peach Entertainment Distribution or Milcap Media Group, agrees to provide a specific minimum number of new titles each month during the term of the agreement, and a licensee normally serves as the exclusive distributor throughout its own country or language territory. Under the various distribution agreements, licensees are normally required to purchase a minimum number of units for each monthly period during the term of the agreement. In countries such as Germany, we have expanded our relationships with our national distributor by entering into exclusive multi-year, multi-product output agreements. In countries such as the United States, the Benelux countries, France and Spain, we have established local subsidiaries for the purpose of owning or controlling local distribution. In general, however, we believe that national distribution agreements enable us to have an ongoing branded presence in international markets and to generate higher and more consistent revenues, than we could achieve selling directly to retailers.

We have licensed many of our original programs to cable television networks and adult pay-per-view television channels. These licenses generally grant the television channel owner a specific right of transmission and we retain the intellectual property rights of every production. We edit many of our new feature movie releases into several versions depending on the media through which they are to be distributed. In general, versions edited for cable, satellite and hotel television programming are less sexually explicit than the versions edited for home video distribution.

The DVD Market

Distribution of DVDs represents one of our fastest growing markets. We believe we set a high standard for DVDs in the adult entertainment industry, with each DVD released by us possessing five language options as well as four other subtitled languages. We believe that our multi-language DVD format provides a significant competitive advantage for us because it attracts consumers worldwide and expands our international marketing and sales potential. This global format allows us to reduce our overall unit production costs and increase profit margins. Currently, the majority of DVDs released by our competitors in the United States and worldwide are produced in only one language since they either license titles country-by-country or manufacture each title in separate languages, thus losing out on economies of scale, which further drives down our competitors profit margins.

Currently, mainstream movie titles are released on DVD in six Regional Codes or Zones. This is required primarily because producers often do not control the worldwide rights to their titles. Our DVDs are playable in any region, in every country in the world, because we own and control the global rights to everything we have produced. Our DVDs are also Internet Activated, which means that when a consumer plays the DVD in a personal computer, that person also gets a direct link to our websites, where they can view our content by purchasing a subscription or visit our extensive on-line shopping area. We also sometimes add `extras to our DVDs, including alternative endings to movies, interviews with the stars, biographical data on the actors, their roles in other in-house productions and publications.

Broadcasting Satellite & Cable

Since launching the broadcasting business in 2000, we have rapidly expanded in Eastern and Western Europe, Latin America and the United States. The broadcasting business was launched through an exclusive joint venture agreement with International Film Productions and Distributions, Ltd., (IFPD). IFPD is a European-based television broadcasting company associated with major content providers that specializes in the distribution of adult cable and satellite television channels. Under the joint venture agreement, IFPD was responsible for promoting and broadcasting PRVT s two adult channels, namely Private Gold (hardcore) and Private Blue (soft core), globally. The agreement provided PRVT with 65% of the gross profits generated from the broadcast of, and advertising on, these channels. Recently, the joint venture was dissolved and PRVT acquired the channel names Private Gold and Private Blue and is currently licensing them to affiliated companies of IFPD under a two-year agreement with a minimum guarantee. The license is worldwide excluding North and Latin America. In August 2003, we announced the launch of The Private Fantasy Channel.

The Private Blue & Private Gold Channels

The Private Blue channel was launched in United Kingdom, under an exclusive joint venture agreement with Zone Vision Enterprises (ZV), a UK-based television company, and IFPD. As mentioned above, PRVT acquired the channel name Private Blue, and is currently licensing it to an affiliate company of IFPD for a fixed fee. Private Blue is available through the analog and digital satellite platforms of BSkyB and the Telewest cable network in the United Kingdom. Private Blue is also available in Turkey on the DigiTurk platform, and in Hungary and Slovakia on the UPC networks, and in the Netherlands with MediaKabel. Private Blue also has an international satellite feed on the SIRIUS 2 satellite, which gives it access to subscribers in all territories of Europe from 23.00 to 05.00 Central European time every day of the year.

The Private Gold television channel is broadcasted under Dutch license, and is available on the HCA Cable Association platform in Hungary, Slovakia and the Czech Republic, and on the UPC Direct satellite network. Private Gold has an international satellite feed on the AMOS 1 satellite, which gives it access to subscribers in all territories in Europe from 24.00 to 04.00 Central European time, every day of the year. Private Gold has a second satellite feed, on the ASTRA satellite with Cryptoworks Encryption. ASTRA is one of the leading satellite systems for direct-to-home transmission of television, radio and multimedia services in Europe, and currently has a fleet of nine satellites and transmits to 22 European countries. The Private Gold channel were launched in Western Europe in 2001, under a joint venture agreement with Canal Digital AS and IFPD. Canal Digital distributes Private Gold in Sweden, Denmark and Finland. Canal Digital is jointly owned by Canal+ and Telenor. In 2001, Canal Digital had more than 1.1 million card customers and over 700,000 subscribers in the Nordic region.

Both Private Gold and Private Blue television channels were launched in Latin America in 2001, via the joint venture agreement with IFPD, and under a distribution agreement with Pramer S.C.A. Presently, PRVT holds this agreement directly with Pramer. Pramer is one of the largest companies in Latin America responsible for producing, distributing and commercializing content for cable and satellite television. Both channels are transmitted on the NSS 806 satellite that covers the entire South American continent, and reaches 15 million satellite and cable subscribers in the region.

In June 2004, we entered into an agreement with Comcast Cable Communications, LLC, (Comcast), to make the Spanish language version of the pay per view channel Private Blue available to Spanish speaking cable TV customers in the U.S. Comcast services over 21 million US cable TV customers.

In October 2004, the Private Gold television channel was launched on the Noos platform in France. Noos is the largest cable television operator in France, Following an agreement with Private Blue and Gold Broadcasting BV, a Private Media Group Licensee, the Private Gold channel will be offered to Noos subscribers on a monthly subscription basis. The adult entertainment channel will be broadcast from midnight to 5 am seven days a week. Noos distributes to more than 1.7 million subscribers.

We believe that currently the *Private Gold* and *Private Blue* channels are available in over 40 territories to approximately 43 million potential viewers worldwide.

The Private Fantasy Channel

Private Fantasy Channel (PFC) is distributed as a Pay-Per-View (PPV) service using PPV technology which enables cable television operators or satellite providers to sell a block of programming, an individual movie, or an event for a set fee. PPV technology also permits cable television operators or satellite providers to sell our programming on a monthly, quarterly, semiannual and annual basis. PPV programming is delivered through any number of delivery methods, including: (a) cable television; (b) DTH (Direct To Home) to households with large satellite dishes receiving a low-power analog or digital signal (C-Band) or DBS (Digital Broadcast Satellite services such as those currently offered in the US by EchoStar Communications Corporation and DirecTV); (c) wireless cable systems; and (d) low speed (dial-up) or broadband Internet connections (i.e., streaming video). The Company is not limited to use any of the described methods of delivery in the future. In order to produce and deliver the channel we have agreements with several subcontractors. The management, programming and output of an encrypted signal is currently carried out in Europe. The encrypted signal is thereafter delivered via cable or satellite to the distributor.

In August 2003, we entered into an agreement with EchoStar Satellite LLC to make the pay per view channel available to more than 9 million DISH Network satellite TV customers in the U.S. On February 4, 2004, the Private Fantasy channel became available to DISH Network satellite TV customers. During 2004 the DISH Network increased its subscription base to 10.5 million U.S. households.

Broadcasting Growth Potential

General growth in the PPV market in the US and Western Europe is expected to result in part from cable system digitization upgrades utilizing fiber-optic, digital compression technologies or other bandwidth expansion methods that provide cable operators additional channel capacity. Cable operators have begun the shift from analog to digital technology in order to upgrade their cable systems and to respond to competition from DBS (Digital Broadcast Satellite) providers who offer programming in a 100% digital environment. When implemented, digital compression technology increases channel capacity, improves audio and video quality, provides fully secure scrambled signals, allows advanced set-top boxes for increased interactivity, and provides for integrated electronic programming guides (EPG). Cable operators are also using their upgraded plants to provide their digital customers with VOD (Video-On-Demand) services. For the most part, the appeal of VOD to adult video consumers is no different than it is to consumers of other genres: VOD gives subscribers the opportunity to purchase movies impulsively, and the ability to watch movies exactly when, where and as often as they want. However, the ability to pause, rewind and fast-forward a VOD program essentially mimicking the functionality of a DVD may hold even more appeal for adult video consumers. We believe adult services will serve as an important driver to cable systems in their efforts to convert analogue subscribers to digital services. We expect all of our future launches to be on a digital platform.

