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THE QUARTO GROUP, INC.

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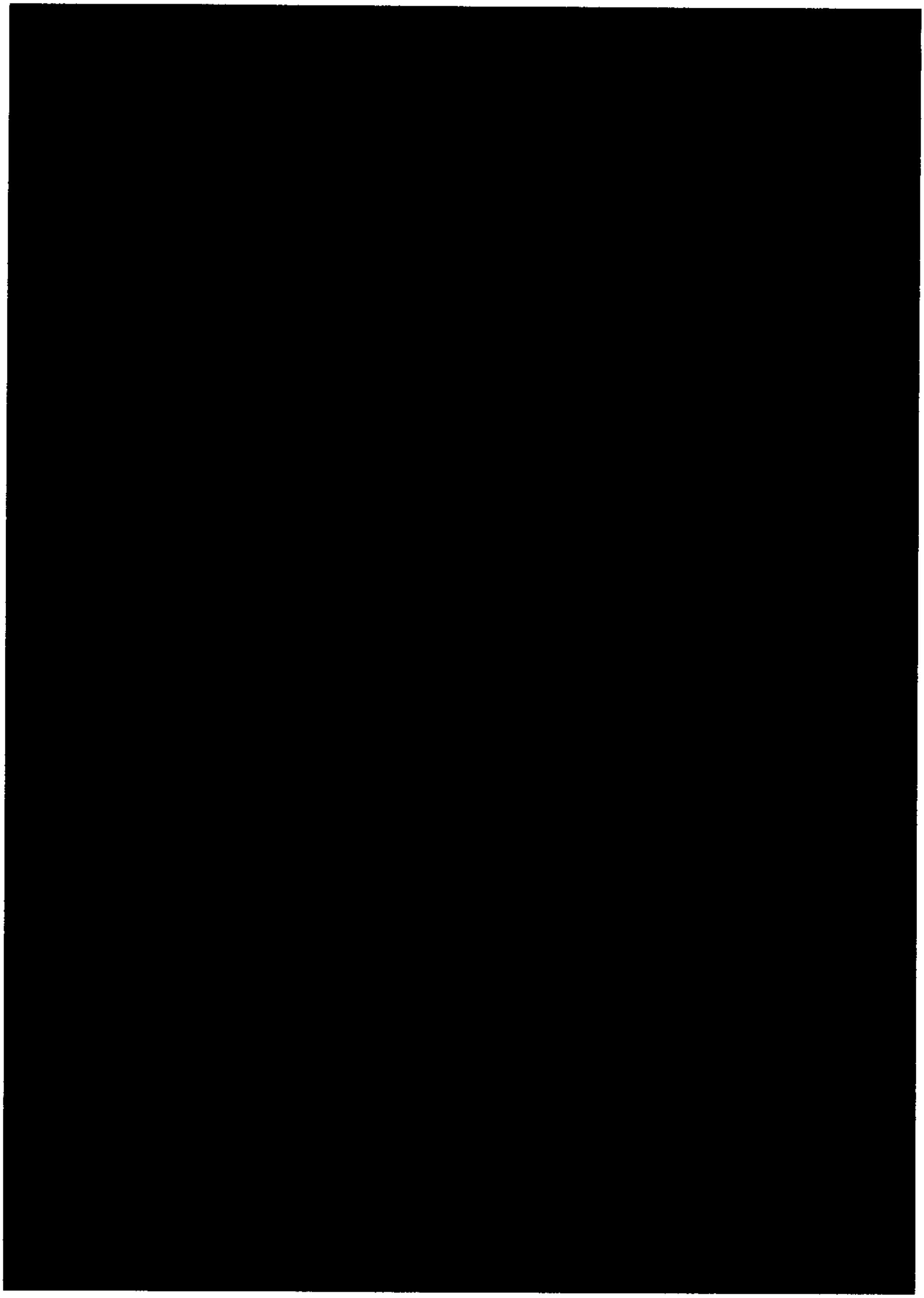
FLOWER PAINTING TECHNIQUES
Simply Pottery
COMO VER Y PINTAR el tiempo
TÉCNICAS DE CERÁMICA



CHAIRMAN'S LETTER

At the time we released our interim statement in September, I wrote that there were tangible signs of improvement in our business. I am pleased now to report that, for the year ended 31st December 1999, sales were up by 2.5% to £76.5 million (1998: £74.6 million), pre-tax profit was 48.9% higher and, at £4.11 million (1998: £2.76 million), was ahead of market expectations. Overall operating margins improved to 7.6%, compared with 6.3% in 1998. This translated into a 23.5% increase in operating profit to £5.83 million (1998: £4.72 million). The accounting policy changes that were announced earlier have reduced our tax bill. The improved trading results and the reduced tax charge led to a more than threefold surge in headline earnings per share to 15.8p (1998: 4.9p).

All these figures exclude the US directory publisher, Broughton Hall, whose operations were discontinued in November 1998. In the 1999 interim results we recorded an exceptional charge of £5.23 million for Broughton Hall, which included a goodwill write-back of £4.94 million that affected neither net assets nor cash. For comparative purposes, the 1998 figures exclude the results of Broughton Hall and have been re-stated to reflect the accounting policy changes introduced during the current year.

During the year, we worked assiduously to reduce our external debt and improve our working capital management. By the end of the year, debt had declined by a net £2.9 million, working capital as a percentage of sales fell by 4%, and overheads were down by 1%. The new accounting policy changes helped us to sharpen the focus of our publishing programmes. This has resulted in a much better return on new titles. They also helped our list publishers to focus on producing improved ranges of books: a virtuous combination that augurs well for the future.

Pre-tax profit was up by 48.9%, and ahead of market expectations. Operating profit increased by 23.5%. *Improved trading and our reduced tax charge led to a threefold surge in headline earnings per share.*

No medium has ever died. People still use pen and ink; newspapers flourish; movies survived the onset of television; books are big business.

DIVIDENDS

The Board is recommending an unchanged final dividend per share of 2.3p, making a total for the year of 4.5p (1998: 4.5p): if approved at the Annual General Meeting on May 3rd 2000, the dividend will be paid on May 5th 2000 to shareholders on the register at the close of business on April 7th 2000.

THE INTERNET

Rather as with the railroads, the telephone, and other transportation and communication industries of the past, the Internet is having a transforming and revolutionary impact on business.

Most of Quarto's commercial activities are business to business. We have no measurable public "face" and sell our products to other publishers and distributors. For some years we have recognised that there is a market for our material in a number of digitised and electronic outlets. Quarto, unlike most book publishers, has always had a policy of owning, rather than licensing, most of the content in our books. This, coupled with the fact that our archive is, in this respect, much vaster than most other publishers, puts us in a very strong position to benefit from the growth of e-commerce. Many investors have not appreciated that very few book publishers "own" what they publish: they are merely licensed by authors to exploit the content in book form. In this respect, Quarto is very different and our content archive is potentially very valuable.

Quarto is already exploiting this archive, and is deriving useful additional revenue at very low cost. At this stage, we have taken the view that to digitise older portions of our archive would not be cost-effective; rather we are happy to license it to other merchants, for a fee, for them to digitise it at their expense. We have established iQu-digital.com as a vehicle to coordinate the exploitation and licensing of this valuable asset.

A few words of caution: the history of media businesses is instructive (and is probably paralleled in other industries). First, no medium has ever died. People still use pen and ink; books are big business; newspapers flourish; movies survived the onset of television, etc., prophets of doom notwithstanding. Media may change, may need to adapt, and may go, in the aggregate, ex-growth, but they don't disappear or die. Second, media businesses have been hopeless (again, this may be paralleled in other industries) at insinuating themselves into new media, with a very few notable exceptions. The skill sets and the business model differ radically, even if there is the appetite to sustain huge start-up losses. The only real successes that I can think of are ones in which the old media business is still entrepreneurially run.

PROSPECTS

After two years of relative disappointment in 1997 and 1998, we see a bright future ahead. We have largely concluded the extensive strategic and operational reviews we commenced at the beginning of 1999. Some of the early benefits of this programme are reflected in these results. We expect that further progress from these initiatives will materialise in the current year. Our major markets remain buoyant, the calibre of our publishing programmes has risen, and we have a stronger overall management team. We have further remedial work to complete in our art publishing business, but have a clear strategy for improvement here. Elsewhere, our new initiatives, in particular Global Publishing, have made an encouraging start. I am confident that we shall continue the improving trend in 2000 and thank our staff, suppliers, and customers for their good work in 1999.

I also want to take this opportunity to record my personal thanks to Stan Patey and Mike Tout. Stan was the founder of Rockport. He retired in June. We have become good friends, so I shall continue to enjoy his company and his good humour. Sadly Mike Tout is no longer with us. A former Quarto employee, he went on to co-found Design Eye, now a member of the Group. His untimely death last year still shocks and his absence leaves a void.

Laurence F Orbach
Chairman & Chief Executive
February 22nd 2000

WHAT IS OUR BUSINESS?

Quarto's business is the creation of illustrated content that is produced for defined consumer segments. Quarto's publishing is very different from high-profile consumer book publishing, centred around well known authors, heavily promoted titles, and the whole razzmatazz of book launches, author tours, and loud publicity. This very visible publishing activity is typical only of the apex of the enormous publishing pyramid.

In 1999 in the UK alone, over 110,000 titles were published; of these, only a tiny number ever featured on best-seller lists. This experience is echoed in all major publishing markets. The major part of publishing output is directed at more enduring special interest areas and audiences. It is here that you will find Quarto books in abundance.

We are different, too, because the greater part of our content is produced for other publishers. In current jargon, we are the business-to-business part of the publishing world, the publisher's publisher. As in the film industry, where the big studios feed off the directors who create and bring life to the raw subject material, so in the book business the large houses rely upon the licences they acquire from agents, authors, and co-edition publishers such as Quarto. Unlike the movie business, which may produce a few thousand films a year, publishing is far more content-rich, and output is measured in the many hundreds of thousands. But analogies only illustrate, they do not prescribe, and they cannot be stretched too far. Unlike film directors, Quarto

HEADLINE

SIMON & SCHUSTER

Harper Collins

Facts On File

Reader's Digest

IN 1999 WE SOLD BOOKS TO OVER 250 DIFFERENT PUBLISHERS AND DISTRIBUTORS. OUR CUSTOMER BASE INCLUDES ALL THE MAJOR INTERNATIONAL GROUPS. OUR BOOKS WERE PUBLISHED IN 35 COUNTRIES AND IN 25 DIFFERENT LANGUAGES.

acts as author, proprietor, and creator of, in this case, book concepts. The target audience is selected by us; our book ideas are presented to potential licensees who we believe have the appropriate market knowledge and channel access and, before granting licences, we satisfy ourselves that the publisher or distributor has quantified the market and reflects this in a substantial pre-production commitment. This is, in effect, a highly disciplined form of market testing.

We operate, in effect, an invisible brand with no measurable public 'face.' Our commercial activities are business-to-business. *We are the publisher's publisher.*

In 1999 we sold books to over 250 different publishers and distributors, including a number of direct-selling businesses. Our customer base includes all the major international publishing groups, including Simon & Schuster, Harper Collins, Penguin, Barnes & Noble, Borders, Random House, Bertelsmann, Reader's Digest and numerous specialist houses. Our books were published in 35 countries and in 25 different languages.

Unlike many other illustrated publishers, we have no consumer brand. Sales, marketing, and brand-building is the responsibility of our licensees. They promote and market according to their own styles and methods. Our books appear on their web sites, and they sell them to Internet retailers such as Amazon. Our customers assume the publishing risk, and manage inventory and returns. We retain all rights to our material.

We do produce series that carry brand recognition, such as our Let's Start™ or Fridge Fun™ series, and RotoVision's widely acclaimed graphics and photography series, but there is no overall house identity. Brand building, in that sense, is a business-to-consumer marketing exercise. Our focus is on the market, rather than on the marketing.

Our books are chiefly instructional and educational, and are aimed mainly at special interest audiences such as art, craft, design and self-help enthusiasts. They are international in scope – we do not have a domestic market. Because we apply rigorous financial criteria before a book is put into production, we believe our business to be low risk. Nothing is produced until it is pre-sold and minimum investment criteria are met. It is creatively liberating: only the best concepts survive.

A publishing model combining creative vision and powerful financial disciplines generates the lifeblood of our business – *long shelf life supported by regular reprinting.*

COMPETITIVE ADVANTAGE

Our publishing model powerfully combines creative vision and financial disciplines. Our ability to road-test our books, and gain material commitments from licensees, is not simply a low-risk form of publishing. It gives us powerful business leverage: we obtain resonant, and generally objective, feedback on what is likely to be viable in a range of key markets. This enables us, indeed forces us, to be relentlessly objective and market-focused about our material; we cannot rely on publishing instinct and "gut feel." The business is not, then, hidebound by the needs of a particular market or trend. We have no choice but to be market-savvy on a global basis.

