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**PARAGON**  
TECHNOLOGIES

ANNUAL REPORT  
**December 31, 2005**





## **WE BUILD PRODUCTIVITY**

**Paragon Technologies, Inc.** is one company, with a wide range of capabilities to meet the material handling needs of an increasingly diverse and demanding marketplace. Paragon is an unparalleled resource for specialized material handling solutions that are delivered to the marketplace under the SI Systems' Production & Assembly and SI Systems' Order Fulfillment brands.

**SI Systems** — renewed excitement in our technologies and our potential. Reputations in material handling are earned through long-term performance. Few companies have a better track record than SI Systems. Its LO-TOW<sup>®</sup>, CARTRAC<sup>®</sup>, and DISPEN-SI-MATIC<sup>®</sup> technologies are relied upon in industries throughout the world. Now, SI Systems has added breadth to those technologies, with software products, diagnostic services, ergonomic improvements, and control system solutions that further enhance productivity.



## FINANCIAL HIGHLIGHTS

	Fiscal Year Ended				
	12/31/05	12/31/04	12/31/03	12/31/02	12/31/01
<i>(Dollars in thousands, except share and per share data)</i>					
<b>Statement of Operations:</b>					
Net sales	\$ 16,676	11,702	12,083	14,906	19,008
Operating income (loss)	\$ (172)	(449)	(236)	1,700	(1,869)
Operating margin	-1.0%	-3.8%	-2.0%	11.4%	-9.8%
Income (loss) from continuing operations before income taxes	\$ 301	(271)	6,034	1,376	(2,114)
Interest expense	\$ 1	4	676	1,046	1,298
EBIT from continuing operations	\$ 302	(267)	6,710	2,422	(816)
Depreciation expense	\$ 90	104	139	233	323
EBITDA from continuing operations	\$ 392	(163)	6,849	2,655	(493)
Income (loss) from continuing operations	\$ 208	(165)	3,685	956	(1,158)
Income (loss) from discontinued operations, net of income taxes	\$ 990	1,638	100	(293)	1,096
Net income (loss)	\$ 1,198	1,473	3,785	663	(62)
Basic earnings (loss) per share:					
Income (loss) from continuing operations	\$ 0.05	(0.04)	0.87	0.23	(0.27)
Income (loss) from discontinued operations	\$ 0.24	0.38	0.02	(0.07)	0.26
Net income (loss)	\$ 0.29	0.34	0.89	0.16	(0.01)
Diluted earnings (loss) per share:					
Income (loss) from continuing operations	\$ 0.05	(0.04)	0.85	0.22	(0.27)
Income (loss) from discontinued operations	\$ 0.24	0.38	0.02	(0.07)	0.26
Net income (loss)	\$ 0.29	0.34	0.87	0.15	(0.01)
<b>Balance Sheet:</b>					
Current assets	\$ 22,134	14,249	14,720	15,444	19,200
Current liabilities	\$ 5,337	7,355	9,583	9,416	13,357
Working capital	\$ 16,797	6,894	5,137	6,028	5,843
Current ratio	4.15	1.94	1.54	1.64	1.44
Total assets	\$ 22,596	33,424	33,803	36,703	41,621
Total long-term debt	\$ -	-	-	7,263	9,900
Total stockholders' equity	\$ 17,066	23,308	22,061	17,885	16,912
Total capitalization	\$ 17,066	23,308	22,061	25,148	26,812
Average return on equity	5.9%	6.5%	19.0%	3.8%	-0.4%
Average return on investment	5.9%	6.5%	16.0%	2.6%	-0.2%
<b>Other Information:</b>					
Book value per share	\$ 4.82	5.46	5.16	4.20	4.01
Shares of common stock outstanding	3,539,019	4,265,310	4,277,595	4,256,098	4,221,635
Basic - weighted average shares outstanding	4,073,252	4,278,065	4,269,274	4,231,878	4,210,819
Diluted - weighted average shares outstanding	4,118,594	4,350,297	4,364,712	4,300,193	4,210,819
Orders	\$ 18,080	13,164	11,301	12,074	10,321
Backlog of orders	\$ 6,918	5,514	4,052	4,834	7,666

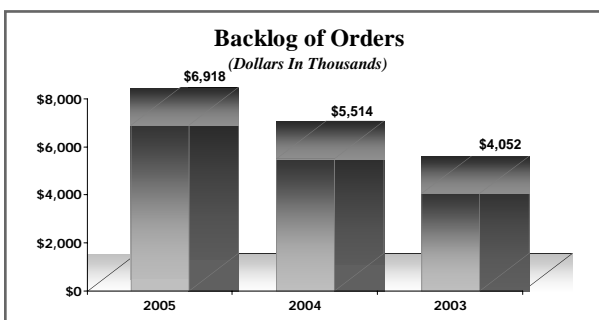
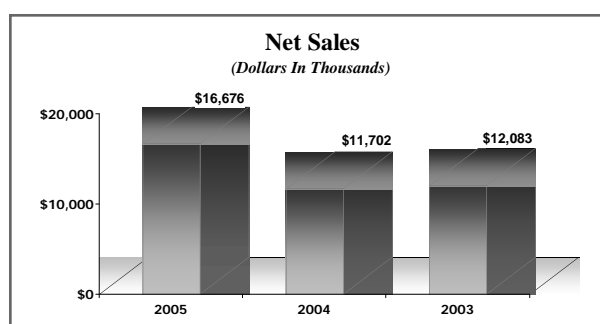
## LETTER TO STOCKHOLDERS