Digital Cable and Satellite Development in the United States

According to the National Cable and Telecommunications Association (NCTA), Cable MSOs (multiple-systems-operators) deliver service to approximately 72 million basic households in the United States as of September 2004 and approximately 24.3 million received digital cable service. The NCTA estimates that by 2006 there will be 48.6 million digital cable subscribers. NCTA reported in its 2004 Year-End Industry Overview that there were a total of 24 million DBS households as of September 2004 (DirecTV provides services to 13.5 million households and EchoStar Communications Corporation s DISH Network (DISH) provides services to 10.5 million households). During 2004, DirecTV and DISH gained 3 million net new subscribers. Kagan estimates that DBS will grow to 26 million subscribers by the year 2006. Based on the above sources, the total estimated number of digital cable and satellite subscribers for 2006 is approximately 75 million households, a growth of 54%.

Video-On-Demand Development in the United States

VOD availability via cable is becoming increasingly widespread and is now on its way to becoming a mainstream content-delivery platform. Kagan research (*Video-On-Demand 2005: A Strategic and Economic Analysis*) indicates that nearly 20 mil. homes had VOD by the end of 2004, a number that is on track to nearly double to 39.2 mil. by the end of 2008. Kagan estimate that VOD revenue and cable VOD revenue from movies and TV series more than doubled from $157 mil. in 2003 to $318 mil. in 2004. By 2006, VOD revenue will comprise the majority of the PPV/VOD revenue sector. In 2007, Kagan estimates that cable VOD revenue (from all sources, including adult and SVOD) will cross the $2 billion mark on its way to $6 billion in 2013.

Digital Cable and Satellite Development in Europe

According to a March 2005 report from Strategy Analytics, Inc. (*Digital TV in Western Europe: Market Outlook & Analysis*), approximately 25 million households received digital satellite service and 7.6 million households received digital cable service. The report estimates that by 2010 there will be 49.1 million digital satellite subscribers and 28.9 million digital cable subscribers. Based on the report, the total estimated number of digital cable and satellite subscribers in Europe for 2010 is approximately 78 million households, a growth of 139%.

Broadcasting Broadband

Internet access is transforming the way that millions of consumers use and pay for news, entertainment, music and other media. Consumers are increasingly using their Internet high-speed, always-on broadband connections to access and pay for entertainment content, including adult content, and services. The Company is engaged in VOD broadcasting of its content over broadband via its proprietary websites and third party revenue share or licensing arrangements with VOD online aggregators and in 2004 the Company has experienced growth in this area.

According to analysis and forecasts, global broadband subscriptions were estimated to have grown by 50% to 150 million[3] during 2004 and by 2009 the number of broadband subscribers is expected to grow to more than 287 million[4]. Although VOD (Video on Demand) online is still in its absolute infancy and VOD via cable is the default delivery pipe at the moment, it is interesting to note that forecasts[5] see global VOD online consumer spend going from US$ 70 million in 2003 to US$ 2.34 billion in 2007, representing a CAGR (compound annual growth rate) of 142%.

Mobile Entertainment

The Company is engaged in licensing its content and trademarks for mobile entertainment services. Currently this is done together with third parties who manipulate the content to make it suitable for distribution via mobile telephone operators to consumers. The Company s content is currently distributed via more than twenty national and multinational mobile telephone operators, and available in thirteen countries in Europe and Asia. The market currently consist of SMS, games and rich-media mobile downloads including; MMS, wallpapers, screensavers, videoclips and videostreaming. Juniper Research estimates in its white paper *Adult to Mobile: Personal Services Second Edition (February 2005)* that the global mobile adult content market will more than triple over the next five years, to nearly US$2.1 billion by 2009.

In-Room Entertainment

In October 2001 we entered into an agreement with Quadriga Worldwide, a leading European hotel entertainment and service provider, to make a wide selection of our movies available to guests in hotels serviced. Quadriga presently provides hotels in 30 countries with interactive entertainment and information services, covering 489,000 hotel rooms worldwide, with an annual audience of 100 million hotel guests. Key customers of Quadriga include leading hotel chains such as: Hilton, Marriott, Intercontinental, Le Meridien, Sofitel, Novotel, Mercure, Sol Melia and Thistle Hotels. In addition to Quadriga we have agreements with other hotel entertainment and service providers.

Broadcasting - Licensing

Private licenses the right to use its content to broadcasters for a limited time period on a per title and territory basis.

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3 Point Topic Ltd's (UK) World broadband market analysis of 16 December 2004.
4 Forecasted by RHK, Inc (USA)
5 Forecasted by RHK, Inc (USA)

INTERNET SERVICES

Overview

Private Media Group s Internet team has combined its extensive media library with the most advanced technology to take advantage of the growth of Internet access and new distribution methods. Private has developed several key product offerings which include a subscription based service, broadband video on demand sites, live sex chat service, adult personals, DVD rental service, and e-commerce shop.

In 2003, Private took the decision to outsource the Internet operations in order to lower operational expenses and increase its profit margin. This move will allow Private to focus solely on its strategic marketing and sales plan for the future growth of its catalogue of online products.

Key Products

Private.com (www.private.com) is the flagship site of Private Media Group s Internet offerings. The site offers access to high-quality adult content that includes over 70 full-length Private movies, photosets, sex-stories, a full library of Private magazines in image and downloadable PDF format, and third-party content. In addition, subscribers receive access to live webcam, live sex shows performed by couples, and a adult personals. Premium content is also accessible through Private.com in a variety of different formats. The ability to purchase full-length DVD quality movies on a rental basis is available through Divx technology at a discounted rate for subscribers. One on one live chat is also accessible to members at a discounted rate. The site offers various payment methods to suit the ever-changing demands of the end-users that include credit card subscriptions, pay-per-minute diallers, debit cards, online cheques, and SMS payments. All payments are made through a secured system and verification process that are in-line with the International and local e-commerce regulations. Our websites are currently generating traffic of approximately 1.5 million visits per month and more than 25 million pages are viewed per month. The Private.com website features the most advance technology to enable Private to protect its digital assets from theft and file sharing through usage of Microsoft digital rights encryption and protection. Private also goes the extra step to protect its library by digitally watermarking all images. Private.com acquires customers primarily through advertising in DVDs, videos, magazines and broadcast programming with minimal incremental cost. It also acquires new customers by establishing partnerships with leading international portals. In 2004, Private.com sold over 72,000 memberships and had approx.10,000 active members at any time.

Private Shop (www.private.com/shop) offers a complete catalogue of Private products including Private DVDs and video titles, magazines, and adult toys available for purchase online. The site provides free pictures and free video clips to those who register with the shop. The site is built upon an extensive technical platform that utilizes real-time, secure transaction processing. In addition, the Shop is available in multi-lingual format and currency options based on a users locale. In 2004, the average order value was US$100.

PrivateSpeed (www.privatespeed.com) is the broadband video on demand channel for Private. PrivateSpeed features an extensive collection of Private movies in both streaming and downloadable formats for rental online. Users of PrivateSpeed are offered a free membership to view trailers of movies and other premium content through a simple sign up process that collects their email address. In 2003, Private licensed the technology of Go Internet for the backend platform for PrivateSpeed. The complete site was redone to include a new design that features a simplified user interface, new streaming, advance account management, and searchable information. Through the partnership with Go Internet, Private has been able to significantly lower costs on it streaming and hosting solution. Since it s relaunch in June of 2003, PrivateSpeed growth has been significant with 58% growth in 2004 compared to 2003.

Private At Home (www.privateathome.com) is an online DVD rental service that launched in May 2003 in the UK. The site allows users to subscribe to a service of renting either 2 3 Private DVDs at any one time, which are then shipped directly to the privacy of their homes. The site offers payment methods especially geared for the UK market including all major credit and debit cards and billing is in local currency. All payments are processed through a recognized and established third party processor.

Licensing. Private licenses the right to use their trademarks and their library of photographs and movies to third parties.

TRADEMARK LICENSING

Private Collection

Together with several licensees, we have developed a program to market and distribute high quality branded merchandise over our websites and the websites of those licensees. Our licensed product lines include clothing, novelties, accessories, fragrances, leather goods, eyewear, nutritional supplements, aphrodisiacs and condoms. These products have been marketed principally through mail-order and retail outlets, including department and specialty stores.

Private Centers

The carefully developed Private Center concept for retailers has taken the adult industry to new levels. Through its Licensing Division, Private is offering a unique opportunity for adult specialist and other retailers to buy into the Private brand through licensing agreements to either upgrade their existing retail points of sale or develop new outlets in order to satisfy the increasingly sophisticated and broad demands of adult consumers. Licensees are required to follow guidelines set by Private and the product range on offer will span from traditional adult products such as sex toys, magazines and DVDs to lifestyle Private-branded products, ranging from streetwear to lingerie. The Private brand, valued by consumers and retailers alike thanks to its enduring focus on quality and innovation, thereby continues to meet new consumer demands, in both niche markets and broader sectors, such as the ever increasing number of female customers.