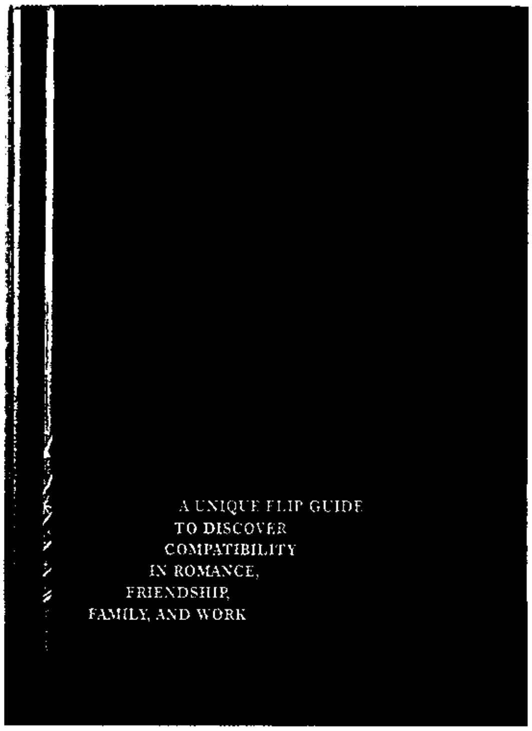
Our books generally have a shelf life of at least 3 years. The more successful a book when first printed, the more productive it will be over time. Long shelf life, characterised by regular reprinting, is the lifeblood of our business. It is not unusual for us to sell many tens of thousands of copies over this time, through consistent reprinting. As the cost of creating the book is expensed on its first publication, the number of times a title goes back to print is the key factor in profitability. Several of our book series count their sales in millions of copies.

Improvements in printing technology have lowered the cost of illustrated book production. Typically, this cost dividend has been reinvested in higher product specification or sharper pricing. By spreading costs across the widest possible range of markets and channels, we are able to maximise potential revenues. As one of the world's largest producers of illustrated books, the production of which remains a complex activity, we can exploit our volume production to achieve competitive pricing for print and related manufacturing. The combination of market focus, extended content life, and operational and manufacturing proficiency has enabled us to achieve operating margins which are consistently in the top quartile of the industry.

As new channels of dissemination emerge, mostly notably now the Internet, investors are appreciating the value of content. Quarto has a considerable material and intellectual repository of several thousand titles, growing annually by several hundred more. This is not simply a quantitative issue, it is qualitative too: our intellectual property has passed the litmus test of relevance, and has already been prepared for a global audience. Because we retain ownership of this content, we are able continually to adapt our material to the needs of new and different markets. It is no accident that over half our turnover already comes from sources outside the traditional book trade.

We use our ability to instruct, and our in-house expertise, to address a wide variety of readers in particular subject areas in a carefully segmented way. This allows us to use our internally generated content across a targeted range of audiences. In photography and graphics, for example, we are able to cover professional, semi-professional, student, hobby, and beginner markets.

THE QUARTO *ENCYCLOPEDIA OF TECHNIQUES* SERIES ILLUSTRATES THE CO-EDITION MODEL WORKING AT ITS MOST EFFICIENT. LAUNCHED 12 YEARS AGO WITH WHAT THEN SEEMED A REVOLUTIONARY CONCEPT, THE SERIES HAS NOW REACHED ITS 34TH TITLE. ALL ARE STILL IN PRINT, REPRINTING REGULARLY, AND AVAILABLE IN 16 LANGUAGES.



OUR PUBLISHING CRITERIA ARE DISCIPLINED ENOUGH TO WEED OUT ALL BUT THE STRONGEST CONCEPTS. TO SURVIVE, OUR BOOK IDEAS MUST BE INNOVATIVE IN CONCEPT, DESIGN, AND FORMAT. ONLY WHEN WE ARE SATISFIED THAT OUR INVESTMENT RISK IS COVERED BY SALES COMMITMENTS IN ENGLISH LANGUAGE TERRITORIES DO THE BOOKS GO INTO PRODUCTION.

BUT EXPERIENCE SHOWS THAT, IF WE STICK TO OUR BUSINESS MODEL, ADDITIONAL SALES FOLLOW ON QUICKLY. *MIX AND MATCH CHINESE ASTROLOGY*, PUBLISHED IN 1998, IS NOW AVAILABLE IN 12 LICENSED EDITIONS, AND IN 8 LANGUAGES. PORTIONS OF THE CONTENT HAVE ALSO BEEN LICENSED FOR MAGAZINE AND INTERNET USE. IN THIS CASE WE MIGHT HAVE SEEN IT IN THE STARS.

STRATEGY

In recent years illustrated book publishing has moved from being a niche sector to a mainstream activity. Advances in desktop publishing have combined with improved printing technology to facilitate considerable growth in the number, range, and stylistic diversity of illustrated books. The public demands books that are well produced. The need for new and original material continues unabated, and market conditions are buoyant. The advent of book superstores and other new channels, including the Internet, has increased the market for, and interest in, books, breathing renewed life and opportunity into both new and existing material. Our strategy is to extend our leading role as a profitable originator of illustrated content, using our creative skills, operational dexterity, and rigorous financial and market-testing techniques. At Quarto, new subject areas and markets represent opportunities to be grasped.

Above all things Quarto is a product company. Our strategy centres on leveraging our creative skills and product drive. In 1999, we appointed a number of new publishers to run existing units or start new ones. At the same time, we enlarged the publishing briefs at many of our operations, expanding the range of titles, formats, and subjects we cover. This will enable us to move our revenue and earnings forward as these new properties come to the market.

The accounting changes we introduced at the half-year are an important part of our plan. As we increase our overall output of titles, we have to put in place demanding benchmarks to ensure that we meet our objectives of longevity, relevance, and return on investment. We aim to optimise, rather than to maximise, the return from our lists. The immediate benefit of these more demanding criteria has been a substantial rise in the initial return on new titles.

The publishing environment continues to be subject to rapid change, as new forms and methods of distribution emerge. Book retailing is anything but the exclusive preserve of traditional, or even superstore, book chains. The expansion of e-commerce and Internet retailing is a positive development for content producers. The convergence of on-line and traditional retailers, the so-called bricks-and-clicks approach, is a positive development for Quarto: it increases the overall market for rights, and raises the profile of and demand for published material, whether in digital or paper-based formats.

We intend to build our current revenue stream from the Internet by concentrating on business-to-business opportunities, that reflect the nature of our current activities. iQu-digital.com will coordinate this activity across the Group.
The potential is considerable. In a rapidly evolving market we wish to ensure our content is managed by licensees who will add to, rather than devalue, this material.

At art publishing, our strategy of developing lists with greater focus and brand personality will continue. In similar vein to book publishing, these are being directed and managed with particular target audiences in mind. These brands are supported through a web presence, to facilitate image searches and enhance our distribution and marketing capabilities.

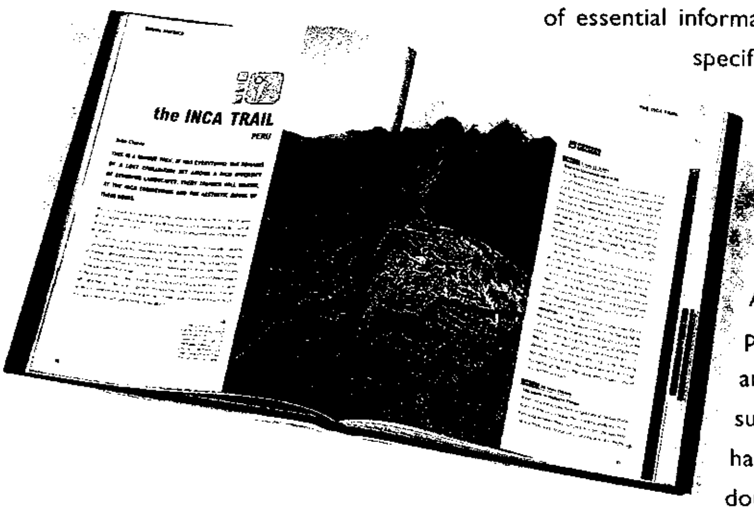
Our strategy is to extend our leading role as a profitable originator of illustrated content. *At Quarto, new subject areas and markets represent opportunities to be grasped.*

THE ANATOMY OF A BOOK

The Creation of *Classic Treks*

by Piers Spence, Publisher, Quarto Publishing

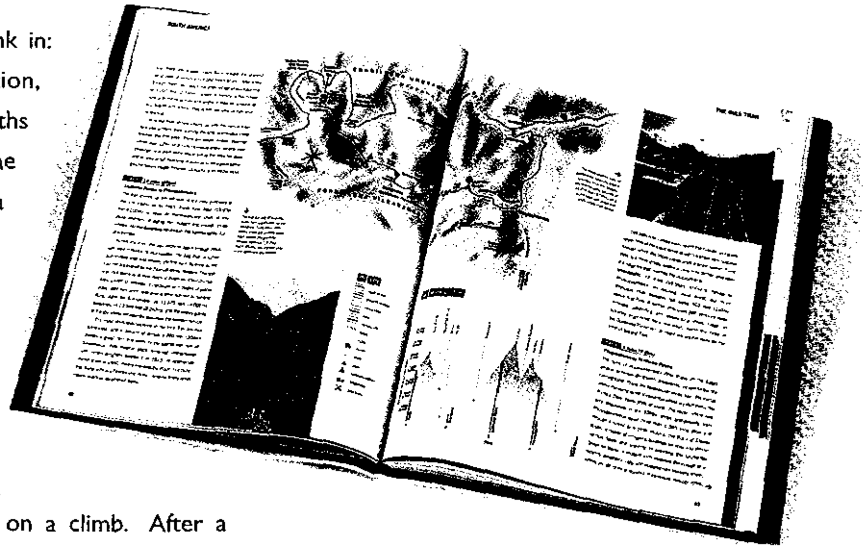
Thirty long distance walks in the world's most spectacular terrains: this was the concept that gave birth to Quarto's recent *Classic Treks*. The appeal of the idea emerging from our editorial meeting was obvious: aimed at serious and would-be walkers, it also offered inspiration and vicarious enjoyment to the much bigger armchair traveller audience. Specifications were rapidly appended to the fledgling concept: 5-6 pages per walk would make 165 pages which, with frontmatter, appendices and index, would take us to a 192-page extent, economical for modern colour presses. We wanted a large page size to make the most of potentially spectacular photography, and chose 295 x 222mm, a fraction wider than an A4 sheet. As to content, each walk would feature a walk description, colour photography, detail mapping, colour artworks, and a checklist of essential information. Satisfied with the outline concept and specification, we now needed to flesh the thing out into a synopsis, or proposal document, and sample pages. This would form the presentation with which the idea would be tested in the market.



A couple of afternoons of desk research pulled in most of the competitor publications and a ream of consumer magazines on the subject of trail walking. Within a fortnight we had a draft text for a synopsis and three sample double page spreads. So far, so good. A Quarto editor knocked the synopsis into shape while our in-house design team set to work on the pages, calling in location photography and searching the extensive Quarto archive for suitable maps and artwork.

Our presentation made a strong showing at the London Book Fair in March 1999, with three US publishers expressing interest, and the sales team negotiated a deal with Bulfinch, an imprint of Little, Brown. Our business model prescribes that we sell our books first into the US market, then add two further English-language territory sales to this first printing. Working from our rough P&L we knew that we could make an acceptable return on a first printing of around 20,000 copies across the three English language markets. Our US sales manager followed up with material and quotes. Not unusually, the customer wanted some changes from the sample material: they suggested a rejigging of the walks by continent; they needed the book to be 7mm wider to match the size of another title on their list; they had some reservations regarding the map styling. These were all fixable, but the request that was to cause us the biggest challenge came last: they needed the book for December that year.

The consequences of this began to sink in: after allowing time for reproduction, printing and shipping, this left us 5 months to write, illustrate, design, and make the book. By any standards this was a challenging schedule. Our earlier selected author also baulked at meeting this time frame and withdrew. Another period of rapid research unearthed a further three names, the likeliest of whom, Bill Birkett, a veteran walking author and photographer, was abroad on a climb. After a dozen attempts, we finally reached Bill on his mobile phone, 7,000 ft up the Matterhorn, and agreed to meet him on his return to the UK the following week.



