NATUZZI S P A
Form 20-F
June 30, 2005

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) (g) OF THE SECURITIES EXCHANGE ACT OF 1934 or**

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Fiscal Year Ended: December 31, 2004

Or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Transition Period from to

1-11854
(Commission file number)

NATUZZI S.p.A.

(Exact name of Registrant as specified in its charter)

NATUZZI S.p.A.
(Translation of Registrant s name into English)
Italy
(Jurisdiction of incorporation or organization)
Via Iazzitiello 47, 70029 Santeramo , Italy
(Address of principal executive offices)

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

Name of each class	Name of each exchange on which registered
American Depositary Shares	**New York Stock Exchange**
Ordinary Shares with a par value of 1.0 each	**New York Stock Exchange***

Securities registered or to be registered pursuant to Section 12(g) of the Act: **None**

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Outstanding shares of each of the issuer s classes of capital or common stock as of December 31, 2004:

54,681,628 Ordinary Shares

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 the past 90 days.

Yes þ No o

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 þ

<u>* Not for trading, but only in connection with the registration of the American Depositary Shares</u>

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

Beginning with the fiscal year ended December 31, 2002, Natuzzi S.p.A. (the Company and, together with its consolidated subsidiaries, the Group) has published its audited consolidated financial statements (the Consolidated Financial Statements) in euro, the single currency established for certain members of the European Union (including Italy) upon the commencement of the third stage of the European Monetary Union (the EMU) on January 1, 1999. For fiscal years ending before December 31, 2002, the audited Consolidated Financial Statements were published in Italian lire, which was legal tender in Italy prior to March 1, 2002. All amounts in the Consolidated Financial Statements for each period prior to January 1, 2002 have been restated into euro amounts using the official lira-euro exchange rate as of January 1, 1999 (euro 1 is equal to lire 1,936.27).

In this annual report, references to or euro are to the euro; references to lira , lire or Lit. are to the Italian lira (singular) or to the Italian lire (plural); and references to U.S. dollars , dollars , U.S.$ or $ are to United States dollars.

Amounts stated in U.S. dollars, unless otherwise indicated, have been translated from the euro amount by converting the euro amounts into U.S. dollars at the noon buying rate in New York City for cable transfers in foreign currencies as certified for customs purposes by the Federal Reserve Bank of New York (the Noon Buying Rate) for euro on December 31, 2004 of U.S.$ 1.3538 per euro.

These foreign currency conversions in this annual report should not be taken as representations that the foreign currency amounts actually represent the equivalent U.S. dollar amounts or could be converted into U.S. dollars at the rates indicated.

The Consolidated Financial Statements included in Item 18 of this annual report are prepared in conformity with accounting principles established by, and (in the absence of such established principles and when applicable) accounting principles of the International Accounting Standards Committee adopted by, the Italian accounting profession (Italian GAAP). These principles vary in certain significant respects from generally accepted accounting principles in the United States (U.S. GAAP). See Note 27 to the Consolidated Financial Statements included in Item 18 of this annual report.

On June 7, 2002 the Company changed its name from Industrie Natuzzi S.p.A. to Natuzzi S.p.A.

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PART I

Item 1. Identity of Directors, Senior Management and Advisers

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

Selected Financial Data

The following table sets forth selected consolidated financial data for the periods indicated and is qualified by reference to, and should be read in conjunction with, the Consolidated Financial Statements and the notes thereto included in Item 18 of this annual report and the Operating and Financial Review and Prospects included in Item 5 of this annual report. The income statement and balance sheet data presented below have been derived from the Consolidated Financial Statements.

The Consolidated Financial Statements, from which the selected consolidated financial data set forth below has been derived, were prepared in accordance with Italian GAAP, which differ in certain respects from U.S. GAAP. For a discussion of the principal differences between Italian GAAP and U.S. GAAP as they relate to the Group s consolidated net earnings and shareholders equity, see Note 27 to the Consolidated Financial Statements included in Item 18 of this annual report.