Private Energy

In 2001 we signed a five-year worldwide distribution agreement with Travel Retail Sales Limited to sell an energy drink called Private Energy. Under this agreement the licensee is responsible for all production, marketing, sales and distribution of the product and guarantees incremental minimum sales each year on which royalties are payable to us.

PROPRIETARY RIGHTS

General

We believe that our branded magazine titles and logos are valuable assets and are vital to the success and future growth of our businesses. We have filed trademark registration applications with respect to most of our trade names and logos. We believe that the name recognition and image that we have developed in each of our markets significantly enhance customer response to our sales promotions. We intend to aggressively defend our trademarks throughout the world, and we constantly monitor the marketplace for counterfeit products. We initiate legal proceedings from time to time to prevent unauthorized use of our trademarks.

Piracy Problems

According to figures from the Motion Picture Association of America, annual losses from video piracy are an estimated $ 250 million a year in the United States alone, and close to $ 3.0 billion a year worldwide. Adult Video News estimated that approximately 20% of the U.S. video market (both rental and sales in 2000) was attributable to adult videos.

Piracy involving adult entertainment products and services is most prevalent in markets where pornography is illegal and in developing countries, including Eastern European countries, such as Russia, Poland and Romania. We believe that piracy is so prevalent in many of these countries that we cannot distribute our products there, as piracy undercuts our price structure and eliminates profit margins. It is very difficult to enforce our proprietary rights in these markets.

Another piracy problem concerns the Internet. We are currently unable to confirm that all mail order sites selling Private products actually sell our original products and not pirated copies. The problem stems from distribution procedures, which in the case of Internet, is straight from the Internet provider s order page to the consumer. Also, video streaming over the Internet renders it difficult for us to control the origin of what is shown.

Our legal counsel handles most piracy problems and attempts to resolve these matters or litigate them on a case-by-case basis.

COMPETITION

General Considerations

Our products compete with other products and services that utilize leisure time or disposable income of adult consumers. The businesses in which we compete are highly competitive and service-oriented. We have few long-term or exclusive service agreements with our customers. Business generation is based primarily on customer satisfaction with key factors in a purchase decision, including reliability, timeliness, quality and price. We believe that our extensive and longstanding international operations, our brand name, image and reputation, as well as the quality of our content and our distributors, provide a significant competitive advantage over many of our competitors.

Although we believe our magazines and videos are well-established in the adult entertainment industry, we compete with entities selling adult oriented products in retail stores, as well as through direct marketing. Many of these products are similar to ours.

Over the past few years, the adult entertainment industry has undergone significant change. Traditional producers of softcore content as well as mainstream providers of media content have shifted to producing hardcore content. As a result, we face greater competition to distribute hardcore content. This shift has also led to industry consolidation, creating fewer, more financially formidable competitors.

Magazines

We meet with minimal direct competition from other publishers of hardcore adult magazines and paperback books. We believe that our print publications are dissimilar to other adult publications in style and format. The only similar business of which we are aware was represented by Rodox N.V., a Dutch/ Danish corporation, which has discontinued its publishing operation. We do not believe there is presently any significant competition in this segment of our business. Magazines such as Playboy and Penthouse and similar print publications do not compete directly with our publications, since we consider them to be softcore publications. There are several hardcore publications in each country where our magazines are sold. In general, these are printed in limited editions and are of lower quality than our publications.

Video and DVD

The distribution of adult entertainment videocassettes and DVDs is a highly competitive business. Each format competes with the other as well as with other forms of entertainment. Revenue generation for motion picture entertainment products depends, in part, upon general economic conditions, but the competitive position of a producer or distributor is still greatly affected by the quality of, and public response to, the entertainment product it makes available to the marketplace. Competition arises from established adult video producers and from independent companies distributing low-quality material.

Our primary competitors in the movie industry are adult motion picture studios, with in-house production and post-production capabilities. These include U.S. producers such as Video Company of America, Hustler, Vivid Film, Wicked Pictures, Evil Angel Productions and Metro Global Media Inc. Some competitors are smaller, but locally or regionally they are capable of quickly identifying niche markets that could compete for our customers. In addition, we also compete with other forms of media, including broadcast, cable and satellite television, direct marketing, electronic media and adult entertainment websites.

Broadcasting

The distribution of adult movies on cable and satellite television systems and hotel pay-per-view systems is highly competitive. Competition in this area is increasing in line with increasing consumer demand for hardcore adult entertainment generally. Our strongest geographical market position for cable and television and distribution is in Europe and United States and Latin America, with our adult channels, *Private Fantasy*, *Private Gold* and *Private Blue*, and licensing arrangements with established European television networks, such as Canal+.

The strength of consumer demand for adult oriented cable programming is evidenced by the acquisition by Playboy of two hardcore U.S. cable channels from Vivid Film in July 2001. Until then, Playboy s business had been largely confined to softcore adult entertainment and it had resisted entry into hardcore markets. Competition in this market has also been impacted by an increase in the number and availability of satellite direct-to-home transmission channels. Our cable and satellite television activities in the United States has historically been limited to licensing our content to channel operators, such as Playboy, however, in 2004 we started broadcasting the Private Fantasy pay-per-view channel over Echo Star s distribution platform.

In licensing, we experience competition from our video and DVD competitors. Our position in U.S. markets is not well established, and competition in this market is strong.

We have only recently entered the hotel pay-per-view market, which is an extremely competitive market. This is due primarily to our unwillingness to enter into a typical hotel pay-per-view agreement, which requires a licensor such as Private Media Group to license the movies to a hotel provider on a fixed fee basis for each movie or video. We have recently entered into license agreements with a major hotel chain which provides for license fees based upon the number of rooms they service, and we are now intensifying our efforts to penetrate this segment of the market.

Internet

The Internet market for adult oriented content has expanded dramatically over the past years. There are numerous adult media content websites competing with ours, operated by companies that possess global distribution, broadcasting and branding.

EMPLOYEES

As of December 31, 2002, 2003 and 2004 we employed 177, 163 and 141 people, respectively, on a full-time basis.

Our full-time editorial and post-production staff consists of an editor-in-chief, six executive editors and approximately seven editors, associate editors and assistant editors who oversee the quality and consistency of the artwork and editorial copy and manage the production schedule of each issue. The production of each issue requires the editors to coordinate the activities of a writer, a pencil artist, an inker, a colorist and a printer over a two-month period. The majority of this work is performed on our premises in Barcelona, Spain.

The photographers and directors consist of freelancers who generally receive a flat fee. We have entered into agreements with some photographers, movie directors and writers under which such people have agreed to provide their services to us on an exclusive basis, generally for a period of one to three years.

We believe that we have a good relationship with our employees. Currently, none of our employees is represented by a labor union.

GOVERNMENT REGULATION

We operate in a highly regulated industry. This requires us to be socially aware and sensitive to government strictures, including laws and regulations designed to protect minors or which prohibit the distribution of obscene material. We take great care to comply with all applicable governmental laws and regulations in each jurisdiction where we conduct business. Moreover, we do not knowingly engage the services of any business or individual that does not adhere to the same standards. Since 1965, we have never been held to have violated any laws or regulations regarding obscenity or the protection of minors.

Regulation of the Adult Entertainment Industry in the U.S.

The following is a description of some of the laws and regulations in the United States which impact the adult entertainment industry. It is not an exhaustive description of all such laws. Moreover, we conduct business in over 35countries around the world, each of which has its own regulatory framework. This regulatory environment is constantly changing in the geographical areas in which we conduct business, and in some instances laws which are enacted are subsequently determined by the courts to be unconstitutional.

The Classification and Rating Administration of the Motion Picture Association of America, MPAA, a motion picture industry trade association, assigns ratings for age group suitability for theatrical and home video distribution of motion pictures. Submission of a motion picture to the MPAA for rating is voluntary, and we do not submit our motion pictures to the MPAA for review. However, with the exception of several titles which have been re-edited for cable television, most of the movies distributed by us, if so rated, would most likely fall into the NC - 17 - No Children Under 17 Admitted rating category because of their depiction of nudity and sexually explicit content.

The right to distribute adult videocassettes, magazines and DVD products in the United States is protected by the First and Fourteenth Amendments to the United States Constitution, which prohibits Congress or the several States from passing any law abridging the freedom of speech.

