Consolidated Balance Sheets
December 31, 1999 and 1998

(Expressed in millions of Italian lire)

Assets	1999	1998
Current assets:		
Cash and cash equivalents (note 4)	312,648	273,211
Marketable securities (note 5)	50	17,028
Trade receivables, net (note 6)	220,190	198,623
Other receivables (note 7)	86,000	73,782
Inventories (note 8)	103,206	106,546
Prepaid expenses and accrued income	705	1,572
Deferred income taxes (note 14)	7,751	4,071
Total current assets	**730,550**	**674,833**
Non current assets:		
Property, plant and equipment (note 9 and 16)	295,858	274,079
Less accumulated depreciation (note 9)	(93,519)	(79,611)
Net property, plant and equipment	**202,339**	**194,468**
Other assets (note 10)	4,309	4,757
Deferred income taxes (note 14)	143	205
Total assets	**937,341**	**874,263**

See accompanying notes to consolidated financial statements.

Liabilities and Shareholders' Equity	1999	1998
Current liabilities:		
Short-term borrowings (note 11)	938	3,890
Current portion of long-term debt (note 16)	1,197	1,684
Accounts payable-trade (note 12)	116,611	110,173
Accounts payable-other (note 13)	20,495	26,761
Allowance for unrealized foreign exchange losses (note 24)	2,545	218
Income taxes (note 14)	2,774	17,872
Salaries, wages and related liabilities (note 15)	16,751	16,566
Total current liabilities	**161,311**	**177,164**
Long-term liabilities:		
Employees' termination indemnity (note 3 (l))	33,618	30,260
Long-term debt (note 16)	1,118	2,315
Deferred income taxes (note 14)	1,743	1,817
Other liabilities	5,821	4,181
Minority interest (note 17)	**1,557**	**1,398**
Shareholders' equity (note 18 and 19):		
Share capital	7,184	7,184
Reserves	62,029	62,241
Additional paid-in capital	15,441	15,441
Retained earnings	647,519	572,262
Total shareholders' equity	**732,173**	**657,128**
Commitments and contingent liabilities (notes 20 and 24)	-	-
Total liabilities and shareholders' equity	**937,341**	**874,263**

See accompanying notes to consolidated financial statements.

Consolidated Statements of Earnings
Years ended December 31, 1999, 1998 and 1997

(Expressed in millions of Italian lire, except per share data)

	1999	1998	1997
Net sales (note 21)	1,091,689	1,066,173	1,063,132
Cost of sales (note 22)	(651,615)	(691,824)	(716,235)
Gross profit	**440,074**	**374,349**	**346,897**
Selling expenses	(164,467)	(171,345)	(171,659)
General and administrative expenses	(43,823)	(38,032)	(39,053)
Operating income	**231,784**	**164,972**	**136,185**
Other income (expense), net (note 23)	(32,476)	20,810	12,318
Earnings before taxes and minority interest	**199,308**	**185,782**	**148,503**
Income taxes (note 14)	(39,441)	(46,335)	(44,148)
Earnings before minority interest	**159,867**	**139,447**	**104,355**
Minority interest	(305)	(148)	(181)
Net earnings	**159,562**	**139,299**	**104,174**
Basic earnings per share (note 3 (r))	**2,776**	**2,434**	**1,832**
Diluted earnings per share (note 3 (r))	**2,776**	**2,433**	**1,817**

See accompanying notes to consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity
Years ended December 31, 1999, 1998 and 1997

(Expressed in millions of Italian lire, except number of ordinary shares)

	Share capital					
	Number of ordinary shares	Amount	Reserves	Additional paid-in capital	Retained earnings	Total
Balances at December 31, 1996	**56,878,800**	**7,110**	**14,508**	**9,238**	**434,892**	**465,748**
Dividends distributed	-	-	-	-	(14,788)	(14,788)
Exchange differences on translation of financial statements	-	-	-	-	2,551	2,551
Grants received	-	-	53,005	-	-	53,005
Taxes due on grants received	-	-	(5,272)	-	-	(5,272)
Net earnings	-	-	-	-	104,174	104,174
Balances at December 31, 1997	**56,878,800**	**7,110**	**62,241**	**9,238**	**526,829**	**605,418**
Dividends distributed	-	-	-	-	(91,006)	(91,006)
Exercise of stock options	590,088	74	-	6,203	-	6,277
Exchange differences on translation of financial statements	-	-	-	-	(2,860)	(2,860)
Net earnings	-	-	-	-	139,299	139,299
Balances at December 31, 1998	**57,468,888**	**7,184**	**62,241**	**15,441**	**572,262**	**657,128**
Dividends distributed	-	-	-	-	(91,950)	(91,950)
Transfers	-	-	(212)	-	212	0
Exchange differences on translation of financial statements	-	-	-	-	7,433	7,433
Net earnings	-	-	-	-	159,562	159,562
Balances at December 31, 1999	**57,468,888**	**7,184**	**62,029**	**15,441**	**647,519**	**732,173**

See accompanying notes to consolidated financial statements.

Consolidated Statements of Cash Flows
Years ended December 31, 1999, 1998 and 1997

(Expressed in millions of Italian lire)

Cash flows from operating activities:	1999	1998	1997
Net earnings	159,562	139,299	104,174
Adjustments to reconcile net income to net cash provided by operating activities:			
• Depreciation and amortization	18,430	23,848	21,954
• Employees' termination indemnity	9,234	8,582	8,094
• Deferred income taxes	(3,692)	(1,150)	(4,121)
• Minority interest	305	148	181
• Provision for unrealized losses on marketable debt securities	-	-	66
• (Gain) loss on disposal of assets	2,579	202	(1,640)
• Change in provision for unrealized foreign exchange losses	2,327	(1,966)	2,184
Change in assets and liabilities:			
• Receivables, net	(33,785)	(23,165)	(14,845)
• Inventories	3,340	8,178	(24,274)
• Prepaid expenses and accrued income	867	(421)	3,507
• Other assets	(993)	(1,342)	(2,528)
• Accounts payable	172	11,871	523
• Income taxes	(15,098)	(1,490)	(1,051)
• Salaries, wages and related liabilities	185	(379)	1,355
• Other liabilities	1,640	764	501
• Employees' termination indemnity	(5,876)	(5,362)	(4,272)
Total adjustments	**(20,365)**	**18,318**	**(14,366)**
Net cash provided by operating activities	**139,197**	**157,617**	**89,808**

See accompanying notes to consolidated financial statements.

	1999	1998	1997

Cash flows from investing activities:

Property, plant and equipment:			
• Additions	(18,496)	(26,199)	(81,084)
• Disposals	1,323	447	1,245
Government grants received	-	-	46,876
Marketable debt securities:			
• Purchases	(71,960)	(17,018)	(102)
• Proceeds from maturities	-	3,284	4,579
• Proceeds from sales	86,142	1,757	70,585
Purchase of minority interest	(167)	-	(288)
Net cash provided by (used in) investing activities	**(3,158)**	**(37,729)**	**41,811**

Cash flows from financing activities:

Long-term debt:			
• Repayments	(1,684)	(3,191)	(3,158)
Short-term borrowings	(2,952)	2,094	(2,071)
Exercise of stock options	-	6,277	-
Dividends paid	(91,950)	(91,006)	(14,788)
Dividends paid to minority shareholders	(108)	(99)	(1,018)
Net cash used in financing activities	**(96,694)**	**(85,925)**	**(21,035)**
Effect of translation adjustments on cash	92	(123)	786
Increase in cash and cash equivalents	39,437	33,840	111,370
Cash and cash equivalents, beginning of the year	273,211	239,371	128,001
Cash and cash equivalents, end of the year	312,648	273,211	239,371

Supplemental disclosure of cash flow information:

Cash paid during the year for interest	370	970	840
Cash paid during the year for income taxes	77,757	46,958	36,199

See accompanying notes to consolidated financial statements.

