KME Group S.p.A.

Report and financial statements at 31 December 2006

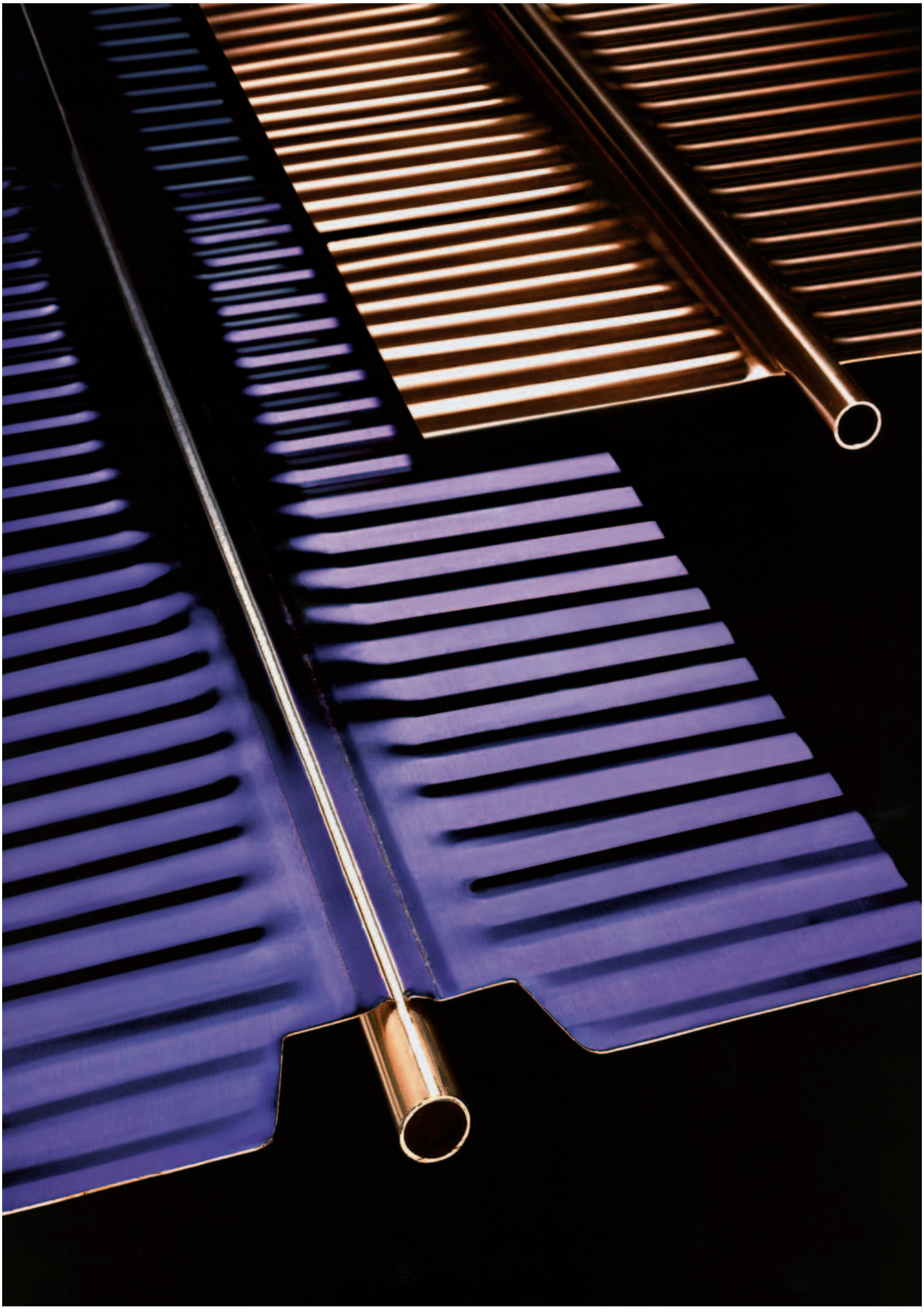
KME Group S.p.A.

122nd Financial Year

Report and financial statements at 31 December 2006

Registered office in Via dei Barucci, 2, 50127 Florence 2
www.kmegroup.it

Share capital Euro 319,685,924.75 fully paid
Companies' register no. 00931330583



Components for solar energy systems.

KME Group S.p.A.

1886 KME Group established

€ 3,557 million in consolidated revenues

670,000 tonnes produced annually

6,609 employees

13,000 shareholders

We mean copper

With 15 manufacturing facilities located in Italy, Germany, France, the United Kingdom, Spain and China, over 6,600 employees, 2 research centres, over 670,000 tonnes produced per year, consolidated turnover of Euro 3,557 million, sales organisations in various European countries and in every continent, GIM is today one of the major global groups in the manufacture of semi-finished copper and copper alloys and of an extensive range of high technology specialised products.

Its products are used in a wide variety of sectors: electronics, telecommunications, biomedical, electromechanical, energy, transport, mechanical and construction.

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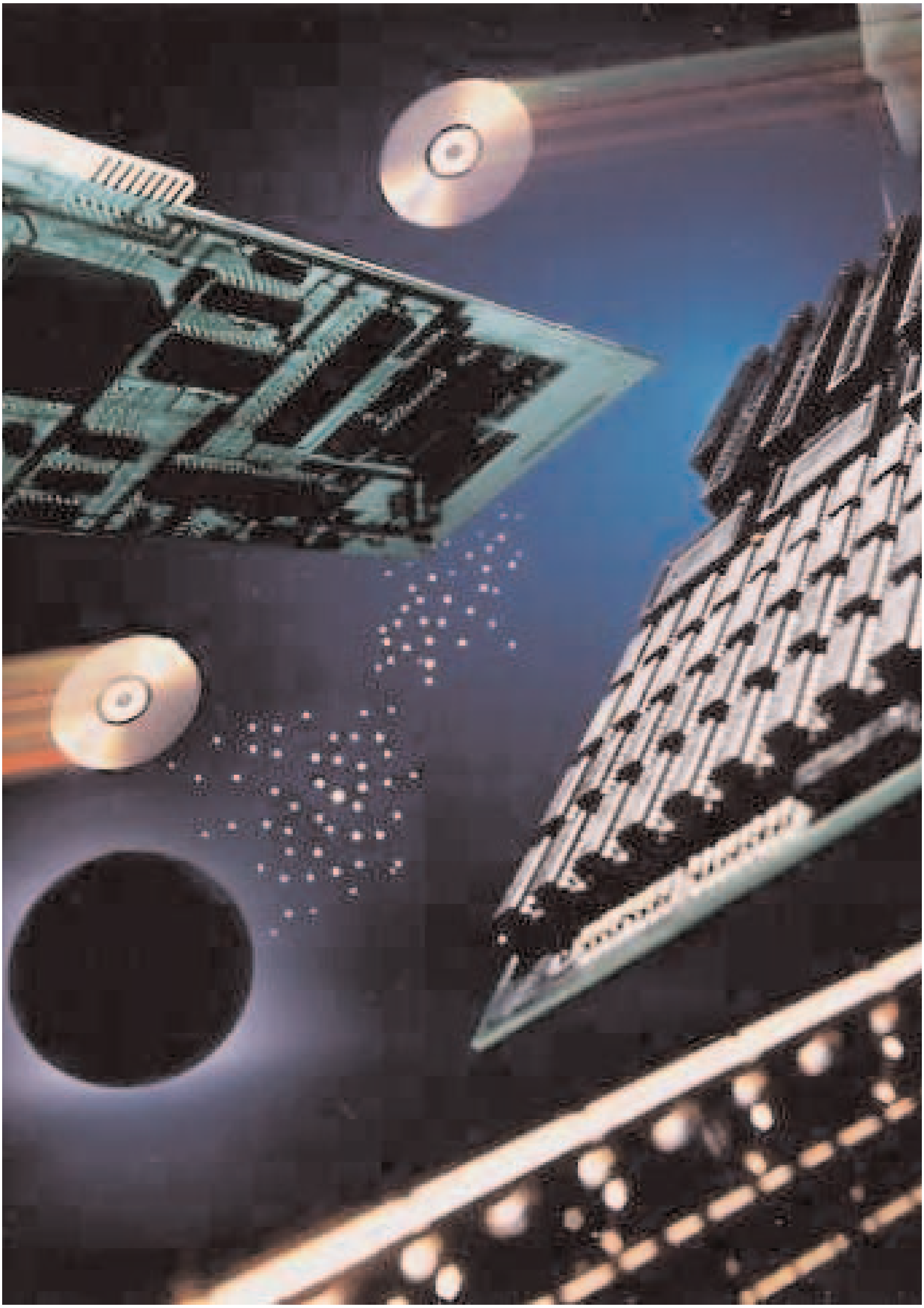


Components for computers.

KME GROUP S.P.A.

Board of Directors

Chairman	Salvatore Orlando
Deputy Chairman	Vincenzo Manes
Managing Director	Vincenzo Cannatelli (3)
	Mario d'Urso (1) (2)
	Marcello Gallo (2)
	Giuseppe Lignana (1)
	Diva Moriani
	Alberto Pecci (2)
	Alberto Pirelli (1)

Board of Statutory Auditors

Chairman	Marcello Fazzini
Standing Statutory Auditors	Pasquale Pace
	Alessandro Trotter
Substitute Auditors	Marco Lombardi
	Angelo Garcea

Independent Auditors

Deloitte & Touche S.p.A.

Representative of the savings shareholders

Romano Bellezza

(1) Members of the Compensation Committee.
(2) Members of the Internal Control Committee.
(3) Mr Cannatelli resigned from the position of Managing Director effective from 31 March 2007.

NOTICE OF MEETING

(Published in Part II of the Official Journal no. 37 dated 29 March 2007)

Notice is hereby given to KME Group S.p.A. shareholders of a shareholders' meeting that will be held in Florence at Via dei Barucci, 2, at 11.00 am:

- 30 April 2007 in the first call;
- 23 May 2007 in the second call;

to discuss and resolve on the following

AGENDA

- Statutory Financial Statements for the year ended December 31, 2006, Report of the Board of Directors on the Company's financial condition and the result from operations, Report of the Board of Statutory Auditors, related and required resolutions;
- appointment of Directors after determining the size of the Board of Directors, and related and required resolutions, including resolutions concerning the determination of the fixed annual Director's fee referred to in article 21 of the Company bylaws;
- Cancellation of the assignment to audit the statutory and consolidated financial statements for the year ending December 31, 2007, perform a limited audit of the semi-annual report at June 30, 2007 and perform regular tests of the accounting records granted to Deloitte & Touche S.p.A. pursuant to articles 155 and following of Legislative Decree No. 58 of February 24, 1998. Pursuant to the abovementioned articles 155 and following of Legislative Decree No. 58 of February 24, 1998, concurrent award to KPMG S.p.A. of the assignment to audit the statutory and consolidated financial statements for the years ending December 31, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015, perform limited audits of the semi-annual reports and consolidated financial statements at June 30, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015, and perform regular tests of the accounting records; related and required resolutions, including resolutions concerning the determination of the fee payable to the Independent Auditors.

Pursuant to law and in accordance with the provisions of article 11 of the bylaws, in order to attend the Meeting, shareholders must file at the Company's registered office, at Via dei Barucci, 2, Florence, at least two days prior to the date of the Meeting, certification issued by an intermediary that attests to their ownership of their shares. Applicable provisions of the proxy collection laws notwithstanding, shareholders may appoint a proxy (who need not be a shareholder) to represent them at the Meeting by means of a simple power of attorney affixed at the bottom of the abovementioned certification.

The Reports of the Board of Directors on all of the items on the Agenda, the corresponding motions and all other documents pertaining to all of the items on the Agenda that are required pursuant to law will be on file at the Company's registered office, at no. 2 Via dei Barucci, Florence, and at the offices of Borsa Italiana S.p.A. within the statutory deadline. Shareholders may request copies of these documents. The documents will also be available on the Company website: www.kmegroup.it.

Votes may also be cast by mail. Ballots and voting instructions will be available at the Company's registered office, Via dei Barucci, 2, Florence, at least 15 days before the date of the Meeting's first calling. Ballots must be mailed to the following address: KME Group S.p.A., Ufficio Affari Societari, Via dei Barucci, 2, (50127) Florence. Ballots must be received at least 48 hours prior to the Meeting's first calling, together with a copy of the certification required under current regulations governing attendance at Shareholders' Meetings.

Florence, 20 March 2007

The Board of Directors

GROUP STRUCTURE AT 31 DECEMBER 2006

INTEK

30.5% (*)

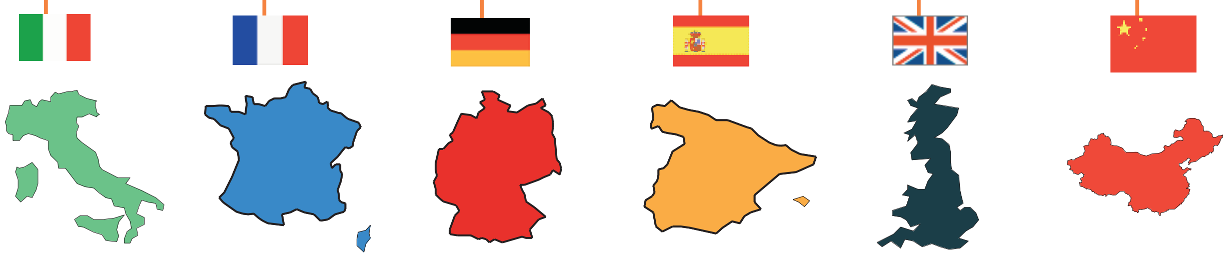
GIM Generale Industrie Metallurgiche

53.8%

KME Group SPA

KME

KME Europa Metal AG
100%



Italy	*France*	*Germany*	*Spain*	*United Kingdom*	*China*
Europa Metalli S.p.A. 100%	Tréfimétaux S.A. 100%	Fricke GmbH & Co. KG 100%	KME Iberica S.A. 99.9%	KME Yorkshire Ltd. 100%	KME Metals (Dongguan) Ltd. 100%
EM Brass S.r.l. 100%	TMX Brass S.a.s. 100%	KME Brass GmbH 100%	KME Ibertubos S.A. 100%		
			LOCSA Laminados Oviedo-Còrdoba S.A. 100%		

(*) Situation before G.I.M. S.p.A.'s incorporation in INTEK S.p.A..

CHANGE OF COMPANY NAME

Dear Shareholders,

Before continuing to the management report for the 2006 financial year, we remind you that at the extraordinary general meeting of shareholders held on 19 May 2006, the Company name was changed from “S.M.I. - Società Metallurgica Italiana S.p.A.” to “KME Group S.p.A.”.