The First and Fourteenth Amendments, however, do not protect the dissemination of obscene material, and several states and communities in which our products are distributed have enacted laws regulating the distribution of obscene material, with some offenses designated as misdemeanors and others as felonies, depending on numerous factors. The consequences for violating these state statutes are as varied as the number of states enacting them. Similarly, specific U.S. federal regulations prohibit the dissemination of obscene material. The potential penalties for individuals (including directors, officers and employees) violating the Federal obscenity laws include fines, community service, probation, forfeiture of assets and incarceration. The range of possible sentences requires calculations under the Federal Sentencing Guidelines, and the amount of the fine and the length of the period of the incarceration under those guidelines are calculated based upon the retail value of the unprotected materials. Also taken into account in determining the amount of the fine, length of incarceration or other possible penalty are whether the person accepts responsibility for his or her actions, whether the person was a minimal or minor participant in the criminal activity, whether the person was an organizer, leader, manager or supervisor, whether multiple counts were involved, whether the person provided substantial assistance to the government, and whether the person has a prior criminal history. In addition Federal law provides for the forfeiture of: (1) any obscene material produced, transported, mailed, shipped or received in violation of the obscenity laws; (2) any property, real or personal, constituting or traceable to gross profits or other proceeds obtained from such offense; and (3) any property, real or personal, used or intended to be used to commit or to promote the commission of such offense, if the court in its discretion so determines, taking into consideration the nature, scope and proportionality of the use of the property in the offense.

With respect to the realm of potential penalties facing an organization such as ours, the forfeiture provisions detailed above apply to corporate assets falling under the statute. In addition, a fine may be imposed, the amount of which is tied to the pecuniary gain to the organization from the offense or determined by a fine table tied to the severity of the offense. Also factored into determining the amount of the fine are the number of individuals in the organization and whether an individual with substantial authority participated in, condoned, or was willfully ignorant of the offense; whether the organization had an effective program to prevent and detect violations of the law; and whether the organization cooperated in the investigation and accepted responsibility for its criminal conduct. In addition, the organization may be subject to a term of probation of up to five years.

Federal and state obscenity laws define the legality or illegality of materials by reference to the U.S. Supreme Court s three-prong test set forth in *Miller v. California*, 413 U.S. 1593 (1973). This test is used to evaluate whether materials are obscene and therefore subject to regulation. *Miller* provides that the following must be considered: (a) whether the average person, applying contemporary community standards would find that the work, taken as a whole, appeals to the prurient interest; (b) whether the work depicts or describes, in a patently offensive way, sexual conduct specifically defined by the applicable state law; and (c) whether the work, taken as a whole, lacks serious literary, artistic, political or scientific value. The Supreme Court has clarified the *Miller* test in recent years, advising that the prurient interest prong and patent offensiveness prong must be measured against the standards of an average person, applying contemporary community standards, while the value prong of the test is to be judged according to a reasonable person standard.

We are engaged in the wholesale distribution of our products to U.S. wholesalers and/or retailers. We have taken steps to ensure compliance with all Federal, State and local regulations regulating the content of motion pictures and print products, by staying abreast of all legal developments in the areas in which motion pictures and print products are distributed and by specifically avoiding distribution of motion pictures and print products in areas where the local standards clearly or potentially prohibit these products. In light of our efforts to review, regulate and restrict the distribution of our materials, we believe that the distribution of our products does not violate any statutes or regulations.

Many of the communities in the areas in which we offer or intend to offer products or franchises, have enacted zoning ordinances restricting the retail sale of adult entertainment products. We supply products only in locations where the retail sale of adult entertainment products is permitted.

In February 1996, the U.S. Congress passed the Telecommunications Act. Some provisions of the Telecommunications Act are directed exclusively at cable programming in general and adult cable programming in particular. In some cable systems, audio or momentary bits of video of premium or pay-per-view channels may accidentally become available to non-subscribing cable customers. This is called bleeding. The practical effect of Section 505 of the Telecommunications Act is to require many existing cable systems to employ additional blocking technology in every household in every cable system that offers adult programming, whether or not customers request it or need it, to prevent any possibility of bleeding, or to restrict the period during which the programming is transmitted from 10:00 p.m. to 6:00 a.m. Penalties for violation of the Telecommunications Act are significant and include fines and imprisonment. Surveying of cable operators and initial results indicate that most will choose to comply with Section 505 by restricting the hours of transmission. We believe that our revenues will be marginally adversely affected as a result of enforcement of Section 505. However, as digital technology (which is unaffected by Section 505) becomes more available, we believe that ultimately the impact will be insignificant.

As discussed above, federal and state government officials have targeted sin industries, such as tobacco, alcohol, and adult entertainment for special tax treatment and legislation. In 1996, U.S. Congress passed the Communications Decency Act of 1996, or the CDA. Recently, the U.S. Supreme Court, in ACLU v. Reno, held certain substantive provisions of the CDA unconstitutional. Businesses in the adult entertainment and programming industries expended millions of dollars in legal and other fees in overturning the CDA. Investors should understand that the adult entertainment industry may continue to be a target for legislation. In the event we must defend ourselves and/or join with other companies in the adult programming business to protect our rights, we may incur significant expenses that could have a material adverse effect on our business and operating results.

Child Pornography and Non-Mainstream Content

We believe that roughly 90% of the adult material produced and distributed over the past 15 years contains mainstream sexual acts between consenting adults. The rest could be classified as specialty material which does not contain explicit sex, but which still involves consenting adults (i.e. fetish, bondage, etc.). Mainstream sex acts means intercourse, oral sex, anal sex, group sex, etc. Our adult movies do not contain any depictions, let alone actual performances of rape, sex with coercion, animals, urination, defecation, violence, incest or child pornography.

Since 1990, the Free Speech Coalition has worked with the U.S. government to create a workable regulatory system designated to prevent minors from working in the adult industry. Child Protection Restoration and Penalties Enhancement Act of

1990 (18 U.S.C. section 2257) requires, in essence, that no one can work without having copies of their passport or driver s license, and a declaration under perjury of their age and true name, on file with a designated Custodian of Records, and available for inspection by law enforcement.

As indicated above, all of our products are all in compliance with 18 U.S.C. Section 2257 and all models performing in our productions are 18 years of age or older.

Internet Regulation

Government regulation of the Internet is a rapidly developing area and, therefore, adds additional uncertainty to our business. New laws or regulations relating to the Internet, or more aggressive application of existing laws, could decrease the growth of our websites, prevent us from making our content available in various jurisdictions or otherwise have a material adverse effect on our business, financial condition and operating results. These new laws or regulations could relate to liability for information retrieved from or transmitted over the Internet, taxation, user privacy and other matters relating to our products and services. For example, the U.S. government has recently enacted laws regarding website privacy, copyrights and taxation. Moreover, the application to the Internet of other existing laws governing issues such as intellectual property ownership and infringement, pornography, obscenity, libel, employment and personal privacy is uncertain and developing.

Regulation of the Internet outside the United States

We may also be subject to claims based upon the content that is available on our websites through links to other sites and in jurisdictions that we have not previously distributed content in. For example, a recent French ruling banning the sale of Nazi memorabilia in France suggests that website operators may be forced to undertake expensive security measures to block certain users or face significant fines. Implementing such security measures to reduce our exposure to this liability may require us to take steps that would substantially limit the attractiveness of our websites and/or their availability in various geographic areas, which could negatively impact their ability to generate revenue.

SEASONALITY

Our businesses are generally not seasonal in nature. However, June, July and August are typically impacted by smaller orders from some European and U.S. distributors, due to the holiday season.

ITEM 2. DESCRIPTION OF PROPERTIES

PROPERTIES

Private Media Group maintains an office in the United States at 3230 Flamingo Road, Suite 156, Las Vegas, Nevada 89121.

In January 2002 Milcap Media Group renewed the lease for the building it currently occupies, located at Carretera de Rubi 22-26, 08190 Sant Cugat del Valles, Barcelona, Spain, for a further term of five years. Average monthly base rental expense is approximately $ 27,000. The building is currently used by all of our operating departments, primarily for marketing, administration and post production. In addition, the building serves as the European headquarters of Private Media Group, Inc. In addition, Milcap Media Group leases warehouse space also located on Carretera de Rubi. The lease expires in 2007 and the average monthly base rental expense is approximately $ 20,300. We recognize the rent expense on a straight-line basis over the term of the leases. Additionally, the leases requires us to pay our proportionate share of the building s real estate taxes and operating expenses.

Effective December 31, 2002, Fraserside Holdings Limited (Purchaser) a wholly-owned subsidiary of Private Media Group, Inc. completed the purchase of all of the outstanding stock of Barbuda B.V., from Luthares Investments N.V. and Stichting de Oude Waag, companies indirectly beneficially owned by the Company s principal shareholder. The principal asset of Barbuda B.V. is an approximately 6.300 square meter office facility and additional parking, located in Barcelona, Spain. The purpose of this transaction was to acquire this property as its European headquarters. Since the acquisition, the Company has been reevaluating its need for additional space and as of February 2005, the Company no longer owns this property.

Currently, in addition to Barcelona, Spain, the group s subsidiaries lease office and warehouse space in Sweden; Stockholm, Knegsel, the Netherlands; Paris, France and Montreal, Canada.