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	Year Ended/At December 31,					
	2004	2004	2003	2002	2001	2000
	(millions of dollars, except per Ordinary Share and ADS amounts)(2)	(millions of euro, except for Ordinary Share and ADS amounts)(1)				
Income Statement Data:						
Amounts in accordance with Italian GAAP :						
Net sales:						
Leather- and fabric-upholstered furniture	$ 901.0	665.5	674.0	734.7	714.0	629.3
Other(3)	119.0	87.9	95.6	70.4	72.1	59.2
Total net sales	1,020.0	753.4	769.6	805.1	786.1	688.5
Cost of sales	(655.9)	(484.5)	(508.8)	(517.4)	(520.1)	(426.3)
Gross profit	364.1	268.9	260.8	287.7	266.0	262.2
Selling expenses	(254.8)	(188.2)	(179.3)	(145.4)	(134.8)	(109.0)
General and administrative expenses	(55.1)	(40.7)	(39.2)	(40.5)	(33.5)	(26.7)
Operating income	54.2	40.0	42.3	101.8	97.7	126.5
Other income (expense), net(4)	(5.3)	(3.9)	3.7	14.5	(0.2)	(21.8)
Earnings before taxes and minority interests	48.9	36.1	46.0	116.3	97.5	104.7
Income taxes	(23.9)	(17.6)	(8.5)	(25.0)	(21.9)	(25.5)
Earnings before minority interests	25.0	18.5	37.5	91.3	75.6	79.2
Minority interests	(0.1)	(0.1)	(0.2)	0.1		
Net earnings	24.9	18.4	37.3	91.4	75.6	79.2
Net earnings per Ordinary Share and ADS	0.46	0.34	0.68	1.67	1.37	1.39
Amounts in accordance with U.S. GAAP :						
Net earnings	25.5	18.8	38.0	92.0	71.1	81.7
Net earnings per Ordinary Share and ADS (basic and diluted)	$ 0.46	0.34	0.70	1.68	1.29	1.43
Cash dividend per Ordinary Share and ADS	$ 0.09	0.07	0.14	0.33	0.29	0.29
Weighted average number of Ordinary Shares and ADSs Outstanding	54,681,628	54,681,628	54,681,628	54,681,628	55,027,496	57,087,391

Balance Sheet Data :							
Amounts in accordance with Italian GAAP :							
Current assets	$	527.2	389.4	383.1	402.6	491.9	354.2
Non-current assets		384.2	283.8	309.3	271.9	224.9	151.7
Total assets		911.4	673.2	692.4	674.5	716.8	505.9
Current liabilities		178.0	131.5	125.2	128.7	252.5	114.0
Long-term debt		6.8	5.0	4.2	3.6	3.3	0.2
Minority interest		1.2	0.9	0.9	0.5	1.5	0.8
Shareholders equity		660.5	487.9	515.1	495.8	428.5	366.5
Amounts in accordance with U.S. GAAP :							
Shareholders equity	$	628.8	464.5	452.3	432.3	364.4	321.9

(1) All amounts in the Consolidated Financial Statements for the fiscal years ending before December 31, 2002 have been restated from lire to euro using the exchange rate of Lit. 1,936.27 per euro established in connection with the commencement of the third stage of the EMU. The Consolidated Financial Statements reported in euro depict the same trends as would have been presented if the Group had continued to present its financial statements in lire.

(2) Amounts are translated into U.S. dollars by converting the euro amounts into U.S. dollars at the Noon Buying Rate for euro on December 31, 2004 of U.S.$ 1.3538 per euro.

(3) Sales included under Other principally consist of sales of polyurethane foam, living room accessories and leather to third parties.

(4) Other income (expense), net is principally affected by gains and losses, as well as interest income and expenses, resulting from measures adopted by the Group in an effort to reduce its exposure to exchange rate risks. See Item 5, Operating and Financial Review and Prospects Results of Operations 2004 Compared to 2003 , Item 11, Quantitative and Qualitative Disclosures about Market Risk and Notes 3, 24 and 25 to the Consolidated Financial Statements included in Item 18 of this annual report.

Exchange Rates

Fluctuations in the exchange rates between the euro and the U.S. dollar will affect the U.S. dollar amounts received by owners of American Depositary Shares (ADSs) on conversion by the Depositary (as defined below) of dividends paid in euro on the Ordinary Shares represented by the ADSs.

In addition, most of the Group s costs are denominated in euro, while a substantial portion of its revenues is denominated in currencies other than the euro, including the U.S. dollar in particular. Accordingly, in order to protect the euro value of its foreign currency revenues, the Group engages in transactions designed to reduce its exposure to fluctuations in the exchange rate between the euro and such foreign currencies. See Item 5, Operating and Financial Review and Prospects Results of Operations 2004 Compared to 2003 and Item 11, Quantitative and Qualitative Disclosures about Market Risk .

The following table sets forth the Noon Buying Rate for the euro expressed in U.S. dollars per euro.

