GLATFELTER P H CO
Form 10-K
March 16, 2007

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

[X]	Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal year ended **December 31, 2006** 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 **1-03560**

P. H. Glatfelter Company
(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	**23-0628360** (IRS Employer Identification No.)
96 South George Street, Suite 500 **York, Pennsylvania 17401** (Address of principal executive offices)	**(717) 225-4711** (Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Class	Name of Exchange on which registered
Common Stock, par value $.01 per share	**New York Stock Exchange**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes _ No ü.

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes _ No ü.

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 preceding 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 at least the past 90 days. Yes ü 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 of 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 a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes _ No ü .

Based on the closing price as of June 30, 2006, the aggregate market value of Common Stock of the Registrant held by non-affiliates was $517.3 million.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.
_ Large Accelerated ü Accelerated _ Non-Accelerated.

Common Stock outstanding on March 8, 2007 totaled 45,472,226 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the following documents are incorporated by reference in this Annual Report on Form 10-K:
Proxy Statement to be dated on or about March 21, 2007 (Part III).

P. H. GLATFELTER COMPANY
ANNUAL REPORT ON FORM 10-K
For the Year Ended

DECEMBER 31, 2006

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ITEM 1. BUSINESS

Overview Glatfelter began operations in 1864 and today we believe we are one of the world s leading manufacturers of specialty papers and engineered products. Headquartered in York, Pennsylvania, we own and operate paper mills located in Spring Grove, Pennsylvania, Chillicothe and Fremont, Ohio, Gernsbach, Germany, Gloucestershire, the United Kingdom and Scaër, France, as well as an abaca pulp mill in the Philippines.

We serve customers in numerous markets, including book publishing, carbonless and forms, envelope and converting, engineered products, food and beverage, composite laminates and other highly technical niche markets. Many of the markets in which we operate are characterized by higher-value-added products and, in some cases, by higher growth prospects and lower cyclicality than commodity paper markets. Examples of some of our key product offerings include papers for:

- trade book publishing;
- tea bags and coffee filters;
- carbonless products;
- specialized envelopes;
- playing cards;
- pressure-sensitive postage stamps;
- metallized labels for beer bottles; and
- digital imaging applications.

Recent Developments On March 13, 2006, we completed our acquisition of certain assets of JR Crompton, a global supplier of wet laid nonwoven products based in Manchester, United Kingdom. Since February 7, 2006, Crompton had been subject to insolvency proceedings before The High Court of Justice Chancery Division, Manchester District.

Under the terms of our agreement with Crompton, we acquired Crompton s Lydney mill, located in Gloucestershire, United Kingdom, for approximately $65 million based on currency exchange rates on that date. The facility employs approximately 240 people and had 2005 revenues of approximately $75 million. The Lydney mill, which is now included in our Composite Fibers business unit, produces a broad portfolio of wet laid nonwoven products, including tea bags and coffee filter papers, clean room wipes, lens tissue and dye filter paper, double-sided adhesive tape substrates and battery grid pasting tissue. The acquisition of the Lydney mill further strengthened our leading position in tea bags and coffee filter papers and is part of our long-term strategy to drive growth in our Composite Fibers business unit.

On April 3, 2006, we completed our acquisition of the carbonless business operations of NewPage Corporation, for $83.3 million in cash. The acquired assets consist of a 400,000 ton-per-year paper making facility in Chillicothe, Ohio and coating operations based in Fremont, Ohio (collectively referred to as Chillicothe). Chillicothe had revenue of $441.5 million in 2005 and approximately 1,700 employees as of December 31, 2006.

We executed the Chillicothe acquisition so that we could take advantage of Chillicothe s scale and efficient manufacturing environment. As part of our integration plan for Chillicothe, we transferred the production of products manufactured at our former Neenah, WI facility to Chillicothe and permanently shut down our Neenah facility on June 30, 2006.

On April 3, 2006, we entered into our new credit facility, which provides for a $200 million revolving credit facility and a $100 million term loan. Proceeds from our new credit facility were used to repay in full all amounts outstanding under our former revolving credit facility due June 2006, to finance the Chillicothe acquisition and for general corporate purposes.

In addition, on April 28, 2006 we completed a $200 million bond offering, the proceeds of which were primarily used to prepay our $150 million bonds.

Our Business Units We manage our business as two distinct units: the Europe-based Composite Fibers business unit and the North America-based Specialty Papers business unit. The following table summarizes consolidated net sales and the relative net sales contribution of each of our business units for the past three fiscal years:

Dollars in thousands	**2006**	2005	2004
Net sales	**$ 986,411**	$ 579,121	$ 543,524
Business unit composition			
Specialty Papers	**70.3%**	65.8%	62.1%
Composite Fibers	**29.7**	34.2	37.8
Other			0.1
Total	**100.0%**	100.0%	100.0%

Net tons sold by each business unit for the past three years were as follows:

	2006	**2005**	**2004**
Specialty Papers	**653,734**	450,900	421,504
Composite Fibers	**68,148**	47,669	48,528
Other	**10**	24	390
Total	**721,892**	498,593	470,422

Specialty Papers Our North America-based Specialty Papers business unit focuses on papers for the production of high-quality hardbound books and other book publishing needs, carbonless papers designed for multiple end-uses, such as credit card receipts, forms and other applications, envelope & converting markets and highly technical customized products for the digital

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imaging, casting and release, pressure sensitive, and several niche technical specialty markets.

Specialty Papers revenue composition by market consisted of the following for the years indicated:

in thousands	**2006**	2005	2004
Book publishing	**$ 166,605**	$ 157,269	$ 142,756
Carbonless & Forms	**266,647**		
Envelope & converting	**103,042**	91,751	81,582
Engineered products	**137,007**	129,936	113,098
Other	**20,359**	1,967	
Total	**$ 693,660**	$ 380,923	$ 337,436

We believe we are the leading supplier of book publishing papers in the United States and one of two carbonless paper market leaders. Specialty Papers also produces paper that is converted into specialized envelopes in a wide array of colors, finishes and capabilities. These markets are generally more mature and, therefore, have modest growth characteristics. The market for carbonless papers is declining approximately 7% to 9% per year.

Specialty Papers highly technical engineered products include those designed for multiple end uses, such as papers for pressure-sensitive postage stamps, greeting and playing cards, digital imaging applications and for release paper applications. Such products comprise an array of distinct business niches that are in a continuous state of evolution. Many of these products are utilized in demanding, specialized customer and end-user applications. Some of our products are new and high growth while others are more mature and further along on the development curve. Because many of these products are technically complex and involve substantial customer-supplier development collaboration, they command higher per ton values and generally exhibit greater pricing stability relative to commodity grade paper products.

As of April 3, 2006, our Specialty Papers business unit includes the Chillicothe operations.

Composite Fibers Composite Fibers, based in Gernsbach, Germany, focuses on higher-value-added products, such as paper for tea bags and coffee pods/pads and filters, decorative laminates used for furniture and flooring, and metallized products used in the labeling of beer bottles.

Composite Fibers revenue composition by market consisted of the following for the years indicated:

in thousands	**2006**	2005	2004
Food & Beverage	**$ 180,258**	$ 103,070	$ 107,482
Composite Laminates	**50,734**	42,948	47,342
Metallized	**40,078**	35,541	33,286
Technical Specialties and Other	**21,681**	16,578	17,122

Total	**$ 292,751**	$ 198,137	$ 205,232

Our focus on products made from abaca pulp has made us one of the world s largest producers of tea bag papers. The balance of this unit s sales are comprised of overlay and technical specialty products, which include flooring and furniture overlay papers, metallized products, and papers for adhesive tapes, vacuum bags, holographic labels and gift wrap. Many of this unit s papers are technically sophisticated. We believe we are well positioned to produce these extremely lightweight papers because we understand their complexities, which require the use of highly specialized fiber and specifically designed papermaking equipment.

As of March 13, 2006, our Composite Fibers business unit includes the Lydney mill.

Additional financial information for each of our business units is included in Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and in Item 8 Financial Statements, Note 20.

Our Competitive Strengths Since commencing operations over 140 years ago, we believe that Glatfelter has developed into one of the world s leading manufacturers of specialty papers and engineered products. We believe that the following competitive strengths have contributed to our success:

Leading market positions in higher-value, niche segments. We have focused our resources to achieve market-leading positions in certain higher-value, niche segments. Our products include various highly specialized paper products designed for technically demanding end uses. Consequently, many of our products achieve premium pricing relative to that of commodity paper grades. In 2006, approximately 82% of our sales were derived from these higher-value, niche products. The specialized nature of these products generally provides greater pricing stability relative to commodity paper products.

Customer-centric business focus. We offer a unique and diverse product line that can be customized to serve the individual needs of our customers. Our size allows us to develop close relationships with our key customers and to be adaptable in our product development, manufacturing, sales and marketing practices. We believe that this approach has led to the development of excellent customer relationships, defensible market positions, and increased pricing stability relative to commodity paper producers. Additionally, our customer-centric focus has been a key driver to our success in new product development.

Significant investment in product development. In order to keep up with our customers ever-changing needs, we continually enhance our product offerings through significant investment in product development. During 2006, 2005 and 2004, we invested approximately $8.0 million, $4.9 million and $5.2 million, respectively, in product development activities. We derive a significant portion of our revenue from products developed, enhanced or improved as a result of these activities. Revenue generated from products developed, enhanced or improved within the five previous years as a result of these activities represented approximately 52%, 52% and 60% of net sales in the years ended 2006, 2005 and 2004, respectively.

Integrated production. As a partially integrated producer, we are able to mitigate changes in the costs of certain raw materials and energy. Our Spring Grove and Chillicothe facilities are vertically integrated operations producing in excess of 85% of the annual pulp required for their paper production. The principal raw material used to produce this pulp is pulpwood, consisting of both hardwoods and softwoods. We own approximately 75,000 acres of timberlands and, in 2006, obtained approximately 20% of our pulpwood requirements for our Spring Grove facility from Glatfelter-owned timberlands, which helps stabilize our fiber costs in a highly fragmented market. Our Spring Grove and Chillicothe facilities also generate 100% of the steam and substantially all of the electricity required for their operations. In addition, our Philippine mill processes abaca fiber to produce abaca pulp, which is a key raw material used by our Composite Fibers business unit.

Our Business Strategy Our vision is to become the global supplier of choice in specialty papers and engineered products. We are continuously developing and refining strategies to strengthen our business and position it for the future. Execution of these strategies is intended to capitalize on our customer relationships, technology and people, as well as our leadership positions in certain product lines. In recent years, our industry has been challenged by a supply and demand imbalance, particularly for commodity-like products. While the industry has responded to take out under-performing capacity, the imbalance continues. To be successful in the current market environment, our strategy is focused on aggressively reducing costs and continually repositioning our product portfolio to increase our focus on higher-value, niche products and to better align our product offerings with our customers ever-changing needs. Certain key elements of our business strategy are outlined below:

Reposition our product portfolio. By leveraging our leadership positions in several specialty niche segments, we plan to accelerate growth, improve margins and generate better financial returns through the optimization of our product portfolio. In 2006, approximately 82% of our total sales were derived from what we consider to be higher-value, niche products. Over time, we plan to increase our concentration on such products by driving growth in our sales of trade book papers, uncoated specialty products, composite fiber products and other specialty products. The recently acquired Chillicothe assets provide a significant scaleable production platform to support this strategy. We believe that this strategy will realign our business more closely with our customers needs and further reduce our exposure to the higher level of cyclicality experienced in commodity paper grades.