ITEM 3. LEGAL PROCEEDINGS

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.

We are from time to time a defendant in suits for defamation and violation of rights of privacy, many of which allege substantial or unspecified damages, which we vigorously defend.

We are presently engaged in litigation, most of which is generally incidental to the normal conduct of our business and is immaterial in amount. We believe that our reserves are adequate and that no such action will have a material adverse impact on our financial condition. However, there can be no assurance that our ultimate liability will not exceed our reserves.

Except as disclosed above, neither Private Media Group, Inc. nor its subsidiaries is or has been, during the last two fiscal years, involved in any other litigation or arbitration proceedings which have had or might have a material influence on our financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Our 2004 Annual Meeting of Shareholders was held on December 20, 2004. At the Annual Meeting each of our five nominees was elected to serve as a director until the next Annual Meeting of Shareholders. The election results were as follows:

Election of Five Directors:

Name	For	Withheld
Berth H. Milton	40,115,290	5,167
Bo Rodebrant	40,176,773	5,167
Ferran Mirapeix	40,176,663	5,167
Johan G. Carlberg	40,170,273	5,167
Daniel Sánchez	40,177,263	5,167

No other matter was submitted to a vote at the 2004 Annual Meeting.

PART II

ITEM 5. MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Market for Private Media Group, Inc. Common Stock

The common stock of Private Media Group, Inc. has traded on the Nasdaq National Market since February 1, 1999 under the symbol PRVT . Previously, our common stock traded on the NASD, Inc. OTC Bulletin Board since March 29, 1996. The following table sets forth the range of representative high and low bid prices for the common stock for the periods indicated, as reported by the Nasdaq National Market. Quotations represent inter-dealer prices, do not include retail markups, markdowns or commissions and may not represent actual transactions.

	High	Low
Fiscal 2004:		
First Quarter	$ 3.69	$ 1.97
Second Quarter	$ 2.68	$ 1.94
Third Quarter	$ 2.80	$ 2.19
Fourth Quarter	$ 4.95	$ 2.42
Fiscal 2003:		
First Quarter	$ 3.31	$ 1.16
Second Quarter	$ 2.48	$ 1.07
Third Quarter	$ 2.85	$ 1.88
Fourth Quarter	$ 2.24	$ 1.30

On March 17, 2005, the last sales price reported on the Nasdaq National Market was $ 4.60. On October 30, 2004, there were 187 shareholders of record and approximately 1,400 beneficial owners of our common stock.

Sale of Unregistered Securities in the Fourth Quarter of 2004

During the three months ended December 31, 2004, we sold unregistered securities in the following transactions.

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 fourth quarter of 2004 we issued an aggregate of 13,037 shares of common stock in payment of $34,032 of accrued interest under the outstanding 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.

Equity Compensation Plan Information

On March 1, 1999 the Company adopted the 1999 Employee Stock Option Plan. In February 2003 the Plan was amended to provide for the issuance of up to 7,200,000 shares of the Company s common stock to employees, consultants and advisors of the company, and was approved by the shareholders.

Full details of the Plan are included in note 2 and 19 to the financial statements and are summarized below as of December 31, 2004:

(a)	Number of securities to be issued upon exercise of outstanding options, warrants and rights	4,661,561
(b)	Weighted-average exercise price of outstanding options, warrants and rights	$ 3.47
(c)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in row (a) above)	2,233,153

Dividend Policy

We did not pay any cash dividends during our last two fiscal years and we do not contemplate doing so in the near future. We currently intend to retain all earnings to finance the development and expansion of our operations, and do not anticipate paying cash dividends on our shares of common stock in the foreseeable future. Our future dividend policy will be determined by our Board of Directors on the basis of various factors, including results of operations, financial condition, business opportunities and capital requirements. The payment of dividends will also be subject to the requirements of Nevada Law, as well as restrictive financial covenants which may be required in credit agreements.

Stock Dividend

We implemented a 3:1 stock dividend whereby each holder of record of our common stock on May 30, 2000, received two additional shares of common stock for each share owned on the record date. Corresponding adjustments have been made to the warrants and options outstanding on the record date as well as the Series A Preferred Stock to reflect adjusted conversion and dividend terms. Accordingly, all share and per share values reflected have been adjusted to give effect to the stock dividend.

Transfer Agent

The transfer agent and registrar for our common stock is InterWest Transfer Co., Inc., 1981 East 4800 South, Suite 100, Salt Lake City, Utah 84117.

ITEM 6. SELECTED FINANCIAL DATA

The following table presents selected consolidated financial information for the five years ended December 31, 2004. The selected financial information has been derived from our audited consolidated financial statements. This selected consolidated financial information should be read along with our historical consolidated financial statements and related notes, and Management s Discussion and Analysis of Financial Condition and Results of Operations included in or appearing elsewhere in this Report.

	Years ended December 31,					
	2004	2004	2003	2002	2001	2000
	USD	EUR	EUR	EUR	EUR	EUR
	(in thousands, except per share data)					
Statement of Income Data:						
Net sales	48,784	35,612	38,491	39,410	38,979	30,553
Cost of sales	24,766	18,080	19,081	17,031	13,827	11,693
Gross Profit	24,017	17,533	19,411	22,379	25,152	18,860
Selling, general and administrative expenses	24,624	17,976	19,871	20,562	16,751	11,469
Offering expenses				1,569	843	
Operating income (loss)	(607)	(443)	(461)	249	7,557	7,391
Sale of controlled entity					1,862	
Interest expense	1,052	768	761	366	194	213
Interest income	225	165	147	327	152	364
Income (loss) before income taxes	(1,434)	(1,046)	(1,075)	210	9,378	7,543
Income taxes (benefit)	(1,760)	(1,284)	(504)	(130)	1,361	1,267
Net income (loss)	326	238	(570)	340	8,017	6,275
Other Comprehensive Income:						
Unrealized loss on short-term investment				(67)	(134)	
Foreign currency translation adjustments	(435)	(318)	642	666	(1,978)	(1,305)
Comprehensive income	(109)	(80)	72	939	5,905	4,970
Income (loss) applicable to common shareholders	326	238	(718)	(1,107)	6,428	4,769
Weighted average of shares outstanding:						
Basic	50,136,203	50,136,203	43,493,163	28,626,327	28,137,817	27,002,220
Diluted	52,377,163	52,377,163	N/A	N/A	49,679,835	48,745,896
Basic income (loss) per share	0.01	0.00	(0.02)	(0.04)	0.23	0.18
Fully diluted income (loss) per share	0.01	0.00	(0.02)	(0.04)	0.16	0.13
Dividends declared per common Share						

	As per December 31,

	2004	2004	2003	2002	2001	2000
	USD	EUR	EUR	EUR	EUR	EUR
			(in thousands)			
Balance Sheet Data:						
Cash and cash equivalents	4,467	3,261	856	1,694	6,408	1,624
Working capital	24,988	18,241	13,293	15,287	22,360	15,864
Total assets	86,686	63,281	68,149	68,989	57,086	43,864
Total debt	13,365	9,756	13,732	16,486	4,750	605
Total shareholders Equity	63,281	46,026	44,157	43,451	42,280	34,195

ITEM 7. 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.

Overview

We are an international provider of adult media content. We acquire still photography and motion pictures from independent directors and process these images into products suitable for popular media formats such as print publications, DVDs, video cassettes and digital media content for Broadcasting, Broadband and Internet distribution. In addition to media content, we also market and distribute branded leisure and novelty products oriented to the adult entertainment lifestyle and generate additional sales through the licensing of our *Private* trademark to third parties.

In June 1998, we acquired Milcap Media Limited, its subsidiaries and Cine Craft. Prior to these acquisitions, we were a holding company. Milcap Media Limited, its subsidiaries and Cine Craft were the acquirees, but for accounting purposes they were deemed to be the acquirors. We became a U.S. reporting company following the 1998 acquisitions.

We operate in a highly competitive, service-oriented market and are subject to changes in business, economic and competitive conditions. Nearly all of our products compete with other products and services that utilize adult leisure time and disposable income.

We generate revenues primarily through:

- sales of movies on DVD and videocassette formats;
- sales of adult feature magazines;
- Internet subscriptions and licensing;
- broadcasting movies through cable, satellite and hotel television programming; and
- content, brand name and trademark licensing.

The following table illustrates our net sales by product group for the periods indicated.

	Years ended December 31,		
	2002	2003	2004
	EUR	EUR (in thousands)	EUR
Net sales by product group			
Magazine	5,777	5,316	5,121
Video	7,986	7,206	2,130
DVD s	15,482	18,309	19,488
Internet	6,059	4,819	4,859
Broadcasting	4,106	2,841	4,014
Total	39,410	38,491	35,612

Over time, we expect net sales from magazines and videocassettes to continue to decline as a percentage of net sales in relation to total net sales from DVDs, the Internet and broadcasting. We expect net sales from DVDs, the Internet and broadcasting to grow during the coming years.