Year:	Average(1)	At Period End
2000	0.9207	0.9388
2001	0.8909	0.8901
2002	0.9495	1.0485
2003	1.1411	1.2597
2004	1.2478	1.3538
Month ending:	**High**	**Low**
December 31, 2004	1.3625	1.3224
January 31, 2005	1.3476	1.2954
February 28, 2005	1.3274	1.2773
March 31, 2005	1.3465	1.2877
April 30, 2005	1.3093	1.2819
May 31, 2005	1.2936	1.2349

(1) The average of the Noon Buying Rates for the relevant period, calculated using the average of the Noon Buying Rates on the last business day of each month during the period.

The effective Noon Buying Rate on June 24, 2005 was 1.2088.

Risk Factors

Investing in the Company s ADSs involves certain risks. You should carefully consider each of the following risks and all of the information included in this annual report.

Demand for furniture is cyclical and may fall in the future

Historically, the furniture industry has been cyclical, fluctuating with economic cycles, and sensitive to general economic conditions, housing starts, interest rate levels, credit availability and other factors that affect consumer spending habits. Due to the discretionary nature of most

furniture purchases and the fact that they often represent a significant expenditure to the average consumer, such purchases may be deferred during times of economic uncertainty.

In 2004, the Group derived 42.0% of its leather- and fabric-upholstered furniture net sales from the United States and the Americas, and 51.1% from Europe. A prolonged economic slowdown in the United States and Europe may have a material adverse effect on the Group s results of operations.

The Group operates principally in a niche area of the furniture market

The Group is a leader in the production of leather-upholstered furniture, with 82.3% of net sales of upholstered furniture in 2004 being derived from the sale of leather-upholstered furniture. Leather-upholstered furniture represents a limited, but growing, portion of the market for upholstered furniture. Consumers have the choice of purchasing upholstered furniture in a wide variety of styles, and consumer preference may change. There can be no assurance that the current market for leather-upholstered furniture will not decrease.

The furniture market is highly competitive

The furniture industry is highly competitive and includes a large number of manufacturers. Competition has increased significantly over the past few years as companies manufacturing in countries with lower manufacturing costs have begun to play an important role in the upholstery industry. No single company has a dominant position in the industry. Competition is generally based on product quality, brand name recognition, price and service.

The Group s principal competitors are other manufacturers of upholstered furniture. In the United States, the Group competes with a number of relatively large companies, some of which are larger than the Group. Other competitors focused on the promotional or lower-priced segment of the market are located in countries, such as China or countries in Eastern Europe or South America, with lower manufacturing costs. The upholstered furniture market in Europe is highly fragmented.

The Group s results are subject to exchange rate risks and other risks related to the Group s international operations

The Group is subject to currency exchange rate risk in the ordinary course of its business to the extent that its costs are denominated in currencies other than those in which it earns revenues. Exchange rate fluctuations also affect the Group s operating results because it recognizes revenues and costs in currencies other than euro but publishes its financial statements in euro. The Group s sales and results may be materially affected by exchange rate fluctuations. For more information, see Item 11, Quantitative and Qualitative Disclosures about Market Risk.

The Group faces other risks relating to its international operations, including changes in governmental regulations, tariffs or taxes and other trade barriers, price, wage and exchange controls, political, social and economic stability, inflation and interest rate fluctuations.

The price of the Group s principal raw material is difficult to predict

Leather is used in approximately 76% of the Group s upholstered furniture production, and the acquisition of cattle hides represents approximately 35% of total cost of goods sold. The raw hides market s dynamics are dependent on the consumption of beef, the levels of worldwide slaughtering, worldwide weather conditions and on different sectors levels of demand: shoe manufacturers, leather automotive, furniture and clothing. The Group s ability to increase product

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prices following increases in raw material costs is limited by market forces, and therefore the Group may not be able to maintain its margins during periods of significant increases in raw material costs.

The Group s past results and operations have significantly benefited from government incentive programs which may not be available in the future

Historically, the Group has derived significant benefits from the Italian Government s investment incentive programs for under-industrialized regions in Southern Italy, including tax benefits, subsidized loans and capital grants. See Item 4, Information on the Company Incentive Programs and Tax Benefits. The Italian Parliament has replaced these incentive programs with a new investment incentive program for all under-industrialized regions in Italy, which is currently being implemented through grants, research and development benefits and tax credits. There can be no assurance that the Group will continue to be eligible for such grants, benefits or tax credits for its current or future investments in Italy.

In recent years, the Group has opened manufacturing operations in China, Brazil and Romania that have been granted with tax benefits and export incentives. There can be no assurance that these tax benefits and export incentives will continue to be available to the Group in the future.