Execute Composite Fibers growth plan. A core component of our long-term strategy is to drive growth in our Composite Fibers business unit. Currently, we are the leading producer of tea bag and coffee pod/pad papers in the world, and with the Lydney mill acquisition we have further strengthened our competitive position. We believe that this segment has promising growth characteristics as certain geographies move toward the use of tea bags as opposed to loose tea leaves. We believe that we are well positioned to capitalize on this growth by leveraging our strong customer relationships and leading position in this segment.

Employ a low-cost approach to specialty product manufacturing. While we are focused on higher-value, niche products, we seek to employ a commodity-like, low-cost approach to our manufacturing activities. In 2004, we initiated the North American Restructuring Program that improved operating results by, among other factors, improving workforce efficiencies and implementing improved supply chain management processes. In the fourth quarter of 2005, we began the implementation of the European Optimization and Restructuring Program, or the EURO Program, a comprehensive series of actions designed to improve the performance of the Composite Fibers business unit. The pre-tax financial benefits of the EURO Program approximated $8 million in 2006. To further improve our production cost profile, in connection with the 2006 Chillicothe acquisition, we closed our Neenah facility and transferred its production to the more efficient Chillicothe facility.

Maintain a strong balance sheet and preserve financial flexibility. We are focused on prudent financial management and the maintenance of a conservative capital structure. We are committed to maintaining a strong balance sheet and preserving our flexibility so that we may pursue strategic opportunities, including strategic acquisitions, that will benefit our company.

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Timberland Strategy. We completed an extensive study to determine the optimal approach for managing our timberlands in a way that creates the greatest value for our company. The study considered many factors including, among others, land valuations, external and internal wood costs and future fiber requirements. We concluded that the most advantageous approach is to sell 60,000 acres of higher and better use, or HBU, properties in an orderly fashion. In some cases, low-cost, low-risk opportunities may exist to add value to some of these acres through entitlements. It is estimated that once all 60,000 HBU acres are sold, earnings will be adversely impacted by approximately $0.04 to $0.07 per share, but we believe that the expected proceeds from these planned sales will outweigh this increased cost. Currently, we intend to retain the pure timberland properties to mitigate the cost of replacing internally generated wood with outside sources. Execution of our Timberland Strategy is expected to take approximately two to four more years to complete and is estimated to provide pre-tax cash proceeds totaling in excess of $150 million, assuming, among other factors, acceptable market conditions and a carefully executed plan of disposition.

Raw Material and Energy The following table provides an overview of the estimated amount of principal raw materials (PRM) to be used by each of our manufacturing facilities on an annual basis:

	Estimated Annual Quantity (short tons)	**Percent of PRM Purchased**
Specialty Papers		
Spring Grove		
Pulpwood	1,026,000	85%
Wood and other pulps	40,000	100
Chillicothe		
Pulpwood	1,164,000	100
Wood and other pulps	36,000	100
Composite Fibers		
Gernsbach		
Wood and other pulps	29,400	100
Abaca pulp	8,500	11
Synthetic fiber	2,350	100
Lydney		
Wood and other pulps	6,850	100
Abaca pulp	5,800	11
Synthetic fiber	2,040	100
Scaër		
Wood pulp	2,150	100
Abaca pulp	1,840	11
Synthetic fiber	1,330	100

Philippines		
Abaca fiber	18,000	100

Our Spring Grove mill is a vertically integrated operation producing approximately 85% of the annual pulp required for paper production. The principal raw material used to produce this pulp is pulpwood, of which both hardwoods and softwoods are used. At December 31, 2006, we owned approximately 75,000 acres of timberlands. In addition to this source of pulpwood, we are committed, under a Supply Agreement expiring in 2011, to buy at market prices a minimum annual amount of pine pulpwood averaging 34,425 tons per annum over the eight-year term of the agreement. The pulpwood purchased under this agreement is to be harvested from land we sold in March 2003.

In addition to these sources, hardwoods are available within a relatively short distance of our mills. Softwoods are obtained primarily from Maryland, Delaware and Virginia. To protect our sources of pulpwood, we actively promote conservation and forest management among suppliers and woodland owners.

Our Spring Grove, Pennsylvania facility generates 100% of the steam and electricity required for its operations. Principal fuel sources used by this facility are coal, recycled pulping chemicals, bark and wood waste, and oil. The facility consumes approximately 300,000 tons of coal annually. A new three year contract became effective January 1, 2007, which will increase our annual cost of coal by approximately $6 million.

The Spring Grove facility produces more electricity than it requires. Excess electricity is sold to the local power company under a fixed-price long-term co-generation contract expiring in 2010. Energy sales, net of costs, were $10.7 million in 2006, $10.1 million in 2005 and $10.0 million in 2004. The continuation of this revenue stream at these levels is dependent on our ability to negotiate a contract for periods beyond 2010. As discussed elsewhere in this report, we entered into a new three-year coal supply agreement beginning in January 2007. The increased cost of coal under this contract will adversely effect net revenue from energy sales.

Our Chillicothe mill is also a vertically integrated operation producing approximately 92% of its annual pulp requirements for paper production in 2006. The principal raw material used to produce this pulp is pulpwood, of which both hardwoods and softwoods are used. Pulpwood is sourced externally at market prices. Both hardwoods and softwoods are sourced primarily from Ohio, West Virginia and Kentucky.

Our Chillicothe facility generates 100% of the steam and 85% of the electricity required for its operations. Principal fuel sources used by the Chillicothe facility are natural gas, coal, waste wood and black liquor, which is a byproduct of the pulp making process. The facility consumes approximately 900,000 MMBTUs of natural gas, 315,000 tons of coal and 300,000 tons of wastewood annually. Two new coal supply agreements were executed in the fourth quarter of 2006 and expire in December 2007 and November 2008.

The Gernsbach, Scaër and Lydney facilities generate all of the steam required for their operations. The Gernsbach facility generated approximately 26% of its 2006 electricity needs and purchased the balance. The Scaër and Lydney facilities purchased all of their 2006 electric power requirements. Natural gas was used to produce substantially all internally generated energy at the Gernsbach, Scaër and Lydney facilities during 2006.

Our Philippines mill processes abaca fiber to produce a specialized pulp. This abaca pulp production provides a unique advantage by supplying a key raw material used by our Composite Fibers business unit. Events may arise from the relatively unstable political and economic environment in which the Philippine facility operates that could interrupt the production of abaca pulp. Management periodically evaluates the availability of abaca pulp for our Composite Fibers business unit. Any extended interruption of the Philippine operation could have a material impact on our consolidated financial position and/or results of operations. We have approximately three months of abaca pulp supply available to us. In addition, we have established contingency plans for alternative sources of abaca pulp. However, the cost of obtaining abaca pulp from such alternative sources, if available, would likely be higher.

Based on information currently available, we believe that we will continue to have ready access, for the foreseeable future, to all principal raw materials used in the production of our products. The cost of our raw material is subject to change, including, but not limited to, costs of wood and pulp products and energy.

New Product Development In order to keep up with our customers ever-changing needs, we are continually enhancing our product offerings through significant investment in product development activities, including product customizations developed in partnership or close collaboration with our customers. We invested approximately $8.0 million, $4.9 million and $5.2 million in 2006, 2005 and 2004, respectively, on product development. Revenue generated from products developed, enhanced or improved within the five previous years as a result of these activities represented approximately 52%, 52% and 60% of net sales in the years ended 2006, 2005 and 2004, respectively. In determining revenue attributable to product development activities, we utilize an independently developed framework, which we believe to be generally accepted in the field of new product management. This framework categorizes products developed, enhanced or improved as those that (i) are new to the world, (ii) represent a product line new to our Company, (iii) are a new product within an existing product line, (iv) are a significant improvement of an existing product, (v) are repositioned into a new application or market, or (vi) are a lower cost alternative to an existing product of the Company and seen by our customers as a new offering. Approximately 42% of our revenue attributable to developed, enhanced or improved products come from products that fit within category (ii) and (iii), above.

Concentration of Customers In 2006, 2005 and 2004, no single customer represented more than 10% of our consolidated net sales.

Competition Our industry is highly competitive. We compete on the basis of the quality of our products, customer service, product development activities, price and distribution. We offer our products throughout the United States and globally in approximately 80 countries. Competition in the markets in which we participate comes from companies of various sizes, some of which have greater financial and other resources than we do.

There are a number of companies in the United States that manufacture printing and converting papers. We believe we are the recognized leader in book publishing papers and compete in these markets with, among others, Domtar and Fraser. In the envelope sector we compete with, among others, International Paper, Domtar and Blue Ridge. In the carbonless paper and forms market, we compete with Appleton Papers. In our Specialty Papers engineered products markets and for the Composite Fibers business unit s markets, competition is product line specific as the necessity for technical expertise and specialized manufacturing equipment limits the number of companies offering multiple product lines. We compete with specialty divisions of large companies such as, among others, Ahlstrom, International

Paper, MeadWestvaco, Sappi and Stora Enso. Service, product performance, technological advances and product pricing are important competitive factors with respect to all our products. We believe our reputation in these areas continues to be excellent.

Despite the production capacity that has been removed, capacity in the worldwide uncoated free-sheet industry continues to exceed demand in recent years.

Environmental Matters We are subject to loss contingencies resulting from regulation by various federal, state, local and foreign governmental authorities with respect to the environmental impact of our mills. To comply with environmental laws and

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regulations, we have incurred substantial capital and operating expenditures in past years. For a discussion of environmental matters, see Item 8. Financial Statements and Supplementary Data Note 19.

Employees The following table summarizes our workforce as of December 31, 2006:

Location	Union	Employees Non-Union	Total
U.S.			
Corporate/Spring Grove	605	360	965
Chillicothe/Fremont	1,293	410	1,703
	1,898	770	2,668
International			
Gernsbach, Germany	370	191	561
Scaër, France	80	47	127
Gloucestershire, UK (Lydney)	205	61	266
Philippines	52	30	82
	707	329	1,036
Total	2,605	1,099	3,704

Different locals of the United Steelworkers of America (USW), represent the hourly employees at our U.S. facilities.

A five-year labor agreement in Spring Grove will end in January 2008. Negotiations for a new contract will begin in the first half of 2007. The negotiation approach is expected to take the same collaborative approach as the last negotiation held in Spring Grove during 2002 due to the continued positive relationship with the employees.

The labor contract with the USW local unions representing the hourly employees at the newly acquired facility in Chillicothe Ohio expired on August 1, 2006. On November 10, 2006, a new 3-year contract was ratified across the multiple local unions.

Various unions represent employees at our European facilities. New labor agreements covering employees at the Gernsbach, Germany and Scaër, France facilities were entered into effective May 1, 2005 that provided for wage increase averaging 1.5% over a 22 month period ending March 2007. Employees at our Lydney mill participate in a national trade agreement pursuant to which we negotiate separate union agreements. Such agreements generally cover a one year period from February 1 to January 31. We expect to begin union negotiations in late March 2007.