We recognize net sales on delivery (for further information, see Critical Accounting Estimates).

Even though we recognize net sales upon delivery, we generally provide extended payment terms to our distributors of between 90 and 180 days. Although our extended payment terms increase our exposure to accounts receivable write-offs, we believe our risk is minimized by our generally long-term relationships with our distributors. In addition, we view our extended payment terms as an investment in our distribution channels which are important to the growth of our business.

Our primary expenses include:

- acquisition of content for our library of photographs and videos;
- printing, processing and duplication costs; and
- selling, general and administrative expenses.

Our magazines and DVD and videocassette covers are printed by independent third-party printers in Spain. We introduced DVDs as a motion picture medium in 1999. The production of each DVD master disc, prior to duplication, costs approximately $10,000. DVDs have a relatively low cost of duplication, inclusive of box and packaging, of approximately $2.00 per unit. Our DVDs are duplicated on an all region format, playable on both NTSC and PAL with multiple languages and sub-titles.

We released 104 titles on DVD during 2004, 111 titles during 2003 and 120 titles during 2002, including both new and archival material. We plan to release approximately 120 proprietary titles on DVDs in 2005. In addition, in 2004 we signed an exclusive three year Agreement with US-based Pure Play Media, Inc. for content distribution in Europe. Under the agreement, we will distribute approximately six to ten newly produced movie titles per month in Europe, our main market for DVDs. The content controlled by Pure Play Media features top US producers and directors such as Michael Ninn, Seymore Butts, and Cousin Stevie. The arrangement is based on a split of gross profit and does not require any up-front or future investment in content by Private. We will start releasing titles on DVD under the agreement in the second quarter of 2005.

Over the years, our cost of sales has been fluctuating relative to net sales due to our use of new mediums for our products, such as the Internet, DVD and broadcasting. Internet and broadcasting sales has historically not carried any cost of sales and variations in these areas affect the overall cost of sales percentage in relation to sales. These new media provide us with additional sales of our existing content

In December 2003, a group-wide review of operations initiated. The objective of the review was to restructure our operations to focus on our core business and reduce or abandon spending on, and investments in, activities not generating sufficient gross profits and/or operating profits. The review resulted in reduced selling, general and administrative expenses in the areas targeted and had a positive impact on the results of operations in 2004.

The group-wide review initiated in 2003 also resulted in the restructuring of our US operations and our US subsidiary outsourced its distribution of physical products, inclusive of Internet shop fulfillment. The restructuring started September 30, 2004 and the impact has initially been a temporary loss of revenues from the US during the fourth quarter transition period. The loss of revenues had a significant impact on gross profit. However, during the first quarter of 2005 distribution resumed and we expect the impact of the restructuring to increase gross profit and reduce selling, general and administrative expenses in 2005 compared to 2004.

We also incur significant intangible expenses in connection with the amortization of our library of photographs and movies and capitalized development costs, which include the Internet. We amortize these tangible and intangible assets on a straight-line basis for periods of between three and five years.

Critical Accounting Estimates

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 as a result of unexpected changes in trends.

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.

The Company sells magazines to wholesalers on firm sale basis and via national newsstand distributors with the right to return. Our magazines are multi-lingual and the principal magazine market is in Europe.

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. Distributors with the right to return are primarily national newsstand distributors. Most of our magazines are bi-monthly (six issues per year) and remain on sale at a newsstand for a period of two months. Normally, all unsolds are reported to us within a period of four to six months from delivery. There are normally two to four national newsstand distributors for all newspapers and periodicals in each country. A majority of our national newsstand distributors are members of Distripress, the international organization for publishers and distributors, and carry out the distribution of the largest national and international newspapers and periodicals, including: Financial Times, Herald Tribune, Time, Newsweek, Vogue, etc.

The Company uses specific return percentages per title and distributor based on estimates and historical data. The percentages vary from 50-80%. Higher percentages generally reflect newer markets and/or products. Percentages are reviewed on an on-going basis.

The magazines have an approximate retail price of EUR 11.50 (USD 15.00) per copy and are printed on glossy high-quality paper at a cost of EUR 1.25 (USD 1.60). They are often shrink-wrapped in order to comply with local regulation or guidance for the sale of adult publications. In view of the high retail price, the margin and the physical quality of the magazines and the fact that the content has a very long shelf-life since it is not particularly linked to time, trends, fashion or current events, the Company has always collected the returns from newsstands in order to make them available for sale again.

The company has scheduled re-distribution of the returned magazines, via national newsstand distributors, as Megapacks or Superpacks (three different copies per pack) where the retail price is EUR 14.95 (USD 19.50). As the national newsstand distributors have the right to return, the packs come back to us and are then broken up in individual copies in order to be sent out in DVD packs, see below, or sold on firm sale basis to wholesalers as back numbers at a lower price than new issues.

The company recently started scheduled re-distribution of returned magazines, via national newsstand distributors, together with DVDs as Magazine/DVD packs as a way of increasing DVD distribution. Since the national newsstand distributors have the right to return, the DVD packs are returned and the magazines are broken out in order to be sold on firm sale basis to wholesalers as back numbers at a lower price than new issues. The company has historically sold all copies printed at an average price higher than, or equal, to cost.

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. Revenues from satellite & cable broadcasting are recognized based on sales reported each month by its cable and satellite affiliates. The affiliates do not report actual monthly sales for each of their systems to the Pay TV Group until approximately 60 - 90 days after the month of service ends. This practice requires management to make monthly revenue estimates based on historical experience for each affiliated system. Revenue is subsequently adjusted to reflect the actual amount earned upon receipt. Adjustments made to adjust revenue from estimated to actual have historically been immaterial.

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 the past and may occur in the future due to the current market environment.

Management reviews the allowance for doubtful accounts on at least a quarterly basis and adjusts the balance based on their estimate of the collectibility of specific accounts as well as a reserve for a portion of other accounts which have been outstanding for more than 180 days. This estimate is based on historical losses and information about specific customers. After collection attempts have failed, the Company writes off the specific account.

Goodwill and Other Intangible Assets

On January 1, 2002 the Company adopted Financial Accounting Standards Board Statement (SFAS) No. 142, Goodwill and Other Intangible Assets . Under SFAS 142, goodwill and indefinite lived intangible assets will no longer be amortized but will be reviewed annually for impairment (or more frequently if indicators of impairment arise).

During 2002, the Company performed an initial impairment test of goodwill and indefinite lived intangible assets as of January 1, 2002. This generally required us to assess these assets for recoverability when events or circumstances indicate a potential impairment by estimating the undiscounted cash flows to be generated from the use of these assets. There was no effect of on the earnings and financial position of the Company as a result of the impairment testing.

Other Intangible Assets represents the value attributable to certain acquisitions (see Note 3 and 8). Amortization expense is calculated on a straight-line basis over 10 years.

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.

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.

Results of Operations

2004 compared to 2003

Net sales. Our net sales in 2004 were EUR 35.6 million compared to EUR 38.5 million in 2003, a decrease of EUR 2.9 million, or 7%. The drop in net sales is primarily the result of the Company s reorganization of its US distribution, *see previous discussion under Overview in this Item 7*, and a decrease in Video sales. The decrease in Video sales of 70% to EUR 2,1 million, was primarily the result of a combination of a general industry decrease in Video sales and 40% less titles being released by the Company as a result of fewer new movie productions available for sale on Video in 2004 compared to 2003. DVD sales, which increased 6%, to EUR 19.5 million, was also affected by the US reorganization and the reduction in new movie productions available for sale. However, the Company managed to offset part of the negative effect from fewer new titles on DVD sales by opening additional distribution channels, thereby increasing sales on a per release basis. Magazine sales decreased 4% to EUR 5.1 million, while Internet sales increased 1% to EUR 4.9 million. Broadcasting sales increased 41% to EUR 4.0 million primarily as a result of the broadcasting launch of our own TV channel in the United States in February 2004.

In 2003 and the first half of 2004, investment in new movie productions was cut back due to reduced cash-flow as a result of overspending in 2002 and 2003. Improvements in cash-flow during 2004 has allowed the Company to increase its investment activity in new movie productions and the impact on sales is expected to show in the first half of 2005, see also Liquidity and Capital Resources - Investing Activities.

Net sales in general were affected by unfavorable changes in exchange rates. During the period the dollar weakened against the euro and since our sales in the United States are translated into euro this had a negative effect. Fluctuations in exchange rates between the euro and the dollar can affect the comparability of our results from year to year. 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 change in average exchange rate for the fiscal year 2004 compared to 2003 was a decrease of 9%. 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.