Notes to Consolidated Financial Statements

(Expressed in millions of Italian lire, except as otherwise indicated)

1 Description of business and Group composition

The consolidated financial statements include the accounts of Industrie Natuzzi S.p.A. ('Natuzzi' or the 'Company') and of its subsidiaries (together with the Company, the 'Group'). The Group's primary activity is the design, manufacture and marketing of contemporary and traditional leather and fabric-upholstered furniture.

The subsidiaries included in the consolidation at December 31, 1999, together with the related percentages of ownership, are as follows:

Name	Percent of ownership	Share Capital	Registered office	Activity
Divani e Poltrone Italia S.r.l.	99.98	Lit. 3,700	Bari, Italy	(1)
Soft Cover S.r.l.	100	Lit. 5,000	Bari, Italy	(1)
Spagnesi International S.r.l.	100	Lit. 800	Bari, Italy	(1)
Spagnesi S.p.A.	99.95	Lit. 1,000	Quarrata, Italy	(1)
Creazioni Ellelle S.p.A.	99	Lit. 2,500	Altamura, Italy	(1)
Natco S.p.A.	99.99	Lit. 8,500	Bari, Italy	(2)
I.M.P.E. S.p.A.	90.83	Lit. 1,500	Qualiano,Italy	(3)
Expan Italia S.r.l.	99	Lit. 90	Bari, Italy	(3)
Natex S.r.l.	100	Lit. 90	Bari, Italy	(4)
Natuzzi Trade Service S.r.l.	100	Lit. 3,500	Bari, Italy	(5)
Natuzzi Americas Inc.	100	US$ 50,000	High Point, NC, USA	(5)
Nagest S.r.l.	100	Lit. 90	Bari, Italy	(6)
Softaly S.r.l.	100	Lit. 190	Bari, Italy	(7)
Finat Ltd	100	Lit. 1,000	Dublin, Ireland	(8)
D.L.S. S.r.l.	100	Lit. 90	Bari, Italy	(9)
Italiana de Sofa Franquiciados S.L.	100	Pta 40,000,000	Madrid, Spain	(9)
Natuzzi Argentina	99	US$ 12,000	Buenos Aires, Argentina	(10)

(1) Manufacture and distribution
(2) Intragroup leather dyeing and finishing
(3) Production and distribution of polyurethane foam
(4) Intragroup production of fibrefill down cushion and polyurethane shaping
(5) Distribution
(6) Intragroup accounting services
(7) Intragroup building management
(8) Intragroup cash management and treasury operations
(9) In liquidation
(10) Non operative

During 1999, the Company acquired all of the minority interest of Natex S.r.l. for a consideration of 167 in cash. Goodwill arising from that acquisition amounted to 146.

During 1998, the Company liquidated Masternat S.r.l., Natuzzi Pacific Ltd. and Tecnolevante S.r.l.

In July 1997, the Company set up a subsidiary in Dublin (Ireland), known as Finat Ltd, which is engaged in the provision of intragroup cash management and treasury operations. The interest of the Group in this subsidiary is 100% for consideration of 140,000, of which 1,000 was recorded as share capital and remaining 139,000 as additional contributed capital. In addition, this subsidiary has received a certificate from the Minister for Finance of Ireland which confirms that all qualifying income derived from financial services activities is subject to corporation tax at a reduced rate of 10%.

During 1997, the Company acquired all of the minority interest of Italiana de Sofa Franquiciados S.L. and Tecnolevante S.r.l. for an aggregate consideration of 288 in cash. Goodwill arising from that acquisition amounted to 360.

2 Basis of preparation and principles of consolidation

The financial statements utilized for the consolidation are the statutory financial statements of each Group company at December 31, 1999, 1998 and 1997. The 1998 and 1997 financial statements have been approved by the respective shareholders of the relevant companies. The 1999 financial statements have been approved only by the directors of the relevant companies.

The financial statements of subsidiaries are adjusted, where necessary, to conform to Natuzzi's accounting principles, which are consistent with Italian legal requirements governing financial statements considered in conjunction with established accounting principles promulgated by the Italian Accounting Profession and, in their absence, by the International Accounting Standards Committee. The consolidated financial statements are classified in accordance with the presentations generally used in international practice.

Established accounting principles in the Republic of Italy vary in certain significant respects from generally accepted accounting principles in the United States of America. Application of generally accepted accounting principles in the United States of America would have affected results of operations for each of the years in the three-year period ended December 31, 1999 and shareholders' equity as of December 31, 1999 and 1998 to the extent summarized in Note 26 to the consolidated financial statements.

The consolidated financial statements include all affiliates and companies that Natuzzi directly or indirectly controls, either through majority ownership or otherwise. Control is presumed to exist where more than one-half of a subsidiary's voting power is controlled by the Company or the Company is able to govern the financial and operating policies of a subsidiary or control the removal or appointment of a majority of a subsidiary's board of directors. Where an entity either began or ceased to be controlled during the year, the results of operations are included only from the date control commenced or up to the date control ceased.

The assets and liabilities of subsidiaries are consolidated on a line-by-line basis and the carrying value of intercompany investments held is eliminated against the related shareholder's equity accounts. The minority interests of consolidated subsidiaries are separately classified in the consolidated balance sheets and statements of earnings for all years presented. All intercompany balances and transactions have been eliminated in consolidation.

3 Summary of established accounting policies

The established accounting policies followed in the preparation of the consolidated financial statements are outlined below.

a Foreign currency

Foreign currency transactions are recorded at the exchange rates applicable at the transaction dates. Assets and liabilities denominated in foreign currency are remeasured at year-end exchange rates, except for certain accounts receivable as discussed below. Foreign exchange gains and losses resulting from the remeasurement of these assets and liabilities are included in other income (expense), net, in the statement of earnings.

Receivables being hedged by forward exchange contracts are remeasured using the related forward exchange rate. Foreign exchange gains and losses resulting from the remeasurement of hedged receivables are recognized in other income (expense), net, in the statements of earnings.

Until December 31, 1998 foreign exchange gains and losses on receivables and payables not hedged were aggregated with the unrealized gains and losses on forward exchange contracts not used to hedge any on-or off-balance sheet items to determine recognition. If a net foreign exchange loss resulted from this aggregation, such loss was recognized in other income (expense), net, in the consolidated statement of earnings. A net foreign exchange gain was not recognized until realized (refer to note 3 (b) for the accounting of foreign exchange contracts).

From January 1, 1999 the Group adopted the new accounting principle on “Translation of transactions in foreign currencies”, issued by the Italian Accounting Profession in June 1999. This statement establishes that companies may record unrealized gains resulting from the remeasurement at year-end of assets and liabilities denominated in foreign currencies and forward exchange contracts not designated as hedges of any on-or off-balance sheet items. The adoption of this new accounting principle by the Company did not have any effect on the consolidated financial statements as of December 31, 1999.