Employees at our pulpmill in the Philippines are covered by a five-year labor agreement, which was negotiated at the end of 2002.

We consider the overall relationship with our employees to be satisfactory.

Available Information Our investor relations website address is www.glatfelter.com/e/investstock.asp. We make available on our site free of charge our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K and other related information as soon as reasonably practical after they are filed with the Securities and Exchange Commission. In addition, our website includes a Corporate Governance page consisting of, among others, our Governance Principles and Code of Business Conduct, Board of Directors and Executive Officers, Nominating, Audit and Compensation Committees of the Board of Directors and their respective Charters, Code of Business Ethics for the CEO and Senior Financial Officers of Glatfelter, our whistle-blower policy and other related material. We intend to satisfy the disclosure requirement for any future amendments to, or waivers from, our Code of Business Conduct or Code of Business Ethics for the CEO and Senior Financial Officers by posting such information on our website. We will provide a copy of the Code of Business Conduct or Code of Business Ethics for the CEO and Senior Financial Officers, without charge, to any person who requests one, by calling (717) 225-2724.

ITEM 1A. RISK FACTORS

Risks Related to Our Business

Our business and financial performance may be adversely affected by downturns in the target markets that we serve.

Demand for our products in the markets we serve is primarily driven by consumption of the products we produce, which is most often affected by general economic conditions. In recent years, the global paper industry in which we compete has been adversely impacted by paper producing capacity exceeding the demand for products. Downturns in our target markets could result in decreased demand for our products. In particular, our business may be adversely affected during periods of economic weakness by the general softness in these target markets. Our results could be adversely affected if economic conditions weaken or fail to improve. Also, there may be periods during which demand for our products is insufficient to enable us to operate our production facilities in an economical manner. These conditions are beyond our ability to control and have had, and may continue to have, a significant impact on our sales and results of operations.

In addition to fluctuations in demand for our products in the markets we serve, the markets for our paper products are also significantly affected by changes in industry capacity and output levels. There have been periods of supply/demand imbalance in the pulp and paper industry, which have caused pulp and paper prices to be volatile. The timing and magnitude of price increases or decreases in the pulp and paper market

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have generally varied by region and by product type. A sustained period of weak demand or excess supply would likely adversely affect pulp and paper prices. This could have a material adverse affect on our operating and financial results.

Our industry is highly competitive and increased competition could reduce our sales and profitability.

In recent years, the global paper industry in which we compete has been adversely affected by paper producing capacity exceeding the demand for products. As a result, the industry has taken steps to reduce underperforming capacity. However, slowing demand or increased competition could force us to lower our prices or to offer additional services at a higher cost to us, which could reduce our gross margins and net income. The greater financial resources of certain of our competitors may enable them to commit larger amounts of capital in response to changing market conditions. Certain competitors may also have the ability to develop product or service innovations that could put us at a disadvantage.

Some of the factors that may adversely affect our ability to compete in the markets in which we participate include:

- the entry of new competitors into the markets we serve, including foreign producers;
- the willingness of commodity-based paper producers to enter our specialty markets when they are unable to compete or when demand softens in their traditional markets;
- the aggressiveness of our competitors pricing strategies, which could force us to decrease prices in order to maintain market share;
- our failure to anticipate and respond to changing customer preferences;
- our inability to develop new, improved or enhanced products; and
- our inability to maintain the cost efficiency of our facilities.

If we cannot effectively compete in the markets in which we operate, our sales and operating results would be adversely affected.

The cost of raw materials and energy used to manufacture our products could increase.

We require access to sufficient and reasonably priced quantities of pulpwood, wood and other pulps, pulp substitutes, abaca fiber and certain other raw materials. Our Spring Grove facility is a vertically integrated manufacturing facility that generates approximately 85% of its annual pulp requirements. In addition, approximately 20% of its annual pulpwood requirements in 2006 were satisfied from company-owned timberlands. However, while our Chillicothe facility makes its own pulp, it purchases wood for use in its pulp mill. Our Philippine mill purchases abaca fiber to make pulp, which we use to manufacture our composite fiber products at our Gernsbach, Scaër and Lydney facilities.

Coal is a principal source of fuel for our Spring Grove facility. Beginning in 2007 a new three-year coal supply contract will increase our annual cost of coal by approximately $6 million.

Natural gas is the principal source of fuel for our Chillicothe and Composite Fibers business unit facilities. Natural gas prices have increased significantly in the United States since 2000 and reached record highs in 2006. Prices for natural gas are expected to remain volatile for the foreseeable future.

We may not be able to pass increased raw materials or energy prices on to our customers if the market will not bear the higher price or where existing agreements with our customers do not allow us to pass along these cost increases. If price adjustments significantly trail increases in raw materials or energy prices our operating results could be adversely affected.

We are subject to substantial costs and potential liability for environmental matters.

We are subject to various environmental laws and regulations that govern our operations, including discharges into the environment, and the handling and disposal of hazardous substances and wastes. We are also subject to laws and regulations that impose liability and clean-up responsibility for releases of hazardous substances into the environment. To comply with environmental laws and regulations, we have incurred, and will continue to incur, substantial capital and operating expenditures. We anticipate that environmental regulation of our operations will continue to become more burdensome and that capital and operating expenditures necessary to comply with environmental regulations will continue, and perhaps increase, in the future. Because environmental regulations are not consistent worldwide, our ability to compete in the world marketplace may be adversely affected by capital and operating expenditures required for environmental compliance. In addition, we may incur obligations to remove or mitigate any adverse effects on the environment, such as air and water quality, resulting from mills we operate or have operated. Potential

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obligations include compensation for the restoration of natural resources, personal injury and property damages.

In connection with the sale of our Ecusta Division in 2001, we are incurring landfill closure costs and may incur additional costs for recognized environmental concerns at the site of our former mill related to the presence of mercury and certain other contamination on and around the site; potentially hazardous conditions existing in the sediment and water column of the site s water treatment and aeration and sedimentation basin (the ASB); and contamination associated with two additional landfills on the site that were not used by us.

We are also liable for the costs of clean-up related to the presence of polychlorinated biphenyls, or PCBs, in the lower Fox River on which our former Neenah, Wisconsin mill was located. We have financial reserves for environmental matters but we cannot be certain that those reserves will be adequate to provide for future obligations related to these matters, that our share of costs and/or damages for these matters will not exceed our available resources, or that such obligations will not have a long-term, material adverse effect on our consolidated financial position, liquidity or results of operations.

Our environmental issues are complicated and should be reviewed in context; please see a more detailed discussion of these matters in Item 8 Financial Statements, Note 19.

We may not achieve our anticipated synergies from our Chillicothe and Lydney acquisitions.

In 2006, we acquired Chillicothe and the Lydney mill. Inherent risks in business combinations such as these include the inability to successfully integrate the acquired production facility and its procurement, marketing and sales requirements, as well as information systems, finance and administration functions. With respect to Chillicothe, although in 2006 we have made progress transitioning book products, we cannot assure you that we will be able to successfully produce the products in a cost effective manner necessary to provide higher levels of return.

With respect to the Lydney mill, in December 2006, we received unconditional regulatory clearance for this acquisition and are in the process of implementing integration plans. However, we cannot assure you that these integration plans will be completed timely or that the full financial benefits of the acquisition will be realized.

Our inability to successfully execute the plans discussed above may adversely affect our relationships with customers, suppliers and employees. Accordingly, our financial results may be adversely affected.

We have operations in a politically and economically unstable location.

We own and operate a pulp mill in the Philippines where the operating environment is unstable and subject to political unrest. Our Philippine pulp mill produces abaca pulp, a significant raw material used by our Composite Fibers business unit. Our Philippine pulp mill is currently the main provider of abaca pulp. There are limited suitable alternative sources of readily available abaca pulp in the world. In the event of a disruption in supply from our Philippine mill, there is no guarantee that we could obtain adequate amounts of abaca pulp from alternative sources at a reasonable price or at all. As a consequence, any civil disturbance, unrest, political instability or other event that causes a disruption in supply could limit the availability of abaca pulp and would increase our cost of obtaining abaca pulp. Such occurrences could adversely impact our sales volumes, revenues and operating results.

We may not be able to develop new products acceptable to our customers.

Our business strategy is market focused and includes investments in developing new products to meet the changing needs of our customers and to maintain our market share. Our success will depend in large part on our ability to develop and introduce new and enhanced products that keep pace with introductions by our competitors and changing customer preferences. If we fail to anticipate or respond adequately to these factors, then we may lose opportunities for business with both current and potential customers. The success of our new product offerings will depend on several factors, including our ability to,

- anticipate and properly identify our customers needs and industry trends;
- price our products competitively;
- develop and commercialize new products and applications in a timely manner;
- differentiate our products from our competitors products; and
- invest in research and development activities efficiently.

Our inability to develop new products could adversely impact our business and ultimately harm our profitability.

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Our international operations pose certain risks that may adversely impact sales and earnings.

We have significant operations and assets located in Germany, France, the United Kingdom, and the Philippines. Our international sales and operations are subject to a number of special risks, in addition to the risks of our domestic sales and operations, including differing protections of intellectual property, trade barriers, labor unrest, exchange controls, regional economic uncertainty, differing (and possibly more stringent) labor regulation, risk of governmental expropriation, domestic and foreign customs and tariffs, differing regulatory environments, difficulty in managing widespread operations and political instability and unrest. These factors may adversely affect our future profits. Also, in some foreign jurisdictions we may be subject to laws limiting the right and ability of entities organized or operating therein to pay dividends or remit earnings to affiliated companies unless specified conditions are met. Any such limitations would restrict our flexibility in using funds generated in those jurisdictions.

Foreign currency exchange rate fluctuations could adversely affect our results of operations.

We own and operate paper and pulp mills in Germany, France, the United Kingdom and the Philippines. The local currency in Germany and France is the Euro, in the UK the British Pound Sterling, and in the Philippines the currency is the Peso. During 2006, Euro functional currency operations generated approximately 21% of our sales and 19.8% of operating expenses and British Pound Sterling operations represented 6.1% of net sales and 6.4% of operating expenses. The translation of the results from these international operations into U.S. dollars is subject to changes in foreign currency exchange rates.

Our ability to maintain our products price competitiveness for our international operations is reliant, in part, on the relative strength of the currency in which the product is denominated compared to the currency of the market into which it is sold and the functional currency of our competitors. Changes in the rate of exchange of foreign currencies in relation to the U.S. dollar and other currencies may adversely impact our ability to offer products in certain markets at acceptable prices or our results of operations.

We may be unable to generate sufficient cash flow to simultaneously fund our operations, finance capital expenditures, satisfy obligations and make dividend payments on our common stock.

Our business is capital intensive and requires significant expenditures for equipment maintenance and new or enhanced equipment, for environmental compliance matters and to support our business strategies and research and development efforts. We expect to meet all of our near- and longer-term cash needs from a combination of operating cash flow, cash and cash equivalents, sale of timberlands, our existing credit facility or other bank lines of credit and other long-term debt. If we are unable to generate sufficient cash flow from these sources, we could be unable to meet our near and longer-term cash needs or make dividend payments.