Dear Stockholders:

The past year has been a year of structural change, whereas the upcoming year will be one of transition to a new marketing initiative. In the third quarter, the Company completed the sale of substantially all of the assets and liabilities of Ermanco Incorporated, Paragon's wholly owned conveyor and sortation subsidiary. This sale allows the Company to focus its efforts and redirect its assets to potentially higher growth and broader market segments.

In parallel with structural changes, SI Systems' Production & Assembly and Order Fulfillment brands have experienced vigorous growth in bookings, backlog, and sales. Basic earnings per share from continuing operations for 2005 increased to \$0.05 as compared to a loss of \$0.04 in 2004.

Net sales for 2005 were 43% higher than 2004, and we expect a continuing rising trend as our marketing efforts gain traction. We have added seasoned technical sales and sales support professionals to our staff to jumpstart and energize our penetration into a broader customer base.



A good barometer of the success of our marketing and sales strategy is the backlog of orders. The backlog of orders at the end 2005 was 25% higher than at the end of 2004. Order backlog typically transforms to revenue during the current year, so it is reasonable to expect that a 25% increase in backlog at the beginning of the year is one indicator of a potential increase in sales during the current year.

The Company strengthened its Balance Sheet over the last three years by retiring its long-term debt and eliminating the goodwill associated with Ermanco. An increased cash position from the sale of Ermanco allowed the Company to end the year with a high current ratio of 4.15.

<b>Selected Financial Data</b> (Dollars In Thousands)					
	<u>12/31/05</u>	<u>12/31/04</u>	<u>12/31/03</u>	<u>12/31/02</u>	<u>12/31/01</u>
<b>Cash and Cash Equivalents,</b>					
<b>Restricted Cash, and</b>					
<b>Short-Term Investments</b>	\$ 17,397	3,602	5,591	6,250	6,114
<b>Long-Term Debt</b>	\$ -	-	-	7,263	9,900
<b>Tangible Net Worth</b>	\$ 17,066	5,651	4,404	228	(745)

Paragon Technologies is transforming from a specialized, engineered product company into a process solution company that is fueled by our extensive knowledge base. The software engine that powers our technology has evolved from the first mini-computers that were available three decades ago to the personal computer platforms that are favored by most of our clients today. The Company's goal is to use our reservoir of talent, experience, and goodwill among our customer base as a foundation, coupled with alliances with and potential acquisitions of complementary business partners, to promote sustained growth and recurring revenues.

Your Company has quietly transformed the way America manufactures and distributes its products. Hundreds of millions of people are using items that have been touched by Paragon's technology at some point in time. These items include automobiles, all terrain vehicles, golf carts, pharmaceuticals, nutritional supplements, health and beauty aids, contacts lenses, and entertainment media. Many of these products are automatically selected and guided by our technology in the distribution centers that serve retail outlets or customers directly.

Although we have been successful in the higher tier markets that we serve, there are literally thousands of potential corporate customers in the lower tiers that we have targeted. In earlier years, our rich engineering capability led us to believe that we were an "engineered" product company, even though our capability to provide broad software-driven solutions had been proven in many projects. Customers expect suppliers to address their problems aggressively and to propose solutions that require a systems approach. We stepped up to that challenge and over the years, we undertook many complex and comprehensive systems.

During the last six months, we have focused on our true strength and core competencies. Our Production & Assembly Systems brand, which focuses on the manufacturing sector, and our Order Fulfillment Systems brand, which addresses the warehousing and distribution sector, each understand that it is process knowledge and systems capability that is the Company's strength. Our mantra is that Paragon Technologies will establish life cycle partnerships with customers through their evolutionary expansion processes, wherein we offer products and services that match their requirements in every stage. We will be intensely focused on our customers' needs and will meet or exceed their expectations in every engagement. Our reward will be a recurring revenue stream that steadily grows as our customers embrace us as partners in their success.

This message is being conveyed to our customers via direct and publication advertising, through trade magazine case studies via our website, and through direct interaction with customers. To bring this message to the marketplace, we are aggressively expanding our advertising and marketing activities during the upcoming year.