This decision was made to underline how much Company activity is linked to international Group operations in the non-ferrous metallurgy sector, in which the Company has been present since its founding in 1886. The new name allows the Company to make a more immediate and direct connection to its current industrial and productive situation, in which it is present in the main Western European countries.

REPORT OF THE BOARD OF DIRECTORS

Dear Shareholders,

The results of the 2006 financial year shown here highlight the structural improvements of the KME Group, not only regarding income but also regarding industrial management and financial standing.

The measures adopted for the rationalisation of production and reinforcement of market position within the approved industrial plan aim at raising Group competitiveness and set the conditions for further profitability, growth and consolidation at sustainable levels, consistent with returns on invested capital.

Industrial activity aims at redefining the Group's organisational and productive structure through:

– Focalisation on productive businesses and sites within a wider process of improving efficiency and operational flexibility while containing costs. In this regard, the Board decided to close two mid-sized production units, one in Italy and one in France, thus concentrating assets in the remaining locations. This and other efficiency measures resulted in a workforce reduction of 1,000 employees from the beginning of 2005 (–14%).
– Focalisation and selection of investments.
– The development of professional expertise in service departments, with changes in the organisational models finalised towards the centralisation and specialisation of corporate functions for a more efficient and synergetic use of human resources.

In a sector that is characterised by structural productive overcapacity, marketing actions aim at reinforcing the Group's market position through:

– The optimisation and development — through agreements and joint efforts — of products with higher added value, specifically regarding some special product lines in which the Group has a leading position worldwide.
– The innovation and diversification of products and services offered to clients at competitive conditions which also contrast the market effects on increases in the prices of raw materials.
– The reinforcement of advantages deriving from the recognition and acknowledgement of brands that characterise the main products, especially in the construction products sector.
– An increase of Group presence on international markets, with special attention both on Eastern European and Chinese markets, as demonstrated through the recent acquisition of the controlling interest in DD Heavy Machinery Co. Ltd.

The economic effects of the productive rationalisation and market positioning reinforcement measures were enhanced during the 2006 financial year by a more favourable economic outlook.
During the past year, the rates of expansion of the world economy were maintained at high levels, and the forecasts are for a continuation of this favourable phase of the cycle, though at slightly lower rates.
After many years of what was almost stagnation, more satisfying rates of growth appeared, being bolstered first by a recovery in exports — which were propelled by international business growth — and subsequently by an acceleration of internal demand, especially regarding investments in the European economy, the Group's main business area.

This favourable outlook was reflected in the demand for semi-finished products made of copper and alloys; however these signs of improvement were not evenly distributed geographically or across the production range.
In Western Europe, growth in the production of semi-finished goods in copper and alloys (excluding conductors) was just under 7%, reaching 2.9 million tonnes, largely recovering 2004 levels after a 2005 that saw European production touching the lowest levels of the past ten years.
The growth in production did not involve all European countries, and regarded above all the two main producer countries: Germany, where production returned to sustained growth rhythms (over 12%), and Italy (+7.9%), where growth was concentrated above all on extruded copper alloy products.

Demand from industrial sectors gradually consolidated at positive levels, which mostly involved the electrical goods, air conditioning, refrigeration and thermal exchange sectors, while smaller increases were recorded in white goods and cars.
Demand from the construction sector for semi-finished products remained weak despite the recovery of investments in new residential housing; some specific factors contributed to this trend, such as the high price of raw materials and additional competition coming from Central-Eastern European countries.

During the 2006 financial year, raw materials price trends influenced the market.
Growth in the price of raw materials, especially copper — the metal most used by the Group — reached record levels in the first months of this year, hitting growth levels of 80% from January to May. This trend was reversed in subsequent months.
The persistence of the high prices and high price volatility of raw materials provoked market uncertainty, above all in the first part of the year, causing clients to delay purchase commitments as well as keep stockpiles at minimum levels, therefore making it more difficult to forecast the growth of demand and plan production.
The weight of raw materials on overall sales prices of semi-finished products went from 63% to 75%.

The improvement in the European economic outlook, as well as the marketing activities undertaken, caused a growth in 2006 **Group turnover** of 63%, going from Euro 2,176 million in 2005 to Euro 3,557 million. Net of raw materials, this increase was 11.8%, going from Euro 758 million to Euro 847 million.

A more satisfying sales trend and positive contributions from production re-organisation and rationalisation measures caused significant improvements in the Group's financial results.

Net consolidated profits for 2006 were Euro 51.7 million, while for 2005 a profit of Euro 4.3 million was recorded.
Contributing to the year's results were both an improvement in profitability for ordinary operations and a restatement of raw materials in the inventory following price increases.
Regarding ordinary operations, **gross operating profits (EBITDA)** climbed to Euro 126.5 million; this total discounts the deduction of the Euro 8.1 million factoring cost of trade receivables, an operation that was made to obtain new bank loans in September 2006, which was previously booked to financial charges.
Gross of this last figure, operating profits for 2006 totalled Euro 134.6 million, with an increase of Euro 41.8 million (+45) on the previous year; this represents 15.9% of sales (12.2% in 2005), and was higher than the objective set in the industrial plan.
The restatement of the raw materials (a gross total of Euro 79 million, which fell to Euro 53 million net of related taxes), which was partially compensated by industrial re-organisation reserves and other non-recurring costs (Euro 26.5 million), brought **net operating profits (EBIT)** to Euro 125.4 million (in the previous year they were Euro 44.8 million).

The Group's net **financial debt** at 31 December 2006 was Euro 534 million (Euro 559 million at the end of 2005).
A growth in exposure to customers due to an increase in raw material prices was compensated by a higher level of non-recourse factoring of trade receivables transactions, which went from Euro 60 million at the end of 2005 to Euro 367 million.
These types of transactions were made possible thanks to the new bank loans obtained by the Group's financing banks based on agreements signed 30 September 2006.
These agreements allowed for available lines to be increased through formulas that permit more flexibility in terms of their amount and their use for working capital fluctuations.
Specifically, two new bank loans were conceded to the Group, for a total of Euro 1.6 billion.
The first agreement, signed with Deutsche Bank (the Initial Mandated Lead Arranger, Agent and Coordinating Bank) and seven other important Mandated Lead Arrangers (Banca Nazionale del Lavoro, Unicredit, Capitalia, Mediobanca, Commerzbank, Dresdner Bank and HSH Nordbank) involve two blocks of financing:

– a three-year line of revolving credit of a maximum of Euro 650 million to cover Group company working capital requirements, specifically regarding inventory stocks, which may be extended for a further two years;

- a five-year loan of Euro 200 million to cover the Group's other financial requirements (pre-payment over three years).

The second agreement, signed with General Electric Corporate Finance Bank S.A. lasting five years, allows for the non-recourse factoring of trade receivables within a revolving credit limit of up to Euro 800 million.

The Group was able to eliminate the commitments undertaken according to the previous banking agreement, which allowed dividends to be distributed only under certain pre-arranged conditions.
To guarantee the repayment of the bank loans, the following was arranged:

- the shares of KM Europa Metal A.G.'s Italian and French subsidiaries which are owned by them were lodged as collateral;
- a first-tier mortgage was made on KM Europa Metal A.G.'s real estate property and other fixed assets;
- the warehouse inventory of the industrial companies, excluding the Spanish ones, was lodged as collateral;
- a lien was made on factoring and insurance contracts.

All economic and financial covenants regarding shareholder equity, indebtedness and consolidated EBITDA, as well as the EBITDA/consolidated net interest ratio, will be respected.
At 31 December 2006, all the covenants were respected in full.

The refinancing of the Group's debt positions was accompanied by a capital increase of Euro 129.9 million, approved at the general meeting of shareholders' held on 19 May 2006 and executed in July and August; the transaction included the issuing of ordinary shares at a unit price of Euro 0.35, paired with bonus warrants. This increase was made to fully extinguish the subordinated loan given by the subsidiary G.IM. - Generale Industrie Metallurgiche S.p.A..

KME Group's capital increase represents the last stage of the recapitalisation of the entire Group held by G.I.M., initiated in 2005 with a G.I.M. capital increase of Euro 152 million.
Regarding transactions made to inject funds into operational companies, G.I.M. used part of the proceeds of the increase to make a subordinated loan of Euro 130 million to its subsidiary. In turn, KME Group subscribed part of this loan to make a capital increase for KM Europa Metal AG, the fully-owned German subsidiary which heads the manufacturing companies of the Group, for a total of Euro 111.8 million.

Through the KME Group S.p.A. capital increase that was offered to all shareholders, the latter was also given the possibility to participate in the Group's recapitalisation.
G.I.M. S.p.A. subscribed its interest (of Euro 56.1 million) and covered the unopted remainder (of Euro 34.2 million) through the partial conversion of the subordinated loan. This in turn was fully reimbursed by KME Group S.p.A. with the part of the capital increase that was subscribed by the market (of Euro 39.6 million).

After this increase, KME Group's share capital rose to Euro 319.6 million, and its shareholder equity reached Euro 500 million.

These financial transactions rationalised and reinforced the Group's equity structure.
The Italian National Commission for Companies and Markets (henceforth CONSOB) — recognising that the present corporate situation was different from the management crisis that occurred at the time that the provision was made — on 9 November 2006 revoked its decision which since 14 April 2004 had obliged the Company to make monthly press releases giving details of its financial situation.

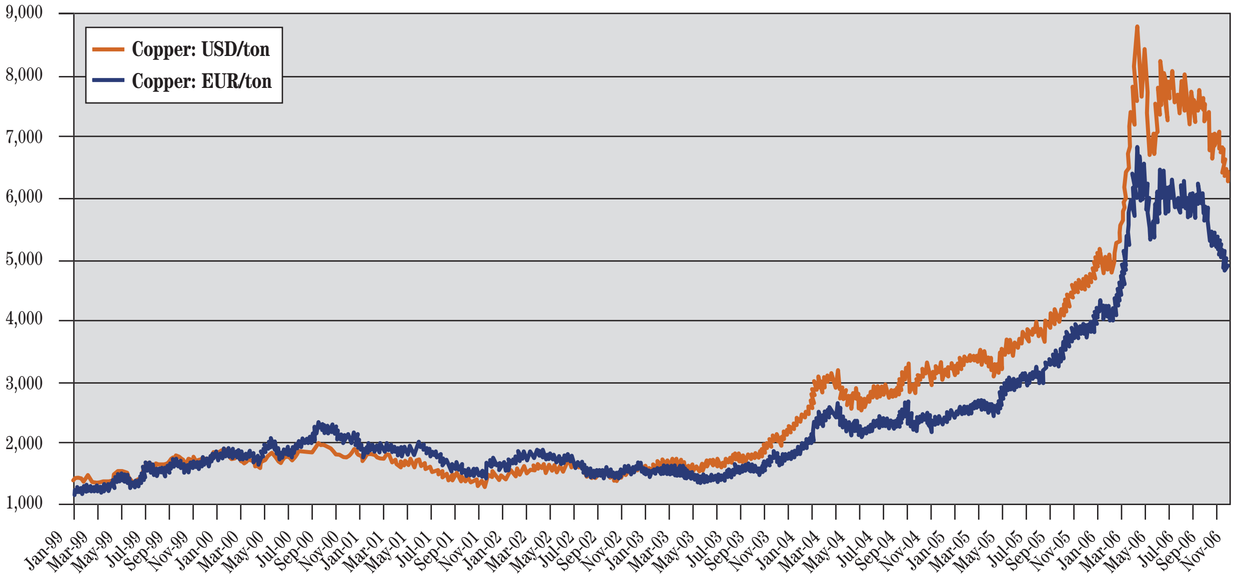
Copper Prices and Market Situation

Average copper prices in 2006 were higher than in the past year by 82.7% in both US dollar terms (going from USD 3,679/ton to USD 6,722/ton) and in Euro terms (from Euro 2,970/ton to Euro 5,340/ton).
The maximum daily price hit USD 8,788/ton on 12 May 2006, and then dropped in the following months.

In gradual terms, the average price of the last quarter of 2006 versus the prices from the same period 2005 were higher by 64.3% in USD (from USD 4,301/ton to USD 7,068/ton), and 51.6% higher in Euro terms (from Euro 3,620/ton to Euro 5,487/ton) due to an increase in the Euro in this reference period.

In the first two months of 2007, the price of copper fell further; in February it reached an average of USD 5,677/ton (corresponding to Euro 4,340/ton), and then began to increase again at the beginning of March.

LME SETTLEMENT COPPER PRICES



Group Financial Trends

The following table summarises the Group's consolidated financial results for the 2006 financial year.
The comparative figures are homogenous since the new international accounting standards (henceforth IAS/IFRS) were adopted for both reference periods.
In order to better highlight the Group management's operational performance, some items in the components contributing to the calculation of **gross operating profits** were reclassified (*), specifically:

– within sales, the effects due to the change in accounting policy regarding raw materials inventory were counted separately, as were the effects deriving from the fair value measurement of hedging operations made on the London Metal Exchange. Please note that the introduction of new international accounting standards caused a change in the metals inventory assessment from the LIFO method to the weighted average cost system. This change, which took place in a context of rising prices, provoked a restatement of raw material stocks;

– the extraordinary items are presented below the gross operational profits line; they also include the costs related to the renegotiation of bank loans, which according to IAS principles should be included in financial charges.

Pre-tax profits correspond to those in the consolidated income statement shown in the Notes, and conform to the new IAS/IFRS accounting principles.