We may be unable to achieve expected proceeds from a sale of our timberlands.

One of our primary business strategies is to sell 60,000 acres of higher and better use, or HBU, properties over a two to four year period. Our ability to sell these timberlands for the expected price depends on market conditions, including the availability of similar properties for sale that would compete with our properties. As a result, we may be unable to generate the pre-tax proceeds of more than $150 million we expect from the sale of these timberlands. It is estimated that our pre-tax cost of fiber will increase when all HBU acres are sold. These costs could be higher than estimated which could adversely affect our financial results.

Our indebtedness could adversely affect our financial health and prevent us from fulfilling our obligations under the notes.

We have now and will continue to have, a significant amount of indebtedness. As of December 31, 2006, we had $64.8 million of indebtedness outstanding under our revolving credit facility, $96.0 million of indebtedness outstanding under our term loan facility, $200 million of indebtedness outstanding under our 71/8% fixed rate bonds and $34.0 million of indebtedness outstanding under our note payable to SunTrust. Our indebtedness could materially and adversely affect us in a number of ways. For example, it could:

make it more difficult for us to satisfy our obligations with respect to the notes;

increase our vulnerability to adverse economic and industry conditions;

- require us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures and other general corporate purposes;

- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;

- place us at a disadvantage compared to our competitors that have less debt; and

- limit our ability to borrow additional funds, including for future acquisitions, to meet our operating expenses and for other purposes.

In addition, a substantial portion of our debt, including borrowings under our new credit facility, bears interest at variable rates. If market interest rates increase, variable-rate debt will create higher debt service requirements, which could adversely affect our cash flow. While we may enter into agreements limiting our exposure to higher interest rates, any such agreements may not offer complete protection from this risk.

ITEM 2. PROPERTIES

Our leased corporate offices are located in York, Pennsylvania. We own and operate paper mills located in Spring Grove, Pennsylvania; Chillicothe, Ohio; the United Kingdom; Gernsbach, Germany; and Scaër, France. In addition, we own and operate a pulp mill in the Philippines. Substantially all of the equipment used in our papermaking and related operations, with the exception of some leased vehicles, is also owned. All of our properties, other than those that are leased, are free from any material liens or encumbrances. We consider all of our buildings to be in good structural condition and well maintained and our properties to be suitable and adequate for present operations.

The following table summarizes the estimated production capacity of each of our facilities:

	Estimated Annual Production Capacity (short tons)	
Specialty Papers		
Spring Grove	315,000	Uncoated
	66,000	Coated
Chillicothe	400,000	Uncoated
	7,500	Coated
Composite Fibers		
Gernsbach	38,000	Lightweight
	11,400	Metallized
Scaër	6,100	Lightweight
Lydney	15,700	Lightweight
Philippines	12,240	Abaca pulp

The Spring Grove facility includes five uncoated paper machines that have been rebuilt and modernized from time to time. It has an off-line combi-blade coater and a Specialty Coater (S-Coater), which together yield a potential annual production capacity for coated paper of approximately 66,000 tons. Since uncoated paper is used in producing coated paper, this is not additional capacity. We view the S-Coater as an important asset that allows us to expand our more profitable engineered paper products business.

The Spring Grove facility also includes a pulpmill that has a production capacity of approximately 650 tons of bleached pulp per day. We have a precipitated calcium carbonate (PCC) plant at our Spring Grove facility that produces PCC at a lower cost than could be purchased from others and lowers the need for higher-priced raw material typically used for increasing the opacity and brightness of certain papers.

The Chillicothe facility operates four paper machines which together yield a potential annual production capacity of uncoated and carbonless paper of approximately 400,000 tons. In addition, this location has produces 7,500 tons per year of other coated paper. This facility also includes a pulpmill that has a production capacity of approximately 955 tons of bleached pulp per day.

Our Philippines facility consists of a pulpmill that supplies a majority of the abaca pulp requirements of the Composite Fibers paper mills.

The Gernsbach facility includes five uncoated paper machines with an aggregate annual lightweight capacity of about 38,000 tons. In 2003, we rebuilt a paper machine with new state-of-the-art inclined wire technology. We believe this machine provides us greater flexibility and technological capabilities. The Gernsbach facility also has the capacity to produce 11,400 tons of metallized papers annually, using a lacquering machine and two metallizers. We purchase the base paper used to manufacture the metallized paper.

The Scaër facility operates two paper machines with an annual lightweight capacity of 6,100 tons and the Lydney facility operates three paper machines with an annual lightweight capacity of 15,700 tons.

ITEM 3. LEGAL PROCEEDINGS

We are involved in various lawsuits that we consider to be ordinary and incidental to our business. The ultimate outcome of these lawsuits cannot be predicted with certainty; however, we do not expect such lawsuits individually or in the aggregate, will have a material adverse effect on our consolidated financial position, liquidity or results of operations.

For a discussion of commitments, legal proceedings and related contingencies, see Item 8 Financial Statements and Supplementary Data Note 19.

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

Not Applicable no matters were submitted to a vote of security holders during the fourth quarter of 2006.

EXECUTIVE OFFICERS

The following table sets forth certain information with respect to our executive officers as of March 1, 2007.

Name	Age	Office with the Company
George H. Glatfelter II	55	Chairman and Chief Executive Officer
Dante C. Parrini	42	Executive Vice President and Chief Operating Officer
John P. Jacunski	41	Senior Vice President and Chief Financial Officer
Timothy R. Hess	40	Vice President and General Manager, Specialty Papers Business Unit
Jeffrey J. Norton	48	Vice President, General Counsel and Secretary
Martin Rapp	47	Vice President and General Manager, Composite Fibers Business Unit
Mark A. Sullivan	52	Vice President Global Supply Chain
William T. Yanavitch II	46	Vice President Human Resources and Administration
David C. Elder	38	Corporate Controller and Chief Accounting Officer

Officers are elected to serve at the pleasure of the Board of Directors. Except in the case of officers elected to fill a new position or a vacancy occurring at some other date, officers are generally elected at the organizational meeting of the Board of Directors held immediately after the annual meeting of shareholders.

George H. Glatfelter II is our Chairman and Chief Executive Officer. From April 2000 to February 2001, Mr. Glatfelter was Chairman, President and Chief Executive Officer. From June 1998 to April 2000, he was Chief Executive Officer and President.

Mr. Glatfelter serves as a director of Met-Pro Corporation.

Dante C. Parrini became Executive Vice President and Chief Operating Officer in February 2005. Prior to this, Mr. Parrini was Senior Vice President and General Manager, a position he held since January 2003. From December 2000 until January 2003, Mr. Parrini was Vice President Sales and Marketing. From July 2000 to December 2000, he was Vice President Sales and Marketing, Glatfelter Division and Corporate Strategic Marketing.

John P. Jacunski became Senior Vice President & Chief Financial Officer in July 2006. From October 2003 until July 2006, he was Vice President and Corporate Controller. Mr. Jacunski was previously Vice President and Chief Financial Officer at WCI Steel, Inc. from June 1999 to October 2003. From May 1995 to June 1999 he was WCI s Corporate Controller. Prior to joining WCI, Mr. Jacunski was with KPMG, an international accounting and consulting firm, where he served in various capacities.

Timothy R. Hess has been Vice President and General Manager Specialty Papers Business Unit since February 2006. Prior to this he was the Company s Director of Specialty Papers Business Unit, a position he held since January 2004. From 1994 until January 2004, Mr. Hess held various technical, manufacturing, sales and business development positions with Glatfelter.

Jeffrey J. Norton joined us in May 2005 and serves as Vice President, General Counsel and Secretary. Prior to joining Glatfelter, Mr. Norton was with Exelon Corporation, a $15 billion energy corporation, for 14 years where he was Assistant General Counsel.

Martin Rapp joined Glatfelter in August 2006 and serves as Vice President and General Manager Composite Fibers Business Unit. Prior to this Mr. Rapp was Vice President and General Manager of Avery Dennison s Roll Materials Business in Central and Eastern Europe since August 2002. From May 2000 until July 2002 Mr. Rapp was Partner and Managing Director of BonnConsult.

Mark A. Sullivan was appointed Vice President, Global Supply Chain in February 2005. Mr. Sullivan joined our company in December 2003, as Chief Procurement Officer. His experience includes a broad array of operations and supply chain management responsibilities during 20 years with the DuPont Company. He served with T-Mobile USA as an independent contractor during 2003, and Concur Technologies from 1999 until 2002.

William T. Yanavitch II rejoined the Company in May 2005 as Vice President Human Resources and Administration. Mr. Yanavitch served as Vice President Human Resources from July 2000 until his resignation in January 2005 at which time he became Corporate Human Resources Manager of Constellation Energy. From October 1998 to July 2000, Mr. Yanavitch was Director of Human Resources for the Ceramco and Trubyte Divisions of Dentsply.

David C. Elder became Corporate Controller and Chief Accounting Officer in July 2006 after joining the company in January 2006. Prior to joining the company, Mr. Elder was Corporate Controller for YORK International Corporation, a position he held since December 2003. Prior thereto, he was the Director, Financial Planning and Analysis for YORK International Corporation from August 2000 to December 2003.

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PART II

ITEM 5. MARKET FOR THE REGISTRANT S COMMON STOCK AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Common Stock Prices and Dividends Declared Information

The following table shows the high and low prices of our common stock traded on the New York Stock Exchange under the symbol GLT and the dividend declared per share for each quarter during the past two years.

Quarter	High	Low	Dividend
2006			
Fourth	$ 15.95	$ 13.26	$ 0.09
Third	16.23	12.98	0.09
Second	19.84	14.45	0.09
First	18.65	13.12	0.09
2005			
Fourth	$ 15.11	$ 12.41	$ 0.09
Third	14.92	12.00	0.09
Second	14.93	10.95	0.09
First	15.47	12.86	0.09

As of March 8, 2007, we had 1,726 shareholders of record. A number of the shareholders of record are nominees.

STOCK PERFORMANCE GRAPH

The following chart compares the yearly percentage change in the cumulative total return on our common stock during the five years ended December 31, 2006, with the cumulative total return on the S&P MidCap 400 Index and the Company s Peer Group (1). The comparison assumes $100 was invested on December 31, 2001, in our common stock, and in each of the foregoing indices and assumes reinvestment of dividends.

1) The Company s Peer Group consists of companies in the same industry as the Company. The returns of each Company in the Peer Group have been weighted according to their respective stock market capitalization for purposes of arriving at the Peer Group average. The members of the Peer Group are as follows: Bowater, Inc., Chesapeake Corporation, MeadWestvaco Corporation, Pope and Talbot, Inc., Potlatch Corporation, Schweitzer-Mauduit International, Inc., and Wausau Mosinee Paper Mills Corporation. Certain of the comparable companies are included in the S&P MidCap 400, and therefore are represented in both indices in the performance chart.