The financial statements of foreign subsidiaries for which the functional currency is not the Italian Lira are translated at (i) year-end exchange rate for assets and liabilities, (ii) historical exchange rates for share capital and reserves, and (iii) average exchange rates during the year for statements of earnings. The resulting exchange differences on translation are recorded as a direct adjustment to shareholders' equity.

b *Forward exchange contracts*

The Group enters into forward exchange contracts (known in Italian financial markets as domestic currency swaps) to manage its exposure to foreign currency risks. The accounting for forward exchange contracts depends on their use as follows:

- Forward exchange contracts used to hedge accounts receivable are considered when remeasuring the related balance sheet item at the contract rate. Foreign exchange gains and losses from the remeasurement of the accounts receivable at contract rate are recorded within other income, net, in the consolidated statements of earnings.
- Forward exchange contracts are used to hedge future sales if the sales are supported by sales orders and customer's indications of future purchases as of the balance sheet date which are confirmed by sales orders received within the earlier of four months after the year-end or the issuance of the consolidated financial statements. Unrealized gains and losses on these forward contracts are deferred.
- Until December 31, 1998 unrealized gains and losses on forward exchange contracts not hedging any on-or off-balance sheet items were aggregated with the foreign currency gains and losses resulting from the remeasurement of unhedged accounts receivable and payable (refer to note 3 a). From January 1, 1999 unrealized gains and losses on forward exchange contracts not hedging any on-or off-balance sheet items are recorded in other income (expense), net, in the consolidated statements of earnings.

c *Cash equivalents*

The Group considers time deposits to be cash equivalents.

d *Marketable debt securities*

Marketable debt securities are valued at the lower of cost or market value determined on an individual security basis. A valuation allowance is established and recorded as a charge to other income, net, for unrealized losses on securities. Unrealized gains are not recorded until realized. Recoveries in the value of securities are recorded as part of other income, net, but only to the extent of previously recognized unrealized losses.

Gains and losses realized on the sale of marketable debt securities were computed based on a weighted-average cost of the specific securities being sold.

Realized gains and losses are charged to other income (expense), net.

e *Accounts receivable and payable*

Receivables are stated at nominal value net of an allowance for doubtful accounts. Payables are stated at face value.

f *Inventories*

Raw materials are stated at the lower of cost (determined under the specific cost method for leather hides and under the weighted-average method for other raw materials) or replacement cost. Goods in process and finish goods are valued at the lower of production cost or net realizable value.

g *Property, plant and equipment*

Property, plant and equipment is stated at historical cost, except for plant which were revalued in 1983 and 1991 according to Italian revaluation laws. Maintenance and repairs are expensed; significant improvements are capitalized and depreciated over the useful life of the related assets. The cost or valuation of fixed assets is depreciated on the straight-line method over the estimated useful lives of the assets (refer to note 9).

h *Other assets*

Other assets in the consolidated financial statements primarily include trademarks and patents, goodwill and certain deferred costs. These assets are stated at the lower of amortized cost or recoverable amount. The carrying amount of other assets are reviewed to determine if they are in excess of their recoverable amount, based on undiscounted cash flows, at the consolidated balance sheet date. If the carrying amount exceeds the recoverable amount, the asset is written down to the recoverable amount.

Trademarks, patents and goodwill are amortized on a straight-line basis over a period of five years.

i *Impairment of Long-lived Assets*

The Company reviews long-lived assets, including intangible assets, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Estimated fair value is generally based on either appraised value or measured by discounted estimated future cash flows. Accordingly, actual results could vary significantly from such estimates.

j *Income taxes*

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss. Deferred tax assets are reduced by a valuation allowance to an amount that is more likely than not to be realized. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

k *Government grants*

Capital grants from government agencies are recorded when there is reasonable assurance that the grants will be received and that the Group will comply with the conditions applying to them. Capital grants are recorded, net of tax, within reserves in shareholders' equity.

The capital grants are part of the Italian government's investment incentive program, under which the Group receives amounts generally equal to a percentage of the aggregate investment made by the Group in the construction of new manufacturing facilities, or in the improvement of existing facilities, in designated areas of the country.

Cost reimbursement grants relating to training and other personnel costs are credited to income when received from government agencies.

l *Employees' termination indemnities*

Termination indemnities represent amounts accrued for each Italian employee that are due and payable upon termination of employment determined in accordance with applicable labor laws and agreements. The Group accrues the full amount of employees' vested benefit obligation as determined by such laws and agreements for termination indemnities.

The expense recorded for termination indemnities for the years ended December 31, 1999, 1998 and 1997 was 9,234, 8,582 and 8,094 respectively.

The number of workers employed by the Group totalled 3,492 and 3,363 at December 31, 1999 and 1998, respectively.

m *Net Sales*

A sale is recorded when title passes to the customer, which is at the time of shipment. Sales are recorded net of returns and discounts.

n *Advertising costs*

Advertising costs are expensed in the periods incurred. Advertising expenses recorded for the years ended December 31, 1999, 1998 and 1997 were 20,722, 22,918 and 17,956 respectively.

o *Commission expense*

Commissions payable to sales representatives and the related expenses are recorded at the time shipments are made by the Group to customers. Commissions are not paid until payment for the related sale's invoice is remitted to the Group by the customer.

p *Contingencies*

Liabilities for loss contingencies are recorded when it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated.

q *Use of estimates*

The preparation of financial statements in conformity with established accounting policies requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

r *Earnings per share*

Basic earnings per share is calculated by dividing net earnings attributable to ordinary shareholders by the weighted-average number of ordinary shares outstanding during the period. Diluted earnings per share include the effects of possible issuance of ordinary shares under share options in the determination of the weighted-average number of ordinary share outstanding during the period. The following table provides the amounts used in the calculation of earnings per share:

	1999	1998	1997
Net earnings attributable to ordinary shareholders	**159,562**	**139,299**	**104,174**
Weighted-average number of ordinary shares outstanding during the year	57,468,888	57,223,018	56,878,800
Increase resulting from assumed conversion of share options	-	29,834	458,711
Weighted-average number of ordinary shares and potential shares outstanding during the year	**57,468,888**	**57,252,852**	**57,337,511**

4 Cash and cash equivalents

Cash and cash equivalents are composed of the following items:

	1999	1998
Cash on hand	33	45
Bank accounts in Italian lire	267,425	149,971
Bank accounts in foreign currency	28,949	58,060
Time deposits in Italian lire	16,241	65,135
Total	**312,648**	**273,211**

Time deposits have various maturities extending for 1999 and 1998 through January 17, 2000 and April 30, 1999, respectively.

5 Marketable debt securities

Details regarding marketable debt securities are as follows:

	1999	1998
Foreign corporate bonds	12	10,351
Foreign government bonds	-	6,639
Italian government bonds	38	38
Total	**50**	**17,028**

Further information regarding the Group's investments in marketable debt securities is as follows:

1999	Cost	Gross unrealized Gains	Gross unrealized Losses	Fair value
Foreign corporate bonds	12	-	-	12
Italian government bonds	38	-	-	38
Total	**50**	**-**	**-**	**50**

1998	Cost	Gross unrealized Gains	Gross unrealized Losses	Fair value
Foreign corporate bonds	10,351	662	-	11,013
Foreign government bonds	6,639	100	-	6,739
Italian government bonds	38	-	-	38
Total	**17,028**	**762**	**-**	**17,790**

	1999	1998	1997
Proceeds from sales	86,142	1,757	70,585
Realized gains	-	363	2,252
Realized losses	(2,804)	(114)	(408)

The contractual maturity of the Group's marketable debt securities at December 31, 1999 is between 1 – 5 years.

6 Trade receivables, net

Trade receivables are analyzed as follows:

	1999	1998
North American customers	102,082	80,411
Other foreign customers	75,150	70,366
Domestic customers	47,979	54,100
Trade bills receivable	5,260	4,061
Total	230,471	208,938
Allowance for doubtful accounts	(10,281)	(10,315)
Total trade receivables, net	**220,190**	**198,623**

Trade receivables are due primarily from major retailers selling directly to customers.