After a dozen attempts, we finally reached Bill on his mobile phone... 7,000 ft up the Matterhorn

Bill sat in our offices and listened carefully to our predicament. When we'd finished, he said in a dry Yorkshire accent: "I can't do it." As our faces fell, he added: "But I know a few people who might be able to help." Together we hatched a plan. Bill, in his capacity as chairman of the Outdoor Writers' Guild, would contact his trekking friends around the world, getting as many of them as possible to write and photograph one walk in the book. We would co-ordinate from London, using email and the Internet to pull everything together. A logistical headache, it nevertheless seemed our best chance.

News on the sales front was good. Following on from our lead US edition, the team had made a UK sale to David & Charles, and confirmed several thousand copies for the Australian market. With these sales in the bag and a healthily positive P&L, we had "made the model", and could now draw up a preliminary working budget.

Serious work commenced on the content. We would have to give each writer the clearest possible brief on the detailed "ingredients" of each walking entry. In our pre-briefing meeting we brainstormed a host of value-added features for the walk contents. What started out as a checklist now became a detailed Factfile, setting out all the necessary information on access, health and safety, currency, climate, politics and religion, and much more. In addition to the

specially commissioned plan maps we decided to include graphical walk profiles, to give at-a-glance information on the ascent and descent involved in each stage of the walk. And, in a flash of inspiration, we thought it would be fun to add detailed charts showing month-by-month temperature and precipitation along the walk's route. Our writers-in-the-field were contacted, briefed, and given six weeks to submit their work. Meantime there were maps to commission, artworks to brief, tourist offices to be contacted, reference guides to be consulted. It was now 30 June: we had four months to get the book ready for the press.

Where exactly were the nearest food supplies on Borneo's Mount Kinabalu? What number bus runs from Lima to Chiquian in the Peruvian Cordillera?

Text and pictures arrived throughout the summer, from all corners of the globe. The standard of work was good, but occasionally frustratingly patchy, with vital details missing. Where exactly were the nearest food supplies on Borneo's Mount Kinabalu? What number bus runs from Lima to Chiquian in the Peruvian Cordillera? Having set ourselves such a comprehensive brief, we were beginning to feel the straightjacket of our own requirements. Every piece of data had to be painstakingly assembled and checked over intercontinental distances. But the pages were looking good, and the photography superb. Suddenly the whole complex project started to look achievable.

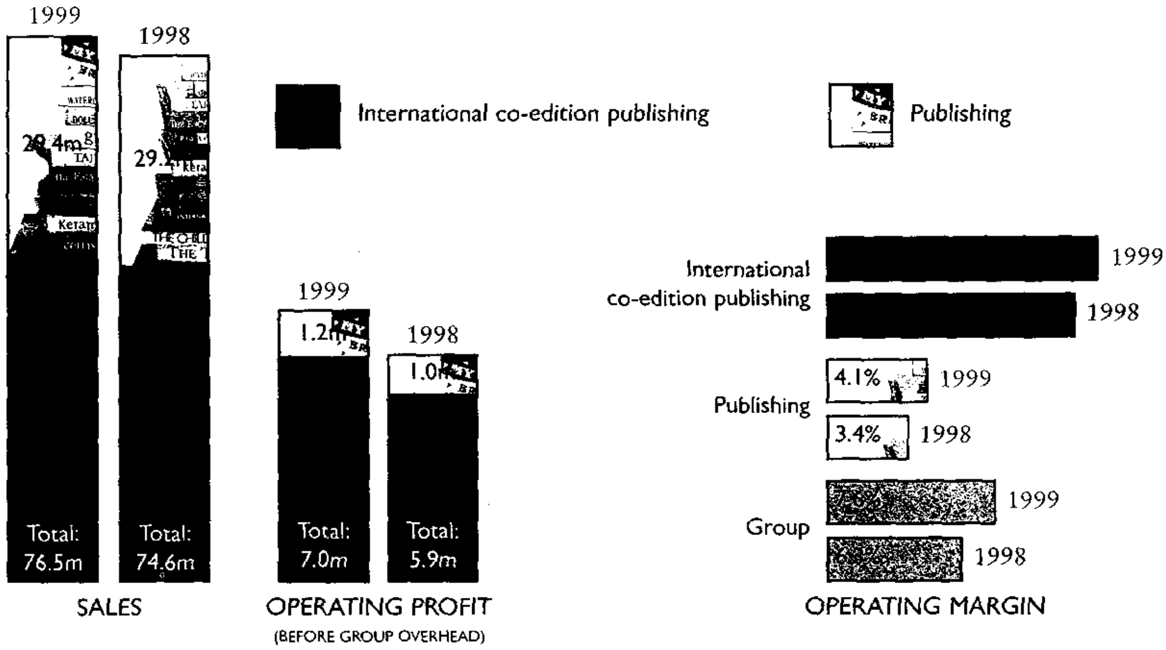
Final pages began to go out for reproduction in mid-September, but the climate charts were holding us up: it seemed near impossible to get January to December rainfall and temperature data for the Atlas Mountains, the Inca Trail, and half a dozen other important locations. Abject pleading with officials at various embassies finally did the trick, and the information appeared. Colour proofs of the final pages began arriving in house.

The idea that had been born one dull Monday in February had transformed itself – by dint of hard work, imagination, and a great team effort – into a book that far exceeded our expectations.

Our Hong Kong printer had been warned to expect a tight schedule and we signed off final proofs some ten days after our final, final deadline. But printing went off without a hitch. The books were shipped on schedule, arrived in time, and everyone was satisfied. The idea that had been born one dull Monday in February had transformed itself – by dint of hard work, imagination, and a great team effort – into a book that far exceeded our expectations. Prospects for further sales, already looking good, were only strengthened by a glowing review in the market-leading *Trail* magazine, which concluded by saying: "Informative, easy to read, and packed with stunning photography, *Classic Treks* will have no trouble keeping pride of place on your coffee table."

GROUP OPERATING REVIEW

Good progress was made on a wide range of key performance measures during 1999. We eschewed sales growth that did not meet our internal investment objectives and worked continuously to manage costs, improve working capital management, and keep overheads in line. As a result both divisions recorded strong growth in operating profits. A summary of operating performance is given below:



During 1999, Quarto reorganised from four divisions into two: International co-edition publishing, and Publishing, in order to reflect more appropriately our core activities.

INTERNATIONAL CO-EDITION PUBLISHING

Co-edition publishing remains at the heart of Group activities. In 1999 it produced 62% of Group revenue (1998: 61%) and over 200 new book titles were published. The eight separate lists that comprise the division produce titles in the how-to and self-improvement areas, specialising in art, crafts, gardening, self-help, health, photography, and design, all produced for adults; and interactive books aimed at both children and adults. The largest single market in 1999 was North America (38%), followed by mainland Europe (34%), UK (15%) and the rest of the world (13%). In addition to these book imprints, our Far Eastern-based pre-press and print broking businesses were merged into this division in 1999 and produced many titles for Group and third-party clients.

The strategic and operational reviews that we undertook in 1999 yielded immediate benefits. Operating profits for the division rose 18% to £5.81 million

(1998: £4.92 million) on sales 4% higher at £47.1 million (1998: £45.4 million). Equally gratifying, the operating margin rose to 12.3% (1998: 10.8%), indicating that we are making good progress towards our divisional target of 15%, which is well ahead of the norms in the consumer book publishing industry.

There were a number of key initiatives in 1999:

- New publishing appointments were made at Quarto, Quarto Children's Books, Quantum, and Rockport. In addition, we recruited Gordon Cheers from Random House in Australia to establish our new Global Publishing list. These moves resulted in a substantial improvement in the overall creative skills in the division, and the relevance of our publishing programmes.

- We refined our publishing criteria to ensure that our investments in new books yield acceptable returns and that titles subsequently have an enduring shelf life. As a result, we saw an average 40% improvement in the investment return on new titles. Reprints continue to comprise over two-thirds of total revenue.

- We re-doubled our efforts at controlling our costs, and we improved our operating performance generally. In 1999, divisional gross margins rose by 2%, as direct labour and material book making costs declined. Printing costs rose only marginally, and overheads were tightly controlled.

At QUARTO PUBLISHING, we had much success with our self-help titles, a relatively recent publishing initiative. *The Little Box of Inner Calm, Atlas of the New Age,* as well as more traditional titles including *Catch that Fish* and *Classic Treks,* illustrate the range of the list. QUINTET consolidated its reputation for stylish cookery, craft, and lifestyle books, and was particularly successful with *Barbie Collectibles, Colossal Cookie Book,* and *Classic Mosaics.* At QUARTO CHILDREN'S, our established pre-school series *Fit-a-Shape,* and our juvenile *Keepsakes* range, continued to grow their substantial sales. We also added colourful, new series to these, including *Pop it in the Pocket* and *George.* QUANTUM, our promotional publishing business, was less successful, and we appointed a new publisher in the middle of the year. There has since been a sharp improvement in performance.

DESIGN EYE publishes highly innovative kit books for both adults and children. Sales in 1999 reached almost £11 million, and operating profits rose to a new high. We have now sold over 5.6 million copies in our *Workstations* series for adults, and 1.5 million copies of the *Let's Start*™ educational series aimed at 4-6 year old children. These excellent achievements owe much to the vision and energy of one of the founders of Design Eye, Michael Tout, who died unexpectedly and tragically at the early age of 42 on August 16, 1999. We feel his loss very deeply and hope that we can continue to do justice to his legacy.

In July, we established a new subsidiary, GLOBAL PUBLISHING. Its mission is to publish definitive reference books, with as many as 1000 pages per title, over a broad range of subject areas. We are using a large team of writers, editors, illustrators, and cartographers from around the world, each a specialist in his or her area. In 2000, we will launch *Anatomica*, the most definitive, illustrated family reference book on the human body yet published. This will be followed by the *Global Wine Encyclopedia* and *America: The Complete Story*. These titles have attracted very substantial pre-publication orders from leading publishers around the world. As each of these massive productions contains around a million words and a vast resource of photographs and illustrations in digital form, we are negotiating with a number of companies to make our extensive material available on the Internet.

We have widened the publishing programmes at both ROCKPORT and ROTOVISION, our graphics and commercial art publishing units, reducing the output of showcase books and annuals, and increasing the range of practical and educational titles that they produce. Rockport's operating profits rose considerably on level sales. At RotoVision, sales advanced substantially, and cash generation improved. We also directed more of RotoVision's efforts into co-edition publishing, and took a sharp knife to inventory, as a result of which the operating profit declined. We anticipate a strong turnaround in 2000, as the publishing programme develops apace.

Hong Kong-based REGENT and Singapore-based PROVISION provide important services to the Group and third parties, using their local presence to leverage competitive print buying and exercising close quality control. During 1999, additional sales offices were opened in Washington, DC and London to develop further the third-party customer base. In an extremely competitive market, overall sales rose 10%. Operating profit was flat, but we expect profits to resume their upward path in the current year.

In 2000 we will launch *Anatomica*, the most definitive illustrated reference book on the human body ever published. We are already negotiating to make it available on the Interne

PUBLISHING

The Publishing division now includes our book, magazine, and art publishing imprints, in addition to the UK-based screen printing businesses. Our operations are based in the United States, Australia, and the UK, and work largely within their respective domestic markets. Divisional performance is stated on a like-for-like basis, excluding the Broughton Hall business.

Sales increased by 0.5% to £29.4 million. Operating profits advanced by 22.3% to £1.21 million, helped by better inventory management and reduced overhead. The operating margin for the division increased to 4.1% (1998: 3.4%).

The art and craft retail market in the USA continued its consolidation trend during 1999. This change had been anticipated at WALTER FOSTER, where we continued to expand our children's and teenage book and book-kit ranges. These are aimed largely at the speciality retail market and utilise our existing sales and distribution networks. This strategy resulted in an encouraging 18% rise in annual revenues.

In Australia, our art publishing business made considerable strides. Our distribution business, PARMUR, acquired several new high profile lists and reduced inventory and overhead. ARTWORKS, the publishing side of the business, has successfully extended its product range and customer base. Under the new SIGNATURE SPORTS imprint, we launched a new limited edition sports print list. These successful new ranges, together with a rigorous focus on overheads, virtually eliminated the 1998 operating loss and by the end of the year the business was trending positively.

In the USA, our art publishing business also improved, but remained loss-making. There is much more work to be done in 2000 to produce the kind of excellent profit returns we have traditionally earned in this line of business. In 1999, overheads were reduced further. We combined back-office operations and unified the management of the lists by appointing, from within the business, a new CEO for the whole operation. We also took steps to reposition our lists away from less profitable mass-market areas.