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ITEM 6. SELECTED FINANCIAL DATA

Summary of Selected Consolidated Financial Data

As of or for the year ended December 31 *In thousands, except per share*	**2006**	2005	2004	2003	2002
Net sales	**$ 986,411**	$ 579,121	$ 543,524	$ 533,193	$ 540,347
Energy sales, net	**10,726**	10,078	9,953	10,040	9,814
Total revenue	**997,137**	589,199	553,477	543,233	550,161
Shutdown and restructuring charges and unusual items	**(30,318)**	(1,564)	(20,375)	(24,995)	(2,241)
Gains on dispositions of plant, equipment and timberlands	**17,394**	22,053	58,509	32,334	1,304
Gains from insurance recoveries	**205**	20,151	32,785		
Income (loss) from continuing operations	**(12,236)**	38,609	56,102	12,986	37,637
Income (loss) per share from continuing operations					
Basic	**(0.27)**	0.88	1.28	0.30	0.87
Diluted	**(0.27)**	0.87	1.27	0.30	0.86
Total assets	**1,225,643**	1,044,977	1,052,270	1,027,019	953,202
Total debt	**397,613**	207,073	211,227	254,275	220,532
Shareholders equity	**388,368**	432,312	420,370	371,431	373,833
Cash dividends declared per common share	**0.36**	0.36	0.36	0.53	0.70

1. The above Summary of Selected Consolidated Financial Data, and the comparability thereof, includes the impact of certain charges and gains from asset dispositions and insurance recoveries. For a discussion of these items that affect the comparability of this information, see Item 8 Financial Statements and Supplemental Data Notes 4 to 6.

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact, including statements regarding industry prospects and future consolidated financial position or results of operations, made in this Report on Form 10-K are forward looking. We use words such as anticipates , believes , expects , future , intends and similar expressions to identify forward-looking statements. Forward-looking statements reflect management s current expectations and are inherently uncertain. Our actual results may differ significantly from such expectations. The following discussion includes forward-looking statements regarding expectations of, among others, net sales, costs of products sold, non-cash pension income, environmental costs, capital expenditures and liquidity, all of which are inherently difficult to predict. Although we make such statements based on assumptions that we believe to be reasonable, there can be no assurance that actual results will not differ materially from our expectations. Accordingly, we identify the following important factors, among others, which could cause our results to differ from any results that might be projected, forecasted or estimated in any such forward-looking statements:

i. variations in demand for, or pricing of, our products;

ii. changes in the cost or availability of raw materials we use, in particular market pulp, pulp substitutes, and abaca fiber, and changes in energy-related costs;

iii. our ability to develop new, high value-added Specialty Papers and Composite Fibers;

iv. the impact of competition, changes in industry paper production capacity, including the construction of new mills, the closing of mills and incremental changes due to capital expenditures or productivity increases;

v. our ability to successfully integrate the operations of the recently acquired Chillicothe and Lydney facilities;

vi. cost and other effects of environmental compliance, cleanup, damages, remediation or restoration, or personal injury or property damages related thereto, such as the costs of natural resource restoration or damages related to the presence of polychlorinated biphenyls (PCBs) in the lower Fox River on which our former Neenah mill was located; and the costs of environmental matters at our former Ecusta Division mill;

vii. the gain or loss of significant customers and/or on-going viability of such customers;

viii. risks associated with our international operations, including local economic and political environments and fluctuations in currency exchange rates;

ix. geopolitical events, including war and terrorism;

x. enactment of adverse state, federal or foreign tax or other legislation or changes in government policy or regulation;

xi. adverse results in litigation;

xii. disruptions in production and/or increased costs due to labor disputes;

xiii. our ability to successfully execute our timberland strategy to realize the value of our timberlands; and

xiv. our ability to finance, consummate and integrate future acquisitions.

Introduction We manufacture, both domestically and internationally, a wide array of specialty papers and engineered products. Substantially all of our revenue is earned from the sale of our products to customers in numerous markets, including book publishing, envelope & converting, carbonless papers and forms, food and beverage, decorative laminates for furniture and flooring, and other highly technical niche markets.

Overview Our results of operations for 2006 reflect stronger market conditions in each of our business units when compared with 2005. Domestically, the Specialty Papers business unit s results in the comparison are positively influenced by additional volumes associated with the April 2006 Chillicothe acquisition and improved selling prices. However, input costs in 2006 are higher, primarily energy and raw material costs.

Our Composite Fibers business unit s results have also been positively influenced by additional volumes associated with the Lydney acquisition as well as improved demand across all of this unit s product categories. Average selling prices, however, have remained flat to lower in the comparison.

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The analysis of our financial results for 2006 reflects the following significant items:

1) We completed the $65 million acquisition of J R Crompton s Lydney mill on March 13, 2006. This mill s revenue in 2005 was approximately $75 million;

2) On April 3, 2006, we completed the acquisition of Chillicothe, the carbonless paper operation of NewPage Corporation with 2005 revenue of $441.5 million, for $83.3 million in cash;

3) In April 2006, we refinanced our bank credit facility with a $100 million term loan and a $200 million revolving credit facility in addition to the issuance of $200 million 71/8% bonds to replace our $150 million 67/8% notes due July 2007;

4) On June 30, 2006, we ceased production at our Neenah, WI facility and recorded shutdown related charges totaling $54.4 million;

5) We incurred acquisition integration costs totaling $13.6 million in connection with the Chillicothe and Lydney acquisitions; and

6) During 2006, we sold 5,923 acres of timberland for aggregate proceeds of $17.1 million.

RESULTS OF OPERATIONS

2006 versus 2005

The following table sets forth summarized results of operations:

	Year Ended December 31	
In thousands, except per share	**2006**	2005
Net sales	**$ 986,411**	$ 579,121
Gross profit	**105,294**	97,176
Operating income	**94**	70,183
Net income (loss)	**(12,236)**	38,609
Earnings (loss) per diluted share	**(0.27)**	0.87

The consolidated results of operations for the years ended December 31, 2006 and 2005 include the following significant items:

In thousands, except per share	After-tax Income (loss)	Diluted EPS
2006		
Gains on sale of timberlands	**$ 8,812**	**$ 0.20**

Shutdown and restructuring charges	**(35,212)**	**(0.79)**
Acquisition integration costs	**(8,647)**	**(0.19)**
Debt redemption premium	**(1,820)**	**(0.04)**
Insurance recoveries	**130**	
2005		
Gains on sale of timberlands	**11,258**	0.26
Insurance recoveries	**12,719**	0.29
Restructuring charges	**(1,017)**	(0.02)

These items decreased earnings by $36.7 million, or $0.82 per diluted share in 2006. Comparatively, the items identified above positively affected earnings in 2005 by $23.0 million, or $0.53 per diluted share.

Business Units Results of individual business units are presented based on our management accounting practices and management structure. There is no comprehensive, authoritative body of guidance for management accounting equivalent to accounting principles generally accepted in the United States of America; therefore, the financial results of individual business units are not necessarily comparable with similar information for any other company. The management accounting process uses assumptions and allocations to measure performance of the business units. Methodologies are refined from time to time as management accounting practices are enhanced and businesses change. The costs incurred by support areas not directly aligned with the business unit are allocated primarily based on an estimated utilization of support area services or included in Other and Unallocated in the following table. Certain prior period information has been reclassified to conform to the current period presentation.

Management evaluates business unit results of operations before non-cash pension income, shutdown and restructuring related charges, acquisition integration costs, effects of asset dispositions and insurance recoveries because it believes this is a more meaningful representation of the operating performance of its core papermaking businesses, the profitability of business units and the extent of cash flow generated from core operations. This presentation is closely aligned with the management and operating structure of our company. It is also on this basis that the Company s performance is evaluated internally and by the Company s Board of Directors.

Jnit Performance	Year Ended December 31							
ds, except tons	Specialty Papers		Composite Fibers		Other and Unallocated		Total	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	20
	$693,660	$380,923	**$292,751**	$198,137	**$**	$61	**$986,411**	$579
, net	**10,726**	10,078					**10,726**	10
ne	**704,386**	391,001	**292,751**	$198,137		61	**997,137**	589
ucts sold	**635,143**	340,629	**246,797**	166,153	**9,903**	(14,759)	**891,843**	492
(loss)	**69,243**	50,372	**45,954**	31,984	**(9,903)**	14,820	**105,294**	97
	50,285	39,876	**28,458**	21,282	**13,738**	6,475	**92,481**	67
nd restructuring					**30,318**	1,564	**30,318**	1
positions of plant, nd timberlands					**(17,394)**	(22,053)	**(17,394)**	(22
urance recoveries					**(205)**	(20,151)	**(205)**	(20
ing income (loss)	**18,958**	10,496	**17,496**	10,702	**(36,360)**	48,985	**94**	70
g income					**(22,322)**	(10,043)	**(22,322)**	(10
s) before income	**$18,958**	$10,496	**$17,496**	$10,702	**$(58,682)**	$38,942	**$(22,228)**	$60
tary Data								
d	**653,734**	450,900	**68,148**	47,669	**10**	24	**721,892**	498
n expense	**$32,824**	$35,781	**$17,197**	$14,866	**$**	$	**$50,021**	$50

Sales and Costs of Products Sold

	Year Ended December 31		
In thousands	**2006**	2005	Change
Net sales	**$986,411**	$579,121	$407,290
Energy sales net	**10,726**	10,078	648
Total revenues	**997,137**	589,199	407,938

Costs of products sold	**891,843**	492,023	399,820
Gross profit	**$105,294**	$97,176	$8,118
Gross profit as a percent of Net sales	**10.7%**	16.8%	

The following table sets forth the contribution to consolidated net sales by each business unit:

	Percent of total	
	2006	2005
Business Unit		
Specialty Papers	**70.3%**	65.8%
Composite Fibers	**29.7**	34.2
Total	**100.0%**	100.0%

Net sales totaled $986.4 million for the year ended December 31, 2006, an increase of $407.3 million, or 70.3%, compared to the same period a year ago. Net sales from the acquisition of Chillicothe s carbonless and forms business and the Lydney mill totaled $329.9 million. These acquisitions are reported in the Specialty Papers and Composite Fibers business units, respectively. Organic growth was driven by a 4.0% increase in volume and $21.3 million from higher average selling prices in the Specialty Papers business unit. Excluding results of the Lydney mill, Composite Fibers volumes shipped increased 15.6%. The translation of foreign currencies unfavorably impacted this business unit s net sales by $2.5 million and average selling prices declined $3.5 million compared to the same period a year ago.

In connection with the Chillicothe acquisition, we permanently shutdown our Neenah, WI facility. Products previously manufactured at the Neenah facility have been transferred to Chillicothe. The results of operations for 2006 include related pre-tax charges of $54.4 million, of which $25.4 million is reflected in the consolidated income statement as components of cost of products sold and $29.0 million is reflected as Shutdown and restructuring charges.

Costs of products sold totaled $891.8 million for 2006, an increase of $399.8 million compared with the previous year As discussed above, the 2006 costs of products sold includes a $25.4 million charge for inventory write-downs and accelerated depreciation on property and equipment abandoned in connection with the Neenah shutdown.

In addition to the shutdown charges, the increase in costs of products sold was primarily due to the inclusion of the Chillicothe and Lydney acquisitions and the effect of increased shipping volumes. In addition, higher raw material and energy prices increased costs of products sold by approximately $12.1 million.