No account receivable from any customer at December 31, 1999 and 1998 exceeded 10,000. The Company has insured its collection risk in respect of approximately 80% of accounts receivable outstanding balances and, estimates an allowance for doubtful accounts based on insurance in place, the credit worthiness of its customers as well as general economic conditions.

The following table provides the movements in the allowance for doubtful accounts:

	1999	1998	1997
Balance, beginning of year	10,315	8,354	8,516
Charges-bad debt expense	478	4,278	1,634
Reductions-write off of uncollectible accounts	(512)	(2,317)	(1,796)
Balance, end of year	**10,281**	**10,315**	**8,354**

Trade receivables denominated in foreign currencies at December 31, 1999 and 1998 and, where applicable, translated at the rate of the related domestic currency swaps, totalled 160,597 (174,827 translated at year-end exchange rates) and 134,904 (131,745 translated at year-end exchange rates), respectively. These receivables consist of the following:

	1999	1998
U.S. dollars	100,818	79,744
German marks	11,435	13,953
Australian dollars	9,290	8,252
British pounds	8,882	6,777
Canadian dollars	5,873	3,114
French francs	4,030	6,014
Belgian francs	2,773	2,899
Spanish pesetas	2,498	2,859
Dutch guilders	2,233	2,344
Other currencies	12,765	8,948
Total	**160,597**	**134,904**

7 Other receivables

Other receivables are analyzed as follows:

	1999	1998
VAT	62,144	44,551
Receivable from tax authorities	8,635	4,426
Government grants	6,441	6,459
Advances to suppliers	4,207	4,327
Securities bought under agreements to resell	-	10,357
Other	4,573	3,662
Total	**86,000**	**73,782**

The VAT receivable includes value added taxes and interest thereon reimbursable to various companies of the Group. While currently due at the balance sheet date, the collection of the VAT receivable may generally extend over a maximum period of up to two years.

During February 2000 the Company has collected VAT and interest thereon for an amount of approximately 27,000. The receivable from tax authorities represents taxes paid in excess of the amounts due in Italy and interest thereon.

8 Inventories

Inventories are analyzed as follows:

	1999	1998
Leather	36,574	42,631
Other raw materials	29,927	28,656
Goods in process	19,310	18,747
Finished products	17,395	16,512
Total	**103,206**	**106,546**

9 Property, plant and equipment and accumulated depreciation

Fixed assets are listed below together with accumulated depreciation.

1999	Cost or valuation	Accumulated depreciation	Annual rate of depreciation
Land	9,661	-	-
Industrial buildings	156,755	23,299	3 - 10%
Machinery and equipment	95,202	48,345	11.5 - 25%
Office furniture and equipment	23,810	16,425	12 - 20%
Transportation equipment	5,513	4,114	20 - 25%
Leasehold improvements	1,636	1,336	10 - 20%
Advances to suppliers	3,281	-	-
Total	**295,858**	**93,519**	

1998	Cost or valuation	Accumulated depreciation	Annual rate of depreciation
Land	9,131		-
Industrial buildings	147,371	18,523	3 - 10%
Machinery and equipment	89,221	41,472	11.5 - 25%
Office furniture and equipment	20,496	14,000	12 - 20%
Transportation equipment	5,237	3,868	20 - 25%
Leasehold improvements	2,211	1,748	10 - 20%
Advances to suppliers	412	-	-
Total	**274,079**	**79,611**	

10 Other assets

Other assets consist of the following:

	1999	1998
Trademarks and patents	21,811	24,529
Goodwill	2,770	4,864
Others	8,509	7,740
Total, gross	33,090	37,133
Less accumulated amortization	(28,781)	(32,376)
Total, net	**4,309**	**4,757**

11 Short-term borrowings

Short-term borrowings consist of the following:

	1999	1998
Bank overdrafts	938	736
Export financing	-	3,154
Total	**938**	**3,890**

The weighted average interest rates on the above-listed short-term borrowings are as follows:

	1999	1998
Bank overdrafts	4.1%	4.0%
Export financing	10.7%	10.8%

Credit facilities available to the Group, including amounts guaranteed under surety bonds, amounted to approximately 281,000 and 157,000 at December 31, 1999 and 1998, respectively. The unused portion of these facilities amounted to approximately 265,500 and 137,000 at December 31, 1999 and 1998, respectively.

12 Accounts payable-trade

Accounts payable-trade totalling 116,611 and 110,173 at December 31, 1999 and 1998, respectively, represent principally amounts payable for purchases of goods and services in Italy and abroad, and include 15,663 and 24,296 at December 31, 1999 and 1998, respectively, denominated in foreign currencies.

13 Accounts payable-other

Accounts payable-other are analyzed as follows:

	1999	1998
Withholding taxes on dividends distributed	-	8,059
Withholding taxes on payroll	6,298	5,857
Withholding taxes other	129	105
Cooperative advertising and quantity discount	7,057	5,393
Provision for returns and other discounts	4,108	4,549
Payable to customers for returns and financial discounts	2,234	2,224
Other	669	574
Total	**20,495**	**26,761**

14 Taxes on income

Italian companies are subject to two income taxes:

	1999	1998	1997
IRPEG (state tax)	37.00%	37.00%	37.00%
ILOR (regional tax)	-	-	16.20%
IRAP (regional tax)	4.25%	4.25%	-

During December 1997, the Italian Government approved two legislative decrees which introduced two new income tax schemes, one denominated the 'IRAP' and the other the 'Dual Income Tax'. The general guidelines regulating the new taxes are the following:

(a) for fiscal years beginning on or after January 1, 1998 IRAP replaced ILOR, net equity tax and other minor taxes. For 1998 and 1999 fiscal years the tax rate is 4.25%. Thereafter, each Italian Region will have the power to increase the rate by a maximum of 1%. In general, the taxable base is a form of gross profit determined as the difference between gross revenues (excluding interest and dividend income) and direct production costs (excluding labor costs, interest expenses and other financial costs); (b) for fiscal years beginning on or after January 1, 1997 the IRPEG was modified to introduce a dual income tax for the purpose of encouraging companies to use equity rather than debt finance. A first portion of the taxpayer's taxable income is calculated by applying an interest rate percentage (based on the return on government and private sector bonds) to the net increase in shareholders' equity of such taxpayer, subject to certain restrictions. This portion is subject to IRPEG at the reduced rate of 19%. The remaining profit will be subject to tax at the ordinary IRPEG tax rate (at present 37%). The combined application of IRPEG and the dual income tax cannot generate an overall tax charge lower than 27%. The application of the provisions of the modified IRPEG had no significant effect on the Group's income taxes for 1999, 1998 and 1997.

Furthermore, on December 18, 1997, the Italian Government approved a legislative decree that effectively eliminated income taxes imposed on the remittance of dividends to a parent company. The legislative decree is effective for fiscal years beginning after December 31, 1997.

Under Italian investment incentive schemes for under-industrialized regions, certain of the Group's operating entities are currently entitled to enjoy a full exemption from IRPEG and a significant part of IRAP (full exemption for ILOR for 1997) for ten years. A very significant portion of the Group's consolidated earnings before minority interest in 1999, 1998 and 1997 is derived from companies entitled to some extent to the aforementioned exemptions, the most significant of which presently are not due to expire until 2002. See the table below for the effect of such exemptions on the Group's 1999, 1998 and 1997 income tax charge.

During 1998 and 1997, domestic subsidiaries of the Company distributed previously unremitted earnings to the parent company in the form of a dividend generating taxable income.