The Group is dependent on qualified personnel

The Group s ability to maintain its competitive position will depend to some degree upon its ability to continue to attract and maintain highly qualified managerial, manufacturing and sales and marketing personnel. There can be no assurance that the Group will be able to continue to recruit and retain such personnel. In particular, the Group has been dependent on certain key management personnel in the past, and there can be no assurance that the loss of key personnel would not have a material adverse effect on the Group s results of operations.

Control of the Company

Mr. Pasquale Natuzzi, who founded the Company and is currently Chairman of the Board of Directors and Chief Executive Officer, owns 47.7% of the issued and outstanding Ordinary Shares of the Company (52.8% of the Ordinary Shares if the Ordinary Shares owned by members of Mr. Natuzzi s immediate family (the Natuzzi Family) are aggregated) and controls the Company, including its management and the selection of its Board of Directors. Since December 16, 2003, Mr. Natuzzi has held his entire beneficial ownership of Natuzzi S.p.A. shares (other than 196 ADSs) through INVEST 2003 S.r.l., an Italian holding company (having its registered office at Via Gobetti 8, Taranto, Italy) wholly-owned by Mr. Natuzzi.

In addition, the Natuzzi Family has a right of first refusal to purchase all the rights, warrants or other instruments which The Bank of New York, as Depositary under the Deposit Agreement dated as of May 15, 1993, as amended and restated as of December 31, 2001 (the Deposit Agreement), among the Company, The Bank of New York, as Depositary (the Depositary), and owners and beneficial owners of American Depositary Receipts (ADRs), determines may not lawfully or feasibly be made available to owners of ADSs in connection with each rights offering, if any, made to holders of Ordinary Shares.

Investors may face difficulties in protecting their rights as shareholders or holders of ADSs.

The Company is incorporated under the laws of the Republic of Italy. As a result, the rights and obligations of its shareholders and certain rights and obligations of holders of its ADSs are governed by Italian law and the Company s *Statuto* (or By-laws). These rights and obligations

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are different from those that apply to U.S. corporations. Furthermore, under Italian law, holders of ADSs have no right to vote the shares underlying their ADSs, although under the Deposit Agreement, ADS holders have the right to give instructions to The Bank of New York, the ADS depositary, as to how they wish such shares to be voted. For these reasons, the Company s ADS holders may find it more difficult to protect their interests against actions of the Company s management, board of directors or shareholders than they would as shareholders of a corporation incorporated in the United States.

Forward Looking Information

Natuzzi makes forward-looking statements in this annual report. Statements that are not historical facts, including statements about the Group s beliefs and expectations, are forward-looking statements. Words such as believe , expect , intend , plan and anticipate and similar expressions are intended to identify forward-looking statements but are not exclusive means of identifying such statements. These statements are based on current plans, estimates and projections, and therefore readers should not place undue reliance on them. Forward-looking statements speak only as of the dates they were made, and the Company undertakes no obligation to update or revise any of them, whether as a result of new information, future events or otherwise.

Forward-looking statements involve inherent risks and uncertainties. The Company cautions readers that a number of important factors could cause actual results to differ materially from those contained in any forward-looking statement. Such factors include, but are not limited to: effects on the Group from competition with other furniture producers, material changes in consumer demand or preferences, significant economic developments in the Group s primary markets, significant changes in labor, material and other costs affecting the construction of new plants, significant changes in the costs of principal raw materials, significant exchange rate movements or changes in the Group s legal and regulatory environment, including developments related to the Italian Government s investment incentive or similar programs. Natuzzi cautions readers that the foregoing lists of important factors are not exhaustive. When relying on forward-looking statements to make decisions with respect to the Company, investors and others should carefully consider the foregoing factors and other uncertainties and events.

Item 4. Information on the Company

Introduction

The Group is primarily engaged in the design, manufacture and marketing of contemporary and traditional leather- and fabric-upholstered furniture, principally sofas, loveseats, armchairs, sectional furniture, motion furniture and sofa beds, and living room accessories. The Group has positioned its products principally in the medium price range and emphasizes value, quality, style, variety and service

The Group is the world s leader in the production of leather-upholstered furniture and has a leading share of the market for leather-upholstered furniture in the United States and Europe (as reported by CSIL (CSIL), an Italian market research firm, with reference to market information related to the year 2004). In 2000, the Company launched Italsofa , a new promotional brand aimed at the lower-priced segment of the upholstery market, while in January 2002, the Company introduced the new logo for the Natuzzi brand, which is aimed at identifying the Company s medium to high end of the market products. The Group currently designs 100% of its products and manufactures, directly or through third parties, approximately 65% of its products in Italy. Production outside of Italy is solely for the Italsofa brand. Within Italy, the Group sells its

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furniture principally through franchised Divani & Divani by Natuzzi furniture stores. As at April 30, 2005, 138 Divani & Divani by Natuzzi stores were located in Italy. Outside of Italy, the Group sells its furniture principally on a wholesale basis to major retailers and also through 128 Natuzzi and Divani & Divani by Natuzzi stores. The Group also sells furniture through six Kingdom of Leather stores, which it purchased in 2003.