Non-Cash Pension Income Non-cash pension income results from the over-funded status of our pension plans. The amount of pension income recognized each year is determined using various actuarial assumptions and certain other factors, including the fair value of our pension assets as of the beginning of the year. The following summarizes non-cash pension income, before the curtailment charges recorded in connection with the Neenah shutdown during 2006:

	Year Ended December 31		
In thousands	**2006**	2005	Change
Recorded as:			
Costs of products sold	**$15,480**	$14,844	$636
SG&A expense	**1,513**	1,673	(160)
Total	**$16,993**	$16,517	$476

Selling, general and administrative (SG&A) expenses totaled $92.5 million in 2006 compared to $67.6 million a year ago. The increase was due to $13.6 million of acquisition integration costs and $16.2 million from the inclusion of the Chillicothe and Lydney acquisitions in the current period s results of operations. SG&A expenses in 2005 included a

$2.7 million charge for certain matters related to our former Ecusta division. In addition, the comparison was favorably affected by lower professional and legal fees in the period to period comparison.

Gain on Sales of Plant, Equipment and Timberlands During 2006, 2005 and 2004, we completed sales of timberlands and, in 2004, the corporate aircraft. The following table summarizes these transactions.

Dollars in thousands	**Acres**	**Proceeds**	**Gain**
2006			
Timberlands	**5,923**	**$ 17,130**	**$ 15,677**
Other	**n/a**	**3,941**	**1,717**
Total		**$ 21,071**	**$ 17,394**
2005			
Timberlands	2,488	$ 21,000	$ 20,327
Other	n/a	1,778	1,726
Total		$ 22,778	$ 22,053
2004			
Timberlands	4,482	$ 56,586	$ 55,355
Corporate Aircraft	n/a	2,861	2,554
Other	n/a	724	600
Total		$ 60,171	$ 58,509

Insurance Recoveries During the 2006 and 2005, we reached successful resolution of certain claims under insurance policies related to the Fox River environmental matter. Insurance recoveries included in the results of operations totaled $0.2 million in 2006 and $20.2 million in 2005. All recoveries were received in cash prior to the end of the applicable period.

Shutdown and Restructuring Charges Neenah Facility Shutdown As of June 30, 2006 we permanently shutdown our Neenah facility. The charge incurred in connection with this action was recorded as follows:

In thousands	Year Ended December 31, 2006

Recorded as:		
Costs of products sold	$	**25,371**
Shutdown and restructuring charge		**29,074**
Total	$	**54,445**

The following table summarizes shutdown reserve activity during 2006:

In thousands	Beg. balance	Amount Accrued	Less non-cash-charges and cash payments	Balance
Non-cash charges				
Accelerated depreciation	**$**	**$22,466**	**$(22,466)**	**$**
Inventory write-down		**2,905**	**(2,905)**	
Pension curtailments and other retirement benefit charges		**7,675**	**(7,675)**	
Total non cash charges		**33,046**	**(33,046)**	
Cash charges				
Severance and benefit continuation		**7,653**	**(6,026)**	**1,627**
Contract termination costs		**11,367**	**(11,367)**	
Other		**2,379**	**(1,229)**	**1,150**
Total cash charges		**21,399**	**(18,622)**	**2,777**
Total	**$**	**$54,445**	**$(51,668)**	**$2,777**

The Neenah facility supported our Specialty Papers business unit. Shutdown of this facility resulted in the elimination of approximately 200 positions. We do not expect any material additional shutdown related charges in 2007.

As part of the Neenah shutdown, we terminated our long-term steam supply contract, as provided for within the agreement, resulting in a termination fee of approximately $11.4 million.

The results of operations for 2006 and 2005, also include $1.2 million and $1.6 million, respectively, of charges related to the European Restructuring and Optimization (EURO) Program.

Non-operating income (expense) During April 2006, we completed the placement of a $200 million bond offering, the proceeds of which were used to redeem the then outstanding $150 million notes scheduled to mature in July 2007. In connection with the early redemption, a charge of $2.9 million, related to a redemption premium and the write-off of unamortized debt issuance costs, was recorded in Consolidated Statement of Income as Non-operating expense under the caption Other-net .

Income taxes In 2006 we recorded an income tax benefit at an effective rate of 45.0% compared to an income tax provision at an effective rate of 35.8%. The beneficial higher effective tax rate in 2006 was primarily due to the effect of state tax law changes and the effect of tax credits, partially offset by the resolution of certain tax matters.

Foreign Currency We own and operate paper and pulp mills in Germany, France, the United Kingdom and the Philippines. The local currency in Germany and France is the Euro, in the UK the British Pound Sterling, and in the Philippines the currency is the Peso. During 2006, Euro functional currency operations generated approximately 21.0% of our sales and 19.8% of operating expenses and British Pound Sterling operations represented 6.1% of net sales and 6.4% of operating expenses. The translation of the results from these international operations into U.S. dollars is subject to changes in foreign currency exchange rates. The table below summarizes the effect from foreign currency translation on 2006 reported results compared to 2005:

In thousands	Year Ended December 31
	Favorable (unfavorable)
Net sales	**$2,455**
Costs of products sold	**(4,045)**
SG&A expenses	**(258)**
Income taxes and other	**37**
Net loss	**$(1,811)**

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The above table only presents the financial reporting impact of foreign currency translations. It does not present the impact of certain competitive advantages or disadvantages of operating or competing in multi-currency markets.

RESULTS OF OPERATIONS

2005 versus 2004

The following table sets forth summarized results of operations:

	Year Ended December 31	
In thousands	2005	2004
Net sales	$ 579,121	$ 543,524
Gross profit	97,176	92,414
Operating income	70,183	103,394
Net income	38,609	56,102
Earnings per diluted share	0.87	1.27

The consolidated results of operations for the years ended December 31, 2005 and 2004 include the following significant items:

In thousands, except per share	After-tax Income (loss)	Diluted EPS
2005		
Gains on sale of timberlands	$11,258	$0.26
Insurance recoveries	12,719	0.29
Restructuring charges	(1,017)	(0.02)
2004		
Gains on sale of timberlands and corporate aircraft	$34,151	$0.78
Insurance recoveries	21,310	0.48
Restructuring charges	(12,723)	(0.29)

The above items increased earnings from continuing operations by $23.0 million, or $0.52 per diluted share in 2005, and by $42.7 million, or $0.97 per diluted share, in 2004.

Business Units The following table sets forth profitability information by business unit and the composition of consolidated income from continuing operations before income taxes:

led December 31				
nds, except tons	Specialty Papers	Composite Fibers	Other and Unallocated	Total

	2005	2004	2005	2004	2005	2004	2005	200
	$380,923	$337,436	$198,137	$205,232	$61	$856	$579,121	$543,
es, net	10,078	9,953					10,078	9,
ue	391,001	347,389	198,137	205,232	61	856	589,199	553,
ducts sold	340,629	312,136	166,153	163,843	(14,759)	(14,916)	492,023	461,
t	50,372	35,253	31,984	41,389	14,820	15,772	97,176	92,
	39,876	36,617	21,282	23,067	6,475	255	67,633	59,
ng charges					1,564	20,375	1,564	20,
ispositions of oment and s					(22,053)	(58,509)	(22,053)	(58,
surance recoveries					(20,151)	(32,785)	(20,151)	(32,
ting income (loss)	10,496	(1,364)	10,702	18,322	48,985	86,436	70,183	103,
ng income					(10,043)	(12,631)	(10,043)	(12,
ss) from operations before es	$10,496	$(1,364)	$10,702	$18,322	$38,942	$73,805	$60,140	$90,
tary Data								
ld	450,900	421,504	47,669	48,528	24	390	498,593	470,
on expense	$35,781	$37,186	$14,866	$14,412			$50,647	$51,

Sales and Costs of Products Sold

In thousands	Year Ended December 31 2005	2004	Change
Net sales	$ 579,121	$ 543,524	$ 35,597
Energy sales net	10,078	9,953	125
Total revenues	589,199	553,477	35,722
Costs of products sold	492,023	461,063	30,960
Gross profit	$97,176	$92,414	$4,762

Gross profit as a percent of Net sales	16.8%	17.0%

The following table sets forth the contribution to consolidated net sales by each business unit:

	Year Ended December 31	
	2005	2004
Business Unit		
Specialty Papers	65.8%	62.1%
Composite Fibers	34.2	37.8
Tobacco Papers		0.1
Total	100.0%	100.0%

Net sales totaled $579.1 million in 2005, an increase of $35.6 million, or 6.6%, compared to a year ago. This growth was primarily driven by strengthened product pricing and a 7.0% increase in volumes shipped in the Specialty Papers business unit compared with the same period of 2004. Higher pricing for Specialty Papers products increased revenue by $17.6 million compared to 2004. Composite Fibers volumes shipped declined approximately 1.8% and lower selling prices, on a constant currency basis, decreased revenue by $7.4 million. Costs of products sold increased $31.0 million in the comparison. In addition to the effect of increased shipping volumes, higher raw material and energy prices increased costs of products sold by approximately $11.1 million. Lower labor costs realized from the 2004 North American Restructuring Program were substantially offset by higher spending on supplies and maintenance and by the impact of significant market related downtime in the Composite Fibers business unit.

Non-Cash Pension Income Non-cash pension income results from the considerably over-funded status of our pension plans. The amount of pension income recognized each year is determined using various actuarial assumptions and certain other factors, including the fair value of our pension assets as of the beginning of the year. The following summarizes non-cash pension income for each period:

	Year Ended December 31		
In thousands	2005	2004	Change
Recorded as:			
Costs of products sold	$14,844	$15,937	$(1,093)
SG&A expense	1,673	1,405	268
Total	$16,517	$17,342	$(825)

The following summarizes SG&A expenses, restructuring charges, gains from asset dispositions and other nonrecurring items:

	Year Ended December 31		
In thousands	2005	2004	Change
SG&A expenses	$67,633	$59,939	$7,694
Restructuring charges	1,564	20,375	(18,811)
Gains on dispositions of plant, equipment and timberlands	(22,053)	(58,509)	36,456
Gains from insurance recoveries	(20,151)	(32,785)	12,634

Selling, General and Administrative (SG&A) expenses increased $7.7 million in the comparison primarily due to a $2.7 million charge to increase our reserve for costs associated with environmental matters at the former Ecusta facility located in North Carolina, $2.1 million of additional variable compensation and $2.0 million of higher litigation related costs.

Restructuring Charges In 2005 we announced the EURO Program, a comprehensive series of initiatives designed to improve the performance of our Composite Fibers business unit. In the fourth quarter of 2005 we recorded restructuring charges totaling $1.6 million associated with the related work force efficiency plans at the Gernsbach, Germany facility. This charge reflects severance, early retirement and related costs for the 55 effected employees. We expect to incur cash out lays in this amount over the next 24 month period.

The restructuring charge incurred in 2004 related to the North American Restructuring Program and certain actions related to the Neenah facility.