Approximately 98.9%, 95.2% and 97.2% respectively, of the Group's consolidated earnings before taxes were generated by its domestic Italian operations during 1999, 1998 and 1997.

The effective income tax rates for the years ended December 31, 1999, 1998 and 1997 were 19.8%, 24.9% and 29.7%, respectively. The actual income tax expense differs from the 'expected' income tax expense (computed by applying the state tax of 37% to income before income taxes and minority interest) as follows:

	1999	1998	1997
Expected income tax charge at full tax rates	73,744	68,739	54,946
Effects of:			
• Tax exempt income	(48,261)	(32,613)	(26,712)
• Aggregate effect of different tax rates in foreign jurisdictions	(449)	(2,295)	(153)
• Tax effect of unremitted earnings of domestic subsidiaries	-	-	433
• Effect of net change in valuation allowance established against deferred tax assets	226	878	(1,439)
• Non-deductible expenses and others	2,948	2,803	3,006
• Regional tax	11,233	8,823	14,067
Actual tax charge	**39,441**	**46,335**	**44,148**

Total taxes for the years ended December 31, 1999, 1998 and 1997 were allocated as follows:

	1999	1998	1997
Earnings from operations	39,441	46,335	44,148
Shareholders' equity, for deferred taxes on government grants (excluding minority interest)	-	-	5,283
	39,441	**46,335**	**49,431**

Income taxes on earnings, which primarily relate to Italian operations, are further analyzed as follows:

	1999	1998	1997
Current taxes	43,133	47,485	48,269
Deferred taxes	(3,692)	(1,150)	(4,121)
Total	**39,441**	**46,335**	**44,148**

Total current taxes for the years ended December 31, 1999, 1998 and 1997 were allocated as follows:

	1999	1998	1997
Italian State tax	31,404	37,697	32,841
Italian Regional tax	11,233	8,823	14,067
Tax of foreign subsidiaries	496	965	1,361
Total	**43,133**	**47,485**	**48,269**

Tax years for Italian companies are open from 1993 and subject to review pursuant to Italian tax laws.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 1999 and 1998 are presented below:

	1999	1998
Deferred tax assets:		
• Unrealized foreign exchange losses	4,678	5
• Allowance for doubtful accounts	3,553	3,544
• Provision for termination indemnities of sales representatives	1,741	1,177
• Provision for returns and discounts	1,656	1,684
• Intercompany profit in assets	1,143	1,703
• Tax loss carryforwards	524	1,056
• Trademarks	412	1,031
• Other temporary differences	879	814
Total gross deferred tax assets	14,586	11,014
• Less valuation allowance	(4,962)	(4,556)
Net deferred tax assets	9,624	6,458
Deferred tax liabilities:		
• Government grants related to capital expenditures	(3,286)	(3,860)
• Other temporary differences	(187)	(139)
Total deferred tax liabilities	(3,473)	(3,999)
Net deferred tax assets	**6,151**	**2,459**

A valuation allowance has been established principally for the allowance for doubtful accounts, provision for termination indemnities of sales representatives and for contingencies of certain subsidiaries.

The valuation allowance for deferred tax assets as of December 31, 1999 and 1998 was 4,962 and 4,556 respectively. The net change in the total valuation allowance for the years ended December 31, 1999 and 1998 was an increase of 406 and 878, respectively. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not than some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and the tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods during which the deferred tax assets are deductible, management believes it is more likely the not that the Company will realize the benefits of these deductible differences, net of the existing valuation allowances at December 31, 1999. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

Net deferred income tax assets is included in the consolidated balance sheets as follows:

1999	Current	Non current	Total
Gross deferred tax assets	11,401	3,185	14,586
Valuation allowance	(2,851)	(2,111)	(4,962)
Net deferred tax assets	8,550	1,074	9,624
Deferred tax liabilities	(799)	(2,674)	(3,473)
Net deferred tax assets (liabilities)	7,751	(1,600)	6,151

1998	Current	Non current	Total
Gross deferred tax assets	8,174	2,840	11,014
Valuation allowance	(3,009)	(1,547)	(4,556)
Net deferred tax assets	5,165	1,293	6,458
Deferred tax liabilities	(1,094)	(2,905)	(3,999)
Net deferred tax assets (liabilities)	4,071	(1,612)	2,459

The tax loss carryforwards of the Group total 1,415 and expire as follows:

2002	899
2003	438
2004	78
Total	**1,415**

Losses may be carried forward for five years from the year of declaration for offset against IRPEG taxes only.

See Note 23 for a description of the tax liability settlement effected in 1999, and Note 26(g) for the difference between Italian GAAP and US GAAP in reporting such tax settlement.

15 Salaries, wages and related liabilities

Salaries, wages and related liabilities are analyzed as follows:

	1999	1998
Salaries and wages	9,747	7,992
Social contribution	6,673	6,659
Vacation accrual	331	1,915
Total	**16,751**	**16,566**

16 Long-term debt

Long-term debt is repayable in semi-annual installments with 1,197, 645, 312 and 161 maturing in the years ended December 31, 2000, 2001, 2002 and 2003, respectively. Interest rates on long-term debt range from 3.7% to 7.3% at December 31, 1999 and 1998. All long-term debt is secured by mortgages on the Group's properties for a total of 8,000.

17 Minority interest

Minority interest shown in the accompanying consolidated balance sheet at December 31, 1999 of 1,557 (1,398 at December 31, 1998) includes 53 pertaining to the majority shareholders of the Group (101 at December 31, 1998).

18 Employee stock option plan

In February 1994 the Board of Directors of the Company adopted an employee stock option plan (the “Plan”) pursuant to which managers and certain key employees of the Group may be granted options to purchase an aggregate of up to 1,680,000 ordinary shares from the Company at an exercise price per share equal to 95% of the May 1993 initial public offering price, or 10,637.5 per share (U.S. dollars 5,52 at December 31, 1999 exchange rate). Employees receiving options may exercise such options over four years during exercise periods from May 15 to May 31, as follows: (i) with respect to 25% of the options, in the year in which they were granted; (ii) with respect to 35% of the options, in the second year thereafter; and (iii) with respect to the remaining 40% of the options, in the fourth year thereafter. Following each exercise period, the Company must seek shareholder approval to increase its capital and comply with certain requirements of Italian law, after which the ordinary shares may be delivered.

A summary of the status of the Plan as of December 31, 1999, 1998 and 1997, and changes during the years ended on those dates is presented below:

	1999	
	Shares	**Exercise price**
Outstanding at the beginning of the year	40,400	10,637.5
Granted	-	-
Exercised	-	-
Forfeited	-	-
Outstanding at the end of the year	**40,400**	**10,637.5**
Options exercisable at year-end	-	
Weighted-average remaining contractual life	0.42	

1998

	Shares	Exercise price
Outstanding at the beginning of the year	620,000	10,637.5
Granted	19,240	10,637.5
Exercised	(590,088)	10,637.5
Forfeited	(8,752)	10,637.5
Outstanding at the end of the year	**40,400**	**10,637.5**
Options exercisable at year-end	-	
Weighted-average remaining contractual life	1.42 years	

1997

	Shares	Exercise price
Outstanding at the beginning of the year	620,000	10,637.5
Granted	-	-
Exercised	-	-
Forfeited	-	-
Outstanding at the end of the year	**620,000**	**10,637.5**
Options exercisable at year-end	-	
Weighted-average remaining contractual life	0.55 years	

The 590,088 Ordinary Shares with respect to which options were exercised in 1998 included 534,448 and 36,400 Ordinary Shares in respect of options granted to employees in 1994 and 1996, respectively, as well as 19,240 Ordinary Shares in respect of options received as a one-time bonus in 1998.