BOOK SALES, our promotional publisher in the USA, did less well than in 1998. The focus on improving margins and cash generation was well-intentioned but too intense. The consequence was that sales declined slightly, and this produced lower operating profits. We have already responded to this by increasing the level of third-party business, and encouraging a wider publishing range.

APPLE, our small UK trade publisher, had a mixed year. Sales rose by 4% but, because we also took a sharp knife to inventory levels, slashing them by 40%, there was an operating loss for the period. *The Artist's & Illustrator's Magazine* maintained its position as the leading practical art instruction publication in the UK. Attendance at the annual Fine Art Materials Exhibition was at a record.

AP & WESTERN, our UK based screen printing businesses, had a banner year. The strategy of focusing on productivity gains via process improvement and new equipment investment, together with new business wins, meant overall revenues increased during the year by 30%. Operating profits more than tripled.

CHIEF FINANCIAL OFFICER'S REPORT

A year of strong earnings growth and cash flow

TURNOVER AND OPERATING PROFIT FROM ONGOING ACTIVITIES

Turnover from ongoing activities increased by 2.5% from £74.6m to £76.5m. Improved gross profit margins, up from 33.5% to 33.9%, together with lower overheads, which were down 1%, led to a strong advance in operating profits from £4.7m to £5.8m. Operating profit represented 7.6% of sales compared to 6.3% in 1998.

INTEREST

The net interest charge fell 11% to £1,716,000 [1998: £1,931,000]. Interest cover improved to 3.4 times compared to 2.4 times in 1998 based on operating profit from ongoing activities. Our objective is to improve interest cover to 5 times.

TAXATION

The taxation charge on profit before exceptional items was 9.5% [1998: 27.7%]. In 1999 the Group's tax charge benefited from the taxable losses arising as a result of the change in accounting policy, which is commented on below, together with low tax rates in Hong Kong and Switzerland.

MINORITY INTERESTS

The Group has four trading subsidiaries in which there are minority interests. The reduction in the amount of profit attributable to minority shareholders is principally attributable to the reduced minority shareholding in Design Eye Holdings Limited, following the untimely death of Mike Tout.

SHAREHOLDER RETURN

Underlying earnings per share rose 222% to 15.8p [1998: 4.9p].

The proposed final dividend of 2.3p is unchanged as is the total dividend for the year at 4.5p. The dividend is 3.5 times covered [1998: 1.1 times] by underlying earnings per share.

The market price of the shares of common stock on 31 December, 1999 was 108.5p, up 74% compared to 31 December, 1998 when the market price was 62.5p.

GOODWILL

Goodwill arising on acquisitions is now carried in the balance sheet under the category of intangible fixed assets in accordance with the accounting standard FRS 10. Most of the goodwill arising during the year relates to the purchase of the 12.5% minority interest in Design Eye Holdings Limited, which increases the Group's shareholding to 87.5%.

WORKING CAPITAL

Working capital at the balance sheet dates is summarised below:

	1999	1998
	£m	£m
Stocks and work in progress	16.9	17.9
Trade debtors	24.4	26.8
Trade creditors	(20.2)	(21.4)
Other net liabilities	(2.7)	(2.3)
	18.4	21.0

Working capital is down £2.6m compared to 1998 and as a percentage of turnover fell from 28.1% to 24.0%. This improvement is due to a very strong focus during the year on working capital management.

Stocks and work in progress levels are down £1.0m, despite new initiatives such as Global Publishing. The reduction has been driven by more disciplined publishing decisions and improved inventory turn at most of our operating units.

Trade debtors are down £2.4m; this is principally due to improved collections with trade debtors representing 3.1 months' sales compared to 3.3 months' at the end of 1998. In addition the timing of our sales was improved, particularly in the co-edition business, which resulted in a strong third-quarter sales performance.

CASH FLOW AND NET DEBT

Cash flow in 1999 was very strong as a result of the focus on working capital management as discussed above. Net cash inflow from operating activities was £8.3m [1998: £5.9m]; this represents an excellent return on operating profit of 142% [1998: 118%].

Our year-end net debt was £20.9m, some £2.9m lower than the previous year. Net cash flow before currency translation differences was £3.3m and on a constant currency basis net debt would have been £20.5m. Our total banking facilities at the year end were £43.0m and of this £36.8m was committed.

TREASURY

The Group's borrowings, liquidity, interest rate and foreign exchange exposures and banking relationships are managed at Group level. The following policies have been applied during the year to manage the financial risks faced by the Group with regard to funding and liquidity, interest rate exposure and currency rate exposures:

- **Liquidity risk;** the Group prepares an annual cash flow forecast which is reviewed by the Board covering the next twelve months. This forecast is reviewed in the light of the facilities available to the Group to ensure that we have adequate liquidity. Some £36.8m of our total banking facilities is committed until 2002.

- **Interest rate risk;** most of the Group's borrowings are at floating rates.

- **Currency rate exposure;** the Group's principal operating currency is the US dollar. At Group level our annual US dollar receipts and payments are approximately the same and as a consequence we have a natural hedge in place to help protect our results from exchange rate fluctuations with regard to the US dollar.

In August 1997 we signed a five year, US$55m multi-currency revolving credit agreement with a syndicate of banks on both sides of the Atlantic. This facility gives us a very secure basis on which to finance our plans for the future. In addition it reduces our cost of funds. Most of our borrowings are in US dollars.

The following table sets out the average exchange rates used in translating the results of our overseas subsidiaries:

	1999 £m	1998 £m
US Dollar	1.62	1.66
Hong Kong Dollar	12.57	12.83
Swiss Franc	2.43	2.40
Australian Dollar	2.51	2.63
Singapore Dollar	2.74	2.77

ACCOUNTING POLICY CHANGE

Since flotation in 1986 we have operated an accounting policy that capitalised the development costs of our co-edition titles, writing these off over a thirty-six month period from the date of the first sale of a title. This policy became standard within the industry and had the advantage of reflecting the value of the backlist.

However, this method does not accurately reflect how we make decisions to produce new titles. It also fails to test the financial efficacy of our publishing decisions. We believe our co-edition business is low-risk, as book concepts are sold in advance of production. In practice, the investment decision on a new title is governed by a simple profit calculation based only on orders in hand. We have decided, therefore, to adopt a new accounting policy and charge all the development costs of new titles against the first printing of the book. The benefits of this change include:

- It ensures we account in the most prudent way possible;

- It further sharpens the focus on the use of and return on capital within our publishing businesses;

- It brings the accounting policy into line with the way management reaches business decisions;

- It moves closer to "cash" accounting so that shareholders have a clear view of our progress.

FINANCIAL REPORTING

We have very tight deadlines as we believe that this enables a greater degree of focus to be placed on running the business. It requires a lot of hard work and commitment and I take this opportunity to thank my staff for their continued loyalty and support.

MICHAEL J MOUSLEY
Chief Financial Officer 22 February, 2000

FINANCIAL REVIEW 1999

DIRECTORS' REPORT

The Directors present their report and the audited financial statements of The Quarto Group, Inc., for the year ended 31 December, 1999.

PRINCIPAL ACTIVITIES AND BUSINESS REVIEW

The Group conducts an international business whose principal activity is as a publisher of illustrated non-fiction books in co-edition and under its own imprint, for both adults and children. A detailed review of the development of the business of the Group is given in the Chairman's Letter on pages 5 to 7 and the Group Operating Review on pages 18 to 21.

RESULTS AND DIVIDENDS

The (loss) profit for the year after taxation and minority interests amounted to £(1,963,000) [1998 restated: £1,079,000]. The Directors propose a final ordinary dividend of 2.3p [1998: 2.3p] per share subject to approval at the Annual General Meeting. The deficit for the year was £(3,225,000) [1998 restated: £(199,000)] which has been deducted from reserves.

DIRECTORS

The Directors of the Company, who served as Directors during the year, are as follows:

L. F. Orbach	
R. J. Morley	
M. J. Mousley	
T. Hancock	(Appointed 18 January, 1999)
G. T. Y. Tai	
P. M. M. Campbell (Non-executive)	
P. E. Waine (Non-executive)	
G. L. Collins (Non-executive)	(Appointed 9 March, 1999)

Educated at Eton College, Peter Campbell started his business career with the Booker Group, holding a number of marketing positions in their United Rum Merchants subsidiary. From 1972 to 1989 he was with the Ocean Group, initially on the sales and marketing side, and from 1987 to 1989, he was the General Manager, UK Operations, for the MSAS subsidiary, with responsibility for 27 locations and 800 staff. Since 1989 he has been involved in management training and development, and is currently a Director of Catalyst Development, a member of the Blueprint Group.

Peter Waine has a wide corporate experience gained as a result of holding executive and non-executive Directorships in a variety of different sectors and with companies both public and private, up to £1 billion turnover. The organisations he has worked for include GEC, Coopers & Lybrand, W. R. Royle, and the CBI. He is the co-founder of Hanson Green, the principal source for non-executive appointments in the UK.

Leigh Collins has been a stockbroker since 1970 and is a director of Collins Stewart Limited of which he was a founding director in 1991.

None of the Directors has a service contract of more than one year's duration.

Save as disclosed in Note 23, no Director has had a material interest in any contract of significance with the Company or its subsidiaries during the year.

DIRECTORS' INTERESTS IN SHARES

The Directors who held office at 31 December, 1999 had the following interests in the share capital of the Company.

	Number of US$0.10 shares of common stock	
	31 December, 1999	1 January, 1999*
L. F. Orbach**	2,878,413	2,878,413
R. J. Morley	1,504,424	1,504,424
M. J. Mousley	37,000	37,000
T. Hancock	-	-
G. T. Y. Tai	25,477	25,477
P. M. M. Campbell	1,000	-
P. E. Waine	-	-
G. L. Collins	337,650	287,650

*or date of appointment

**2,678,413 shares in which L. F. Orbach is interested are owned through his family trusts. The remaining 200,000 are held by the Quarto Publishing plc pension scheme, which is for the benefit of both L. F. Orbach and R. J. Morley.

200,000 of the shares in which R. J. Morley is interested are owned through the Quarto Publishing plc pension scheme, which is for the benefit of both L. F. Orbach and R. J. Morley.

M. J. Mousley held 5,000 convertible cumulative redeemable shares of preferred stock of par value US$0.10 each at 31 December, 1999 (At 1 January, 1999: 5,000).

At 1 January, 1999 and 31 December, 1999 L. F. Orbach held options over 50,000 shares exercisable between 10 April, 1995 and 9 April, 2002, at an exercise price of £1.30424, and M. J. Mousley held options over 5,000 shares exercisable between 31 March, 2001 and 30 March, 2008 at an exercise price of 68.5p. On 19 February, 1999, T. Hancock was granted options over 90,000 shares at an excercise price of 62.5p; these options are exercisable between 19 February, 2002 and 18 February, 2009.

During the year the market price of the shares of common stock ranged between 56.5p and 117.5p. The market price at 31 December, 1999 was 108.5p.

Between 31 December, 1999 and 21 February, 2000 there have been no changes in the interests of the Directors.

SUBSTANTIAL SHAREHOLDERS

As at 21 February, 2000 the Directors have been advised of the following shareholders who have an interest of 3% or more in the shares of common stock of the Company:

	Number of US$0.10 Shares of common stock	Percentage
British Gas Pension Fund	681,026	3.6%
Clerical Medical Investment Group	716,132	3.8%
Co-operative Insurance	702,945	3.8%
Herald Investment Trust	711,642	3.8%
Phillips & Drew Fund Management	2,300,166	12.3%
Prudential Corporation Group of Companies	655,524	3.5%
Schroder Investment Management Limited	1,788,636	9.6%
L .F .Orbach	2,878,413	15.4%
R. J. Morley	1,504,424	8.1%
The Quarto Group, Inc.	750,000	4.0%

CORPORATE GOVERNANCE

The Directors have reviewed the governance arrangements of The Quarto Group, Inc. in the context of the Combined Code, issued in June 1998. The principles of the Code have been applied as follows:

a) The Board of Directors represents the shareholders' interests in maintaining and growing a successful business including optimising consistent long-term financial returns.
b) The Board comprises five executive Directors and three non-executive Directors. The non-executive Directors, P. M. M. Campbell, P. E. Waine and G. L. Collins are considered by the Board to be independent.
c) The Board meets eight times a year. A formal agenda is prepared for each meeting and all board papers and information are circulated to the Board forty-eight hours before the meetings.
d) The Board as a whole is responsible for the appointment of its own members.
e) All of the Directors are subject to re-election by the shareholders at the Annual General Meeting.
f) The remuneration of the executive Directors is recommended by the Remuneration Committee. A separate report with respect to Directors' remuneration is included below.
g) The Chairman, Chief Operating Officer and Chief Financial Officer are responsible for investor relations. Shareholders are invited to attend the AGM at least twenty days in advance of that meeting.
h) The Audit Committee, comprising P. M. M. Campbell, P. E. Waine and G. L. Collins, meet with the auditors as necessary.