On June 7, 2002 the Company changed its name from Industrie Natuzzi S.p.A. to Natuzzi S.p.A. The Company, which operates under the trademark Natuzzi , is a *società per azioni* (stock company) organized under the laws of the Republic of Italy and was established in 1959 by Mr. Pasquale Natuzzi, who is currently Chairman of the Board of Directors, Chief Executive Officer and controlling shareholder of the Company. Substantially all of the Company s operations are carried out through various subsidiaries that individually conduct a specialized activity, such as leather processing, foam production and shaping, furniture manufacturing, marketing or administration.

In an effort to maximize the efficiency of the Group s organizational structure, at an extraordinary general meeting on November 21, 2003, the Company s shareholders approved the merger of Style & Comfort S.r.l into the Company (the Company owned 100% of the capital stock of Style & Comfort S.r.l. prior to the merger). The merger became effective on January 1, 2004.

The Company s principal executive offices are located at Via Iazzitiello 47, 70029 Santeramo, Italy, which is approximately 25 miles from Bari, in Southern Italy. The Company s telephone number is: +39 080 8820-111. The Company s distribution subsidiary in the United States is Natuzzi Americas, Inc. (Natuzzi Americas), located at 130 West Commerce Avenue, High Point, North Carolina 27260 (telephone number +1 336 888-0351).

Organizational Structure

As at April 30, 2005, the Company s principal operating subsidiaries are:

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Name	Percentage of ownership	Registered office	Activity
Italsofa Bahia Ltda	97.99	Bahia, Brazil	(1)
Italsofa (Shanghai) Co., Ltd	100.00	Shanghai, China	(1)
SC Italsofa Romania S.r.l.	100.00	Baia Mare, Romania	(1)
Minuano Nordeste S.A.	100.00	Pojuca, Brazil	(1)
Softaly Shanghai, Ltd	100.00	Shanghai, China	(1)
Natco S.p.A.	99.99	Bari, Italy	(2)
I.M.P.E. S.p.A.	90.83	Qualiano, Italy	(3)
Divani Due S.r.l.	100.00	Verona, Italy	(4)
Natuzzi Americas, Inc.	100.00	High Point, NC, U.S.A.	(4)
Natuzzi Ibérica S.A.	100.00	Madrid, Spain	(4)
Natuzzi (Switzerland) AG	97.00	Dietikon, Switzerland	(4)
Natuzzi Nordic ApS	100.00	Copenhagen, Denmark	(4)
Natuzzi Benelux NV	100.00	Geel, Belgium	(4)
Natuzzi Germany GmbH	100.00	Düsseldorf, Germany	(4)
Kingdom of Leather Limited	100.00	London, U.K.	(4)
La Galleria, Ltd	100.00	London, U.K.	(4)
Nacon S.p.A.	100.00	Bari, Italy	(5)
Italholding S.r.l.	100.00	Bari, Italy	(5)
Natuzzi Netherlands Holding B.V.	100.00	Amsterdam, Holland	(5)
Natuzzi United Kingdom, Limited	100.00	London, U.K.	(5)
Natuzzi Trade Service S.r.l	100.00	Bari, Italy	(6)
Kingdom of Leather Trustees Limited	100.00	London, U.K.	(7)
Natuzzi Asia, Ltd	100.00	Hong Kong, China	(7)

(1) Manufacture and distribution

(2) Intragroup leather dyeing and finishing

(3) Production and distribution of polyurethane foam

(4) Distribution

(5) Investment holding

(6) Transportation Services

(7) Non-operative

See Note 1 to the Consolidated Financial Statements for further information on the Company s subsidiaries.