19 Shareholders' equity

The share capital is owned as follows:

	1999	1998
Mr. Pasquale Natuzzi	45.4%	45.4%
Miss Anna Maria Natuzzi	2.4%	2.4%
Mrs. Annunziata Natuzzi	2.4%	2.4%
Public investors	49.8%	49.8%
	100.0%	**100.0%**

An analysis of the reserves follows:

	1999	1998
Legal reserve	2,151	2,151
Monetary revaluation reserve	2,065	2,065
Grants	57,813	58,025
Total	**62,029**	**62,241**

These reserves are all distributable except for the legal reserve which may be utilized to cover losses. Italian law requires that 5% of net income of the parent company and each of its consolidated subsidiaries be retained as a legal reserve until this reserve is equal to one-fifth of the issued capital stock of each relevant company. The combined legal reserves totalled 7,020 and 7,014 at December 31, 1999 and 1998, respectively.

As of December 31, 1999 taxes that would be due on distribution of the portion of shareholders' equity equal to unremitted earnings of foreign subsidiaries would approximate 2.100. The Group has not provided for such taxes as the likelihood of distribution is remote and such earnings are deemed to be permanently reinvested.

The cumulative translation adjustment included in shareholders' equity related to translation of the Group's foreign assets and liabilities at December 31, 1999 and 1998 was a credit of 7,605 and 172, respectively.

20 Commitments and contingent liabilities

Several companies of the Group lease manufacturing facilities under non-cancellable lease agreements with expiration dates through 2006. Rental expense recorded for the years ended December 31, 1999, 1998 and 1997 was 1,608, 1,984 and 2,688, respectively. As of December 31, 1999, minimum annual rental commitments are as follows:

2000	1,764
2001	1,749
2002	1,622
2003	1,159
2004	1,018
Thereafter	1,235
Total	**8,547**

Some banks have provided guarantees at December 31, 1999 to secure the payments to several suppliers of leather and fabric hides amounting to 14,927 (13,871 at December 31, 1998). These guarantees are unsecured and have various maturities extending through December 31, 2000.

VAT reimbursed by tax authorities during 1999 and in prior years is secured by surety bonds for 31,731 (78,572 at December 31, 1998) from certain financial institutions. These surety bonds are unsecured and will expire after a maximum period of up to two years or when the tax authorities perform the final review of VAT claim requests.

In December, 1996, the Company and the 'Contract Planning Service' of the Italian Ministry of the Budget signed a 'Program Agreement' with respect to the 'Natuzzi 2000 project'. In connection with this project, the Natuzzi Group has planned a multi-faceted program of industrial investments for the production of upholstered furniture. Investments are projected to total approximately 571,500. According to the agreement, the Italian government will contribute 281,600. Receipt of the Italian governments funds is based upon, among other things, the Group constructing facilities in accordance with certain specifications and maintaining a minimum number of employees.

During 1997 the Group received under the aforementioned project capital grants for 52,549. Capital expenditures under the Natuzzi 2000 project amounted to approximately 134,000 at December 31, 1999 (121,000 at December 31, 1998). The capital grants are secured by surety bonds for 50,423 from a bank. These surety bonds are unsecured and will expire when the Italian Ministry of Budget releases the final approvals of all investments made.

The Italian tax authorities are currently auditing the corporate income tax returns and VAT declarations for the years ended December 31, 1999 and 1998 filed by a subsidiary enjoying full exemption from IRPEG and IRAP for the aforementioned years.

The Group is also involved in a number of claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters, after considering amounts accrued, will not have a material adverse effect on the Group's consolidated financial position or results of operations.

21 Segmental and geographical information

The Group operates in a single industry segment, that is, the design, manufacture and marketing of contemporary and traditional leather and fabric upholstered furniture. It offers a wide range of upholstered furniture for sale, manufactured in production facilities located in Italy. The Group's products fall into five broad categories: stationary furniture, sectional furniture, motion furniture, sofa beds and lounge chairs. Sales information by products is not available.

The following tables provide information about net sales of upholstered furniture and of long-lived assets by geographical location. Net sales are attributed to countries based on the location of customers. Long-lived assets consist of property, plant and equipment.

Sales of upholstered furniture	1999	1998	1997
United States	444,344	437,930	428,462
Italy	117,860	94,796	75,570
Germany	76,208	75,356	55,984
England	56,318	55,777	56,357
Belgium	41,378	39,288	39,704
The Netherlands	38,739	41,632	42,106
France	16,142	24,329	35,534
Other countries (none greater than 5%)	223,846	226,022	243,742
	1,014,835	**995,130**	**977,459**

Long lived assets	1999	1998
Italy	154,323	152,625
United States of America	48,016	41,843
	202,339	**194,468**

In addition, the Group also sells minor amounts of excess polyurethane foam and leather by-products, and realizes some royalty income which, for 1999, 1998 and 1997 totalled 76,854, 71,043 and 85,673, respectively.

No single customer accounted for more than 5% of net sales in 1999, 1998 or 1997.

22 Cost of sales

Cost of sales is analyzed as follows:

	1999	1998	1997
Opening inventories	106,546	114,724	90,450
Purchases	419,149	453,415	506,666
Labor	148,417	141,621	135,944
Third party manufacturers	47,557	53,184	62,695
Other manufacturing costs	33,152	35,426	35,204
Closing inventories	(103,206)	(106,546)	(114,724)
Total	**651,615**	**691,824**	**716,235**

23 Other income (expense), net

Other income (expense), net is analyzed as follows:

	1999	1998	1997
Interest income	11,335	14,041	13,358
Interest expense and bank commissions	(1,257)	(1,961)	(2,060)
Interest income, net	10,078	12,080	11,298
Gains (losses) on foreign exchange, net (a)	(24,463)	4,445	(1,201)
Provision for unrealized exchange losses on domestic currency swaps	(2,545)	(218)	(2,184)
Gains (losses) on foreign exchange	(27,008)	4,227	(3,385)
Gains (losses) on securities,net	(2,804)	249	1,807
Other, net (b)	(12,742)	4,254	2,598
Total	**(32,476)**	**20,810**	**12,318**

(a) The gains (losses) on foreign exchange are related to the following:

	1999	1998	1997
Realized gains (losses) on domestic currency swaps	(21,088)	418	(8,087)
Realized gains on accounts receivable and payables	5,786	1,893	7,589
Provision for unrealized gains (losses) on accounts receivable and payables	(9,161)	2,134	(703)
Total	**(24,463)**	**4,445**	**(1,201)**

(b) Other, net consists of the following:

	1999	1998	1997
Tax liabilities settlement	(18,190)	-	-
Employment incentive grants	1,457	1,128	370
Other	3,991	3,126	2,228
Total	**(12,742)**	**4,254**	**2,598**

Tax liabilities settlement

During 1998, the Italian tax authorities conducted an audit of the corporate income tax return and VAT declarations for the year ended December 31, 1992 – 1996, of a subsidiary enjoying full exemption from IRPEG and ILOR for the aforementioned years. As a result of the audit, the tax authorities concluded that a portion of the taxable income generated by this subsidiary was not eligible for exemption from ILOR and assessed taxes in the amount of Lit 23,0 billion (excluding penalties and interest, estimated to be approximately Lit 14,0 billion). On May 24, 1999, the tax authorities raised additional tax claims on the basis of even more restrictive interpretations of fiscal rules related to such tax exemption. As a consequence, based on the advice of tax counsel, the Company decided to settle the claims, including assessed taxes and penalties, raised by the tax authorities for all open matters with respect to fiscal years 1992 – 1996 for a payment of 18,190. As a result of such settlement, a cost of 18,190 has been charged to consolidated statement of earnings for the year ended December 31, 1999, and is included in other income (expense), net. The table below gives a further breakdown of the tax liabilities settlement:

Income taxes (Ilor)	14,408
VAT	599
Penalties	3,183
Total	**18,190**

Employment incentive grants

The Company and certain subsidiaries, on the basis of regional laws, received from the regional agencies employment incentives in the form of grants for new permanent employees and subsidies of up to 100% of the cost of training courses for permanent and temporary employees. The incentives received were related to prior years. For the years ended December 31, 1999, 1998 and 1997 these incentives amounted 1,457, 1,128 and 370, respectively.