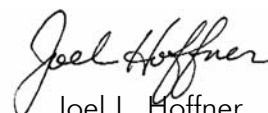
In concert with the re-tooled message that we are delivering to our customer base, we acknowledge our responsibility to communicate the vision and potential of Paragon to our stockholders. Toward that end, we have embarked on an expanded investor relations program. Our goal is to reach a broader base of investors with a clear, balanced, and factual portrayal of the Company's vision and our progress towards it.

The Company appreciates the loyalty of our diverse customer base and the dedication of our seasoned, professional employees who have a vast knowledge of the challenging industry that we serve. The continued support of our investors is equally gratifying.

Sincerely,



Theodore W. Myers  
Chairman of the Board



Joel L. Hoffner  
President and CEO

# INSIDE PARAGON — 2005

## Thought Leadership . . . Industry Innovators



As one of the predominant transport conveyor system suppliers, SI Systems Production & Assembly brand is positioning its venerable LO-TOW® and CARTRAC® technologies in new

automated solutions.

Created in the 1960s LO-TOW®, a towline conveyor, is the workhorse in providing customers significant productivity gains, particularly in the assembly of vehicles of all types and their sub assembly components, such as axles, engines, transmissions, and dash panels. Combined with Ergonomic Towline Vehicles (ETV™), which serve as mobile workstations that lift, lower, and rotate products being assembled, SI's systems solutions improve productivity and reduce worker fatigue.



Radio frequency identification (RFID) and advanced computer controls provide added levels of sophistication that allow communication between the factory floor and customer's Manufacturing Execution System (MES).

As the market demand continues to expand for recreational and utility vehicles, our versatile LO-TOW® conveyors are being selected for a broader base of applications, including lawn mowers, leisure craft, cars, trucks, golf carts, ATV's, garbage trucks, and farm tractors.

The Company's CARTRAC® technologies, designed for niche markets requiring high volume output, extremely accurate positioning, and gentle transport are being successfully repositioned to serve new markets in munitions and energy-related industries.

In concert with the Company's strategy to serve a more diverse base of customers, a business alliance was formed with OCS Intellitrak, Inc. to market and integrate their line of overhead conveyance products for production and assembly applications.



The SI Systems Order Fulfillment brand concentrates its efforts on delivering turnkey automated systems solutions for the constantly expanding North American distribution markets.

In 2005, the Company strengthened its market presence in the pharmaceutical, health and beauty aids, entertainment, and office supply industries by embracing greater levels of involvement within client facilities.

The Company has traditionally accepted the highest degree of challenge and responsibility within a given distribution operation by successfully implementing sophisticated mechanization and software that is at the core of our clients' ability to transact their business. Our mastery of the most difficult distribution problems has become our vehicle for growth.

SI's Order Fulfillment brand launched a new distribution analysis and management tool in 2005. This product, the DC Xcellerator™, is an evolutionary software product that enables engineers and managers in complex distribution facilities to plan and execute the most productive order processing sequence possible.

The development of DC Xcellerator™ was jointly funded by a fortune 500 client who recognized the ability of the Company to produce a product specifically dedicated to the evaluation of sophisticated distribution solutions.



SI's Order Fulfillment brand is expanding its reach in the distribution marketplace. Its analytical abilities, products, and tools have widespread application across a broad base of industries and we embrace the challenges that those potential clients present.

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## OFFICERS

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**Joel L. Hoffner**  
President and CEO  
Paragon Technologies, Inc.

**William J. Casey**  
Executive Vice President  
Paragon Technologies, Inc.

**Ronald J. Semanick**  
Vice President Finance, CFO, Treasurer & Secretary  
Paragon Technologies, Inc.

**John F. Lehr**  
Vice President  
Paragon Technologies, Inc.

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## DIRECTORS

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**Theodore W. Myers**  
Chairman of the Board, Paragon Technologies, Inc.  
Former First Vice President and Branch Manager,  
Tucker Anthony Sutro

**Joel L. Hoffner**  
President and CEO, Paragon Technologies, Inc.  
Former Managing Director, The QTX Group

**Leonard S. Yurkovic**  
Former President and CEO, Paragon Technologies, Inc.

**Anthony W. Schweiger**  
President and CEO, The Tomorrow Group, LLC  
Managing Principal, e-brilliance, LLC  
Director, Radian Group Inc.

**L. Jack Bradt**  
Founder, former Chairman, President and CEO  
of SI Handling Systems, Inc.

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### Stock Listing

The American Stock Exchange  
Trading Symbol: "PTG"

### Transfer Agent & Registrar

American Stock Transfer & Trust Co.  
59 Maiden Lane  
New York, NY 10038

### General Counsel

Pepper Hamilton LLP  
400 Berwyn Park  
899 Cassatt Road  
Berwyn, PA 19312-1183

### Independent Registered Public Accountants

KPMG LLP  
1601 Market Street  
Philadelphia, PA 19103-2499



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600 Kuebler Road  
Easton, PA 18040-9295  
Phone: 610.252.3205  
Fax: 610.252.3102  
[www.ptgamex.com](http://www.ptgamex.com)