(*) Reclassifications shown in detail:

(Millions of Euros)	FY 2006 IAS		Reclassifications	FY 2006 Restated	
Gross sales	3,556.8			3,556.8	
Cost of raw materials	0.0		**(2,709.5)**	(2,709.5)	
Sales net of cost of raw materials	**3,556.8**	***100%***		**847.3**	***100%***
Labour costs	(347.4)			(347.4)	
Other consumables and expenses	(3,029.5)		**2,656.1**	(373.4)	
Gross Operational Profits	**179.9**	***5.06%***		**126.5**	***14.93%***
Non-recurring (charges)/income	0.0		**(26.5)**	(26.5)	
IFRS impact on inventory and LME contracts	0.0		**79.1**	79.1	
Amortisation and depreciation	(51.4)		**(2.3)**	(53.7)	
Net Operational Profits (EBIT)	**128.5**	***3.61%***		**125.4**	***14.80%***
Net financial charges	(44.7)		**3.1**	(41.6)	
Results at equity	0.2			0.2	
Pre-tax profits	**84.0**	***2.36%***		**84.0**	***9.91%***

KME Group S.p.A. – Consolidated Income Statement

(Millions of Euros)	FY 2006		FY 2005		Change %
Gross sales	3,556.8		2,176.1		*63.4%*
Cost of raw materials	(2,709.5)		(1,417.9)		*91.1%*
Sales net of cost of raw materials	**847.3**	***100%***	**758.1**	***100%***	***11.8%***
Labour costs	(347.4)		(341.8)		*1.6%*
Other consumables and expenses	(373.4)		(323.5)		*15.4%*
Gross Operational Profits	**126.5**	***14.93%***	**92.8**	***12.24%***	***36.3%***
Non-recurring (charges)/income	(26.5)		(29.7)		*–10.8%*
IFRS impact on inventory and LME contracts	79.1		36.5		*116.7%*
Amortisation and depreciation	(53.7)		(54.8)		*–2.0%*
Net Operational Profits (EBIT)	**125.4**	***14.80%***	**44.8**	***5.91%***	
Net financial charges	(41.6)		(37.8)		*10.1%*
Results at equity	0.2		0.3		*–33.3%*
Pre-tax profits	**84.0**	***9.91%***	**7.3**	***0.96%***	
Current taxes	(4.9)		(3.8)		*28.9%*
Deferred taxes	(27.4)		0.8		*N/A*
Net profits	**51.7**	***6.10%***	**4.3**	***0.57%***	***N/A***

During 2006, **turnover** was Euro 3,557 million, an increase of 63% over the past year.
Net of raw materials it rose 11.8%, going from Euro 758.1 million to Euro 847.3 million. Sales volumes recorded an increase of 7.2%.
The 2006 turnover net of the cost of raw materials returned to 2004 levels, when it was Euro 852 million.

Total **operational expenses** grew by 7.1% due to increased activity and greater unit production costs, specifically those regarding energy and transport.
The labour costs component increased by only 1.6% despite the higher volumes produced.

Gross operating profits (EBITDA) climbed to Euro 126.5 million; this total discounts a deduction of the Euro 8.1 million factoring cost of trade receivables, an transaction that was made to obtain new bank loans in September 2006.
Gross of this figure, operating profits for the 2006 financial year totalled Euro 134.6 million, an increase of Euro 41.8 million (+45%) on the previous year.
This figure represents 15.9% of turnover net of raw materials; this is higher than the 2005 percentage (12.2%) as well as that of 2004, when it was 12.9% with similar turnover levels.

Net operational profits were positive for Euro 125.4 million (Euro 44.8 million in 2005).
The 2006 financial year benefited consistently from the restatement of raw materials in inventory as a consequence of the adoption of the new IAS accounting principles; these benefits were partially absorbed by extraordinary charges for the industrial restructuring plan (Euro 19 million), expenses for the renegotiation of new bank loans (Euro 3.1 million) and other minor non-recurring expenses.

Financial charges increased due to the higher level of indebtedness linked to the higher value of working capital for the increase in raw materials prices.

After taxes, **net consolidated profits** at 31 December 2006 were Euro 51.7 million (Euro 4.3 million at the end of 2005).

Information by Area of Operations

In Europe, the continent in which the Group has its major presence and which if taken as a whole represents the geographical area in which the Group has most weight at a global level, semi-finished copper and alloy goods (excluding conductors) increased in 2006 by 6.6% compared to the previous year (settling at around 2.9 million tons), and slightly decreased (–0.7%) on 2004 levels.

The production of semi-finished goods fell in the United States, while in Japan production levels once again began to grow.
Amongst emerging markets China continues to be in a class of its own, having doubled its production volumes in the past five years. In the past five years, the Chinese production of semi-finished goods has grown by over 1 million tonnes and today, with production of 2.5 million tonnes, not only has China exceeded the level of production of the United States (which vaunts about 1.4 million tonnes), but is also producing volumes close to that produced by the whole of Western Europe.

The group's industrial production is carried out in the following areas:

Turnover excluding raw materials

(Millions of Euros)	Area of operations							
	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**314.0**	*37.1%*	**533.3**	*62.9%*	**0.0**	*0.0%*	**847.3**	*100.0%*
2005	**277.1**	*36.6%*	**478.0**	*63.1%*	**3.0**	*0.4%*	**758.1**	*100.0%*
Change %	*13.3%*		*11.6%*		*N/A*		*11.8%*	

In 2006, turnover of **industrial products**, excluding the value of raw materials, amounted to 63% of total sales, while that of **construction products** represented 37%.

The **construction market** is an important outlet for the Group's production. Copper sheet is used for roof covers, accessories and façades; copper tubes are used in significant quantities in domestic bathroom and heating equipment; brass plates and brass and bronze fittings are used in internal house finishings. Brass bars are also used in the manufacture of taps, handles, locks, valves and various other accessories.
After the difficulties recorded in 2005, the European construction market showed some signs of recovery, with more dynamic growth in France and Spain, and construction investment consolidation in Germany and the United Kingdom. The Italian market recorded a slight amount of growth (+0.5%).
The division dealing with **copper sheets** used for roof covers recorded a negative year. Contributing to this trend were developments in the Italian construction sector, the high price of raw materials and strong competitive pressure from Central/Eastern Europe. However, the launching of new products and reinforcement in marketing activity allowed the group to acquire supply/procurement contracts for some high-profile urban development plans.
There was a more satisfactory situation regarding **tubes used for bathroom and heating applications**. Despite a contraction in demand linked to the weakness of the construction sector and the aggressive entry of alternative materials introduced due to the high price of copper, the group reacted by investing in the launch of new products and with strong marketing campaigns in some key Central/Eastern European countries, such as Russia and Poland, and in the Middle East.
Brass bars and fittings for use in the production of taps and domestic connections recorded a strong recovery in demand during 2006, benefiting from the end of the heavy de-stocking process that occurred in 2005 and the lower level of Chinese fittings imports.

Semi-finished products in copper and copper-alloys for industrial use are employed to a vast extent in all the various sectors of industry, in the auto sector, in electric and electronic components, in air conditioning and refrigeration equipment, for domestic fixtures and fittings and in engineering in general.
A reversal of the industrial production trend recorded in Europe in 2006 (+3.6% in the 25 EU member states) caused an increase in demand for semi-finished products for industrial use, resulting in overall superior demand (an average of over +5%) on corresponding 2005 levels. Germany, where manufacturing was a particularly dynamic sector (+5.1%), was without doubt the main driver of this uptake.
A closer look at the individual divisions shows that the most encouraging signs came from electrical goods, air conditioning, refrigeration and thermal exchange. Smaller increases appeared in the white goods and automobile sectors however, while demand from domestic fixtures and fittings was very weak.

Bars and brass wire used in making electronic and electromechanical components demonstrated a significant uptake during 2006. Group sales in this sector grew thanks to the availability of a vast range of alloys and products mainly for sectors with a high level of qualitative requirements.
In line with the production increases recorded in the steel sector, optimum results were obtained in 2006 from the sector of **products for the use in the steel industry**. Prospects for 2007 are positive in the entire sector: The increase in production and the strong investments expected in countries with high rates of development such as India and China, together with good growth in the rest of the world, should sustain demand in products for use in the steel industry.
The **special cables** sector obtained sales results in line with forecasts, despite a drop in global consumption of mineral insulation cables due to the sharp acceleration of raw materials prices.

Operating profit

(Millions of Euros)	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**67.6**	*53.9%*	**62.9**	*50.2%*	**(5.1)**	*–4.1%*	**125.4**	*100.0%*
2005	**22.3**	*49.8%*	**20.5**	*45.8%*	**2.0**	*4.5%*	**44.8**	*100.0%*
Change %	*N/A*		*N/A*		*N/A*		*N/A*	

Assets by sector

(Millions of Euros)	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**612.4**	*30.0%*	**1,018.6**	*49.9%*	**411.5**	*20.1%*	**2,042.5**	*100.0%*
2005	**546.4**	*29.7%*	**958.9**	*52.1%*	**336.9**	*18.3%*	**1,842.2**	*100.0%*
Change %	*12.1%*		*6.2%*		*N/A*		*10.9%*	

Liabilities by sector

(Millions of Euros)	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**232.2**	*15.0%*	**389.9**	*25.2%*	**925.1**	*59.8%*	**1,547.2**	*100.0%*
2005	**197.6**	*12.9%*	**342.5**	*22.4%*	**986.9**	*64.6%*	**1,527.0**	*100.0%*
Change %	*17.5%*		*13.8%*		*–6.3%*		*1.3%*	

Depreciation, amortisation and write-downs

(Millions of Euros)	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**17.3**	*32.2%*	**36.4**	*67.8%*	**0.0**	*0.0%*	**53.7**	*100.0%*
2005	**20.9**	*29.3%*	**50.5**	*70.7%*	**0.0**	*0.0%*	**71.4**	*100.0%*
Change %	*–17.2%*		*–27.9%*		*N/A*		*–24.8%*	

Investments

(Millions of Euros)	Construction products		Industrial products		Consolid. and other		Total Group	
2006	**17.3**	*34.5%*	**28.7**	*57.2%*	**4.2**	*8.4%*	**50.2**	*100.0%*
2005	**11.4**	*25.9%*	**32.6**	*74.1%*	**0.0**	*0.0%*	**44.0**	*100.0%*
Change %	*51.8%*		*–12.0%*		*N/A*		*14.1%*	

Employees at 31 December

(Number of employees)	Construction products		Industrial products		Consolid. and other		Total Group	
31.12.2006	**2,173**	*32.9%*	**4,430**	*67.0%*	**6**	*0.1%*	**6,609**	*100.0%*
31.12.2005	**2,160**	*32.7%*	**4,309**	*65.2%*	**144**	*2.2%*	**6,613**	*100.0%*
Change %	*0.6%*		*2.8%*		*–95.8%*		*–0.1%*	

Investments

Investments for the industrial units amounted to Euro 50 million in 2006 (Euro 45 million in 2005).
The investment continued, especially in sectors that are considered strategic for the future of the Group, and which are focused on the optimisation and specialisation of plant and processes. Half of the investments made were related to the sheeting sector, and the other half were divided in practically equal parts amongst the tubes and special/engineering products sectors.
Investments were made which aimed to improved competitiveness in the sectors of copper and steel sheeting used in electronics. Investments were made and are underway for further improvements in the performance of the use of metals in smelting plants similar to those that have been attained, and investments are underway in the post-processing phase of sheeting aiming at attaining excellence in terms of the finished product.
All of the Group's industrial units are involved in programmes of environmental protection, placing particular attention — thanks to the application of cutting-edge technology — on the recycling of the residues from processing and on the consumption of water, which is purified through special closed-circuit plants used in the production cycle. This allows us to reduce the use of such a precious element.

Financial Information

The Group's **net financial position** at 31 December 2006 amounted to Euro 534 million, a decrease of Euro 25 million over the end of December 2005.
The following table shows the Group's consolidated financial position in detail:

(Thousands of Euros)	31.12.2006	31.12.2005
Short-term financial payables	182,723	234,146
Long term financial payables	487,353	459,379
Financial payables to non-consolidated Group companies	80,688	18,472
Total financial payables	**750,764**	**711,997**
Cash and cash equivalent	(162,098)	(151,992)
Short-term financial receivables	(53,425)	0
Financial receivables from non-consolidated Group companies	(915)	(920)
Total liquid funds and financial receivables	**(216,438)**	**(152,912)**
Total net financial position	**534,326**	**559,085**

We specify that the figures shown above reporting the financial situation exclude potential payments regarding the two fines announced by the European Community against the Group's industrial companies for two offences relating to competition matters for a total of Euro 107 million. These fines will generate cash flows only on the completion of the full proceedings before the community bodies having jurisdiction on this issue, and only for an amount to be confirmed. Up until that date, payment is guaranteed by cautionary deposits of Euro 17 million and by bank sureties of Euro 90 million. The length of the proceedings will, however, lead to interest expense.

As previously stated, a growth in exposure to customers due to an increase in raw material prices was compensated for by a higher level of non-recourse factoring transactions for trade receivables, which went from Euro 60 million at the end of 2005 to Euro 367 million. These transactions were made possible thanks to new bank loans that were obtained from the Group's banks, based on agreements signed on 30 September 2006.

Cash flow for the year may be summarised as follows:

Consolidated cash flow statement indirect method (Thousands of Euros)	**December 2006**	**December 2005**
(A) Cash and cash equivalents at beginning of year	**151,992**	**74,035**
Profit before taxation	84,133	7,362
Depreciation and amortisation of tangible fixed assets and intangible assets	53,421	55,030
Write-downs of current assets	1,439	1,538
Write-downs (write-ups) of non-current assets other than financial assets	(2,027)	16,452
Write-downs (write-ups) of current/non-current financial assets	1,149	183
Net interest matured	33,452	29,617
Capital losses (gains) on non-current assets	(789)	(5,292)
Results of associates accounted for using the equity method	(216)	(317)
Changes in pension funds and employees' leaving entitlement	681	(3,125)
Changes in provisions for risks and charges	14,653	9,148
Decrease (increase) in inventories	(238,887)	(56,352)
(Increase) decrease in current receivables	108,694	(24,829)
Increase (decrease) in current payables	55,512	(2,568)
Foreign exchange differences	96	113
Net interest paid in the year	(33,366)	(29,529)
Current taxes paid and refunded during the year	(5,004)	(5,182)
(B) Cash flows from operating activities	**72,941**	**(7,751)**
(Increase) in non-current tangible fixed assets and intangible assets	(50,242)	(44,818)
Decrease in non-current tangible fixed assets and intangible assets	3,512	15,105
(Increase) decrease in equity investments	(479)	–
(Increase) decrease in available-for-sale financial assets	–	–
Increase/decrease in other non-current assets/liabilities	16	(4,106)
Dividends received	1,750	426
(C) Cash flows from investing activities	**(45,443)**	**(33,393)**
Increase in shareholders' equity for consideration	128,835	–
Increase (decrease) in current and non-current financial payables	(84,036)	124,217
(Increase) decrease in current and non-current financial receivables	(60,877)	(5,116)
Dividends paid	(1,314)	–
(D) Cash flow from financing activities	**(17,392)**	**119,101**
(E) Increase in cash and cash equivalents (B + C + D)	**10,106**	**77,957**
(F) Cash and cash equivalents at end of year (A + E)	**162,098**	**151,992**

Personnel

At 31 December 2006, the Group had 6,609 employees, a decrease of 3.5% compared to 31 December 2005 (at which time it had 6,847 employees).