24 Financial instruments and risk management

A significant portion of the Group's net sales, but only approximately 30% of its costs, are denominated in currencies other than the lira, in particular the U.S. dollar. The remaining costs of the Group are denominated principally in lire. Consequently, a significant portion of the Group's net revenues are exposed to fluctuations in the exchange rates between the lira and such other currencies. The Group uses forward exchange contracts (known in Italy as domestic currency swaps) to reduce its exposure to the risks of short-term declines in the value of its foreign currency-denominated revenues. The Group uses such domestic currency swaps to protect the value of its foreign-currency denominated revenues, and not for speculative or trading purposes.

The Group is exposed to credit risk in the event that the counter-parties to the domestic currency swaps fail to perform according to the terms of the contracts. The contract amounts of the domestic currency swaps described below do not represent amounts exchanged by the parties and, thus, are not a measure of the exposure of the Group through its use of those financial instruments. The amounts exchanged are calculated on the basis of the contract amounts and the terms of the financial instruments, which relate primarily to exchange rates. The immediate credit risk of the Group's domestic currency swaps is represented by the unrealized gains on the contracts. Management of the Group enters into contracts with creditworthy counter-parties and believes that the risk of material loss from such credit risk to be remote. The table below summarizes in Italian lire equivalent the contractual amounts of forward exchange contracts used to hedge principally future cash flows from accounts receivable and sales orders at December 31, 1999 and 1998:

	1999	1998
U.S. dollars	283,375	277,562
British pounds	36,810	35,516
Australian dollars	22,385	26,217
Canadian dollars	15,112	14,325
Japanese yen	9,130	8,364
Swiss francs	3,437	5,534
Greek dracma	1,162	-
German marks	-	22,253
French francs	-	7,442
Belgian francs	-	7,714
Dutch guilders	-	7,523
Total	**371,411**	**412,450**

At December 31, 1999, these forward exchange contracts had a net unrealized loss of 27,815, of which 14,230 related to and was included as a reduction in accounts receivable, 11,040 had not been recorded as it related to existing sales commitments and 2,545 had been accrued as a provision for unrealized foreign exchange losses in the balance sheet and charged to other income (expense), net in the statement of earnings, as it did not relate to existing commitments at year - end.

At December 31, 1998, the forward exchange contracts had a net unrealized gain of 15,406, of which 3,386, related to and was included as an increase in accounts receivable (3,159 in trade receivables and 227 in other receivables), 4,601 had not been recorded as it related to existing sales commitments, 7,637 was deferred as it did not relate to existing commitments at year-end and 218 was accrued as a provision for unrealized foreign exchange losses in the balance sheet and charged to other income (expense), net in the consolidated statement of earnings as it did not relate to existing commitments at year end.

The following table presents information regarding the contract amount in Italian lire equivalent amounts and the estimated fair value of all of the Group's forward exchange contracts. Contracts with unrealized gains are presented as ‘assets’ and contracts with unrealized losses are presented as ‘liabilities’.

	1999		1998	
	Contract amount	**Fair value**	**Contract amount**	**Fair value**
Assets	10,971	48	348,393	17,366
Liabilities	360,440	(27,863)	64,057	(1,960)
	371,411	**(27,815)**	**412,450**	**15,406**

25 Fair value of financial instruments

The following table summarizes the carrying value and the estimated fair value of the Group's other financial instruments:

	1999		1998	
	Carrying value	**Fair value**	**Carrying value**	**Fair value**
Assets:				
• Marketable securities	50	50	17,028	17,790
Liabilities:				
• Long-term debt	2,315	2,248	3,999	3,885

Cash and cash equivalents, receivables, payables and short-term borrowings approximate fair value because of the short maturity of these instruments.

Market value for quoted marketable debt securities is represented by the securities exchange prices at year-end. Market value for unquoted securities is represented by the prices of comparable securities, taking into consideration interest rates, duration and credit standing of the issuer.

Fair value of the long-term debt is estimated based on cash flows discounted using current rates available to the Company for borrowings with similar maturities.

The carrying value of forward exchange contracts is determined based on the unrealized loss and gain of such contracts recorded in the consolidated financial statements. Fair value of forward exchange contracts is determined by using exchange rates at year-end.

26 Application of generally accepted accounting principles in the United States of America

The established accounting policies followed in the preparation of the consolidated financial statements (Italian GAAP) vary in certain significant respects from those generally accepted in the United States of America (US GAAP).

Those differences which have a material effect on net earnings and/or shareholders' equity are as follows:

(a) Certain property, plant and equipment have been revalued in accordance with Italian laws. The revalued amounts are depreciated for Italian GAAP purposes. US GAAP does not allow for such revaluations, and depreciation is based on historical costs. The revaluation primarily relates to industrial buildings.

(b) In the application of US GAAP, the Group has classified its investment portfolio as securities available for sale, which are those securities that may be sold prior to maturity as part of asset and liability management or in response to other factors but are not trading securities. Such securities are carried at fair value, and any changes in fair value are recorded in a separate component of shareholders' equity, net of applicable deferred taxes. Under Italian GAAP, all current asset investments are stated at the lower of cost or market value on an individual security basis.

(c) Through December 31, 1998 the Group generally recognized net unrealized foreign exchange losses but deferred net unrealized foreign exchange gains until realized.

In connection with its hedging activities employing forward exchange contracts, net unrealized foreign exchange gains and losses are deferred as they relate to future sales for which commitments are received at the balance sheet date. The Company defines such commitments for Italian GAAP purposes as sales orders on hand and customers' indications of future purchases as of the balance sheet date which are confirmed by sales orders within a designated time period. Unrealized gains and losses on forward exchange contracts not designated to cover accounts receivable or future sales commitments are generally deferred in the case of net unrealized gains and recognized in earnings when resulting in a net unrealized losses. See notes 3 (a) and (b) for the Group's accounting policy.

Under US GAAP, generally both unrealized foreign exchange gains and losses from foreign currency transactions are recognized in the consolidated statement of earnings unless prescriptive hedging criteria are met. The Company's accounting policy for US GAAP purposes is that unrealized gains and losses on forward exchange contracts are deferred only for such contracts designated to cover firmly committed transactions supported by sales orders on hand. Accordingly, under US GAAP, unrealized gains and losses on forward exchange contracts designated to cover anticipated future sales which are not supported by sales orders on hand as of the balance sheet date are credited or charged to the consolidated statement of earnings.

(d) Government grants related to capital expenditures are recorded, net of tax, within reserves in shareholders' equity. For US GAAP purposes, such grants would be classified as a reduction of the cost of the related fixed asset or as a deferred credit and amortized to income over the estimated useful lives of the assets. The adjustments to net income represent the annual amortization of the capital grants based on the estimated useful life of the related fixed assets. The adjustments to shareholders' equity are to reverse the amounts of capital grants credited directly to equity for Italian GAAP purposes, net of the amounts of amortization of such grants for US GAAP purposes. In 1995 and 1997, the

Group received certain grants relating to fixed assets acquired between 1989 and 1997 with various useful lives. For US GAAP purposes, the Group is amortizing such grants over the remaining useful lives of the assets to which the grants relate.