The Group has complied throughout the year with the provisions set out in Section 1 of the Combined Code appended to the Listing Rules of the London Stock Exchange, apart from those listed below. Where non-compliance is reported, this is because, in the opinion of the Board, it is not appropriate to change current practice due to the size and constitution of the Board. The provisions of the Combined Code not complied with are as follows:

a) The Chairman of the Company is also the Chief Executive. The Board sees no value in splitting the roles of Chairman and Chief Executive.
b) A formal schedule of matters specifically reserved for the Board is not required, since the Board forms the executive management of the Group.
c) The Company does not have any formal arrangements for Directors, in the furtherance of their duties, to take independent professional advice.
d) The Chairman, P. M. M. Campbell, P. E. Waine and G. L. Collins fulfil the role of the Remuneration Committee for Directors.
e) Performance-related bonuses are not given.
f) There is no nominated senior non-executive Director.

GOING CONCERN

The Directors, having made enquiries, consider that the Group has adequate resources to continue in operational existence for the forseeable future, and that therefore it is appropriate to adopt the going concern basis in preparing the financial statements.

INTERNAL CONTROLS

The Combined Code, provision D.2.1, requires the Directors to, at least annually, conduct a review of the effectiveness of internal controls and report that they have done so. The guidance on internal controls (the Turnbull guidance) was issued by the ICAEW in September 1999. The board of Directors support the guidance but have taken advantage of the transitional provisions and will report on the compliance with such guidance in the financial statements for the year ending 31 December, 2000. Consequently, the Directors have not undertaken, during the year, a formal review of the effectiveness of the Group's non-financial controls as envisaged by the Combined Code. The procedures necessary to implement the guidance are expected to be in place by 31 August, 2000.

The Directors have, however, reviewed the effectiveness of the Group's internal financial controls during the financial year. The system of internal financial control is designed to provide reasonable, but not absolute, assurance against material misstatement or loss.

The main elements of the internal financial control system are:

a) The results of individual operating units are reported monthly and reviewed by the Board at its eight board meetings a year.
b) The management accounts of each operating unit are tailored to suit the business and management needs of local management. Each operating unit has its own performance indicators and these are regularly reviewed and assessed.
c) In addition to the monthly reporting, individual operating units report certain management information more frequently where it is considered appropriate.
d) All operating units report their bank balances twice weekly and a report is produced summarising the Group position.
e) The Board and the finance department make frequent visits to all operating units. These visits include a review of the internal financial control system.

DIRECTORS' REMUNERATION

The remuneration committee advises the Board on the remuneration and other terms of employment of executive Directors. With respect to Directors' remuneration the Board report that:

a) Remuneration levels are set by reference to individual performance, experience, and market conditions with a view to providing a package that is appropriate for the responsibilities involved.
b) Performance-related bonuses are not given.
c) Each Director has a defined-contribution personal pension plan.
d) No Director has a service contract of more than one year's duration.
e) Full details of Directors' remuneration and benefits are given in note 2 to the financial statements on page 36.

The remuneration committee is constituted in accordance with relevant provisions of Section B of the Combined Code, save that it does not consist exclusively of non-executive Directors and its terms of reference are not formally documented. The remuneration committee has given full consideration to Section B of the Combined Code Provisions in framing its remuneration policy.

SUPPLIER PAYMENT POLICIES

The Group agrees terms and conditions for its business transactions when orders for goods and services are placed, ensuring that suppliers are aware of the terms of payment and including the relevant terms in contracts where appropriate. These arrangements are adhered to when making payments, subject to the terms and conditions being met by the supplier. At 31 December, 1999, Group creditor days amounted to 99 days (1998: 93 days). The holding company does not have any trade creditors.

AUDITORS

Our auditors, KPMG Audit plc, are willing to continue in office and, accordingly, a resolution is to be proposed at the annual general meeting for the reappointment of KPMG Audit plc as auditors of the Company.

YEAR 2000

The Year 2000 issue is one that affects all companies. We have completed a project to ensure that our business systems are Year 2000 compliant. The Group has not experienced any problems to date. The nature of this issue is such that it is not possible to guarantee that no Year 2000 problems will arise. The Group may also be affected by future Year 2000-related problems at third parties with whom it deals. However the Directors consider that appropriate steps have been taken to protect the business in this regard.

The Group incurred costs of approximately £100,000 during 1999 in relation to Year 2000 compliance and we are satisfied that any future costs will not be material to the profitability of the Group.

Cyrus H. Bhote

C. H. BHOTE
Secretary
22 February, 2000

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Company is incorporated in the State of Delaware, United States, and is subject to the law of that state which places no requirement for annual reporting to shareholders upon the directors. However, since the Company has a listing on the London Stock Exchange and a place of business in the UK, it meets the requirements for listed companies and overseas companies, as defined in UK companies legislation, by preparing financial statements in accordance with UK law and accounting standards as if it were incorporated in Great Britain.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss for that period. In preparing these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for maintaining proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

AUDITORS' REPORT TO THE MEMBERS OF THE QUARTO GROUP, INC.

We have audited the financial statements on pages 28 to 46.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

The Directors are responsible for preparing the Annual Report. As described above, the Company is incorporated in the United States but the Directors prepare the financial statements in accordance with United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by the Auditing Practices Board, the Listing Rules of the London Stock Exchange, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by Law or the Listing Rules regarding Directors' remuneration and transactions with the Group is not disclosed.

We review whether the statement on page 25 reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Stock Exchange, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read the other information contained in the Annual Report, including the corporate governance statement, and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

BASIS OF OPINION

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

OPINION

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the Group as at 31 December, 1999 and of the loss of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG AUDIT PLC, Chartered Accountants, Registered Auditor, London, 22 February, 2000

KPMG Audit Plc

CONSOLIDATED PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31 DECEMBER 1999

	NOTES	1999 £000	1998 As restated £000
TURNOVER :Continuing operations		76,456	74,581
:Discontinued operations		-	4,575
	1	76,456	79,156
Cost of sales	2	(50,524)	(51,861)
GROSS PROFIT		25,932	27,295
Distribution costs	2	(2,376)	(2,559)
Administration expenses (including £12,000 goodwill amortisation)	2	(17,821)	(19,826)
Other operating income		78	104
GROUP OPERATING PROFIT		5,813	5,014
:Continuing operations		5,813	4,715
:Discontinued operations		-	299
GROUP OPERATING PROFIT		5,813	5,014
Share of loss of associate		-	(20)
TOTAL OPERATING PROFIT		5,813	4,994
EXCEPTIONAL ITEM: Loss on discontinued operations	2	(5,230)	(580)
		583	4,414
Net interest payable and similar charges	3	(1,716)	(1,931)
(LOSS) PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	2	(1,133)	2,483
Tax on profit on ordinary activities	4	(390)	(849)
(LOSS) PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION		(1,523)	1,634
Minority interests – equity		(440)	(555)
(LOSS) PROFIT FOR THE FINANCIAL YEAR		(1,963)	1,079
Dividends (including non-equity)	5	(1,262)	(1,278)
DEFICIT		(3,225)	(199)
(LOSS) EARNINGS PER SHARE	6	(13.5)p	3.3p
UNDERLYING EARNINGS PER SHARE	6	15.8p	4.9p
DILUTED (LOSS) EARNINGS PER SHARE	6	(9.3)p	3.3p
DILUTED UNDERLYING EARNINGS PER SHARE	6	15.6p	4.9p

BALANCE SHEETS AT 31 DECEMBER 1999

	Notes	1999 £000	1998 As restated £000	1999 £000	1998 £000
FIXED ASSETS					
Intangible assets	7	792	-	-	-
Tangible assets	7	6,341	6,408	-	-
Investments	8	-	-	14,847	14,833
CURRENT ASSETS		7,133	6,408	14,847	14,833
Stocks and work in progress	9	16,849	17,889	-	-
Debtors	10	26,243	29,021	-	-
Investments	11	1	1	-	-
Cash and deposits	12	9,567	5,355	-	-
		52,660	52,266	-	-
CREDITORS: Amounts falling due within one year	13	(26,362)	(27,884)	(1,325)	(412)
NET CURRENT ASSETS/(LIABILITIES)		26,298	24,382	(1,325)	(412)
TOTAL ASSETS LESS CURRENT LIABILITIES		33,431	30,790	13,522	14,421
CREDITORS: Amounts falling due after more than one year	14	(29,833)	(28,496)	-	-
PROVISION FOR LIABILITIES AND CHARGES					
Deferred taxation	15	(1,151)	(1,188)	-	-
NET ASSETS		2,447	1,106	13,522	14,421
CAPITAL AND RESERVES					
Called up share capital	16	1,341	1,341	1,341	1,341
Treasury stock	17	(461)	(461)	(461)	(461)
Reserves – Paid in surplus	18	23,891	23,891	23,891	23,891
– Revaluation		1,018	1,018	-	-
– Profit and loss	19	(26,097)	(27,278)	(11,249)	(10,350)
SHAREHOLDERS' FUNDS		(308)	(1,489)	13,522	14,421
Equity		(5,512)	(6,693)	8,318	9,217
Non-equity		5,204	5,204	5,204	5,204
		(308)	(1,489)	13,522	14,421
MINORITY INTERESTS – EQUITY		2,755	2,595	-	-
		2,447	1,106	13,522	14,421

The financial statements on pages 28 to 46 were approved by the Board of Directors on 22 February, 2000 and were signed on its behalf by:

M. J. MOUSLEY
Director

CONSOLIDATED STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

FOR THE YEAR ENDED 31 DECEMBER 1999

	1999 £000	1998 As restated £000
(LOSS) PROFIT FOR THE FINANCIAL YEAR	(1,963)	1,079
Currency translation differences on foreign currency net investments	(531)	73
TOTAL RECOGNISED GAINS AND LOSSES RELATING TO THE YEAR	(2,494)	1,152
PRIOR YEAR ADJUSTMENT (ACCOUNTING POLICIES NOTE)	(13,315)	
TOTAL RECOGNISED GAINS AND LOSSES SINCE THE LAST FINANCIAL STATEMENTS	(15,809)	

RECONCILIATION OF CONSOLIDATED MOVEMENT IN SHAREHOLDERS' FUNDS

FOR THE YEAR ENDED 31 DECEMBER 1999

	1999 £000	1998 £000
PROFIT FOR THE FINANCIAL YEAR	(1,963)	1,079
Dividends	(1,262)	(1,278)
Deficit for the financial year	(3,225)	(199)
Other recognised gains and losses relating to the year	(531)	73
Purchase of shares	-	(461)
Goodwill adjustment in respect of prior years' acquisitions	-	(340)
Goodwill on closure of operations written back to reserves	4,937	-
Net movement in shareholders' funds	1,181	(927)
Shareholders' funds at 31 December, 1998 (as previously reported)	11,826	11,557
Prior year adjustment (Accounting Policies Note)	(13,315)	(12,119)
SHAREHOLDERS' FUNDS AT 31 DECEMBER, 1999	(308)	(1,489)

CONSOLIDATED CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 1999

	1999 £000	1998 £000
NET CASH INFLOW FROM OPERATING ACTIVITIES	8,259	5,907
RETURN ON INVESTMENT AND SERVICING OF FINANCE		
Interest received	338	216
Interest paid	(2,029)	(2,130)
Interest element of hire purchase payments	(45)	(48)
Preference dividend paid	(455)	(455)
NET CASH OUTFLOW FROM RETURN ON INVESTMENT AND SERVICING OF FINANCE	(2,191)	(2,417)
TAXATION		
UK and overseas corporation tax paid	(594)	(678)
CAPITAL EXPENDITURE		
Purchase of tangible fixed assets	(690)	(1,072)
Sale of tangible fixed assets	225	194
	(465)	(878)
ACQUISITIONS AND DISPOSALS		
Purchase of businesses/subsidiaries	(67)	-
Net cash balance acquired with subsidiaries	-	30
	(67)	30
EQUITY DIVIDENDS PAID		
Dividends paid	(928)	(955)
MANAGEMENT OF LIQUID RESOURCES		
Movement in short term deposits	(1,418)	105
FINANCING		
Purchase of shares	-	(461)
Increase in debt	478	855
NET CASH INFLOW FROM FINANCING	478	394
INCREASE IN CASH	3,074	1,508
RECONCILIATION OF NET CASHFLOW TO MOVEMENT IN FUNDS/(DEBT)		
Increase in cash	3,074	1,508
Increase in debt	(478)	(855)
Management of liquid resources	1,418	(105)
	4,014	548
New finance leases	(726)	(139)
Translation differences	(364)	221
MOVEMENT IN DEBT FOR YEAR	2,924	630
Net debt at beginning of year	(23,818)	(24,448)
Net debt at end of year	(20,894)	(23,818)

See note 22 for an analysis of certain of the items included above.