Average for the year	**2006**		**2005**		**Change %**
Managers and clerical staff	1,782	*26.7%*	1,886	*26.8%*	*–5.5%*
Labourers and technicians	4,896	*73.3%*	5,151	*73.2%*	*–5.0%*
Total employees	**6,678**	***100.0%***	**7,037**	***100.0%***	***–5.1%***

Research and Development

Research programmes are coordinated at a Group level and implemented at the two Research and Development Centres in Osnabrück (Germany) and Fornaci di Barga (Italy).
In recent years the Research area has been involved in a business activities refocusing plan, which is concentrating its resources on base metallurgy research, while activity relating to qualitative processing and control technologies has been transferred to the direct responsibility of the individual production divisions.

The primary areas of research involve the identification of innovative copper-based alloys, aimed at broadening the fields in which copper may be employed by exploiting its specific features of conduction and resistance to the utmost.

Research is also being carried out into the treatment of product surfaces, from both a functional and aesthetic point of view, especially in connection with those to be used in the building sector. This is in order to meet the new demands posed by the market and by customers.

Research and development expenses are booked to the income statement.

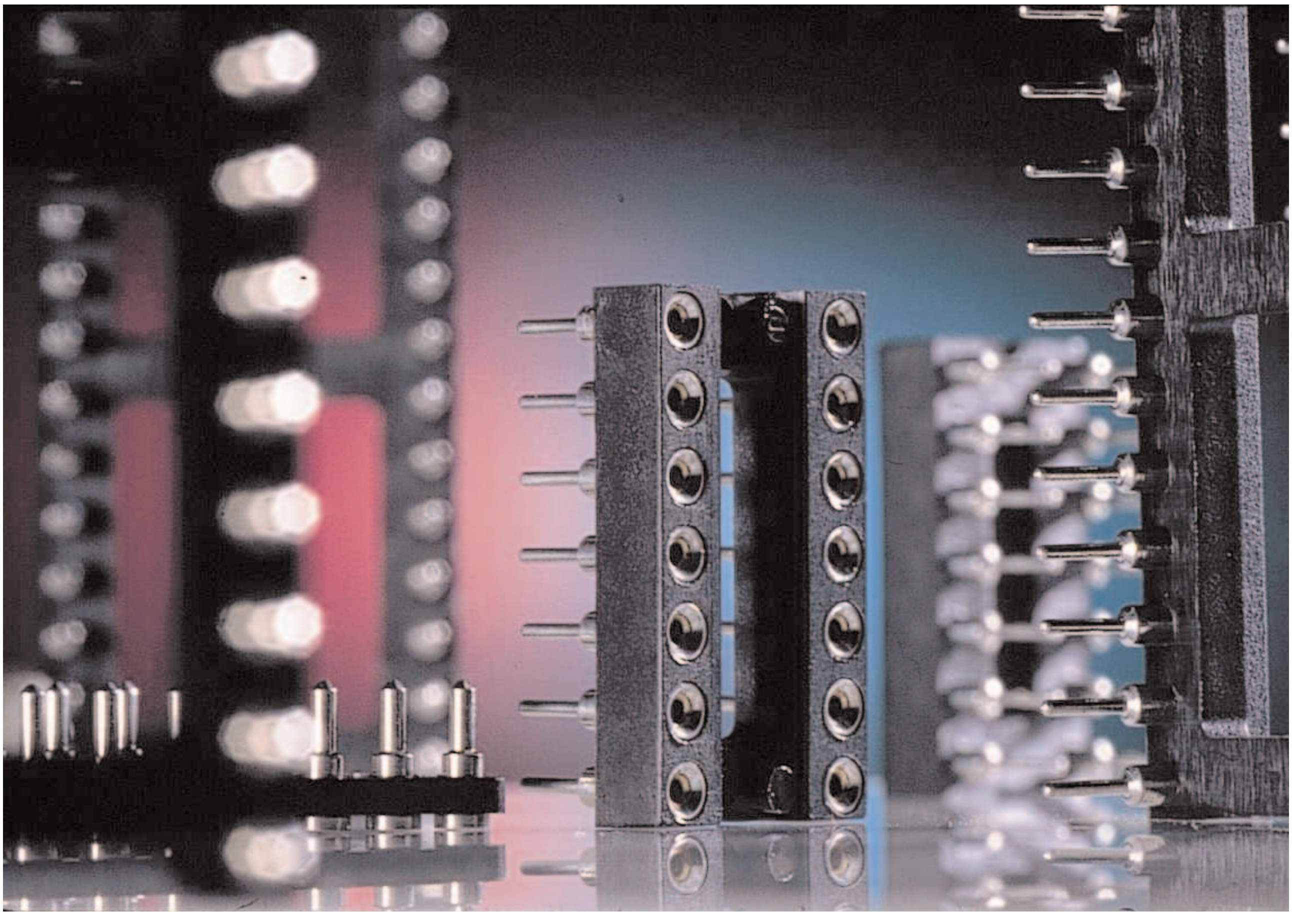
Forecast of Operations

Significant growth in operating profits is forecasted for the first quarter of this year compared to those of the previous year, in line with improving trends that already appeared in the last two quarters of 2006.
If the European macroeconomic outlook remains positive as expected — in the next months as well — the Group's financial results for the entire 2007 financial year could show further improvements in profitability on those attained in 2006.

Related Party Transactions

Transactions with related parties, including intra-group operations, are not classifiable as either atypical or unusual, and form part of the ordinary business carried out by Group companies.

The effects arising from relations between KME Group S.p.A. and its subsidiaries are disclosed in the financial statements of the Parent Company and in the notes to those financial statements, and are eliminated together with any relations between the subsidiaries themselves during the preparation of the consolidated financial statements.



Components for electronic applications.

THE PARENT COMPANY

The 2006 financial statement of the Parent Company **KME Group S.p.A.** closed with a net profit of Euro 7.2 million.

(Thousands of Euros)	2006	2005
Dividends from KME A.G.	0	0
Commissions	2,913	1,289
Cost of stock options	(473)	0
Operating costs	(4,713)	(4,225)
Financial income (expense), net	(1,584)	(3,325)
Ordinary profit (loss)	**(3,857)**	**(6,261)**
Extraordinary income (expense)	498	6,701
Profit (loss) before taxation	**(3,359)**	**440**
Taxation	10,565	955
Net profit (loss)	**7,206**	**1,395**

Ordinary profit for 2006 improved due to the higher commissions for services made to Group companies, and lower financial expenses due to the extinction of the subordinated Euro 130 million loan given by the Parent Company G.I.M. S.p.A. in order to transfer funds resulting from the increase in share capital approved by the shareholders in the general meeting on 19 May 2006, as well as to the adjustment of the fair value of G.I.M. S.p.A. savings shares for Euro 1 million.
The **cost of stock options** is the measurement of the expense for 2006 linked to the KME Group S.p.A. stock option plan that is set aside for executive directors and Group managers, which was executed in July 2006. The characteristics of this plan are reported elsewhere in this report.
Extraordinary items experienced a large drop, while last year they reached high levels. The most significant asset item of 2006 was the capital gain made from the sale of property (Euro 1.5 million), largely compensated for by consultancy charges for the Group's reorganisation programmes (Euro 1.1 million).
The accounting item **taxation** was positive since it includes tax benefits of Euro 10.5 million deriving from the use of the Parent Company's deferred tax assets to pay the taxes of the Group's Italian subsidiaries, who exercised their option to take advantage of the national tax consolidation regulation.

The main figures of the balance sheet of the Parent Company KME Group S.p.A. are set out as follows:

ASSETS (Thousands of Euros)	31.12.2006	31.12.2005
Investment property	10,535	8,985
Shareholdings in KM Europa Metal AG	303,156	302,670
Non-current assets	**313,691**	**311,655**
G.I.M. savings shares	5,242	4,620
Various net receivables	9,684	2,824
Total assets	**328,617**	**319,099**

LIABILITIES (Thousands of Euros)	31.12.2006	31.12.2005
Share capital	319,643	189,775
Reserves	7,920	7,914
Shareholders' equity	**327,563**	**197,689**
Net financial position	**(6,152)**	**(9,985)**
Subordinated loan from G.I.M. S.p.A.	0	130,000
Profit (loss) for the year	**7,206**	**1,395**
Total liabilities and shareholders' equity	**328,617**	**319,099**

Shareholders' equity increased by Euro 129.9 million following the transaction approved by shareholders in the extraordinary meeting on 19 May 2006. The financial proceeds form this transaction were used to reimburse the subordinated loan of Euro 130 million given by G.I.M. in 2005.

There is a positive **current net financial position** of Euro 6.1 million.

(Thousands of Euros)	31.12.2006	31.12.2005
Short term payables to banks	102	123
Long term payables to banks	582	684
Short term payables to subsidiaries	56,016	15,440
Total financial payables	**56,700**	**16,247**
Cash and liquid funds	(376)	(9,378)
Financial receivables from subsidiaries and associates	(62,476)	(16,854)
Total cash, liquid funds and financial receivables	**62,852**	**(26,232)**
Total net financial position	**(6,152)**	**(9,985)**

The following analysis of cash flows for the year shows the reasons for this change:

Cash flow statement (Thousands of Euros)	2006	2005
(A) Cash and cash equivalents at beginning of year	**9,379**	**8,434**
Profit (loss) before taxation	(3,359)	439
Depreciation and amortisation of tangible fixed assets and intangible assets	–	143
Net interest matured	3,186	1,926
Losses (gains) on non-current assets	(43)	–
Provisions for pension funds and similar	446	(131)
Allocation to provisions and other funds	(934)	2,348
(Increase) decrease in current receivables	(7,337)	51,335
Increase (decrease) in current payables	463	(3,954)
Net interest paid in the year	(3,100)	(1,838)
Current taxes (paid) and refunded during the year	10,532	–
(B) Cash flows from operating activities	**(146)**	**50,268**
(Increase) decrease in non-current tangible fixed assets and intangible assets	(1,507)	7,710
Increase/decrease in other non-current assets/liabilities	(8)	(2)
(Increase) decrease in equity investments	–	(119,563)
Dividends received	415	–
(C) Cash flow from investment activities	**(1,100)**	**(111,855)**
Increase in shareholders' equity for consideration	128,835	
Increase (decrease) in current and non-current financial payables	(89,655)	79,386
(Increase) decrease in current and non-current financial receivables	(45,622)	(16,854)
Dividends paid	(1,314)	–
(D) Cash flow from financing activities	**(7,756)**	**62,532**
(E) Net result of cash and cash equivalents (B + C + D)	**(9,002)**	**945**
(F) Cash and cash equivalents at end of year (A + E)	**377**	**9,379**

Forecast of Operations

Since the result of the Parent Company is determined not only by the dividends of the subsidiary KM Europa Metal A.G., whose income depends on industrial performance, please refer to the forecasts on the previous pages for the expected trends of the Group as a whole.

Relations with Subsidiaries

As part of its role as Parent Company, the KME Group provided assistance to Group companies. This activity generated income and expense as follows, divided below by company:

(Thousands of Euros)	31.12.2006		31.12.2005	
	Income	Expense	Income	Expense
G.I.M. S.p.A.	75		120	(111)
Europa Metalli S.p.A.	2,172	(95)	927	(261)
KM Europa Metal A.G.	258		197	
Tréfimétaux S.A.	516		257	
Total	**3,020**	**(95)**	**1,501**	**(372)**

Receivables from subsidiaries at 31 December 2006 are as follows:

(Thousands of Euros)	31.12.2006	31.12.2005	Absolute change	Change %
Financial receivables				
Europa Metalli S.p.A	6,034	3,273	2,761	*0.84*
KM Europa Metal A.G.	54,191	11,334	42,857	*(0.22)*
Tréfimétaux S.A.	817	1,340	(523)	*(0.92)*
Immob. Agricola Limestre	1,433	913	520	*0.6*
Total	**62,476**	**16,860**	**45,616**	***2.71***

Current accounts and the loan made by G.I.M. S.p.A. generated net interest expense of Euro 5.2 million.

* * *

For further information and analyses of consolidated figures of the Parent Company, please see the supplementary notes to the financial statements.

LITIGATION

There are no new matters to report for 2006 in connection with the two European Community proceedings that involve infractions of competition laws by some of the Group's industrial companies.

The appeal against the commission's decision regarding both of the proceedings will be heard before the EU Court of First Instance. At the publication date of this document, the date had not yet been set for the start of the hearing.

Federal class action suits in the states of Tennessee, California and Massachusetts are still pending regarding the above infractions. We believe that it is useful here to summarise the standing of these actions below in detail:

- in Tennessee: a collective class action suit was launched regarding tubes for bathroom and heating applications. Moreover, a collective class action suit was put forth as a result of a meeting of individuals bringing separate class action suits regarding industrial tubes. Both suits are pending before the U.S. federal court;
- in California: a collective class action suit regarding tubes for bathroom and heating applications is pending before the California state court. This may be waived since these claimants have in the meanwhile put forth a collective class action suit before the U.S. federal court against both tubes for bathroom and heating applications and industrial tubes, which on a Group level was until now reported to KME American Inc.;
- in Massachusetts: a class action suit is pending before the Massachusetts state court. The claimants have recently sustained that the suit involves not only bathroom and heating application tubes, but also industrial tubes.

Last October, the Tennessee federal court ruled that it did not have jurisdiction over the matter, and therefore struck down the collective class action suit regarding bathroom and heating application tubes, on grounds that took into consideration the Group's reasoning, which stated that the claimants merely copied the contents of the European Commission's decision without making any further points in order to sustain their accusations that the Group carried out antitrust activities in the United States. In the same month of October, the claimants presented their appeal against the federal court's decision. The trials pending before the California and Massachusetts state courts have been suspended while awaiting the final decision of the federal courts.
At the present state, it is not however possible to ascertain the responsibility of the U.S. Group companies, in that they maintain that the actions made against them are without foundation.

Regarding the original suit against the subsidiary Europa Metalli S.p.A., along with other parties, requesting payments for environmental damages occurring around their industrial areas — which included the plant located in Brescia, the suit mentioned in our half year report — the next hearing has been set for 22 May 2008 regarding the decisions only on the preliminary objections made. We believe that the fact that the initial claimants declared that they would "not accept an adversarial approach" with the parties being sued is favourable to the Group. The total damages requested amount to Euro 8 million, in addition to biological damages and the reimbursement of any decontamination costs that may be sustained. At the moment it is not possible to make any estimates on the outcome of the suit.

Regarding the suits that directly involve the Company, please note that the suit against ex Chairman Luigi Orlando is pending before the Rome Court of Appeal. The next hearing, announcing the conclusion of the suit, has been set for 12 June 2009.
The hearing for the second and final civil suit, involving the means under which the exercising of the right to withdrawal took place during the merger of Europa Metalli - LME S.p.A., has been set for 29 March 2007 before the Italian high court. Please note that first and second degree decisions ruled for the Company.