(e) The Company does not record the compensation cost resulting from the granting of share options. For US GAAP purposes, this intrinsic value (resulting from the excess of the market price of the underlyng shares at the date of grant over the excercise price) is being recognized as compensation cost in the consolidated statement of earnings over the vesting period of the options. For US GAAP purposes, in 1999, 1998 and 1997 the Company recorded a charge of 307, 1,322 and 2,444, respectively, while the remaining unrecognized compensation of 127 will be charged in year 2000.

(f) Included in cash equivalents in 1998 is a deposit of 25,000 with an original maturity of six months. Under US GAAP, this deposit would be classified as a short-term investment and the purchase of this investment would be included within investing activities for purposes of the consolidated statement of cash flows. Subsequent sale on maturity of this deposit would also be classified within investing activities under US GAAP.

(g) Included in other income (expense), net in the consolidated statement of earnings for the year ended December 31, 1999 is the cost of a tax liability settlement (see note 23) as indicated below:

Income taxes (Ilor)	14,408
VAT	599
Penalties	3,183
Total	**18,190**

Under US GAAP, the cost of 14,408 would be classified as income taxes. As a consequence, "earnings before taxes and minority interest" and "income taxes" in the consolidated statement of earnings for the year ended December 31, 1999 would be Lit 213,716 and Lit 53,849, respectively.

The calculation of net earnings and shareholders' equity substantially in conformity with US GAAP is as follows:

Reconciliation of net earnings:

	1999	1998	1997
Net earnings under Italian GAAP	159,562	139,299	104,174
Adjustments to reported income:			
(a) Revaluation of property, plant and equipment	78	77	85
(b) Marketable debt securities	-	(76)	(477)
(c) Unrealized gains (losses) on foreign exchange	(12,789)	8,398	(7,213)
(d) Government grants	2,917	3,782	5,103
(e) Employee share option compensation	(307)	(1,322)	(2,444)
Effect of minority interests on US GAAP adjustments	(2)	(2)	(2)
Tax effect of US GAAP adjustments	4,262	(3,776)	2,872
Approximate net earnings in conformity with US GAAP	**153,721**	**146,380**	**102,098**
Basic earnings per share in conformity with US GAAP	**2,675**	**2,558**	**1,795**
Diluted earnings per share in conformity with US GAAP	**2,675**	**2,557**	**1,781**

Reconciliation of shareholders' equity:

	1999	1998
Shareholders' equity under Italian GAAP	732,173	657,128
(a) Revaluation of property, plant and equipment	(784)	(862)
(b) Marketable debt securities	-	762
(c) Unrealized gains (losses) on foreign exchange	(4,507)	8,282
(d) Government grants	(45,612)	(48,529)
Effect of minority interests on US GAAP adjustments	6	8
Tax effect of US GAAP adjustments	5,472	1,134
Approximate shareholders' equity in conformity with US GAAP	**686,748**	**617,923**

Accounting for Stock-Based Compensation

The Company has elected to continue to apply the provisions of Accounting Principles Board ('APB') Opinion No. 25, Accounting for Stock Issued to Employees, and provide the pro forma disclosure provisions of SFAS No. 123, Accounting for Stock-Based Compensation. The weighted-average fair value of each option granted by the Company during 1996 was estimated on the grant date at 62,500 using the Black-Scholes option pricing model with the following weighted-average assumptions: dividend yield of 0.6%; expected volatility of 25%; risk-free interest rate of 7.29%; and expected lives of 2.55 years. Had compensation cost for the Company's Plan, for US GAAP purposes, been determined consistent with SFAS No. 123, the Company's US GAAP net earnings and earnings per share for the years ended December 31, 1999, 1998 and 1997 would approximate the actual amounts presented in the reconciliation.

Comprehensive Income

The Company has adopted SFAS No. 130, Reporting Comprehensive Income, which established standards for the reporting and presentation of comprehensive income and its components in a full set of financial statements. Comprehensive income/(loss) generally encompasses all changes in shareholders' equity (except those arising from transactions with owners). The Company's comprehensive income differs from net income only by the amount of the exchange differences on translation of financial statements charged to shareholders' equity for the period. Comprehensive income and accumulated other comprehensive income for the years ended December 31, 1999, 1998 and 1997 were as follows:

	Comprehensive income	Accumulated other comprehensive income
Balance at December 31, 1996		**481**
Comprehensive income		
Net income	104,174	
Exchange difference on translation of financial statements	2,551	2,551
Total comprehensive income	**106,725**	
Balance at December 31, 1997		**3,032**
Comprehensive income		
Net income	139,299	
Exchange difference on translation of financial statements	(2,860)	(2,860)
Total comprehensive income	**136,439**	
Balance at December 31, 1998		**172**
Comprehensive income		
Net income	159,562	
Exchange difference on translation of financial statements	7,433	7,433
Total comprehensive income	**166,995**	
Balance at December 31, 1999		**7,605**

Accounting Standards Issued not yet adopted

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133 ('SFAS 133'), 'Accounting for Derivative Instruments and Hedging Activities'. This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as derivatives), and for hedging activities. It requires that an entity recognise all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This statement is effective for all fiscal quarters of fiscal years beginning after June 15, 2000. Management is currently assessing the effect of the adoption of SFAS 133.

Board of Directors *(At June 30, 2000)*

Pasquale Natuzzi	Chairman of the Board of Directors
Giuseppe Desantis	Vice Chairman of the Board of Directors
Giambattista Massaro	Director
Gianluca Monteleone	Director
Stelio Campanale	Director
Claudio Dematté	Outside Director
Pietro Gennaro	Outside Director
Giuseppe Russo Corvace	Outside Director
Cataldo Sferra	Outside Director
Enrico Vitali	Outside Director

Management *(At June 30, 2000)*

Pasquale Natuzzi	Chief Executive Officer
Giuseppe Desantis	Vice Chairman
Michele Bonerba	Human Resources Manager
Stelio Campanale	General Counsel
Giovanni Costantino	Research & Development and Industrialization Manager
Vito Dagostino	Purchasing Manager
Gaetano De Cataldo	Executive Vice President for Natuzzi Americas
Nicola Dell'Edera	Finance Manager
Gaetano Del Re	Production Engineering Manager
Michele D'Ercole	Manager of Leather and Dyeing Operations
Giuseppe Firrao	Communication Manager
Cesare Laberinti	Manager of Polyurethane Foam Operations
Nicola Lassandro	Manager of Management Information Systems
Stefano Lorizio	Production Manager
Dino Lorusso	President of Natuzzi Americas
Nicola Masotina	Sales Manager for Franchising in Italy
Giambattista Massaro	General Purchasing and Logistics Manager
Bruno Mele	Product Manager for Europe
Tommaso Melodia	Corporate Affairs Manager
Giovanni Mercadante	Accounting Manager
Ottavio Milano	Controller Manager
Gianluca Monteleone	Marketing Manager
Anna Maria Natuzzi	Product Development Manager
Annunziata Natuzzi	Internal Relations Manager
Vittorio Pilla	Sales and Marketing Manager for Europe
Giuseppe Stano	Sales Administration Manager
Vito Testini	Quality Manager
Giuseppe Trevissoi	Logistics Manager
Emanuele Valente	Transportation Manager

Board of Internal Auditors

Francesco Venturelli - President
Ferdinando Canaletti
Francesco Barletta

Independent Auditors

KPMG S.p.A.

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