ACCOUNTING POLICIES

The significant accounting policies that have been adopted in the financial statements, which are presented under the historical cost basis of accounting, as modified by the revaluation of freehold property, are as set out below and comply with applicable accounting standards. The Company is an "overseas company" within the meaning of the Companies Act 1985; it therefore complies with the company laws of the state of Delaware, United States, which are different in certain respects from the Companies Act 1985, in particular in relation to distributable reserves and the arrangements with directors. The financial statements have been prepared in accordance with the accounting and disclosure requirements of the Companies Act 1985. The accounts have been prepared in accordance with applicable accounting standards and with the requirements of the Companies Act 1985, except as explained in note 17.

CHANGE IN ACCOUNTING POLICY

During the year, the Group changed its accounting policy in respect of stocks and work in progress. Previously, the Group adopted the accounting policy of capitalising the development costs of books and amortising them over the estimated economic life of the books (of not more than three years), commencing from the date of first printing. The Directors consider the new policy of charging all development costs against the first printing of a book to be a more appropriate and fair presentation of the results and financial position of the Group.

The effect of this change, which has resulted in a prior year adjustment, has been to reduce the consolidated operating profit and profit on ordinary activities before taxation for the year ended 31 December, 1998 by £1,196,000 and the consolidated net assets at 31 December, 1998 by £13,315,000. The comparative figures have been restated to reflect the new policy.

Had the Group continued to adopt the old policy, the consolidated operating profit and profit on ordinary activities before taxation for the current financial year would have been lower by £269,000 and the consolidated net assets at 31 December, 1999 would have been higher by £12,906,000.

BASIS OF CONSOLIDATION

The consolidated financial statements represent a consolidation of the audited accounts of The Quarto Group, Inc. and its subsidiaries, all of which have been made up to 31 December.

The results of subsidiaries acquired during the year and requiring to be acquisition-accounted are included from the date on which control passes. On the acquisition of a business, fair values, reflecting conditions at the date of acquisition, are attributed to the net tangible assets. Where the fair value of the purchase consideration exceeds the values attributable to the Group's share of such net assets, the difference is treated as purchased goodwill and for accounting periods up to 31 December, 1997 this was written off directly to reserves in the year of acquisition. Goodwill on acquisitions subsequent to 31 December, 1997 is capitalised as an intangible fixed asset and written off over its useful economic life (not more than 20 years). Reorganisation and integration costs resulting from the acquisition are charged to the profit and loss account. The profit or loss on the disposal or discontinuation of a previously acquired business is calculated taking account of the attributable amount of purchased goodwill relating to that business.

In accordance with the exemptions allowed by Section 230 of the Companies Act 1985, the Company has not presented its own profit and loss account.

FOREIGN CURRENCY

Assets and liabilities in foreign currencies are translated into sterling at the rates of exchange ruling at the respective balance sheet dates. Profit and loss accounts in foreign currencies are translated at average rates for the respective accounting periods. Exchange differences arising on the translation of the net assets and profit and loss accounts of non-UK companies together with exchange differences on related borrowings are accounted for through reserves. All other exchange differences are recorded as ordinary trading items.

TURNOVER

Turnover represents the invoiced value of goods and services supplied to third parties excluding Value Added Tax.

ACCOUNTING POLICIES

DEPRECIATION

Depreciation is calculated to write off the cost less estimated residual value of fixed assets by annual instalments over their estimated economic lives at the following annual rates:

Long leasehold	: 2% straight line
Short leaseholds	: over the period of the lease
Plant, equipment and motor vehicles	: 10–25% straight line
Fixtures and fittings	: 15–20% straight line

No depreciation is provided on freehold properties because the Directors consider that the lives of these properties and their residual values (determined at the time of acquisition or subsequent valuation) are such that their depreciation is not material. Any impairment in the carrying value of fixed assets is charged against the revaluation reserve or the profit and loss account, as appropriate.

INVESTMENT IN ASSOCIATES

An associated undertaking (associate) is one in which the Group has a long term equity interest, usually from 20% to 50%, and over which it exercises significant influence. The Group's share of the profits less losses of associates is included in the consolidated profit and loss account and its interest in their net assets, other than goodwill, is included in investments in the consolidated balance sheet.

STOCKS AND WORK IN PROGRESS

Stocks and work in progress are valued at the lower of cost, including an appropriate portion of overheads, *and net realisable value. Production costs (excluding unit print costs), including an appropriate proportion* of overheads, in respect of a book are charged against the first printing of a book.

DEFERRED TAXATION

Provision is made, using the liability method, for deferred taxation on all material timing differences which are expected to crystallise.

COPYRIGHTS

Predominately the Group owns the copyright in its titles. No value is attributed to these rights.

LEASE AND HIRE PURCHASE CONTRACTS

Where assets are acquired under finance leases (including hire purchase contracts) the amount representing the outright purchase price of such assets is included in tangible fixed assets. Depreciation is provided in accordance with the accounting policy above. The capital element of future finance lease payments is included in creditors and the interest element is charged to the profit and loss account over the period of the lease in proportion to the capital element outstanding. Expenditure on operating leases is charged to the profit and loss account on a straight line basis.

PENSIONS

Substantially all of the Group's pension costs relate to individual pension plans and are charged to the profit and loss account as they arise.

FINANCIAL INSTRUMENTS

Page 23 *of the Chief Financial Officer's Report provides an explanation of the role that financial* instruments have had during the year in creating or changing the risks the Group faces in its activities. The explanation summarises the objectives and policies for holding or issuing financial instruments and similar contracts and the strategies for achieving those objectives that have been followed during the period.

As permitted by FRS 13, short-term debtors and creditors have been excluded from the disclosures.

NOTES TO THE FINANCIAL STATEMENTS

	1999 £000	1998 £000
1 SEGMENTAL ANALYSIS		
Geographical analysis of turnover by destination		
United Kingdom	15,177	12,505
United States of America	36,164	42,034
Canada	2,429	1,734
Europe	14,576	14,761
Australasia and the Far East	5,628	6,071
Rest of the World	2,482	2,051
	76,456	79,156

	TURNOVER		PROFIT BEFORE TAX		NET OPERATING ASSETS	
	1999 £000	1998 £000	1999 £000	1998 As restated £000	1999 £000	1998 As restated £000
CLASS OF BUSINESS						
Co-edition publishing	47,106	45,384	5,810	4,923	12,148	15,218
Publishing	29,350	33,772	1,208	1,287	13,336	12,148
	76,456	79,156	7,018	6,210	25,484	27,366
Amortisation of goodwill			(12)	-		
Group overheads			(1,193)	(1,196)		
Share of loss of associate			-	(20)		
Exceptional costs			(5,230)	(580)		
Net interest payable			(1,716)	(1,931)		
			(1,133)	2,483		

The group interest expense is arranged centrally and is not attributed to individual activities or geographical areas.

ANALYSIS BY GEOGRAPHICAL AREA OF ORIGIN

	TURNOVER		OPERATING PROFIT		NET OPERATING ASSETS	
	1999 £000	1998 £000	1999 £000	1998 As restated £000	1999 £000	1998 As restated £000
United Kingdom	36,825	34,516	4,833	3,586	6,275	6,636
United States of America	25,925	32,653	1,231	1,548	12,337	13,490
Rest of the World	13,706	11,987	954	1,076	6,872	7,240
	76,456	79,156	7,018	6,210	25,484	27,366

NOTES TO THE FINANCIAL STATEMENTS

		1999 £000	1998 As restated £000
1 SEGMENTAL ANALYSIS (CONTINUED)			
The net operating assets can be reconciled to the consolidated balance sheet as follows:			
Net operating assets		25,484	27,366
Total bank loans and other borrowings		(30,461)	(29,173)
Cash at bank and in hand		9,567	5,355
Corporation tax, deferred tax and advance corporation tax		(1,656)	(1,909)
Dividends payable		(487)	(533)
Net assets		2,447	1,106
2 (LOSS) PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION IS STATED AFTER CHARGING:			
Depreciation		1,056	1,101
Auditors' remuneration	: audit	171	172
	: other	7	10
Operating lease rentals in respect of:			
Plant and machinery		54	57
Other assets		1,019	1,105
EXCEPTIONAL ITEMS:			
Closure costs with respect to the Broughton Hall business		293	580
Goodwill written back		4,937	-
		5,230	580

Operating profit is stated, in 1998, after charging the following amounts relating to discontinued operations: cost of sales £2,284,000, distribution costs £265,000 and administration expenses £1,727,000.

Included under auditors' remuneration are audit fees in respect of the Company, amounting to £38,000 [1998: £38,000]. The fees have been dealt with through the financial statements of Quarto Publishing plc.

A loss of £899,000 [1998: loss £4,711,000] has been dealt with in the accounts of the Company.

EMPLOYEES

STAFF COSTS INCLUDING DIRECTORS' EMOLUMENTS COMPRISE:

	1999 £000	1998 £000
Wages and salaries	10,472	12,128
Social security costs	833	995
Pension costs	317	337
	11,622	13,460

	1999 Number	1998 Number
THE AVERAGE MONTHLY NUMBER OF PERSONS EMPLOYED BY THE GROUP DURING THE YEAR WAS:		
Co-edition publishing	193	202
Publishing	225	309
Group administration	15	15
	433	526

NOTES TO THE FINANCIAL STATEMENTS

		1999 £000	1998 As restated £000

2 (LOSS) PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION (CONTINUED)
DIRECTORS' REMUNERATION

EMOLUMENTS:

		1999 £000	1998 As restated £000
Fees to Non-executive Directors		43	29
Executive Directors	– *remuneration including benefits in kind in respect of motor vehicles and health insurance*	669	678
	– *pension contributions*	96	80
	– *compensation for loss of office*	-	135
		808	922

The Directors' remuneration disclosed above included the following amounts paid in respect of the Chairman (also the highest-paid Director for 1999)

	1999 £000	1998 £000
Remuneration	195	190
Pension contributions	38	38
	233	228

The highest paid Director in 1998, H. Goldstein, received remuneration amounting to £238,000, including £135,000 for compensation of loss of office.

Details of Directors' share options are given in the Directors' report. During the year certain of the Directors maintained current accounts with the Company. The balance on these current accounts can be found under note 23 on page 46.

The remuneration of the Directors was as follows:

	SALARY/ FEES £000	BENEFITS £000	PENSION CONTRIBUTION £000	1999 TOTAL £000	1998 TOTAL £000
L. F. Orbach	192	3	38	233	228
R. J. Morley	151	3	22	176	175
M. J. Mousley	110	2	16	128	118
T. Hancock	115	1	17	133	-
G. Banks	-	-	-	-	33
G. Y. Tai	69	23	3	95	101
H. Goldstein	-	-	-	-	238
E. de Bellaigue	-	-	-	-	8
P. M. M. Campbell	15	-	-	15	13
P. E. Waine	15	-	-	15	8
G. L. Collins	13	-	-	13	-
	680	32	96	808	922

NOTES TO THE FINANCIAL STATEMENTS

	1999 £000	1998 £000
3 NET INTEREST PAYABLE AND SIMILAR CHARGES		
Interest payable:		
On bank overdrafts and other loans repayable within 5 years by instalments	2,010	2,070
On loans repayable after more than 5 years	-	28
Hire purchase	45	48
	2,055	2,146
Interest receivable	(339)	(215)
	1,716	1,931
4 TAXATION		
On profit for the year:		
United Kingdom corporation tax at 30% [1998 31%]	-	736
Deferred taxation – UK	123	(34)
– Overseas	(115)	(6)
Overseas tax	382	153
	390	849

The Group's low taxation charge reflects the benefit of tax losses in the UK, tax relief on the write-off of intangible assets in the US and low tax rates in Hong Kong and Switzerland.