There are no developments in the two cases pending before the court of Hanover regarding the squeeze out and merger transactions in Germany, while the suit launched to recover receivables in Greece was appealed by the defendant, after initial decisions ruled for the Company. The next hearing is set for 27 April 2007.

Lastly, a civil action suit for damages has recently been made against the Company for a total of Euro 25 million, again regarding environmental damages at the Brescia plant. This concerns construction and real estate investment activities made by third parties following its conveyance in 1998, which would have brought about high charges for its environmental recovery. The suit is based on the fact that the Company has incorporated all its subsidiaries that carried out industrial activities which are assumed to have polluted the area.
The next hearing has been set for 19 April 2007, and, as in the other suit involving this plant, it is not possible to make any forecasts regarding the outcome of the dispute.

IMPORTANT EVENTS AFTER THE CLOSE OF THE FINANCIAL YEAR

There are no matters to report.

RESULT FOR THE YEAR AND PROPOSED RESOLUTIONS

The year 2006 closed with a **net profit** of Euro 7,205,770.

Acknowledging the Report of the Statutory Auditors and the Report of the Independent Auditors, we invite you to approve the following resolution:

The Shareholders of KME Group S.p.A., meeting in ordinary session at the company's offices in Via dei Barucci, 2, Florence, acknowledging the Report of the Statutory Auditors and the Report of the Independent Auditors

resolve

a) to approve the Report of the Board of Directors for the year ended 31 December 2006, the financial statements as a whole and as single items and entries, and with the proposed provisions and utilisations, which show a net profit of Euro 7,205,770;

b) to deduct the "capital increase transaction charges" of Euro 1,037,925, and the integration of the "reserve for parent company shares in portfolio" of Euro 101,558, to the "reserve for first adoption IAS/IFRS", thus taking them from Euro 2,784,099 to Euro 1,644,616;

c) to allocate the net profit of Euro 7,205,770 as follows:

– 5% to the legal reserve	Euro	360,289
– to the savings shares (*) at a rate of one dividend of Euro 0.1086 share (**) including preference dividends for the 2006 financial year of Euro 0.0362, and preference dividends for the two previous 2005 and 2004 years, as provided for in the company bylaws, a total of	Euro	6,206,637
– to carry forward the balance of	Euro	638,844

Florence, 20 March 2007

The Board of Directors

(*) Net of the 65,000 Savings shares currently held by the Company, or those held by the Company at the dividend distribution date, withdrawing the necessary amount from the balance of the profits carried forward.

(**) The dividend distribution date will be 7 June 2007, dividend coupon no. 18 on 4 June 2007.

INVESTOR INFORMATIONS

Investor relations:
Tel: 055-44111
Fax: 055-4411681
E-mail: info@kmegroup.it
Website: www.kmegroup.it

(Euros)	
Number of ordinary shares	693,469,382
Number of savings shares	57,216,332
Share capital	319,672,506.80
Ordinary and savings shares do not have nominal values	
KME Group warrants 2006-2009 in circulation	74,125,937

The KME Group S.p.A. has been listed on the stock exchange since 1897.

During the year closed on 31 December 2006, KME Group shares recorded the following changes:

- **KME Group ordinary shares** recorded a maximum price of **Euro 0.596** in December, and a minimum price of **Euro 0.326** in June;
- **KME Group savings shares** recorded a maximum price of **Euro 0.571** in December, and a minimum price of **Euro 0.349** in February.

Stock Exchange price (end 2006 – Euros)	
Ordinary KME Group	0.573
Savings KME Group	0.560
KME Group warrants	0.391

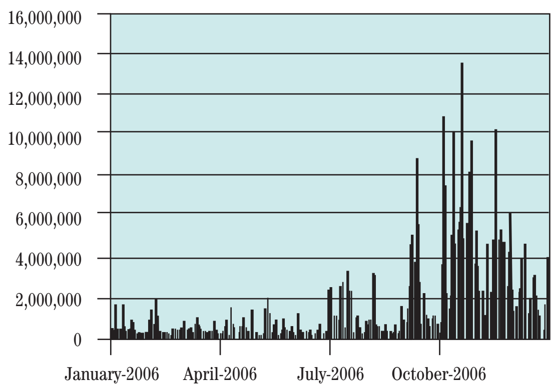
(Euros)	
Capitalisation - ordinary shares	397,357,956
Capitalisation - savings shares	32,041,146
Capitalisation	**429,399,102**

Shareholders	
Number of ordinary shareholders	**13,000**
Main shareholders	
G.I.M. S.p.A.	53.8%
No other shareholders declared owning more than 2% of share capital	

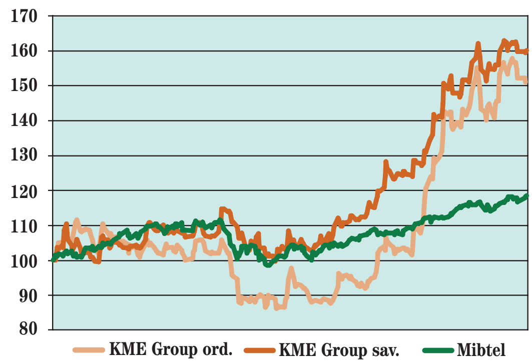
Dividend per share (Euros)	**2003**	**2004**	**2005**
Dividend per ordinary share	–	–	–
Dividend per savings share	–	–	0.023

Stock Market performance (Euros)	**End of 2005**	**End of 2006**	**Change**
KME Group ordinary	0.405	0.573	41.5%
KME Group savings	0.371	0.560	50.9%
Mibtel	26,778	31,892	19.1%

KME Group ordinary share volumes 2006



Share prices 2006



REPORT ON CORPORATE GOVERNANCE AND APPLICATION OF THE CORPORATE CODE OF CONDUCT ADOPTED IN 2006

The changes made in the Italian "TUF", or Consolidated Text on Financial Intermediation (henceforth the "TUF"), made corporate governance regulations even more relevant and visible than they already were. Please remember that article 124 *ii* of the TUF required listed companies to provide information as to the extent of their adherence to the codes of conduct recommended by the companies managing regulated markets, and by trade associations, in accordance with the terms and means set by CONSOB. The consecutive article 124 *iii* provided that CONSOB set the rules by which this information is published.

In a review of their Regulations for Issuers adopted through decision no. 11971/99, CONSOB recently indicated the terms and means by which this information is reported, as well as the related types of publication, specifying that such a Report must:

- be prepared according to guidelines set by the issuer of the Code of Conduct;
- give data regarding the adherence to each requirement of the Code;
- give grounds for the failure to comply with any requirements;
- highlight any conduct which may not conform to these requirements;
- be published in a dedicated section of the Company's web site;
- be deposited at the Company's registered office no later than 15 days hitherto the date of the meeting set to approve the financial statements.

Moreover, CONSOB also stated that the Report must be included in full in the Report of the Board of Directors or in an attachment thereof, and that notice must be given that it has been deposited with CONSOB, Borsa Italian S.p.A. and the market.

We also remind you that in 2006 the Code of Conduct as set by Borsa Italiana S.p.A.'s Corporate Governance Committee (henceforth "the Code of Conduct" or simply "the Code") has been reviewed, and that the Company's Board of Directors at their meeting on 10 November 2006, giving notice to the market through a press release issued simultaneously with the Quarterly Report at 30 September 2006, declared that they would adopt the 2006 edition of the Code, and would gradually proceed to introduce its principles in the Company structures, giving notice of the activities made towards the completion of this objective in the Report on Corporate Governance prepared for the 2006 financial statements.

This Report on Corporate Governance, which accompanies the Report of the Board of Directors for the financial statements closed at 31 December 2006, was prepared according to indications set in the 2006 edition of the Code of Conduct, and aims at describing the extent to which the company's structure complies with the provisions of the Code, identifying any situation in which it may differ and explaining the reason for this.

Please remember that the Company has been providing corporate governance information as from the financial statements closed on 30 June 2000, continuously improving the quality and quantity of this information. These Reports are available on the website www.kmegroup.it within the financial statements of the individual financial years. As from the year closed 31 December 2006, the corporate governance reports are available in a dedicated section of the site.

Indications furnished by Assonime in their memo no. 5 dated 12 February 2007 were considered in the preparation of this report, as were the guidelines issued by Borsa Italiana S.p.A. and in the "Guide to the preparation of the Report on Corporate Governance" issued by Assonime jointly with Emittenti Titoli S.p.A. (2004 edition).

As an additional introductory comment, we remind you that the so-called "Savings Law", which came into effect in January 2006 and was reviewed in December of the same year, has led to numerous changes in the provisions of the Civil Code for corporate matters regarding the TUF, changes that in many cases involve the issuance of specific regulations by CONSOB and that will require the company's bylaws to be revised by 30 June 2007. As a consequence, shareholders will also be convened in an extraordinary meeting to make the necessary changes to the bylaws. Please note that the current version of the bylaws is available on the KME Group website at www.kmegroup.it.

Obviously, the issuance of new provisions on such strict terms and the brief period allowed for them to be applied to the Company (the most recent changes in fact were put into effect on 25 January 2007, and the CONSOB regulations have not yet been finalised) have caused this annual report to be more weighty in terms of content and preparation, and therefore also in terms of perusal, which is especially complex also considering the fact that the company bylaws will soon be changed.

For simplicity's sake, we would like to inform you in advance, with convenient references, of the matters that will have to be addressed for the change of the bylaws.

Therefore, we would like to invite our shareholders to peruse this Report alongside the one that will be issued regarding the updating of the bylaws, in order to have a complete and full view of the situation regarding:

- the Company's organisational structure and gradual development;
- the changes that will be subject to shareholder approval at the extraordinary meeting.

* * *

This report, which may also be found on the website www.kmegroup.it, is divided into two parts:

a) the first part is dedicated to the system of corporate governance adopted by the company;

b) the second part has as its objective a comparison between the system adopted and the provisions of the Code of Conduct.

The actions taken and those planned for the implementation of the above Code into Company structures are highlighted in both sections.

General Part

The Company has a traditional corporate governance structure, with a General Meeting of Shareholders, a Board of Directors and a Board of Statutory Auditors.

Share Capital

At the approval date for this Report (i.e. in reference to the last exercising of the company warrants on 28 February 2007), Company share capital was Euro 319,685,924.75 and composed of 750,724,051 shares, of which 693,507,719 are ordinary shares and 57,216,332 are savings shares, all without nominal value according to approvals made at the Extraordinary General Meeting on 19 May 2006.

At the date of approval of this Report, there were 74,087,600 warrants outstanding, issued through the same Extraordinary General Meeting approval, the possible exercising of which (at a unit price of Euro 0.35) by the final date at 11 December 2009 could cause the issue of a maximum of 74,087,600 ordinary shares without nominal value and with a corresponding share capital increase of a maximum of Euro 25,930,660. The possible exercising of these warrants would cause a change in share capital, and consequently of the Company bylaws on a monthly basis. Updates regarding this matter are reported to the market through a notice (for more information on the "NIS" market information system please see the following paragraph entitled "Shareholder and Market Communications"), and thereafter displayed on the www.kmegroup.it website.

G.I.M. - Generale Industrie Metallurgiche S.p.A. is the controlling shareholder, with 53.83% of the ordinary shares. We remind you that at the date of this Report a merger of the above-mentioned Company with Intek S.p.A. is currently being finalised.

The Company's ordinary shareholders number approximately 13,000, a figure based on the results from the share capital increase that was concluded in August 2006. Besides the controlling shareholder, no other shareholder declared possessing more than 2% of ordinary shares.

For the sake of completeness, we remind you that the agreement between G.I.M. - Generale Industrie Metallurgiche S.p.A. shareholders and Pirelli & C. S.p.A. was resolved amicably on 19 December 2006.

The General Meeting of Shareholders

The General Meeting of Shareholders is made up of ordinary shareholders and has the responsibilities and competence provided for by the Civil Code and the TUF.

Company bylaws permit the Board of Directors to approve resolutions regarding the location of the company's registered office and secondary office, the issue of convertible bonds, the merger of subsidiaries and amendments to the bylaws for withdrawal and for modification as the result of new legislation.

Provisions regarding the correct constitution of the meeting and regarding voting procedures are those applicable pursuant to articles 2368 and following of the Civil Code and article 126 of the TUF.

For the provisions that regulate shareholder meeting participation, please see the extra sections of our Report regarding the proposed changes of articles 10 (convening of shareholder meetings) and 11 (participation and representation at shareholder meetings), specifically the changes relating to the recent provisions governing minority shareholders for the nomination of Directors and Auditors. We will also propose that the convocation of shareholders' meetings be announced in a daily newspaper as an alternative to the Official Journal.

One aspect that differs from the Code is that the Company has not adopted its own "Regulations for Shareholders' Meetings", as the respective provisions are already contained in Chapter III of the bylaws.
To protect the rights of shareholders regarding this matter, we remind you that article 12 of the bylaws expressly requires the Chairman of the Meeting to guarantee the correct proceedings of the meetings, overseeing and regulating debate and intervening on the length of individual contributions if necessary.

Savings shareholders may not participate in the ordinary shareholders' meetings, and the rights of the former are displayed in articles 5, 8 and 28 of the bylaws. Their representative, who may participate and intervene in ordinary shareholder meetings and whose rights are displayed in article 26 of the bylaws, is Mr Romano Bellezza, nominated for the 2006/2008 period at the special savings shareholders' meeting that was held on 5 May 2006.

The Board of Directors

The Board of Directors has the widest powers for the organisation, administration and ordinary and extraordinary management of the company (article 14 of the bylaws). The Board determines the strategic line to be followed by the company and takes such action necessary to achieve this, guarantees the continuity of administration and delegates executive directors (articles 15 and 16 of the bylaws).

The present Board of Directors was appointed by shareholders' general meeting on 19 April 2006 for a term covering the years 2006, 2007 and 2008, expiring at the general meeting of shareholders which will be held to approve the financial statements for the year ending 31 December 2008.

The Board may consist of a varying number of Directors, from a minimum of nine to a maximum of twelve. The general shareholders' meeting held on 19 May 2006 set the number of directors at nine, compared to the ten directors previously. The names of the members of the Board, together with an indication of their respective functions, including those on committees, are as always stated at the beginning of the booklet issued on the occasion of shareholders' meetings and on the publication of the annual financial statements and half-year and quarterly reports.

Specifically regarding the new provisions regarding representation of minority shareholders on the Board of Directors, we note that no Director was appointed through the presentation of a voting list by a minority shareholder, and article 17 of the bylaws needs to be updated at an extraordinary meeting of shareholders.