Strategy

The Group s primary objective is to expand and strengthen its presence in the global upholstered furniture market in terms of sales and production, while at the same time increasing the Group s profit. To achieve these objectives, the Group s principle strategic objectives include:

Geographical expansion. The Group first targeted the United States market in 1983 and subsequently began diversifying its geographic markets, particularly in the highly fragmented European markets (outside of Italy). According to the most recent data available referring to year 2004 (source CSIL, an Italian market research firm), the Group is the leader in the leather-upholstered furniture segment in the United States, with a 9.6% market share, and in Europe, with 8.5%. The Group continues to focus on sales and to expand its retail presence outside of its core markets.

Product diversification. The Group has taken a number of steps to broaden its product lines, including the development of new models, such as motion furniture, and the introduction of new materials and colors, including select fabrics and microfibers. See Manufacturing Raw Materials The Group also strives to expand and add value to its product offerings through its Decorator concept, which provides customers with total look room package solutions. See Products and Design Products. The Group believes that this approach will also strengthen its relationships with the world s leading distribution chains, which are interested in offering branded propositions. The Group has invested in Natuzzi Syle Centers in Sateramo and Milan to serve as a creative hub for the Group s design activities.

Expansion in all price segments. The Group is expanding in all price segments of the leather and non-leather upholstered furniture market. The Italsofa lower-priced brand, launched in October 2000, competes in the lower end of the upholstered furniture market and represented about 35% of total seats sold by the Group in 2004. Faced with increased competition in this price range, the Group has increased its production capacity and efficiency by investing in production facilities in Brazil, China and Romania, while continuing to emphasize the style and quality associated with the Natuzzi brand. The Pasquale Natuzzi Collection competes in the higher end of the upholstered furniture market and offers customers products that are of the highest quality and distinctive in terms of design, materials and project development.

Retail program and brand development. The Group has made significant investments to improve its existing distribution network and strengthen its brand, primarily through the establishment of new distribution subsidiaries and the increase of the number of Natuzzi stores and Natuzzi Galleries worldwide. As of April 30, 2005, there were 272 Natuzzi stores worldwide, including Divani and Divani by Natuzzi stores, Kingdom of Leather stores, and one La Galleria store. The Natuzzi Galleries program was launched in 2002 and the number of galleries worldwide reached 541 as at April 30, 2005. By using the same creative concepts and internal decorations in Natuzzi stores and Natuzzi Galleries, the Group has created a coherent identity for the Natuzzi brand. The Group plans to open additional stores and Natuzzi Galleries in strategic geographical locations and is committed to making the marketing investments necessary to increase brand recognition in these markets.

Improving efficiency and reducing operating costs. Due to persisting unfavorable currency conditions, pricing pressure in the U.S. and general economic conditions that have negatively affected order flows for our Natuzzi-branded products, and in consideration of the ongoing efforts of the Group to become more efficient and competitive, on May 18, 2005, the Board approved a restructuring plan. The restructuring plan includes a temporary work force reduction (cassa integrazione) of 1,320 positions, by the end of 2005, in all departments across the Group, with a focus on reducing manufacturing costs in Italy, increasing overall efficiencies and improving productivity.

Manufacturing

As at April 30, 2005, the Group manufactured its products in 12 production facilities located in Italy. Nine of the facilities are engaged in the cutting, sewing and assembling of semi-finished and finished products and employ 2,941 workers, 34.0% of which are not directly involved in production. Ten of these assembly facilities are located in or within a 25 mile radius of Santeramo, where the Company has its headquarters.

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The assembly operations conducted in the Group s facilities involve stretching elastic webbing onto the furniture s frames (which are constructed either at the Group s principal assembly facility or by subcontractors), attaching foam to the frames, and cutting and sewing the upholstery and attaching it to the frames. These operations, which retain many characteristics of production by hand, are coordinated at the Group s principal assembly facilities through the use of the management information system, which identifies by number each component of a piece of furniture *e.g.*, frame, cushions, leather and facilitates its automated transit and storage within the factory, in part through a bar-coded bin and pick system. As part of an effort to decrease costs through increased productivity and flexibility, automatic guided vehicles supervised by a central computer have been installed at one of the Group s principal assembly facilities to move products through the production chain. In other facilities, materials are currently moved by hand or conveyor belt, rather than on an automated basis. Operations at all of the Group s production facilities are normally conducted Monday through Friday with two eight-hour shifts per day.