Insurance Recoveries During 2005 and 2004, we reached successful resolution of certain claims under insurance policies related to the Fox River environmental matter. Insurance recoveries included in the results of operations totaled $20.2 and $32.8 million in 2005 and 2004, respectively, and were received in cash. Any additional insurance recoveries are expected to be insignificant.

Income Taxes The Company s effective tax rates for 2005 and 2004 were 35.8% and 38.2%, respectively. The lower effective tax rate in 2005 was primarily due to decreased amounts of timberland sales in 2005, which are taxed at higher effective rates, and the effect of tax credits and the related impact on valuation allowances relative to the level of pre-tax income.

Foreign Currency We own and operate paper and pulp mills in Germany, France and the Philippines. The local currency in Germany and France is the Euro, while in the Philippines the currency is the Peso. During the year ended December 31, 2005, these operations generated approximately 29% of our sales and 30% of operating expenses. The translation of the results from these international operations into U.S. dollars is subject to changes in foreign currency exchange rates.

LIQUIDITY AND CAPITAL RESOURCES

Our business is capital intensive and requires significant expenditures for new or enhanced equipment, for environmental compliance matters and to support our business strategy and research and development efforts. The following table summarizes cash flow information for each of the years presented.

	Year Ended December 31	
In thousands	**2006**	2005
Cash and cash equivalents at beginning of period	**$57,442**	$39,951
Cash provided by (used for)		
Operating activities	**(28,427)**	42,868
Investing activities	**(181,831)**	(8,029)
Financing activities	**173,388**	(15,158)
Effect of exchange rate changes on cash	**1,413**	(2,190)
Net cash (used) provided	**(35,457)**	17,491
Cash and cash equivalents at end of period	**$21,985**	$57,442

During 2006, operations used $28.4 million of cash compared to $42.9 million of cash provided by operating activities in the prior year. The change in the comparison was primarily due $20.0 million of lower insurance recoveries in the year-to-year, the use of $21.7 million to settle a cross currency rate swap that matured in June 2006, $22.4 million used for working capital associated with the Lydney acquisition, $18.6 million of Neenah shutdown related payments made during 2006, partially offset by improved earnings from operations.

The changes in investing cash flows primarily reflect the use of approximately $158.4 million to fund the Chillicothe and Lydney mill acquisitions and increased capital expenditures of $13.4 million. The acquisitions were financed with borrowings under our revolving credit facility and new term loan.

During 2006 and 2005, cash dividends paid on common stock totaled approximately $16.0 million and $15.8 million. Our Board of Directors determines what,

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if any, dividends will be paid to our shareholders. Dividend payment decisions are based upon then-existing factors and conditions and, therefore, historical trends of dividend payments are not necessarily indicative of future payments.

As more fully discussed in Item 8 Financial Statements, Note 17, on April 3, 2006 we refinanced the revolving credit facility set forth in the table below. The significant terms of the new credit facility are also set forth therein. In addition, on April 28, 2006, we completed a private placement offering of $200 million aggregate principal amount of our 71/8% Senior Notes due 2016. We used the net proceeds to redeem $150 million aggregate principal amount of our outstanding 67/8% notes due July 2007, plus the payment of the applicable redemption premium and accrued interest. The following table sets forth our outstanding long-term indebtedness:

	December 31	
In thousands	**2006**	2005
Revolving credit facility, due April 2011	**$64,795**	$
Term Loan, due April 2011	**96,000**	
Revolving credit facility, due June 2006		19,650
71/8% Notes, due May 2016	**200,000**	
67/8% Notes, due July 2007		150,000
Note payable SunTrust, due March 2008	**34,000**	34,000
Total long-term debt	**394,795**	203,650
Less current portion	**(19,500)**	(19,650)
Long-term debt, excluding current portion	**$375,295**	$184,000

The significant terms of the debt obligations are set forth in Item 8 Financial Statements and Supplementary Data, Note 17.

We are subject to loss contingencies resulting from regulation by various federal, state, local and foreign governmental authorities with respect to the environmental impact of mills we operate, or have operated. To comply with environmental laws and regulations, we have incurred substantial capital and operating expenditures in past years. We anticipate that environmental regulation of our operations will continue to become more burdensome and that capital and operating expenditures necessary to comply with environmental regulations will continue, and perhaps increase, in the future. In addition, we may incur obligations to remove or mitigate any adverse effects on the environment resulting from our operations, including the restoration of natural resources and liability for personal injury and for damages to property and natural resources. See Item 8 Financial Statements Note 19 for a summary of significant environmental matters.

We expect to meet all of our near- and longer-term cash needs from a combination of operating cash flow, cash and cash equivalents, sales of timberland, our existing credit facility or other bank lines of credit and other long-term debt. However, as discussed in Item 8 Financial Statements and Supplementary Data Note 19, an unfavorable outcome of various environmental matters could have a material adverse impact on our consolidated financial position, liquidity and/or results of operations.

Off-Balance-Sheet Arrangements As of December 31, 2006 and 2005, we had not entered into any off-balance-sheet arrangements. A financial derivative instrument to which we are a party and guarantees of indebtedness, which solely consists of obligations of subsidiaries and a partnership, are reflected in the consolidated balance sheets included herein in Item 8 Financial Statements and Supplementary Data.

Contractual Obligations The following table sets forth contractual obligations as of December 31, 2006.

			Payments Due During the Year Ended December 31,		
In thousands	Total	2007	2008 to 2009	2010 to 2011	2012 and beyond
Long-term debt (1)	$562,275	$44,649	$119,331	$136,545	$261,750
Operating leases (2)	18,699	3,539	5,102	1,973	8,085
Purchase obligations (3)	63,651	45,733	17,778	140	
Other long term obligations (4)	103,410	8,850	16,596	18,290	59,674
Total	$748,035	$102,771	$158,807	$156,948	$329,509

(1) Represents principal and interest payments due on long-term debt. We have $200 million of debt maturing in May 2016 and bearing a fixed rate of interest at 71/8%, payable semiannually, $34 million note maturing in March 2008 and bearing a fixed rate of interest of 3.82%. In addition, at December 31, 2006, $65 million was outstanding under our revolving credit facility and $96 million was outstanding under a term loan. Both the revolving credit facility and the term loan bear a variable interest rate (6.20% as of December 31, 2006) and mature in April 2011.

(2) Represents rental agreements for various land, buildings, and computer and office equipment.

(3) Represents open purchase order commitments and other obligations, primarily for pulpwood contracts with minimum annual purchase obligations. In certain situations, prices are subject to variations based on market prices. In such situations, the information above is based on prices in effect at December 31, 2006 or expectations based on historical experience and/or current market conditions.

(4) Represents expected benefits to be paid pursuant to medical retirement plans and nonqualified pension plans over the next ten years.

Critical Accounting Policies and Estimates The preceding discussion and analysis of our consolidated financial position and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to inventories, long-lived assets, pension and post-retirement obligations, environmental liabilities and income taxes. We base our estimates on historical experience and on various other assumptions that we believe are 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 apparent from other sources. Actual results may differ from these estimates.

We believe the following represent the most significant and subjective estimates used in the preparation of our consolidated financial statements.

Inventory Reserves We maintain reserves for excess and obsolete inventories to reflect our inventory at the lower of its stated cost or market value. Our estimate for excess and obsolete inventory is based upon our assumptions about future demand and market conditions. If actual market conditions are more or less favorable than those we have projected, we may need to increase or decrease our reserves for excess and obsolete inventories, which could affect our reported results of operations.

Long-lived Assets We evaluate the recoverability of our long-lived assets, including property, equipment and intangible assets periodically or whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. Our evaluations include analyses based on the cash flows generated by the underlying assets, profitability information, including estimated future operating results, trends or other determinants of fair value. If the value of an asset determined by these evaluations is less than its carrying amount, a loss is recognized for the difference between the fair value and the carrying value of the asset. Future adverse changes in market conditions or poor operating results of the related business may indicate an inability to recover the carrying value of the assets, thereby possibly requiring an impairment charge in the future.

Pension and Other Post-Retirement Obligations Accounting for defined-benefit pension plans, and any curtailments thereof, requires various assumptions, including, but not limited to, discount rates, expected rates of return on plan assets and future compensation growth rates. Accounting for our retiree medical plans, and any curtailments thereof, also requires various assumptions, which include, but are not limited to, discount rates and annual rates of increase in the per capita costs of health care benefits. We evaluate these assumptions at least once each year or as facts and circumstances dictate and make changes as conditions warrant. Changes to these assumptions will increase or decrease our reported income, which will result in changes to the recorded benefit plan assets and liabilities.

Environmental Liabilities We maintain accruals for losses associated with environmental obligations when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated based on existing legislation and remediation technologies. These accruals are adjusted periodically as assessment and remediation actions continue and/or further legal or technical information develops. Such undiscounted liabilities are exclusive of any insurance or other claims against third parties. Recoveries of environmental remediation costs from other parties, including insurance carriers, are recorded as assets when their receipt is assured beyond a reasonable doubt.

Income Taxes We record the estimated future tax effects of temporary differences between the tax bases of assets and liabilities and amounts reported in our balance sheets, as well as operating loss and tax credit carry forwards. These deferred tax assets and liabilities are measured using enacted tax rates and laws that will be in effect when such amounts are expected to reverse or be utilized. We regularly review our deferred tax assets for recoverability based on historical taxable income, projected future taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies. If we are unable to generate sufficient future taxable income, or if there is a material change in the actual effective tax rates or time period within which the underlying temporary differences become taxable or deductible, we could be required to increase the valuation allowance against our deferred tax assets, which may result in a substantial increase in our effective tax rate and a material adverse impact on our reported results.

Other significant accounting policies, not involving the same level of uncertainties as those discussed above, are nevertheless important to an understanding of the Consolidated Financial Statements. Refer to Item 8 Financial Statements and Supplementary Data Notes to Consolidated Financial Statements for additional accounting policies.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

	Year Ended December 31					At December 31, 2006	
Dollars in thousands	2007	2008	2009	2010	2011	Carrying Value	Fair Value
Long-term debt							
Average principal outstanding							
At fixed interest rates Bond	$200,000	$200,000	$200,000	$200,000	$200,000	$200,000	$204,980
At fixed interest rates SunTrust Note	34,000	8,500				34,000	32,914
At variable interest rates	149,983	134,545	114,858	92,358	19,574	160,795	160,795
Weighted-average interest rate						$394,795	$398,689
On fixed interest rate debt Bond	7.13%	7.13%	7.13%	7.13%	7.13%		
On variable interest rate debt SunTrust Note	3.82	3.82					
On variable interest rate debt	6.20	6.19	6.19	6.18	6.17		

Our market risk exposure primarily results from changes in interest rates and currency exchange rates. At December 31, 2006, we had long-term debt outstanding of $394.8 million, of which $160.8 million or 40.7% was at variable interest rates.

The table above presents average principal outstanding and related interest rates for the next five years. Fair values included herein have been determined based upon rates currently available to us for debt with similar terms and remaining maturities.

Variable-rate debt outstanding represents borrowings under our revolving credit facility that incur interest based on the domestic prime rate or a Eurocurrency rate, at our option, plus a margin. At December 31, 2006, the interest rate paid was 6.20%. A hypothetical 100 basis point increase or decrease in the interest rate on variable rate debt would increase or decrease annual interest expense by $1.6 million.