The Board of Directors meets at least four times a year (article 18 of the company's bylaws). Meetings may also be held by teleconference or by videoconference (article 19 of the company's bylaws) and are called at reasonable notice with notification of the agenda of the matters to be discussed (article 18 of the company's bylaws). Minutes of the meetings are distributed, keeping in mind the need to ensure the confidential nature of some individual matters.

Resolutions of the Board are passed with the attendance of the majority of directors holding office and by an absolute majority of those attending. In the case of a split decision, the Chairman has the casting vote (article 19 of the company's bylaws).

The Board of Directors may establish committees, determining the powers, responsibilities and competence of these (article 14 of the company's bylaws), and has provided for the establishment of the following committees:

- the Committee for Internal Control;
- the Compensation Committee.

Their members and duties are detailed further on in this report.

The Board of Directors did not establish an Executive Committee — as it had nominated a Managing Director — nor a Nominations Committee, since the Company has a controlling shareholder.

The Board of Directors met nine times during the year compared to ten times in the previous year.

The individual attendance records of each meeting are shown in a table at the end of this Report. However, we inform you that participation at the meetings by Directors and Auditors averaged 86% and 77%, respectively.

The Board of Statutory Auditors

The Board of Statutory Auditors governs the observance of laws and bylaws, ensures that the principles of proper company administration are adhered to, especially regarding the organisational, administrative and accounting structures of the Company, and oversees its physical workings.

The present Board of Statutory Auditors was appointed by G.I.M. - Generale Industrie Metallurgiche S.p.A., at the general meeting of shareholders held on 19 May 2006, for the years 2006, 2007 and 2008, and therefore will dissolve at the general meeting held to approve the financial statements at 31 December 2008.

The Board consists of three standing members and two alternate members, and, as is the case for the Directors, their names are stated in the periodic accounting documents made available by the company. The following paragraphs give brief curriculum vitae for each member.

Marcello Fazzini (Chairman)

Mr Marcello Fazzini, born in 1932, graduated from the University of Florence in Social Sciences and Economics, and is registered with the National Accountants and Accounting Auditors Boards. He works in Florence. He has held and holds management positions in the administration and control of many important companies, and was the managing director of Banca Toscana S.p.A. from 1986 to 1996. He is involved at a high level in significant Florentine cultural institutions such as the Gabinetto Scientifico Letterario G.P. Vieusseux (as Chairman), and is a co-founder/member of the International University of Art.

Alessandro Trotter (Standing Auditor)

Mr Alessandro Trotter, born in 1940, graduated in Business and Economics, and is registered with the National Accountants and Accounting Auditors Boards. He works in Milan. He holds positions on the Boards of Auditors of many important companies.

Pasquale Pace (Standing Auditor)

Mr Pasquale Pace, born in 1938, graduated in Business and Economics, and is registered with the National Accountants and Accounting Auditors Boards. He works in Bari. He is a member of other Boards of Auditors, and, besides having held judicial offices, is an expert court assessor regarding legal administration and penal matters.

Marco Lombardi (Alternate Auditor)

Mr Marco Lombardi, born in 1959, graduated in Political Science, and is registered with the National Accountants and Accounting Auditors Boards. He works in Florence. He holds positions on other Boards of Auditors and legal boards. He has written various works on tax law.

Angelo Garcea (Alternate Auditor)

Mr Angelo Garcea, born in 1969, graduated in Business and Economics, and is registered with the National Accountants and Accounting Auditors Boards. He works in Florence. He is the author of many works on tax law.

No auditor was appointed through any lists presented by a minority shareholder; according to article 22 of the bylaws, minority shareholders are those owning 3% or less of ordinary shares. Regarding an update of the bylaws, we would like to inform you in advance that this level will probably be changed in light of new provisions on the subject.

Article 22 of the bylaws is entirely dedicated to the Board of Statutory Auditors and, in addition to providing the requisites that must be held by members of the Board and the procedure by which they are appointed, requires that each candidate deposit his curriculum vitae at least two days prior to the shareholders' meeting at which the appointment will be made, instead of the fifteen days prior to the meeting as indicated by the Code of Conduct and the Regulations for Issuers. Moreover, this article provides that Auditors no hold more than five similar roles in other companies listed in Italy, which was already the case hitherto the introduction of a similar provision in article 148 ii of the TUF, and much more specific governance is currently being drawn up by CONSOB.
As indicated above, please see the comments and proposals in the Report of the Board of Directors regarding the changes to article 22 of the bylaws.

The members of the Board declared on appointment that they possess the characteristics of professionalism and honour required by prevailing legislation and the company's current bylaws and stated that they are no impediments to their holding office. Following their appointment, the Board periodically checks that each of its members possesses the requirements of independence based on the criteria included in the combined provisions in articles 10.C.2. and 3.C.1. of the Civil Code.

In this regard, the Board verified that Mr Alessandro Trotter was appointed Standing Auditor of the Company for the first time at the general meeting of shareholders held on 14 November 1997 for the years closed on 30 June 1998, 1999 and 2000, and therefore has held this role without interruption for over nine calendar years over 10 financial years, including the one closed at 31 December 2006.

The Board, in accordance with the optional faculty provided by the Code in evaluating the independence of its members, believe that the Standing Auditor Alessandro Trotter may be held "independent" according to a substantial evaluation of the report that considered both the personality of the subject and the economic and professional "significance" of the role he performs in service of the Company. Please note that Mr Trotter's position will expire upon the approval of the financial statements that will close on 31 December 2008.

Similarly, please note that the Board's inquiry also involved the role of the Chairman of the Board, Mr Marcello Fazzini, which displayed largely the same situation in reference to the current financial year, his ninth consecutive year as auditor. He was first appointed at the general meeting of shareholders held on 28 October 1999 for the financial year closed on 30 June 2000, but had previously been an Alternate Auditor, becoming a Standing Auditor on 8 June 1999, starting his role with the financial year closed on 30 June 1999.

Beyond the formal reference to the calendar year instead of the financial year as per article 3.C.1. letter e), the Board believes, for the same reasons indicated above, that Mr Marcello Fazzini also possesses the necessary requirements of independence.

As a result, the Board gave notice that they had adhered to the provisions of article 149, paragraph I, letter c-*ii* of the TUF, which requires them to oversee the regulations of the physical implementation of the Code of Conduct.

The administration and control positions held by the Auditors in other companies are shown below, and were made available at the general meeting of shareholders in which they were appointed. All Auditors that held such positions during 2006 are included in this list.

The Board of Statutory Auditors performs its activities on a regular basis, attends meetings of the Board of Directors and committees established by that Board and maintains continuous contact with the company's offices, which it addresses directly and in full autonomy. Relations with the Independent Auditors are distinguished by collaboration and by the exchange of data and information.

The fees received by members of the Board are shown in the table below, in accordance with CONSOB provisions:

Name (figures in Euros)	**Position**	**Position held since-to**	**Expiry of position**	**Fees collected for position**	**Non-monetary benefits**	**Bonuses and other incentives**	**Other compensation**
Marcello Fazzini	Chairman	01.01.06-31.12.06	31.12.08	33,429	–	–	27,629 (1)
Massimo Mandolesi	Standing Statutory Auditor	01.01.06-19.05.06	31.12.05	8,556	–	–	–
Pasquale Pace	Standing Statutory Auditor	19.05.06-31.12.06	31.12.08	14,143	–	–	–
Alessandro Trotter	Standing Statutory Auditor	01.01.06-31.12.06	31.12.08	22,803	–	–	–

(1) Fees collected for positions held in subsidiaries.

The Board met six times during the year; there were seven meetings in the previous year. There was 100% attendance by members at these meetings.

Facade in Tecu® Patina – Helmond Palace, Holland.

Offices held by the Statutory Auditors

The following table sets out for each Statutory Auditor the positions held at 31 December 2006 as either Director or Statutory Auditor in stock corporations, in partnerships and in limited liability companies.

Name	Company	Position
Marcello Fazzini	HDI Assicurazioni S.p.A.	Chairman of the Board of Statutory Auditors
	HDI Finanziaria S.p.A.	Chairman of the Board of Statutory Auditors
	FINOA S.p.A.	Chairman of the Board of Statutory Auditors
	Europa Metalli S.p.A.	Chairman of the Board of Statutory Auditors
	Lanificio Roberto Draghi S.p.A.	Chairman of the Board of Statutory Auditors
	F.lli Reali S.p.A.	Chairman of the Board of Statutory Auditors
	InChiaro Assicurazione S.p.A.	Standing Statutory Auditor
Massimo Mandolesi (until 19.05.06)	PREVIRA INVEST SIM S.p.A.	Managing Director
	Cassa Nazionale di Previdenza e Assistenza Ragionieri	Member of the Board of Directors
	CESPA Costruzioni Edili S.p.A.	Chairman of the Board of Statutory Auditors
	Bluestone S.p.A.	Chairman of the Board of Statutory Auditors
	H1 Holding S.p.A.	Chairman of the Board of Statutory Auditors
	Acentro Turismo S.p.A.	Standing Statutory Auditor
	Albergo Centrale S.r.l.	Standing Statutory Auditor
	Albrofin S.p.A.	Standing Statutory Auditor
	Bellavista Imm.re 1ª S.r.l.	Standing Statutory Auditor
	Car Life Italia S.p.A.	Standing Statutory Auditor
	Le Palme S.r.l.	Standing Statutory Auditor
	S.G.I.R. S.r.l.	Standing Statutory Auditor
Pasquale Pace	ASECO S.r.l. (Gruppo Gesteco)	Chairman of the Board of Statutory Auditors
	Edil Vacanze S.p.A.	Chairman of the Board of Statutory Auditors
	CE,DI APULIA S.r.l. in liquidation	Chairman of the Board of Statutory Auditors
	New Team S.r.l.	Chairman of the Board of Statutory Auditors
	Fidanzia Sistemi S.r.l.	Standing Statutory Auditor
	Marzocca S.r.l.	Standing Statutory Auditor
	Supercar S.p.A.	Standing Statutory Auditor
Alessandro Trotter	Autostrade Lombarde S.p.A.	Member of the Board of Directors
	BREBEMI S.p.A.	Member of the Board of Directors
	Immobiliare Lombarda	Member of the Board of Directors
	ADRIAOIL S.p.A.	Chairman of the Board of Statutory Auditors
	Autostrade per l'Italia S.p.A.	Chairman of the Board of Statutory Auditors
	Euricom S.p.A.	Chairman of the Board of Statutory Auditors
	Faro S.p.A.	Chairman of the Board of Statutory Auditors
	Fillatice S.p.A.	Chairman of the Board of Statutory Auditors
	Petraco S.p.A.	Chairman of the Board of Statutory Auditors
	Pietro Fiorentini S.p.A.	Chairman of the Board of Statutory Auditors
	Radiall Elettronica S.r.l.	Chairman of the Board of Statutory Auditors
	Rebosio S.p.A.	Chairman of the Board of Statutory Auditors
	Rotolito Lombarda S.p.A.	Chairman of the Board of Statutory Auditors
	SITECH in liquidation	Chairman of the Board of Statutory Auditors
	TLX S.p.A.	Chairman of the Board of Statutory Auditors
	UNICREDIT Banca S.p.A.	Chairman of the Board of Statutory Auditors
	Autostrade S.p.A.	Standing Statutory Auditor
	Autostrade Sud America S.r.l.	Standing Statutory Auditor
	FIDIA S.p.A.	Standing Statutory Auditor
	Mediobanca S.p.A.	Standing Statutory Auditor
	Schemaventotto	Standing Statutory Auditor
	Siena Mortgages 00-1 S.p.A.	Standing Statutory Auditor
	Sistemi Tecnologici Holding S.p.A.	Standing Statutory Auditor
	T.A.F. Abrasivi S.p.A.	Standing Statutory Auditor
	UBM S.p.A.	Standing Statutory Auditor
	Ulisse S.p.A.	Standing Statutory Auditor
	UNICREDIT Clarima Banca S.p.A.	Standing Statutory Auditor

Name	Company	Position
Angelo Garcea	Travertino Toscano S.p.A.	Chairman of the Board of Statutory Auditors
	Polimoda S.r.l.	Chairman of the Board of Statutory Auditors
	Cesvit S.p.A. (in liquidation)	Standing Statutory Auditor
	Immobiliare S. Gemignanello S.p.A.	Standing Statutory Auditor
	Cooperativa Borgo Pinti 80 Scarl	Standing Statutory Auditor
Marco Lombardi	RECS S.r.l.	Sole Director
	Brandini S.p.A.	Chairman of the Board of Statutory Auditors
	Car Sharing Firenze S.r.l.	Chairman of the Board of Statutory Auditors
	C.P.F. Costruzioni S.p.A.	Chairman of the Board of Statutory Auditors
	D&D La Certosa Firenze S.p.A.	Chairman of the Board of Statutory Auditors
	Daliana Andrea & C. S.p.A.	Chairman of the Board of Statutory Auditors
	Fattoria dei Barbi S.r.l.	Chairman of the Board of Statutory Auditors
	L.A. Fashion S.p.A.	Chairman of the Board of Statutory Auditors
	Jaguar Firenze S.p.A.	Chairman of the Board of Statutory Auditors
	Villa Donoratico S.r.l.	Chairman of the Board of Statutory Auditors
	Firenze Industria Finance S.p.A.	Standing Statutory Auditor
	Europa Metalli S.p.A.	Standing Statutory Auditor
	Grifoni & Masini S.p.A.	Standing Statutory Auditor
	SAIF Servizi Ass.ni Industriali Firenze S.r.l.	Standing Statutory Auditor

The Independent Auditing Company

Deloitte & Touche S.p.A. is the company appointed pursuant to articles 155 and following of the TUF to perform an audit of the annual and consolidated financial statements, as well as to perform a review of the half year report, including that prepared on a consolidated basis. The auditors' activities cover 100% of the subsidiaries included in the scope of consolidation.

The current engagement, which is for the second of the two renewal terms permitted, was approved by shareholders in the general meeting on 27 April 2005 and ends with the financial statements for the year ending 31 December 2007.

In charge of the project on behalf of the Independent Auditing Company is Mr Paolo Guglielmetti, who has held this office since 2005 with reference to certification made on 6 April 2005 for the 2004 financial year, thus respecting article 160, Paragraph I *iv* of the TUF, which states that this position may be held for a maximum of six financial years.

The auditors' present annual fee amounts to Euro 65,000, inflation-linked on an annual basis to the ISTAT retail price index.

The Independent Auditing Company carried out the following additional engagements during the year:

- the compilation of a report on the assumptions made and underlying factors upon which the Group's accounting figures are based, including in the Prospectus prepared for the options deal relating to the capital increase approved on 19 May 2006;
- the compilation of a report on the market value of the issue price of the shares relating to the capital increase, not including the options rights pursuant to article 2441, Paragraph IV, *ii* of the Civil Code;
- a review of the Company's income tax declaration and the simplified 770 tax form.