Cost of Sales. Our cost of sales was EUR 18.1 million for 2004 compared to EUR 19.1 million for 2003, a decrease of EUR 1.0 million, or 5%. The decrease was the result of reduced sales. Cost of sales as a percentage of sales was 51% for 2004, an increase of 1% compared to 2003. The increase in cost of sales as a percentage of sales was primarily the result of the impairment of the value of video cassettes in inventory as of December 31, 2004 made to reflect the change in market conditions for video cassettes.

Included in cost of sales is printing, processing and duplication, amortization of library and broadcasting costs. Printing, processing and duplication cost was EUR 10.9 million for 2004 compared to EUR 11.8 million for 2003, a decrease of EUR 0.9 million, or 7%. The decrease was the result of reduced sales. Printing, processing and duplication cost as a percentage of sales was 31% for 2004, which represents no change compared to 2003. As a result of changing market conditions, we wrote off video cassette inventory to a value of EUR 1.5 million during the fourth quarter, which increased printing, processing and duplication cost with the same amount. Amortization of library was EUR 6.6 million for 2004 compared to EUR 7.1 million for 2003, a decrease of EUR 0.5 million, or 7%. Amortization of library does not vary with sales since it reflects the amortization of our investments in content which has been available for sale for a period of three to five years. The decrease was the result of lower amounts invested in content released during the period subject to amortization in 2004 compared to 2003. Broadcasting cost was EUR 0.6 million for 2004 compared to EUR 0.2 million for 2003, an increase of EUR 0.4 million. Broadcasting cost represents programming and transmission cost and the increase relates to the start-up of the Private Fantasy Channel in the United States.

Gross Profit. Our gross profit for 2004 was EUR 17.5 million, or 49% of net sales, compared to EUR 19.4 million, or 50% of net sales for 2003. This represented a decrease of EUR 1.9 million, or 10%, compared to 2003. The decrease was the result of lower sales. Gross profit as a percentage of sales was down 1% for 2004 compared to 2003. The decrease in gross profit as a percentage of sales was the result of the impairment of the value of video cassettes in inventory as of December 31, 2004 made to reflect the change in market conditions for video cassettes.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 18.0 million for 2004 compared to EUR 19.9 million for 2003. Despite increases in bad debt provision and depreciation of EUR 0.9 million and EUR 0.9 million, respectively, selling, general and administrative expenses decreased by EUR 1.9 million, or 10%. The increased bad debt provision in 2004 related primarily to one specific receivable which was written off completely as collection attempts failed. We attribute the decrease in selling, general and administrative expenses to an overall program started in 2003 where the objective is to review and reduce all controllable selling, general and administrative expenses in low or non-profitable areas. We expect lower bad debt provisions and reduced depreciation in 2005. We also expect selling, general and administrative expenses in low or non-profitable areas to continue to decrease in 2005.

Operating profit/loss. We reported an operating loss of EUR 0.4 million for 2004 compared to an operating loss of EUR 0.5 million for 2003, a decrease of EUR 1.0 million. The decrease in loss was primarily the result of reduced selling, general and administrative expenses.

Interest expense. Our interest expense was EUR 0.8 million for 2004, compared to EUR 0.8 million for 2003.

Income tax expense/benefit. Our income tax benefit was EUR 1.3 million for 2004, compared to 0.5 million for 2003.

Net income/loss. Our net income was EUR 0.2 million for 2004, compared to a net loss of EUR 0.6 million for 2003. We attribute this increase in net income in 2004 of EUR 0.8 million primarily to increased income tax benefit.

2003 compared to 2002

Net sales. Our net sales in 2003 were EUR 38.5 million compared to EUR 39.4 million in 2002, a decrease of EUR 0.9 million, or 2%. We attribute this change to a decrease in Video and Magazine, Internet and Broadcasting sales. Video and Magazine sales decreased 9% to EUR 12.5 million, primarily as a result of DVD taking over from video in the marketplace. Internet sales decreased 20% to EUR 4.8 million as a result of a weaker US dollar and lower license sales. Broadcasting sales decreased 31% to EUR 2.8 million as a result of a decrease in license sales. The reduction in Broadcasting license sales is a result of the Company s strategy to start operating its own TV channels in the United States. The launch of the channels requires the Company to refrain from selling its broadcast rights to third parties for the period leading up to the launch. The decrease in Video and Magazine, Internet and Broadcasting sales was offset by a increase in DVD sales of 18% to EUR 18.3 million. We attribute the growth in sales of DVDs to the increasing number of DVD players being sold in all of our markets. We believe that the growth in DVD sales will continue through the remainder of 2004.

Net sales in general were affected by unfavorable changes in exchange rates. During the period the dollar weakened against the euro and since our sales in the United States are translated into euro this had a negative effect. Fluctuations in exchange rates between the euro and the dollar can affect the comparability of our results from year to year. 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 change in average exchange rate for the fiscal year 2003 compared to 2002 was a decrease of 17%. 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.

Cost of Sales. Our cost of sales was EUR 19.1 million for 2003 compared to EUR 17.0 million for 2002, an increase of EUR 2.0 million, or 12%. The increase was the result of a combination of an increase in sales volume in areas generating cost of sales and unfavorable exchange rate changes. Cost of sales as a percentage of sales was 50% for 2003, an increase of 7% compared to 2002. The increase in cost of sales as a percentage of sales was primarily the result of sales mix, see *Gross Profit*.

Gross Profit. Our gross profit for 2003 was EUR 19.4 million, or 50% of net sales, compared to EUR 22.4 million, or 57% of net sales for 2002. This represented a decrease of EUR 3.0 million, or 13%, compared to 2002. Gross profit as a percentage of sales was down 7% for 2003 compared to 2002. The decrease in gross profit was primarily the result of sales mix, with higher sales volume in products generating cost of sales, such as Videos, Magazines and DVDs combined, and lower sales in products not generating cost of sales, such as Internet and Broadcasting sales.

Selling, general and administrative expenses. Our selling, general and administrative expenses were EUR 19.7 million for 2003 compared to EUR 20.6 million for 2002, a decrease of EUR 0.9 million, or 4%. We attribute the decrease to an overall program started in 2003 where the objective is to review and reduce all controllable selling, general and administrative expenses in low or non-profitable areas, offset by our expansion in Canada through our new subsidiary Private Media Group Canada which became fully operational during the second half of the year. We expect selling, general and administrative expenses in low or non-profitable areas to continue to decrease in 2004.

Operating profit/loss. We reported an operating loss of EUR 0.5 million for 2003 compared to an operating profit of EUR 0.2 million for 2002, a decrease of EUR 0.7 million. Discounting non-recurring charges of EUR 1.6 million in offering expenses made in 2002, the decrease was EUR 2.4 million. The decrease was primarily the result of lower gross profit.

Interest expense. Our interest expense was EUR 0.8 million for 2003, compared to EUR 0.4 million for 2002.

Income tax expense/benefit. Our income tax benefit was EUR 0.5 million for 2003, compared to 0.1 million for 2002. The increase of EUR 0.4 million is primarily attributable to more of the Company s losses being recorded in tax jurisdictions where there is a higher corporate tax than compared to other tax jurisdictions.

Net income/loss. Our net loss was EUR 0.6 million for 2003, compared to a net income of EUR 0.3 million for 2002. We attribute this change in net income in 2003 of EUR 0.9 million to decreased operating profit.

Liquidity and Capital Resources

We generate cash from our operating activities, borrowings from third parties, the exercise of warrants and private sales of our equity securities. Our principal uses of cash typically include, building our library of photographs and movies.

We reported a working capital surplus of EUR 18.2 million at December 31, 2004, an increase of EUR 4.9 million compared to the year ended December 31, 2003. The increase is principally attributable to increases in cash and cash equivalents and prepaid expenses and other current assets and decreases in borrowings and accrued other liabilities.

We reported a working capital surplus of EUR 13.3 million at December 31, 2003, a decrease of EUR 2.0 million compared to the year ended December 31, 2002.

Operating Activities

Net cash provided by our operating activities was EUR 8.3 million for 2004 compared to EUR 10.3 million for 2003, and was primarily the result of net income and adjustments to reconcile net income to net cash flows from operating activities. We adjusted our net income of EUR 0.2 million to reconcile it to net cash flows from operating activities. Adjustments included (1) depreciation of EUR 2.1 million, (2) convertible note adjustment of EUR 0.1 million, (3) bad debt provision of EUR 1.6 million, (4) amortization of goodwill and other intangible assets of EUR 0.1

million and (5) amortization of photographs and videos of EUR 6.6 million making a total of EUR 10.8 million which was offset by EUR 0.7 million from deferred income taxes, providing a net balance of EUR 10.1 million. Changes in operating assets and liabilities reduced the net balance by EUR 1.8 million through trade accounts receivable, related party receivable, accounts payable trade, income taxes payable and accrued other liabilities totaling EUR 3.1 million, offset by EUR 1.3 million from inventories and prepaid expenses and other current assets.