	1999 £000	1998 £000
5 DIVIDENDS		
Equity: Ordinary: Interim paid of 2.2p per share [1998: 2.2p per share]	395	411
Ordinary: Final proposed of 2.3p per share [1998: 2.3p per share]	412	412
	807	823
Non-equity: Preference	455	455
	1,262	1,278

6 EARNINGS PER SHARE

The calculation of earnings per share is based on 17,925,306 shares (1998: 18,644,484) and a loss, after minority interests and preference dividends, of £2,418,000 (1998: profit of £624,000).

The calculation of underlying earnings per share is based on earnings of £2,824,000 (1998: £905,000) calculated as follows:

	1999 £000	1998 £000
Earnings after minority interests and preference dividends	(2,418)	624
Exceptional items	5,230	580
Amortisation of goodwill	12	-
Earnings of discontinued operations	-	(299)
	2,824	905

Diluted earnings per share is based on 21,063,732 shares (1998: 18,653,004) and a loss, after minority interest of £1,963,000 (1998: profit of £624,000). The number of shares for 1999 incorporates 3,122,414 with regard to the conversion of the preference shares and 16,012 with regard to dilutive options (1998: 8,520 with regard to dilutive options). Diluted underlying earnings per share is based on 21,063,732 shares and earnings of £3,279,000 (1998: 18,653,004 shares and earnings of £905,000).

NOTES TO THE FINANCIAL STATEMENTS

	FREEHOLD PROPERTY £000	LEASEHOLD PROPERTY £000	PLANT EQUIPMENT AND MOTOR VEHICLES £000	FIXTURES AND FITTINGS £000	TOTAL £000
7 FIXED ASSETS					
TANGIBLE FIXED ASSETS					
Group					
Cost or valuation:					
At 1 January, 1999 (as restated)	2,948	1,001	5,388	1,167	10,504
Exchange differences	(68)	8	(6)	(15)	(81)
Additions	-	24	1,326	66	1,416
Disposals	-	(54)	(1,162)	(116)	(1,332)
At 31 December, 1999	2,880	979	5,546	1,102	10,507
Depreciation:					
At 1 January, 1999	30	320	3,022	724	4,096
Exchange differences	-	2	(10)	(20)	(28)
Charge for the year	-	104	792	160	1056
Disposals	-	(54)	(803)	(101)	(958)
At 31 December, 1999	30	372	3,001	763	4,166
Net book value:					
At 31 December, 1999	2,850	607	2545	339	6,341
At 31 December, 1998	2,918	681	2,366	443	6,408
Cost or valuation at 31 December, 1999 is represented by:					
Surplus on valuation	1,018	-	-	-	1,018
Cost	1,862	979	5,546	1,102	9,489
	2,880	979	5,546	1,102	10,507

The net book value of plant, equipment and motor vehicles included £830,000 [1998: £446,000] in respect of assets held under hire purchase contracts. The depreciation charged on these assets during the year was £144,000 [1998: £201,000]. Included in leasehold property at cost is £344,000 [1998: £340,000] in respect of a long leasehold property; the net book value was £293,000 [1998: £299,000]. The principal freehold property in the UK, with a historic cost of £382,000, was revalued on the basis of an open market value for existing use at 31 December, 1989 by Conway Kersh, Professional Valuers. The valuation was £1.7 million but the Directors ascribed a value of £1.4 million, on the grounds of prudence. The valuation was in accordance with RICS Statements of Asset Valuation Practice and Guidance Notes.

As noted in the Accounting Policies no depreciation is provided on freehold property.

INTANGIBLE FIXED ASSETS

Intangible fixed assets comprises goodwill on acquisition at a cost of £804,000 less amortisation of £12,000. The goodwill arising during the year principally relates to the acquisition, at a cost of £913,000, of the 12.5% interest in Design Eye Holdings Limited. No fair value adjustments were made.

NOTES TO THE FINANCIAL STATEMENTS

	SHARES AT COST £000	LOANS £000	TOTAL £000
8 FIXED ASSET INVESTMENT			
At 1 January, 1999	8,806	6,027	14,833
Additions	1,035	(1,021)	14
At 31 December, 1999	9,841	5,006	14,847

The Company has the following principal trading subsidiaries (*Directly held by The Quarto Group, Inc.), all of which operate in their country of incorporation.

NAME	PLACE AND DATE OF INCORPORATION	ISSUED AND FULLY PAID SHARE CAPITAL	PERCENTAGE HELD	BUSINESS
Quarto Publishing plc	England 1 April, 1976	100,000 shares of £1 each	100*	Co-edition publishing
Quarto Inc.	Delaware, USA 16 October, 1986	60 shares of no par value	100*	Co-edition publishing
Western Screen and Sign Limited	England 24 November, 1961	1,500 shares of £1 each	100*	Publishing
Quarto Magazines Limited	England 20 May, 1986	1,000 shares of £1 each	100	Publishing
Regent Publishing Services Limited	Hong Kong 23 October, 1985	1,000 shares of HK$10 each	75	Co-edition publishing
Apple Press Limited	England 5 June, 1984	100 shares of £1 each	100	Publishing
Quarto Australia Pty Ltd.	Australia 14 September, 1981	8 redeemable preference shares of A$1 each and 103 ordinary shares of A$1 each	100*	Publishing
AP Screenprinters Limited	England 30 September, 1980	1,000 shares of £1 each	100	Publishing
RotoVision S.A.	Switzerland 18 July, 1977	1,500 shares of SFr500 each	100*	Co-edition publishing
Rockport Publishers Inc.	Massachusetts, USA 4 December, 1985	4,000 shares of no par value	100	Co-edition publishing
Book Sales Inc.	Delaware, USA 13 December, 1972	85 shares of no par value	80	Publishing
Quarto Children's Books Limited	England 6 January, 1976	2 shares of £1 each	100	Co-edition publishing
Scafa-Tornabene Art Publishing Co., Inc.	Delaware, USA 29 June, 1987	1,210 shares of no par value	100	Publishing
Front Line Graphics, Inc.	Delaware, USA 29 April, 1994	1,000 shares of US$1 each	100	Publishing
Walter Foster Publishing, Inc.	Delaware, USA 10 February, 1988	19,625 shares of US$0.01 each	100	Publishing
Design Eye Holdings Limited	England 22 June, 1992	200 shares of £1 each	87.5*	Co-edition publishing

NOTES TO THE FINANCIAL STATEMENTS

	1999 £000	1998 As restated £000	1999 £000	1998 £000
9 STOCKS AND WORK IN PROGRESS				
Finished goods	12,437	14,198	-	-
Work in progress	4,143	3,318	-	-
Raw materials	439	611	-	-
Less: Payments on account	(170)	(238)	-	-
	16,849	17,889	-	-
10 DEBTORS				
Trade debtors	24,381	26,790	-	-
Prepayments and accrued income	1,554	1,719	-	-
Other debtors	308	409	-	-
Corporation tax and advance corporation tax recoverable	-	103	-	-
	26,243	29,021	-	-
11 CURRENT ASSET INVESTMENTS				
Listed investments at cost (market value £1,000) [1998: £1,000]. Listed other than on the *International Stock Exchange in London*	1	1	-	-
12 CASH AND DEPOSITS				
Cash at bank	6,969	4,201	-	-
Short term deposits	2,598	1,154	-	-
	9,567	5,355	-	-
13 CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR				
Bank overdrafts	631	980	-	-
Current loan instalments	138	171	-	-
Hire purchase creditors	278	207	-	-
Total borrowings	1,047	1,358	-	-
Trade creditors	20,293	21,372	-	-
Other creditors including taxation and social security:				
Corporation tax	505	664	-	-
Advance corporation tax payable	-	160	-	-
Dividend payable	412	412	412	412
Dividend payable to minority shareholders	75	121	-	-
Social security	416	294	-	-
Other creditors	1,481	614	913	-
Accruals and deferred income	2,133	2,889	-	-
	26,362	27,884	1,325	412

NOTES TO THE FINANCIAL STATEMENTS

	1999 £000	1998 £000	1999 £000	1998 £000
14 CREDITORS: Amounts falling due after more than one year				
Bank and other loans	29,164	27,699	-	-
Hire purchase liabilities	250	116	-	-
Total borrowings	29,414	27,815	-	-
Other creditors	419	681	-	-
	29,833	28,496	-	-
Total borrowings are repayable as follows:				
Bank loans and overdrafts:				
In one year or less, or on demand	769	1,151	-	-
Between one and two years	116	188	-	-
Between two and five years	29,048	27,511	-	-
	29,933	28,850	-	-
Other borrowings (hire purchase liabilities):				
In one year or less, or on demand	278	207	-	-
Between one and two years	198	107	-	-
Between two and five years	52	9	-	-
	528	323	-	-
Total loans and other borrowings:				
In one year or less, or on demand	1,047	1,358	-	-
Between one and two years	314	295	-	-
Between two and five years	29,100	27,520	-	-
	30,461	29,173	-	-

The above borrowings carry interest at commercial rates ranging from 0.9% to 7.5%.

NOTES TO THE FINANCIAL STATEMENTS

	AMOUNT PROVIDED		POTENTIAL LIABILITY	
	1999	1998	1999	1998
	£000	£000	£000	£000
15 DEFERRED TAXATION				
Deferred taxation provided in the financial statements is as follows:				
Excess of capital allowances over depreciation	144	149	144	149
Other – UK	21	(107)	21	(107)
Other – overseas	986	1,146	1,121	1,504
Revaluation of freehold property	-	-	305	316
	1,151	1,188	1,591	1,862

The movement on the provision for deferred taxation is as follows:

	£000
Provision at 1 January, 1999	1,188
Exchange difference	(45)
Transfer to profit and loss account	8
Provision at 31 December, 1999	1,151

16 SHARE CAPITAL

Authorised:

28,000,000 [1998: 28,000,000] shares of common stock of par value US$0.10 each ("shares of common stock") with an aggregate nominal value of *US$2,800,000 [1998: US$2,800,000]*.

5,212,587 [1998: 5,212,587] 8.75p (net) convertible cumulative redeemable shares of preferred stock of US$0.10 each ("shares of preferred stock") with an aggregate nominal value of *US$521,258 [1998: US$521,258]*.

	1999	1998
	£000	£000
Equity share capital		
Allotted, called up and fully paid:		
18,675,306 shares of common stock of par value US$0.10 each [1998: 18,675,306]	1,063	1,063
Non-equity share capital		
Allotted, called up and fully paid:		
5,204,024 shares of preferred stock of US$0.10 each [1998: 5,204,024]	278	278
	1,341	1,341

NOTES TO THE FINANCIAL STATEMENTS

At 31 December, 1999, the following options over shares of common stock were outstanding under the Company's Executive Share Option Schemes:

NUMBER OF SHARES	DATE EXERCISABLE	OPTION PRICE PER SHARE
65,000	10 April, 1995 – 9 April, 2002	£1.30424
34,000	26 October, 1996 – 25 October, 2003	£2.82
55,500	31 March, 2001 – 30 March, 2008	£0.685
5,000	18 August, 2001 – 17 August, 2008	£0.84
90,000	19 February, 2002 – 18 February, 2009	£0.625
10,000	29 March, 2002 – 28 March, 2009	£0.84

The shares of preferred stock are convertible into shares of common stock on 1 June, 1990 and annually thereafter at a rate of 60 shares of common stock for every 100 shares of preferred stock. The Company may at any time purchase shares of preferred stock in accordance with the rights attaching to such shares. The Company is obliged to redeem all outstanding shares of preferred stock in 2005 at a price of £1. The holders of the preferred stock are not entitled to vote at any meeting of shareholders unless their dividend payment is more than six months overdue or the meeting is being held to consider a resolution for liquidation, dissolution, winding up or the appointment of a receiver. On liquidation, dissolution or other winding up the holders of the preferred stock are entitled to be paid out of the available assets of the Company the sum of £1 per share and the amount of all accrued dividends payable in priority to any payment being made to the holders of common stock. There are no special rights to dividends in respect of holders of common stock.

	1999 £000	1998 £000	1999 £000	1998 £000
17 TREASURY STOCK				
At 1 January, 1999	461	-	461	-
Purchase of 750,000 shares of common stock of par value US $0.10 each	-	461	-	461
At 31 December, 1999	461	461	461	461

The Company purchased its own shares during 1998. As a US company, it is permitted to hold these shares as treasury stock, without cancelling them, and to reissue them. Companies are not permitted to own their own shares in the same way under UK law and therefore the Directors consider that the presentation of own shares as fixed asset investments that is required by paragraph 8 of Schedule 4 to the Companies Act 1985 would not give a true and fair view in the case of this Company. In accordance with section 226 of that Act, the Directors have overridden the detailed requirement and adopted the presentation normally used by US companies in order to show a true and fair view. The effect is to reduce fixed asset investments and shareholders' funds in the balance sheets of the Group and of the Company by £461,000.