Please note that regulations regarding audit review have recently been modified, and note the "grounds for proposals" made by the Board of Statutory Auditors relating to the second point of the agenda of the ordinary general meeting of shareholders, and relating to the cancellation and transferral of the independent auditing appointment to KPMG S.p.A..

The Directors

The directors have a three-year term of office and may be re-elected (article 17 of the company's bylaws). On being presented with the proposal to appoint a new director, shareholders in the general meeting are provided with information on the curriculum vitae of the candidate and on management positions and positions of control held in other companies. Their names, stated alongside their appointed positions, are stated below, along with a short curriculum vitae. The date of the initial appointment for the independent directors is also shown below.

Salvatore Orlando (Chairman)

Mr Salvatore Orlando, born in 1957, is a Political Science graduate. He entered the Group as a manager in 1984. Subsequently he became a member of the Boards of Directors of the Group's main industrial companies, and became Deputy Chairman of the KM Europa Metal AG Supervisory Council in January 2003. He has been a Company director since 1991.

Vincenzo Manes (Deputy Chairman)

Mr Vincenzo Manes was born in 1960 and graduated in Business and Economics. He is Chairman of Intek S.p.A., a company that holds the majority shareholding in KME Group S.p.A..

Vincenzo Cannatelli (Managing Director)

Mr Vincenzo Cannatelli, born in 1952 and holder of a degree in Mechanical Engineering, has a significant amount of experience in national and foreign companies. He started his career with the Stet and Elsag Bayley groups before being hired by ENEL, where he held a decisive position in the operational companies as COO of the Infrastructure and Networks and Market Divisions.
He has been Managing Director since 19 May 2006.

Mario d'Urso (Independent Director)

Mr Mario d'Urso, born in Naples in 1940, holds a degree in Law and has held positions in the financial sector and the government. He has been a Senator and an undersecretary for the Italian government in the past.
He was co-opted on 14 February 2005 and his position was subsequently confirmed through approval at the general meeting of shareholders held on 27 April 2005 for the financial year closed on 31 December 2005.

Marcello Gallo

Mr Marcello Gallo, born in Syracuse in 1958 and holding a degree in Political Economics, is a director for I2 Capital S.p.A., a company owned by Intek S.p.A.. He took on the position of Deputy Chairman after being Managing Director from 1998 to 2003. He holds positions on the Boards of Directors of companies owned by INTEK S.p.A..

Giuseppe Lignana (Independent Director)

Born in 1937, Mr Giuseppe Lignana graduated in Electronic Engineering, and was Managing Director of CEAT Cavi S.p.A., and a director of Banca Commerciale S.p.A. and SIRTI S.p.A.. He entered Cartiere Burgo S.p.A. in 1984, and was Managing Director, CEO and thereafter Chairman up until 2004. Currently he is Honorary Chairman.
He was co-opted on 12 February 2005 and his position was subsequently confirmed through approval at the general meeting of shareholders held on 27 April 2005 for the financial year closed on 31 December 2005.

Diva Moriani

Mrs Diva Moriani graduated in Business and Economics, and has been with Intek S.p.A. since 1999. She became part of the Board of Directors of the company in 2002, and is responsible for extraordinary transactions.

Alberto Pecci (Independent Director)

Mr Alberto Pecci, born in 1943 and holding a degree in Political Science, has been on the Company's and Group's Boards of Directors for many years. He is Chairman of the Board of Directors of the companies in the Pecci Industrial Group, which operates in the textile sector, and is a member of the Boards of Directors for ElEn S.p.A. and Alleanza Assicurazioni S.p.A.. He has been Chairman of Fondiaria S.p.A. and a director of Assicurazioni Generali S.p.A., Mediobanca S.p.A. and Banca Intesa S.p.A..
He was appointed at the general meeting of shareholders held on 28 June 1996 for the financial years 1996 and 1997.

Alberto Pirelli (Independent Director)

Mr Alberto Pirelli, born in 1954 and holding an American degree in Ichthyology and Aquaculture, holds operational positions in the Pirelli Group, and is currently the Deputy Chairman of Pirelli & C. S.p.A. and a director of Camfin S.p.A. and Olimpia S.p.A.. He is also Deputy Chairman of Gruppo Partecipazioni Industriali S.p.A..
He was appointed at the general meeting of shareholders held on 27 October 2000 for the financial years 2001, 2002 and 2003.

Currently no preliminary deposit of the appointment nominees is being made, and no voting list has been prepared. However, as mentioned previously, at the extraordinary meeting of shareholders, important changes of article 17 of the bylaws will be put forth for shareholder approval in order to introduce this type of election, therefore allowing the appointment of a Director on the part of the minority shareholders.

The Board of Directors has appointed a Chairman, a Deputy Chairman, and a Managing Director, a practical and effective choice that allows the concentration of decisive positions into the hands of one person to be avoided, and which also adheres to provisions in the Code of Conduct.

Pursuant to article 20 of the company's bylaws, the Chairman is the legal representative of the company and has the power to represent it when dealing with third parties and in court.

In addition, the Chairman has the power, operating in agreement with the Deputy Chairman, to draw up strategies regarding the Group's general direction and its growth policies, presenting these from time to time for the approval of the Board of Directors, which has the sole responsibility.
Powers of ordinary management are also delegated to the Chairman. These involve:

- relations with shareholders and providing information to them;
- external communications of all types, in accordance with the Deputy Chairman and the Managing Director;
- the definition, in agreement with the Deputy Chairman, of extraordinary operations, to be presented to the Board of Directors;
- the selection of candidates, in agreement with the Deputy Chairman, for the positions of Managing Director, members of the Executive Committee (or other committees), as well as, in agreement with the Deputy Chairman and the Managing Director, General Managers of the company and the selection of candidates for the same positions, including that of Director, in all other Group companies. This includes setting the remuneration levels for these positions. All of the above is to be presented to the prevailing corporate bodies responsible for the appointment.

Furthermore, the Chairman of the Board of Directors has the right to be consulted in advance on matters regarding transactions which would lead to a significant change in the industrial, financial or asset and equity structure of the Company or Group.

Pursuant to article 16 of the company's bylaws, the Deputy Chairman has the same powers as the Chairman, to be exercised in case of urgency and in case of the absence or impediment of the Chairman.

In addition, the Board has reserved the following powers for the Deputy Chairman:

- the power to guide, coordinate and supervise the activities of the Managing Directors;
- powers of ordinary and extraordinary management, consistent with the directives and strategies decided by the Board of Directors, of the company's activities in the areas of administration, finance, control, legal matters, fiscal matters, insurance and information technology as well as in industrial and commercial matters; in carrying out this function, he has the power to guide and co-ordinate all Group companies;
- the power of ordinary and extraordinary management of restructurings of the company or Group of an industrial and financial nature, or regarding the restructuring of the balance sheet or equity of the company or Group, keeping the Board of Directors constantly informed.

The Managing Director has been given the following powers by the Board of Directors:

- powers relating to Company management, consistent with the directives and strategies decided by the Board of Directors and the Deputy Chairman, in the areas of administration, finance, control, legal matters and information technology as well as in industrial and commercial matters. In carrying out this function, he has the power to guide and co-ordinate all Group companies.

Lastly, the director Diva Moriani has been given the role of operations director to conduct and co-ordinate Company and Group financial restructuring strategies, including the mandate for the execution of extraordinary activities for the acquisition or disposal of companies, as well as the negotiation and attainment of strategic agreements for the Company and the Group.

In light of the responsibilities attributed to them, the Chairman, Deputy Chairman, Managing Director and Director Diva Moriani are to be considered Executive Directors.

Executive Directors have the obligation of informing the Boards of Directors and Statutory Auditors on a quarterly basis about general management performance and its financial outlook, as well as the most significant transactions made by the Company and its subsidiaries.

The Board of Directors hereby states that its composition is adequate and appropriate, both in terms of size and in terms of the professional profiles of its members, to the size of the company and the issues it must face. The Board of Directors also believes this to be true of the various Committees it has established.

Furthermore, it believes that the organisational, administrative and accountancy structures of the Company and its subsidiaries are adequate and appropriate, particularly with regard to internal control and the management of conflicts of interest.

Specifically, having Executive Directors with specialised and in-depth multi-disciplinary professional experience in financial and industrial matters allows it to adequately "cover" the most significant part of company activity.

Through the decisions undertaken within their respective positions, the non-executive directors have brought an unfailing contribution to the Board of Directors and the Committees to which they belong in terms of professionalism and experience, and have participated at meetings with continuity.

Regarding the application criteria proposed in article 3.C.1. of the Code of Conduct and also considering article 147 iii paragraph IV of the TUF, the Board of Directors has deemed that the Directors Mario d'Urso, Giuseppe Lignana, Alberto Pecci and Albert Pirelli are independent directors (the latter two as a result of the dissolving of the "G.I.M. - Generale Industrie Metallurgiche S.p.A. Shareholders' Agreement"). The Board of Statutory Auditors agrees with this evaluation. No regulations have been set regarding meetings of the independent directors pursuant to article 3.C.6. of the Code.

Please note that Mr Alberto Pecci has been deemed to have the necessary requisites of independence even though his appointment arose during approval at the general meeting of shareholders held on 28 June 1996 for the financial years ending 31 December 1996 and 1997, and therefore he has held this position continuously for more than nine years, which appears to violate the criteria pursuant to article 3.C.1. paragraph e) of the Code of Conduct. However, please also note that — as regards similar considerations made concerning the fundamental and personal characteristics of some members of the Board of Statutory Auditors — the Board does not believe that this individual should be excluded only because he has belonged to the Board of Directors for such a long period of time.

The Board of Directors did not appoint a Lead Independent Director, who would co-ordinate the possible requests and contributions of the non-executive directors, specifically those of the independent directors. This is mainly because the position is subdivided amongst three different individuals.

Positions Held by Directors

The following table sets out for each Director the positions held at 31 December 2006 as either Director or Statutory Auditor in joint stock corporations, in partnerships and in limited liability companies of significant size (i.e. having a turnover of more than Euro 500 million). As for the members of the Board of Statutory Auditors, all Directors that held such positions during 2006 are included in the following list.

Name	Company	Position
Salvatore Orlando	Orlando & C. - Gestioni Finanziarie Sapa	General Partner
	G.I.M. - Gen. Ind. Metall. S.p.A.	Chairman of the Board of Directors
	Europa Metalli S.p.A.	Chairman of the Board of Directors
	KM - Europa Metal AG	Deputy Chairman of the Supervisory Council
Luigi De Angelis (until 17.02.06)	Europa Metalli S.p.A.	Member of the Board of Directors
Vincenzo Manes	INTEK S.p.A.	Chairman of the Board of Directors
	I_2 Capital S.p.A.	Chairman of the Board of Directors
	422 Holding B.V.	Chairman of the Board of Directors
	G.I.M. - Gen. Ind. Metall. S.p.A.	Deputy Chairman of the Board of Directors
	APEI Sgr	Member of the Board of Directors
Vincenzo Cannatelli	Aledia S.p.A.	Chairman of the Board of Directors
	Energetica Invest S.p.A.	Chairman of the Board of Directors
Albert Scherger (until 19.05.06)	Europa Metalli S.p.A.	Member of the Board of Directors
	Gesellschfat fur Stromwirtschaft mbH	Member of the Board of Directors
	KM Europa Metal AG	Member of the Management Committee
Mario d'Urso	No positions held	
Marcello Gallo	Drive Rent S.p.A.	Chairman of the Board of Directors
	Intek S.p.A.	Deputy Chairman of the Board of Directors
	I_2 Capital S.p.A.	Managing and General Director
	Tecsinter S.p.A.	Member of the Board of Directors
	APEI Sgr	Member of the Board of Directors
	Drive Service S.p.A.	Member of the Board of Directors
	Ducati Energia S.p.A.	Member of the Board of Directors
Giuseppe Lignana	No positions held	
Diva Moriani	INTEK S.p.A.	Member of the Board of Directors
	APEI SGR S.p.A.	Member of the Board of Directors
	G.I.M. - Gen. Ind. Metall. S.p.A.	Member of the Board of Directors
Alberto Pecci	Gruppo Industriale Pecci	Chairman of the Board of Directors
	El.En. S.p.A.	Member of the Board of Directors
	Alleanza Assicurazioni	Member of the Board of Directors
Alberto Pirelli	Pirelli & C. S.p.A.	Deputy Chairman of the Board of Directors
	Gruppo Partecipazioni Industriali S.p.A.	Deputy Chairman of the Board of Directors
	Camfin S.p.A.	Member of the Board of Directors
	Pirelli Tyre S.p.A.	Member of the Board of Directors
	G.I.M. - Gen. Ind. Metall. S.p.A.	Member of the Board of Directors
	FIN.AP di Alberto Pirelli & C. ApA	Chairman of the Board of General Partners

The Board of Directors, in consideration of the following:

- the personal and professional qualifications of its members;
- the number and importance of the above-mentioned positions;
- and the high level of participation in Board of Directors' meetings of its members;

does not believe that it is appropriate to limit the number of positions that each Director may hold.

Regulations on Transactions with Related Parties

Please remember that the Directors with duties involving the above refer to the Boards of Directors and Statutory Auditors regarding transactions that are potentially in conflict of interest, an obligation pursuant to article 14 of the bylaws.

This internal regulation, adopted in March 2003 and reviewed first in November 2003 and subsequently in September 2005 and November 2006 (when a reference to articles 2391, 2391 *ii* and 2369 *ii* of the Civil Code, and to the related CONSOB regulation, was introduced in the forward), gave weight to company bylaws by setting the criteria by which related parties are identified, and the relative operating procedures which include quarterly audits and meetings to be held with the Head of Internal Control, following the guidelines indicated in the Code of Conduct regarding this point specifically. The Board of Statutory Auditors is invited to participate in these meetings.

The definition of related parties contained in the version of IAS 24 that was in force at the time was fully adopted.

The regulation reminds the Company's Directors and Auditors who have potential or indirect interests in a transaction that they must fully and in a timely manner inform the Board of Directors about this potential conflict. The Board may avail itself of the services of independent experts in making its decisions.

Please remember that the meeting did not make recourse to the dispensations in the anti-competitiveness regulations pursuant to article 2390 of the civil code.

Furthermore, the members of the KME Europa Metal A.G. management board ensure that information on intra-company transactions and other possible large transactions with related parties made by Group Companies are reported to Company executives, thus adopting the guidelines indicated in the Code of Conduct.