Two of the Group s production facilities are involved in the processing of leather hides to be used as upholstery. One of the facilities is a leather dyeing and finishing plant located near Udine that employed 306 workers as at April 30, 2005. The Udine facility receives both raw and tanned cattle hides, sends raw cattle hides to subcontractors for tanning, and then dyes and finishes the hides. The other facility, located near Vicenza, is a warehouse that receives semi-finished hides and sends them to various subcontractors (who operate under the supervision of Natuzzi technicians) for processing, drying and finishing, and then arranges for the finished leather to be shipped to the Group s assembly facilities. The Vicenza operation employed 28 workers as at April 30, 2005. Hides are tanned, dyed and finished on the basis of orders given by the Group s central office in accordance with the Group s on demand planning system, as well as on the basis of estimates of future requirements. The movement of hides through the various stages of processing is monitored through the management information system. See Supply-Chain Management .

The Group produces, directly and by subcontracting, 10 grades of leather in approximately 40 finishes and 274 colors. The hides, after being tanned, are split and shaved to obtain uniform thickness and separated into top grain and split (top grain leather is used, in varying quantities, in the manufacture of all Natuzzi-branded leather products, while split leather is used in addition to top grain leather in some of the Group s lower priced products). The hides are then colored with dyes and treated with fat liquors to soften and smooth the leather, after which they are dried. Finally, the semi-processed hides are treated to improve the appearance and strength of the leather and to provide the desired finish. The Group also purchases finished hides from third parties.

One of the Group s production facilities, which is located near Naples and, as at April 30, 2005, employed 61 workers, is engaged in the production of flexible polyurethane foam and, because the facility s production capacity is in excess of the Group s needs, also usually sells foam to third parties. The foam produced at the Naples facility pursuant to a patented process results in a high-quality material without using any auxiliary blowing agent and is sold under the Eco-Flex™ trade name. A material specially designed for mattresses is also produced and sold under the Greenflex™ trade name.

The Group owns the land and buildings for its principal assembly facilities located in Santeramo, Matera and Altamura, its leather dyeing and finishing facility located near Udine, its foam-production facility located near Naples and its facilities located in Ginosa, Laterza, Brazil, Romania and the new plant in China (for the use of which the land is franchised by the Government for 50 years), while the land and buildings of the remaining production facilities are leased from lessors, with several of whom the Group enjoys long-term relationships. Although the lease terms are of varying lengths, Italian law provides that any such lease must have a minimum term of six years. This minimum term, however, is enforceable only by the lessee. The lease agreements provide for rents that generally increase each year in line with inflation. Management believes that the prospects are good for renewing the agreements on acceptable terms when they expire. The Group owns substantially all the equipment used in its facilities.

In 2000, the Group announced the launch of a new, lower-priced upholstered furniture collection, known as Italsofa. The Group currently manufactures the Italsofa Collection outside Italy at plants located in Brazil, China and Romania; if orders exceed production capacity at these other plants, Italsofa products are also manufactured in the Company s Italian plants.

Historically, the Group has entrusted some of its production work relating to the assembly of finished products from raw materials and finished parts to subcontractors located within a 20-mile radius of Santeramo (about 20% of Natuzzi s production as at December 31, 2004). The Group s contracts with these subcontractors provide that the Group will supply to each subcontractor product designs, finished leather, pre-cut cushions, wooden frames and other assembly materials. The subcontractors are required to assemble these materials into finished products under the supervision of the Group s technicians, who are responsible for quality control. The furniture is assembled at a fixed cost per unit that is set to increase annually in line with inflation. These contracts have an indefinite term, subject to termination by either party with prior notice (generally two months). The Group recently sent a notice of termination to all of these subcontractors. The Group s decision to terminate these contracts is a result of the reduction in orders for Natuzzi-branded products. All such contracts are expected to be terminated by the end of September 2005.

Raw Materials. The principal raw materials used in the manufacture of the Group s products are cattle hides, polyurethane foam, polyester fiber, wood and wood products.

The Group purchases hides from slaughterhouses and tanneries located mainly in Italy, Brazil, Colombia, Australia, Germany, Uruguay, Scandinavian countries, the United States, and Eastern Europe. The hides purchased by the Group are divided into several categories, with hides in the lowest categories being purchased mainly in Brazil, Colombia, and Ukraine; those in the middle categories being purchased mainly in Australia, Uruguay, Italy and the United States and those in the highest categories being purchased in Germany and Scandinavian countries. A significant number of hides in the lowest categories are purchased at the wet blue stage *i.e.*, after tanning while some hides purchased in the middle and highest categories are unprocessed. The Group has implemented a leather purchasing policy according to which a percentage of leather is purchased at a finished or semi-finished stage. Therefore, the Group has had a smaller inventory of split leather to sell to third parties. Approximately 80% of the Group s hides are purchased from 20 suppliers, with whom the Group enjoys long-term and stable relationships. Hides are generally purchased from the suppliers pursuant to orders given every one/two months specifying the number of hides, the purchase price and the delivery date.