We are subject to certain risks associated with changes in foreign currency exchange rates to the extent our operations are conducted in currencies other than the U.S. Dollar. During 2006, Euro functional currency operations generated approximately 21% of our sales and 19.8% of operating expenses and British Pound Sterling operations represented 6.1% of net sales and 6.4% of operating expenses.

ITEM 8. *FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA*

MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of P. H. Glatfelter Company (the Company) is responsible for establishing and maintaining adequate internal control over financial reporting. The Company s internal control over financial reporting is a process designed under the supervision of the chief executive and chief financial officers to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company s financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States.

As of December 31, 2006, management conducted an assessment of the effectiveness of the Company s internal control over financial reporting based on the framework established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). We excluded from our assessment the internal control over financial reporting at the Lydney and Chillicothe facilities, which were acquired on March 13, 2006, and April 3, 2006, respectively, and whose total assets constitute a combined 24% of total assets, and which represented a combined 33% percent of total net sales, of the consolidated financial statement amounts as of and for the year ended December 31, 2006. Based on this assessment, management has determined that the Company s internal control over financial reporting as of December 31, 2006 is effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company s financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States.

Our internal control over financial reporting includes policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets; provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States, and that receipts and expenditures are being made only in accordance with authorizations of management; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company s assets that could have a material effect on our financial statements.

Management s assessment of the effectiveness of the Company s internal control over financial reporting as of December 31, 2006, has been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report appearing herein, which expresses unqualified opinions on management s assessment and on the effectiveness of the Company s internal control over financial reporting as of December 31, 2006.

The Company s management, including the chief executive officer and chief financial officer, does not expect that our internal control over financial reporting will prevent or detect all errors and all frauds. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system s objectives will be met. The design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Further, because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based, in part, on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of
P. H. Glatfelter Company

We have audited management s assessment, included in the accompanying Management s Report on Internal Control Over Financial Reporting, that P. H. Glatfelter and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2006, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. As described in Management s Report on Internal Control Over Financial Reporting, management excluded from its assessment the internal control over financial reporting at the Lydney and Chillicothe facilities, which were acquired on March 13, 2006, and April 3, 2006, respectively, and whose total assets constitute a combined 24% of total assets, and which represented a combined 33% percent of total net sales, of the consolidated financial statement amounts as of and for the year ended December 31, 2006. Accordingly, our audit did not include the internal control over financial reporting at the Lydney and Chillicothe facilities. The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed by, or under the supervision of, the company s principal executive and principal financial officers, or persons performing similar functions, and effected by the company s board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended December 31, 2006, of the Company and our report dated March 15, 2007, expressed an unqualified opinion on these financial statements and included an explanatory paragraph regarding the adoption of Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R), as of December 31, 2006.

Deloitte & Touche LLP

Philadelphia, Pennsylvania
March 15, 2007

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of
P. H. Glatfelter Company

We have audited the accompanying consolidated balance sheets of P. H. Glatfelter Company and subsidiaries (the Company) as of December 31, 2006 and 2005, and the related consolidated statements of income, shareholders equity, and cash flows for each of the three years in the period ended December 31, 2006. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company s management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of P. H. Glatfelter Company and subsidiaries as of December 31, 2006 and 2005, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 12 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R), as of December 31, 2006.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 15, 2007, expressed an unqualified opinion on management s assessment of the effectiveness of the Company s internal control over financial reporting and an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

Deloitte & Touche LLP

Philadelphia, Pennsylvania
March 15, 2007

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P. H. GLATFELTER COMPANY and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME

In thousands, except per share amounts	Year Ended December 31 **2006**	2005	2004
Net sales	**$986,411**	$579,121	$543,524
Energy sales net	**10,726**	10,078	9,953
Total revenues	**997,137**	589,199	553,477
Costs of products sold	**891,843**	492,023	461,063
Gross profit	**105,294**	97,176	92,414
Selling, general and administrative expenses	**92,481**	67,633	59,939
Shutdown and restructuring charges	**30,318**	1,564	20,375
Gains on disposition of plant, equipment and timberlands, net	**(17,394)**	(22,053)	(58,509)
Insurance recoveries	**(205)**	(20,151)	(32,785)
Operating income	**94**	70,183	103,394
Other nonoperating income (expense)			
Interest expense	**(24,453)**	(13,083)	(13,385)
Interest income	**3,132**	2,012	2,012
Other net	**(1,001)**	1,028	(1,258)
Total other nonoperating expense	**(22,322)**	(10,043)	(12,631)
Income (loss) before income taxes	**(22,228)**	60,140	90,763
Income tax provision (benefit)	**(9,992)**	21,531	34,661
Net income (loss)	**$(12,236)**	$38,609	$56,102
Weighted average shares outstanding			
Basic	**44,584**	44,013	43,856
Diluted	**44,584**	44,343	44,023
Earnings (loss) Per Share			
Basic	**$(0.27)**	$0.88	$1.28
Diluted	**(0.27)**	0.87	1.27

The accompanying notes are an integral part of the consolidated financial statements.

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P. H. GLATFELTER COMPANY and SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

Dollars in thousands, except par values	December 31 **2006**	2005
Assets		
Current assets		
Cash and cash equivalents	**$21,985**	$57,442
Accounts receivable (less allowance for doubtful accounts: 2006 $3,613; 2005 $931)	**128,255**	62,524
Inventories	**192,281**	81,248
Prepaid expenses and other current assets	**32,517**	22,343
Total current assets	**375,038**	223,557
Plant, equipment and timberlands net	**528,867**	478,828
Other assets	**321,738**	342,592
Total assets	**$1,225,643**	$1,044,977
Liabilities and Shareholders Equity		
Current liabilities		
Current portion of long-term debt	**$19,500**	$19,650
Short-term debt	**2,818**	3,423
Accounts payable	**86,488**	31,132
Dividends payable	**4,035**	3,972
Environmental liabilities	**5,489**	7,575
Other current liabilities	**74,960**	74,126
Total current liabilities	**193,290**	139,878
Long-term debt	**375,295**	184,000
Deferred income taxes	**182,659**	206,269
Other long-term liabilities	**86,031**	82,518
Total liabilities	**837,275**	612,665
Commitments and contingencies		
Shareholders equity		

Common stock, $.01 par value; authorized 120,000,000 shares; issued 54,361,980 shares (including shares in treasury: 2006 9,540,770; 2005 10,229,734)	**544**	544
Capital in excess of par value	**42,288**	43,450
Retained earnings	**519,489**	547,810
Deferred compensation		(2,295)
Accumulated other comprehensive loss	**(32,337)**	(5,343)
	529,984	584,166
Less cost of common stock in treasury	**(141,616)**	(151,854)
Total shareholders equity	**388,368**	432,312
Total liabilities and shareholders equity	**$1,225,643**	$1,044,977

The accompanying notes are an integral part of the consolidated financial statements.

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P.H. GLATFELTER COMPANY and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31		
In thousands	**2006**	2005	2004
Operating activities			
Net income (loss)	**$(12,236)**	$38,609	$56,102
Adjustments to reconcile to net cash (used) provided by operations:			
Depreciation, depletion and amortization	**50,021**	50,647	51,598
Pension income	**(16,993)**	(16,517)	(17,342)
Restructuring charges and unusual items	**37,066**	1,564	16,483
Deferred income tax provision	**(12,726)**	3,020	17,364
Gains on dispositions of plant, equipment and timberlands, net	**(17,394)**	(22,053)	(58,509)
Share-based compensation	**2,335**	630	655
Change in operating assets and liabilities			
Accounts receivable	**(17,622)**	(5,876)	470
Inventories	**(8,869)**	(6,195)	(4,276)
Other assets and prepaid expenses	**4,413**	3,995	(12,721)
Liabilities	**(36,422)**	(4,956)	(10,240)
Net cash (used) provided by operations	**(28,427)**	42,868	39,584
Investing activities			
Purchase of plant, equipment and timberlands	**(44,460)**	(31,024)	(18,587)
Proceeds from disposal of plant, equipment and timberlands	**21,071**	22,450	60,171
Proceeds from sale of subsidiary, net of cash divested		545	525
Acquisition of Chillicothe	**(89,217)**		
Acquisition of Glatfelter UK (Lydney)	**(69,225)**		
Net cash (used) provided by investing activities	**(181,831)**	(8,029)	42,109
Financing activities			
Net proceeds from (repayments of) revolving credit facility	**42,527**	(733)	(44,888)
Net proceeds from $100 million term loan facility	**94,829**		
Net proceeds from $200 million 71/8% note offering	**196,440**		
Repayment of $150 million 67/8% notes	**(152,675)**		
Payment of dividends	**(16,023)**	(15,839)	(15,782)
Proceeds from stock options exercised	**7,498**	1,414	917
Tax benefit of stock options exercised	**792**		
Net cash provided (used) by financing activities	**173,388**	(15,158)	(59,753)
Effect of exchange rate changes on cash	**1,413**	(2,190)	2,445
Net increase (decrease) in cash and cash equivalents	**(35,457)**	17,491	24,385

Cash and cash equivalents at the beginning of period	**57,442**	39,951	15,566
Cash and cash equivalents at the end of period	**$21,985**	$57,442	$39,951
Supplemental cash flow information			
Cash paid for			
Interest	**$26,218**	$12,378	$11,713
Income taxes	**17,579**	17,443	3,256

The accompanying notes are an integral part of the consolidated financial statements.

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P. H. GLATFELTER COMPANY and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY
For the Years Ended December 31, 2006, 2005 and 2004

In thousands, except shares outstanding	Common Stock	Capital in Excess of Par Value	Retained Earnings	Deferred Compen-sation	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Shareholders Equity
Balance at January 1, 2004	$ 544	$ 40,469	$ 484,756	$	$ 2,690	$ (157,028)	$ 371,431
Net income			56,102				56,102
Other comprehensive income							
Foreign currency translation adjustments					6,078		
Other comprehensive income					6,078		6,078
Comprehensive income							62,180
Tax effect on employee stock options exercised		38					38
Cash dividends declared			(15,802)				(15,802)
Issuance of restricted stock units, net		1,725		(1,275)			450
Delivery of treasury shares							
Performance shares		(57)				275	218
401(k) plans		(170)				1,015	845
Director compensation		(12)				105	93
Employee stock options exercised net		(165)				1,082	917
Balance at December 31, 2004	544	41,828	525,056	(1,275)	8,768	(154,551)	420,370
Net income			38,609				38,609
Other comprehensive income							
Foreign currency translation adjustments					(9,619)		
Additional minimum pension liability, net of tax benefits of $2,831					(4,492)		
Other comprehensive income					(14,111)		(14,111)
Comprehensive income							24,498
Tax effect on employee stock options exercised		76					76
Cash dividends declared			(15,855)				(15,855)
Issuance of restricted stock units, net		1,894		(1,020)			874
Delivery of treasury shares							
Restricted stock awards							
401(k) plans		(84)				917	833

Director compensation	(21)	123	102
Employee stock options exercised net	(243)		