Net cash provided by our operating activities was EUR 10.3 million for 2003 compared to EUR 4.3 million for 2002, and was primarily the result of net income and adjustments to reconcile net income to net cash flows from operating activities. We adjusted our net income of EUR 0.6 million to reconcile it to net cash flows from operating activities. Adjustments included (1) depreciation of EUR 1.2 million, (2) convertible note adjustment of EUR 0.1 million, (3) bad debt provision of EUR 0.8 million, (4) amortization of goodwill and other intangible assets of EUR 0.1 million and (5) amortization of photographs and videos of EUR 7.1 million making a total of EUR 8.7 million which was offset by EUR 1.2 million from deferred income taxes, providing a net balance of EUR 7.5 million. Changes in operating assets and liabilities added a total of EUR 2.8 million through trade accounts receivable, prepaid expenses and other current assets, accounts payable trade, accrued other liabilities and income taxes payable totaling EUR 4.7 million, offset by EUR 1.9 million from inventories.

Net cash provided by our operating activities was EUR 4.3 million for 2002 compared to EUR 7.5 million for 2001, and was primarily the result of net income and adjustments to reconcile net income to net cash flows from operating activities. We adjusted our net income of EUR 0.3 million to reconcile it to net cash flows from operating activities. Adjustments included (1) depreciation of EUR 1.0 million and (2) amortization of photographs and videos of EUR 5.8 million offset by (3) deferred income taxes of EUR 0.2 million, providing a total of EUR 6.9 million. We reduced the total of EUR 6.9 million by the increases in related party receivable, inventories, prepaid expenses and other current assets and income taxes payable totaling EUR 6.7 million, and we offset this reduction with EUR 4.2 million from trade accounts receivable accounts payable trade and accrued other liabilities.

Investing Activities

Net cash used in investing activities for the fiscal year ended December 31, 2004 was EUR 5.1 million. The investing activities were investment in library of photographs and videos of EUR 4.9 million, which were carried out in order to maintain the 2003 and 2004 release schedules for magazines, videos, DVDs and broadcasting. In addition to investment in library of photographs and videos, EUR 3.3 million was invested in capital expenditures, which was principally related to the completion of our building, and EUR 1.3 million was invested in a note receivable which was acquired in connection with our US subsidiary s restructuring of its US distribution. The total cash used in investing activities was offset by EUR 4.4 million from sale of part of the building. The decrease over the comparable twelve-month 2003 period is principally due to decreases in investment in library of photographs and videos and building related activities included in capital expenditures and sale of part of building, offset by the net effect of note receivable and the absence of investment in other intangible assets and sale of short-term investment. 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 latter half of 2004 cash-flow improved and we increased the acquisition of movie productions and the Company expects to attain optimum release frequency of new movie productions during the first half of 2005.

Net cash used in investing activities for the fiscal year ended December 31, 2003 was EUR 9.6 million. The investing activities were investment in library of photographs and videos of EUR 7.0 million, which were carried out in order to maintain the 2003 and 2004 release schedules for magazines, videos, DVDs and broadcasting. In addition to investment in library of photographs and videos, EUR 3.3 million was invested in other intangible assets and EUR 2.0 million was invested in capital expenditures. The total cash used in investing activities was offset by EUR 2.7 million from sale of short-term investment, which was used to reduce the related party note payable. The decrease over the comparable twelve-month 2002 period is principally due to the absence of investments in a building included in capital expenditures in 2002.

Net cash used in investing activities for the fiscal year ended December 31, 2002 was EUR 21.6 million. The investing activities were investment in library of photographs and videos of EUR 8.5 million, which were carried out in order to maintain the 2002 and 2003 release schedules for magazines, videos, DVDs and broadband. In addition to investment in library of photographs and videos, EUR 13.1 million was invested in capital expenditures. The increase over the comparable twelve-month 2001 period is principally due to investments in a building included in capital expenditures primarily financed by related party note payable.

Financing Activities

Net cash used in financing activities for the fiscal year ended December 31, 2004 was EUR 0.5 million, represented primarily by EUR 4.8 million in repayments on short- and long-term borrowings offset by EUR 2.6 million in cash provided by short- and long-term borrowings and EUR 1.8 million in cash received for conversion of warrants. The main movements resulting in a net decrease of EUR 2.3 million in borrowings during the twelve-month period ended December 31, 2004 are described as follows:

The $2.0 million and $3.0 million loans from Beate Uhse AG were reduced by EUR 2.2 million, inclusive of exchange rate changes. As of December 31, 2004 the $2.0 million was repaid and the remaining balance on the $3.0 million loan was EUR 0.7 million. The $4.0 million Note held by Consipio Holding b.v. was reduced by EUR 0.4 million inclusive of exchange rate changes. As of December 31, 2004 the remaining balance on the Note was EUR 2.2 million.

In May 2003 Euro 1.65 million of the related party note payable to Luthares 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. During the twelve months ended December 31, 2004, the Company repaid Euro 0.3 million and subsequently the remaining balance was Euro 1.4 million.

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. In 2004 an additional EUR 2.45 million was received in order to pay for the completion of the construction of the building. In connection with the sale of part of the property in 2004 EUR 1.9 million was repaid and as of December 31, 2004 the remaining balance on the loan was EUR 2.3 million.

Net cash used in financing activities for the fiscal year ended December 31, 2003 was EUR 2.2 million, represented primarily by EUR 7.7 million in repayments on short- and long-term borrowings and related party note payable offset by EUR 5.5 million in cash received provided by short- and long-term borrowings and convertible notes. We attribute the change over the comparable twelve-month 2002 period to the following:

The $2.0 million and $3.0 million loans from Beate Uhse AG were reduced by EUR 2.0 million, inclusive of exchange rate changes. As of December 31, 2003 the remaining balance on the Loans was EUR 2.9 million. The $4.0 million Note held by Consipio Holding b.v. was reduced by EUR 1.2 million inclusive of exchange rate changes. As of December 31, 2003 the remaining balance on the Note was EUR 2.6 million.

In May 2003 Euro 1.65 million of the related party note payable to Luthares 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. In December 2003 the Company sold its short-term investment and paid Euro 2.7 million on the related party note payable. The note was originally payable at December 31, 2004, but has been re-negotiated and matures December 31, 2008. The note carries interest payable annually at EURIBOR + 1%. As of December 31, 2003, the balance outstanding on the note was EUR 2.2 million.

Effective September 2003, pursuant to securities purchase agreements entered into 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 (see Note 11 to the financial statements). Pursuant to the conditions of the agreements, the financing was completed October 27, 2003 and an aggregate net cash amount of EUR 1.9 million was received.

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 purposes of financing the construction of an office building and is secured by a mortgage on the building. The balance of the loan will be paid out over the remaining period of construction of the building, which is expected to be completed in May 2004.

Net cash provided by our financing activities for the fiscal year ended December 31, 2002 was EUR 12.0 million, represented primarily by related party note payable, short-term borrowings and conversion of warrants during the year offset by repayments of long-term borrowings. We attribute the increase over the comparable twelve-month 2001 period to related party note payable and short-term borrowings which result from loans provided by Beate Uhse in November and December 2002.

Non-Cash Transaction

The Company has a note payable to an entity controlled by the Company s principal shareholder. The amount payable at December 31, 2004 was EUR 0.7 million. In September 2004, the amount payable under the note was reduced by EUR 1.5 million as a result of certain adjustments provided for under the December 2002 Share Purchase Agreement for the outstanding stock of Barbuda BV for which the note payable relates to.

Contractual obligations

The table below describes the Company s future contractual obligations, including items not included in the consolidated balance sheet, as of December 31, 2004:

	Amounts due in				
	Less than one year	One to three years	Three to five years	More than five years	Total
	EUR	EUR	EUR	EUR	EUR
	(in thousands)				
Long-term debt:					
Banks(1)	701	1,378	743	1,413	4,236
Non-institutional debt(1)	3,081	46	751		3,879
Convertible Note(2)(3)	100	1,523			1,623
Total long-term debt	3,883	2,948	1,494	1,413	9,738
Operating leases(4)(5)	525	1,037	103		1,664
Capital lease obligations(5)	47	28			74
	4,455	4,012	1,597	1,413	11,476

The pro-forma table below has been adjusted to show the effects of matters discussed in subsequent events, see Note 22 to the financial statements, and describes the Company s future contractual obligations, including items not included in the consolidated balance sheet, as of December 31, 2004:

	Amounts due in				
	Less than one year	One to three years	Three to five years	More than five years	Total
	EUR	EUR	EUR	EUR	EUR
	(in thousands)				
Long-term debt:					
Banks(1)	2,800	839	205		3,844
Non-institutional debt(1)	3,786				3,786
Convertible Note(2)(3)	100	1,523			