Hides purchased from Europe are delivered directly by the suppliers to the Group s leather facilities near Udine and Vicenza, while those purchased overseas are inspected overseas by technicians of the Group, delivered to an Italian port and then sent by the Group to the Udine facility and subcontractors. Management believes that the Group is able to purchase leather hides from its suppliers at reasonable prices as a result of the volume of its orders, and that alternative sources of supply of hides in any category could be found quickly at an acceptable cost if the supply of hides in such category from one or several of the Group s current suppliers ceased to be available or was no longer available on acceptable terms. The supply of raw cattle hides is principally dependent upon the consumption of beef, rather than on the demand for leather.

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During 2004, notwithstanding the unstable market for cattle hides, the price paid by the Group decreased slightly due to the Group s purchasing policy, which is focused on finding quality hides in easily-accessible markets and aimed at establishing strong relationships with suppliers. The factors influencing availability and prices of leather in recent periods were, besides the uncertain worldwide economic trend, a reduction in red meat consumption and the exchange rate of the currencies in the markets where we operate. The Group believes that these same conditions will continue to influence price of cattle hides in 2005. During 2004 and the first quarter of 2005, worldwide levels of red meat consumption have been mostly flat (source: United States Department of Agriculture).

The Group also purchases fibers and microfibers for use in coverings. Both kinds of coverings are divided into several price categories: most fabrics are in the highest price categories, while the most inexpensive of the microfibers are in the lowest price categories. Fabrics are purchased exclusively in Italy from six suppliers who provide the product at the finished stage. Microfibers are purchased in Italy, South Korea, Taiwan and Japan from four suppliers who provide them at the finished stage. Microfibers purchased from the Group s Italian supplier are in some cases imported by the supplier at the greige or semi-finished stage and then finished (dyed and bonded) in Italy. The microfibers purchased from the Group s Japanese supplier are the only microfibers the Group purchases in the highest price category. Fabrics and microfibers are generally purchased from the suppliers pursuant to orders given every week specifying the quantity (in linear meters) and the delivery date. The price is determined before the fiber or microfiber is introduced into the collection.

Fabrics and microfibers purchased by the Italian suppliers are delivered directly by the suppliers to the Group s facility in Matera, while those purchased overseas are delivered to an Italian port and then sent to the Matera facility. Only fabrics and microfibers purchased in Taiwan and South Korea are delivered directly by the suppliers to Chinese and Brazilian ports and then sent to the Shanghai, Salvador de Bahia and Pojuca facilities. The Group is able to purchase such products at reasonable prices as a result of the volume of its orders. The Group continuously searches for alternative supply sources in order to obtain always the best product at the best price.

Price performance of fabrics is quite different from that of microfibers. Because fabrics are purchased exclusively in Italy and are composed of natural fibers, their prices are influenced by the cost of labor and the quality of the product. During 2004, fabric prices went unchanged, due to long-term relationships with suppliers and the large volumes purchased by the Group, despite the increases in the cost of raw materials and oil. Microfiber prices have decreased due to the introduction of new suppliers and the renegotiation of prices with current suppliers. The price of microfibers is mainly influenced by the international availability of high-quality products and raw materials at low costs especially from Asian markets.

The Group obtains the chemicals required for the production of polyurethane foam from major chemical companies located in Europe (including Germany, Italy and the United Kingdom) and the polyester fiber filling for its polyester fiber-filled cushions from several suppliers, located mainly in Korea, China and Taiwan. The chemical components of polyurethane foam are petroleum-based commodities, and the prices for such components are therefore subject to, among other things, fluctuations in the price of crude oil. The Group obtains wood and wood products for its wooden frames from suppliers in Italy and Eastern Europe and through its plants located in Romania, the Group began directly engaging in the cutting and transformation of wood from Romanian forests.

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With regard to the Group s collection of home furnishing accessories (tables, lamps, carpets, home accessories in different materials), most of the suppliers are located in Italy and other European countries, while some hand-made products (such as carpets) are made in India.

Supply-chain Management

Organization. In order to speed up the processing of information and material, the Group has set up a new organization. Starting in June 2004, all functions of the supply chain have been aggregated in the HQ Logistics Department according to modern models of Supply Chain Organizations. This type of organization assures that information and material flows are organized, synchronized and efficient, and consequently improves customer service as well.

Planning (order management, production, procurement). The Group schedules its