NOTES TO THE FINANCIAL STATEMENTS

	1999 £000	1998 £000	1999 £000	1998 £000
18 RESERVES – PAID IN SURPLUS				
At 1 January, 1999	23,891	23,891	23,891	23,891
At 31 December, 1999	23,891	23,891	23,891	23,891
19 RESERVES – PROFIT AND LOSS ACCOUNT				
At 1 January, 1999 (as restated)	(27,278)	(26,812)	(10,350)	(5,639)
Deficit for the year	(3,225)	(199)	(899)	(4,711)
Goodwill adjustment in respect of prior years' acquisitions	-	(340)	-	-
Goodwill relating to closure of operations written back to reserves	4,937	-	-	-
Difference on translation of net assets and profit and loss accounts of non-UK companies	(531)	73	-	-
At 31 December, 1999	(26,097)	(27,278)	(11,249)	(10,350)
This is analysed as follows:				
Profit and loss account	(1,383)	2,373	(11,249)	(10,350)
Goodwill	(24,714)	(29,651)	-	-
	(26,097)	(27,278)	(11,249)	(10,350)

NOTES TO THE FINANCIAL STATEMENTS

	LAND AND BUILDINGS 1999 £000	OTHER 1999 £000	LAND AND BUILDINGS 1998 £000	OTHER 1998 £000
20 FINANCIAL COMMITMENTS				
At 31 December, 1999 the Group had commitments to make payments under operating leases during the next year as follows for leases expiring:				
Within one year	131	18	114	27
Between two and five years	776	61	481	25
Over five years	116	-	460	-
	1,023	79	1,055	52

The land and buildings leases are subject to rent reviews.

Capital commitments at the end of the year for which no provision had been made amounted to £24,000 [1998: £350,000]. This expenditure was authorised and contracted for.

21 CONTINGENT COMMITMENTS AND LIABILITIES

On 28 February, 1996 the Group acquired Walter Foster Publishing, Inc. Of the purchase price US$966,242 was settled by the issue of promissory notes. The principal values of the promissory notes is adjustable upwards to reflect the increase, if any, in the value (in US dollars) of The Quarto Group, Inc.'s common stock over US $3.83. As at 21 February, 2000 the value of the common stock was US$1.78 and accordingly no adjustment has been made in these financial statements.

Quarto Inc. has an agreement to purchase the common stock from the minority shareholder in Book Sales Inc. at the end of a five year period, which was October 1996. The purchase price shall be based on the shareholder's investment in Book Sales Inc., adjusted for subsequent earnings. At 31 December, 1999 there was a potential liability, based on Book Sales Inc.'s financial statements, of approximately US$1,945,000. No provision has been made because the minority shareholder has not exercised their option. At 31 December, 1999 the minority interest in the consolidated financial statements of The Quarto Group, Inc. was US$1,330,000.

The Quarto Group, Inc. has issued guarantees in respect of £631,000 of overdrafts of subsidiaries [1998: £980,000] and bank loans of £28,867,000 [1998: £27,198,000].

The Group has also issued guarantees in respect of £528,000 of hire purchase creditors of subsidiaries [1998: £323,000].

There are other contingent liabilities, arising in the ordinary course of business, in respect of litigation, which the Directors believe will not have a significant effect on the financial position of the Group.

NOTES TO THE FINANCIAL STATEMENTS

22 NOTES ON THE CONSOLIDATED CASH FLOW STATEMENT	1999 £000	1998 As restated £000
RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOWS FROM OPERATING ACTIVITIES		
Operating profit	5,813	5,014
Exceptional costs	(291)	(36)
Depreciation and amortisation charge	1,068	1,101
(Loss) Profit on sale of fixed assets	149	(34)
Decrease (Increase) in stocks and work in progress	984	(1,140)
Decrease in creditors	(2,470)	(1,083)
Decrease in debtors	3,006	2,085
Net cash inflow from operating activities	8,259	5,907

	AS AT 1 JAN 99 £000	CASH FLOW £000	EXCHANGE DIFFERENCE £000	NEW HIRE PURCHASE £000	AS AT 31 DEC 99 £000
ANALYSIS OF NET DEBT					
Cash at bank and in hand	4,201	2,768	-	-	6,969
Bank overdrafts < 1 year	(980)	306	43	-	(631)
	3,221	3,074	43	-	6,338
HP creditors	(323)	521	-	(726)	(528)
Current loan instalments < 1 year	(171)	33	-	-	(138)
Bank loans >1 year	(27,469)	(1,102)	(433)	-	(29,004)
Mortgages	(230)	70	-	-	(160)
	(28,193)	(478)	(433)	(726)	(29,830)
Management of liquid resources	1,154	1,418	26	-	2,598
Net Debt	(23,818)	4,014	(364)	(726)	(20,894)

23 RELATED PARTY TRANSACTIONS

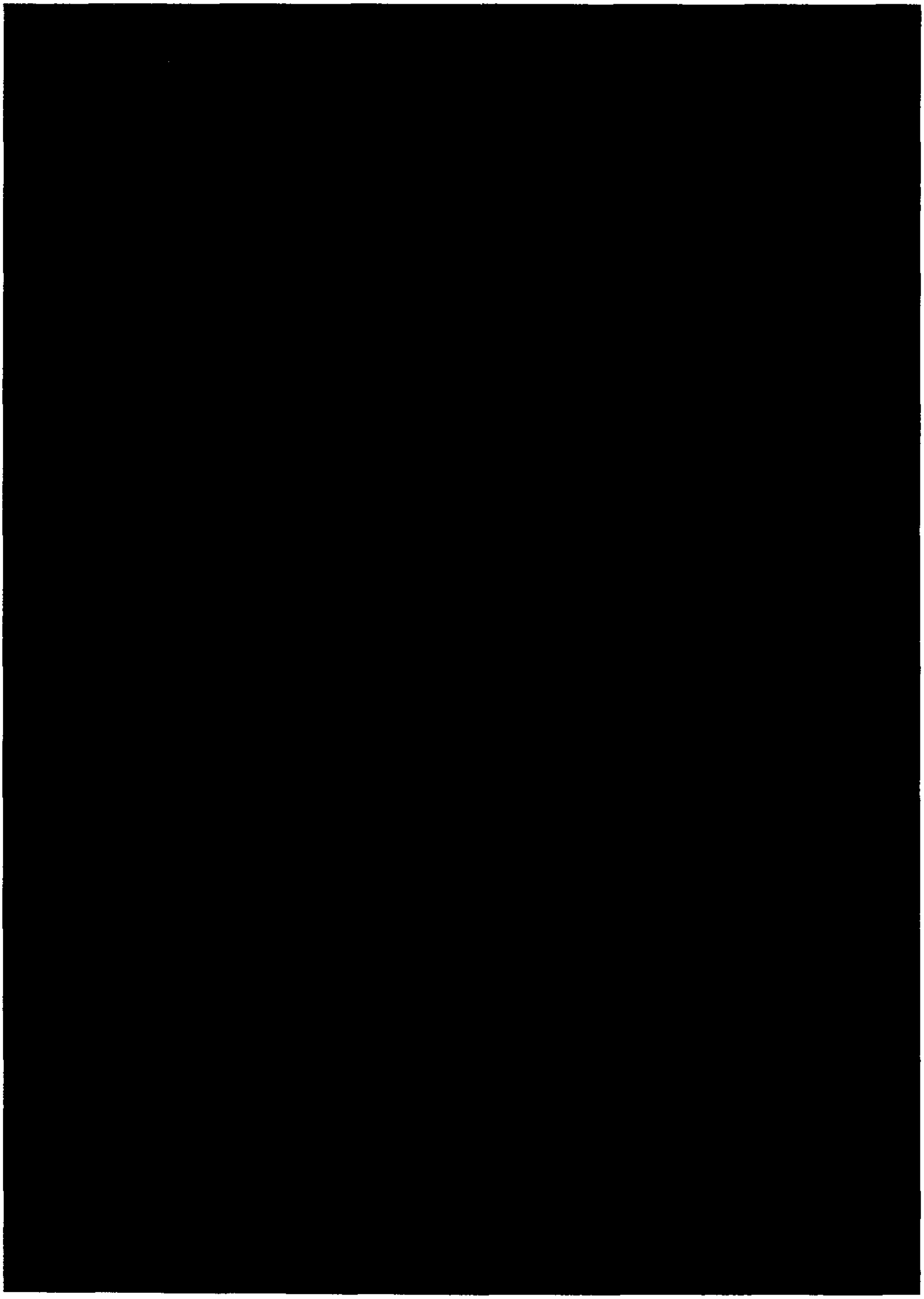
During the year L. F. Orbach and R. J. Morley maintained current accounts with the Group. The balances on these accounts were less than £5,000 throughout the year.

HISTORICAL COST FIVE-YEAR SUMMARY

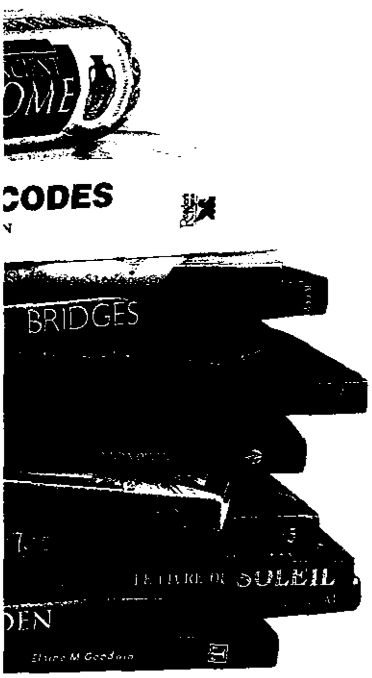
	1995 £000	1996 £000	1997 £000	1998 £000	1999 £000
PROFIT AND LOSS ACCOUNT					
Turnover	66,469	80,619	81,820	79,156	76,456
Operating profit before exceptional charges	6,021	7,162	4,585	4,994	5,813
Net interest	(840)	(1,329)	(1,941)	(1,931)	(1,716)
Profit before exceptional charges and taxation	5,181	5,833	2,644	3,063	4,097
LOSS ON CLOSURE OF OPERATIONS	-	-	(1,160)	(580)	(5,230)
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION	5,181	5,833	1,484	2,483	(1,133)
Taxation	(1,747)	(1,906)	(636)	(849)	(390)
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION	3,434	3,927	848	1,634	(1,523)
Minority interests	(241)	(528)	(500)	(555)	(440)
PROFIT FOR THE FINANCIAL YEAR	3,193	3,399	348	1,079	(1,963)
Dividends	(1,800)	(1,944)	(1,296)	(1,278)	(1,262)
RETAINED PROFIT	1,393	1,455	(948)	(199)	(3,225)
EARNINGS PER SHARE					
Underlying	13.9p	13.5p	3.9p	4.9p	15.8p
Basic	14.8p	15.8p	(0.6p)	3.3p	(13.5p)
DIVIDENDS PER SHARE	7.25p	8.0p	4.5p	4.5p	4.5p
BALANCE SHEET					
Fixed assets	6,787	7,392	6,759	6,408	7,133
Other net assets	14,774	17,712	19,362	18,516	16,208
	21,561	25,104	26,121	24,924	23,341
Net borrowings	(12,497)	(22,444)	(24,448)	(23,818)	(20,894)
Net assets	9,064	2,660	1,673	1,106	2,447
CASH FLOW					
Net cash inflow from operating activities		1,807	4,903	5,907	8,259
Return on investment and servicing of finance		(1,691)	(2,427)	(2,417)	(2,191)
Taxation		(996)	(1,453)	(678)	(594)
Capital expenditure and financial investment		(1,009)	(28)	(878)	(465)
Acquisition and disposals		(7,552)	(565)	30	(67)
Equity dividends paid		(1,386)	(1,587)	(955)	(928)
Other		880	(847)	(379)	(1,090)
Movement in (debt)/funds for year		(9,947)	(2,004)	630	2,924
Net debt at beginning of year		(12,497)	(22,444)	(24,448)	(23,818)
Net debt at end of year		(22,444)	(24,448)	(23,818)	(20,894)

The summary cash flow information in respect of 1995 is not readily available in the manner required by the accounting standard, FRS1, Cash Flow Statements.

The prior year figures have been restated to reflect the accounting policy change in 1999.



No medium has ever died.
People still use pen and ink;
newspapers flourish, movies
survived the onset of television;
books are big business.



THE QUARTO GROUP, INC.