The Board of Directors believes that the procedures contained in the Regulations, available in the appropriate section of the website www.kmegroup.it, are adequate in order to manage conflicts of interest.

Compensation for Directors and upper management

Article 8 of the Company bylaws states that Directors have the right to participate in 2% of profits after the allocation of the portion for legal reserves. The subsequent article 21 allows shareholders in the general meeting to allocate a fixed amount to them, while, for those having certain powers, the Board of Directors may set specific compensation after having consulted the Board of Statutory Auditors in this respect.

The total fixed fee for the Directors has been set at Euro 138,000.00, to be allocated equally between them but with a 50% increase for those taking part in the two established Committees, pursuant to the resolutions made at the general meeting of shareholders held on 19 May 2006. Regarding the payment of compensation pursuant to article 8 of the Company bylaws, the amounts received as fixed fees are considered as advances of the compensation.

A breakdown of Directors' compensation, received for any reason and in any form, even from subsidiaries, is reported in the following table set according to CONSOB guidelines:

Name (figures in Euros)	**Position**	**Period of responsibility**	**Expiry of position**	**Compensation for position**	**Non-monetary benefits**	**Bonuses and other incentives**	**Other compensation**
Salvatore Orlando	Chairman	01.01.06-31.12.06	31.12.08	681,500	–	–	80,000 (1)
Vincenzo Manes	Vice-chairman	01.01.06-31.12.06	31.12.08	1,096,500	–	–	25,000 (1)
Vincenzo Cannatelli	Managing Director	19.05.06-31.12.06	31.12.08	889,002	2,399	–	–
Mario d'Urso	Director	01.01.06-31.12.06	31.12.08	23,000	–	–	–
Marcello Gallo	Director	01.01.06-31.12.06	31.12.08	19,050	–	–	–
Giuseppe Lignana	Director	01.01.06-31.12.06	31.12.08	19,650	–	–	–
Diva Moriani	Director	01.01.06-31.12.06	31.12.08	11,500	3,082	–	244,142 (4)
Alberto Pecci	Director	01.01.06-31.12.06	31.12.08	17,250	–	–	–
Alberto Pirelli	Director (2)	01.01.06-31.12.06	31.12.08	17,250	–	–	–
Albert Scherger	Director (3)	01.01.06-19.05.06	19.05.06	4,379	–	–	911,000 (1)

(1) Compensation received for positions held in subsidiaries. The Chairman and Vice-chairman have asked the company to allocate part of their compensation to charity (Euro 75,000 from the Chairman and Euro 150,000 from the Vice-chairman).

(2) Compensation for Mr Alberto Pirelli was made to Pirelli & C. S.p.A..

(3) Managing Director until 19.05.2006.

(4) Compensation as an employee.

In July 2006 the "KME Group S.p.A. stock option plan" for executive Directors and Group Managers was put into action.
The options give each beneficiary the right to subscribe to a number of Company ordinary shares equal to the number of options held at a price of Euro 0.343 each, through the means and terms established by the plan. The price is calculated based on the official average share price recorded on the Milan Stock Exchange in the month of July 2006.
One third of the options held may be exercised starting from 1 September 2007, one third starting from 1 September 2008, and one third from 1 September 2009.
The last date on which the options may be exercised is 28 February 2011.
Executive Directors were given 20,408,162 options corresponding to a total value of Euro 7 million, based on the exercise price. A total of 23,323,614 options, with a total value of Euro 8 million, were given to 19 Group managers.

A breakdown of the assignment of these options, given for each individual Director and in aggregate for the Managers, is shown in the table below, which was drawn up according to CONSOB guidelines:

Directors' and Managers' Stock Options

Name	**Position**	**Options held at start of year**			**Options assigned during year**			**Options exercised during year**			**Options expired during year**	**Options held at end of year**		
		No. options	**Av. exercise price**	**Av. expiry**	**No. options**	**Av. exercise price**	**Maturity**	**No. options**	**Av. exercise price**	**Av. expiry**	**No. options**	**No. options**	**Av. exercise price**	**Maturity**
Vincenzo Manes	Deputy Chairman	–	–	–	7,580,174	0.343	28.2.2011	–	–	–	–	7,580,174	0.343	28.2.2011
Vincenzo Cannatelli	Managing Director	–	–	–	11,661,807	0.343	28.2.2011	–	–	–	–	11,661,807	0.343	28.2.2011
Diva Moriani	Director	–	–	–	1,166,181	0.343	28.2.2011	–	–	–	–	1,166,181	0.343	28.2.2011
19 Managers	–	–	–	–	23,323,614	0.343	28.2.2011	–	–	–	–	23,323,614	0.343	28.2.2011

A results-based incentive plan for upper management has also been introduced by the Group.

Compensation Committee

The Compensation Committee is comprised of the Directors Alberto Pirelli (Chairman), Mario d'Urso and Giuseppe Lignana, all of whom are non-executive and independent Directors.

The Committee presents proposals to the Board of Directors for the compensation of the Chairman, the Deputy Chairman, the Managing Directors and the Directors who carry out certain functions, monitoring that their decisions are correctly applied.

The Committee also evaluates the criteria adopted for the compensation of managers with strategic responsibilities, and draws up related general recommendations for the Board of Directors, monitoring that these systems are also adopted.

The standing members of the Board of Statutory Auditors attend the Committee's meetings, ensuring that the requirements of article 21 of the company bylaws are followed.

The Committee met three times during the year (in the previous year they met twice). All of the members of the Committee participated in all of the meetings.

Internal Control and the Internal Control Committee

The Internal Control Committee is appointed by the Board of Directors, which has system responsibility, and is composed of the Directors Mario d'Urso (Chairman), Marcello Gallo and Alberto Pecci. None of them is an executive Director, and Mario d'Urso and Alberto Pecci are also independent Directors.

Qualitatively, the composition of the Committee does not adhere to requirements of the Code in that there are only two independent Directors instead of the three required by the Code when the Company is owned by another listed Company. The fact that the majority of the Directors are independent Directors is currently considered adequate.

The responsibilities of the Committee are as follows:
- to assist the Board of Directors in setting the criteria for directing and monitoring the internal control system in order to identify and manage the main business risks;
- to assess the activities carried out by the internal control officers;
- to assess the suitability of the accounting principles used and their consistency in the preparation of the Group's consolidated financial statements;
- to assess the proposals made by the independent auditors, and assess their activities.

The Committee reports to the Board of Directors on at least a half-yearly basis.

The Chairman, the Deputy Chairman (as the Director responsible for control), and the Chairman of the Board of Statutory Auditors, or a standing Auditor appointed by the Chairman, are invited to attend the meetings of the Committee.

The Committee met twice during the year, as they did in the previous year. All of the members of the Committee participated in both meetings, as did the Chairman of the Board of Statutory Auditors.

The Head of Internal Control was appointed by the Deputy Chairman by mandate of the Board of Directors. He reports to the Deputy Chairman on a continuous basis rather than at preset time intervals. Hierarchically, he is independent from all heads of operating areas. Moreover, he reports to the Committee for Internal Control and to the Board of Statutory Auditors.

His objective is to examine and assess the adequacy and effectiveness of the company's internal control system, as well as ensuring that the activities carried out by the various business functions adhere to procedures, company policies, the law and any other regulations, paying special attention to the reliability and completeness of the information being processed, the safeguarding of the company's assets, the suitability of the accounting principles used and their consistency in the preparation of the group's consolidated financial statements. His work is carried out in conjunction with the heads of administration and the independent auditors.

The Company has adopted an "Organisational and management model pursuant to Leg. Dec. no. 231/01".

Pursuant to article 8 of the Code, the Board of Directors believe that the Company's system of internal control is suitable to protect it against the typical risks of the main activities performed by the Company, and is able to guarantee the safeguarding of its assets, the effectiveness and efficiency of company operations, the reliability of financial reporting, and that laws and regulations will be respected.

Corporate Information

In order to ensure that communications of corporate events to the market are timely, complete, adequate and not selective, in 2002 the Company introduced a "Code of Conduct regarding Company information on important events", thus responding to the requirements in the Code of Conduct and thereby formalising the principles contained in the "Market Information Guide".

Subsequent innovations introduced into legislation regarding company information, as a result of amendments made to the TUF during 2005 and 2006, as well as those to CONSOB regulations, led to it being revised in March and November 2006. Specifically, we remind you of the new wording of article 114 of the TUF and, with reference to article 115 ii, the consequent identification of "relevant persons" who have access to "sensitive information" and the establishment of a related register to record the names of these individuals, effective as from 1 April 2006.

The procedure reminds the Directors and Statutory Auditors to respect the confidentiality of sensitive information. This principle is extended to others in the Company who, owing to their functions, may have access to information of this nature, requesting them to limit the handling of this data to those persons who are aware of CONSOB and Borsa Italiana S.p.A. requirements on this matter, and of the security measures to be taken.

The position of *investor relations manager* is *temporarily* held by the Managing Director, who works together with the individual company managers regarding their respective areas of expertise. This choice takes into account the Company's current internal resources and structures, and allows it to ensure an adequate level of service to meet its various requirements.

Code of Conduct Regarding Internal Dealing

As of 1 April 2006, and following the entry into force of regulations regarding internal dealing introduced through Law no. 62 of 18 April 2005 and subsequent amendments contained in CONSOB Regulations for Issuers in resolution no. 15232 dated 29 November 2005, the Board of Directors of the Company, in its meetings held on 15 March and 10 November 2006, considered it appropriate to take suitable action by preparing a new internal procedure to replace the previous one with the purpose of:

- ensuring that the new regulations are widely communicated, and making it as simple as possible for "relevant persons" to become aware of them;
- establishing an updated internal procedure to put the respective changes into effect.

Furthermore, please note that as a particularly unusual matter, relevant persons were subject to a black-out period regarding transactions on the Company's financial instruments.

Interests in the Company and its subsidiaries held by the Directors and Statutory Auditors are indicated in the following table:

Name	Interest held in	No. of shares held at the end of FY 2005	No. of shares purchased	No. of shares sold	No. of shares held at end of FY 2006
Alberto Pecci	KME GROUP	41,500 sav. shares (1)	–	20,000 sav. shares (1)	21,500 sav. shares (1)
	KME GROUP	300,000 sav. shares (2)	–	104,049 sav. shares (2)	195,951 sav. shares (2)
	KME GROUP	–	4,197 warrants (1) (4)	–	4,197 warrants (1)
	KME GROUP	–	44,176 warrants (2) (4)	–	44,176 warrants (2)
Alessandro Trotter	KME GROUP	50,000 sav. shares (3)	–	–	50,000 sav. shares (3)

(1) Directly owned.
(2) Indirectly owned but fully imputed through a subsidiary.
(3) Indirectly owned but fully imputed through spouse.
(4) From subscription of capital increase.

The full text of the procedure is available in the appropriate section of the website at www.kmegroup.it, as are the individual transactions involved.

Market and Shareholders relations

Whilst underlining the fact that the Shareholders' General Meeting is the best way for the Board of Directors to inform shareholders of the Company's course of events and expected trends, the Company nevertheless believes in timely information of good quality which is continuously made available through an appropriate market information network.

The Company website at www.kmegroup.it has been mainly used and developed for this purpose, and it is updated almost simultaneously with the issue of publications through the *Network Information System* (NIS) managed by Borsa Italiana S.p.A.. We remind you that this system allows for the publication of press releases issued by the Company by sending them to the press agencies linked to the system, to Borsa Italiana S.p.A., which issues its own notice, and to CONSOB.

For information regarding the activities and products of the Group's individual manufacturing companies, please see www.thecopperlink.com, which available for consultation in various languages.

Given the scope for which these sites have been created, they include not only news of a historical, documentary or accounting nature (particularly the annual financial statements and half yearly and quarterly reports) regarding important events (the exercising of rights and shareholder convocation), but also news regarding the Company's product range, their applications and other information of interest to suppliers and customers.

A significant part of the website www.kmegroup.it is dedicated to corporate governance documents (company bodies, Bylaws, Warrant Regulations, Internal Code of Conduct and Regulations, minutes of the shareholders' meetings), with individual areas dedicated to possible extraordinary transactions underway. Furthermore, as of last year a "Annual Information Document" is available pursuant to article 54 of the Regulations for Issuers.
Following the approval of the Shareholders Extraordinary General Meeting of the changes proposed to the Company bylaws regarding participation in shareholders meetings and the appointment of Directors and Statutory Auditors, a section of the website dedicated to these matters will be introduced, giving special attention to the depositing of the lists for the nomination of Directors and Statutory Auditors, and to the exercising of voting rights.

Some of this information, particularly press releases, financial statements and half-yearly reports, is already available in English too.

During 2006, the site www.kmegroup.it had about 113,000 hits and over 350,000 pages of various types were consulted, numbers that are more than double the figure from the previous year (55,000 hits and 128,000 pages, respectively). Moreover, a continuous communication service of press releases and documents issued by the Company was carried out through its mailing list (1,084 subscribers compared to the 903 in 2005). It is also possible to send requests via email to the Company, a service that is not only used by shareholders.

Please note that the two sites are being updated so that they can be merged in order to provide a full and comprehensive picture of the Company and the Group, thus allowing for an immediate link between the Group's manufacturing activities and its financial and company data.

Company Bylaws, Minority Shareholder Protection and Shareholders' Meetings

The Company bylaws contain regulations to protect the rights of minority shareholders at shareholders' meetings (article 10) and in the appointment of the Board of Statutory Auditors (article 22), regarding the possibility of collecting proxies and postal voting (article 11) and obtaining information from the Board of Statutory Auditors (articles 14 and 18) and the Representative of the savings shareholders (article 24).

Under article 22, shareholders who hold more than 3% of ordinary shares, also jointly, may present lists for the appointment of members of the Board of Statutory Auditors, whereas under article 10 there is a threshold of 10% for those minority shareholders wishing to call a shareholders' meeting, a level which corresponds to that in article 125 of the TUF.

The bylaws must be adequately updated to reflect these new regulations protecting minority shareholder rights, especially regarding the appointment of Directors and Statutory Auditors.

We also remind you of those provisions of the bylaws that govern the calling, the constitution and the proceedings of shareholders' meetings and the participation and representation of shareholders at these meetings (articles 10, 11, 12 and 13). As a result, it has been considered unnecessary to adopt specific Regulations for Shareholders' Meetings.
A review of the bylaws containing regulations involving the latter is also underway. It will be subject to shareholder approval.

For full informational purposes, we remind you that the agreement between G.I.M. - Generale Industrie Metallurgiche S.p.A. and Pirelli & C. S.p.A. shareholders was dissolved on 19 December 2006.

TABLE 1

Structure of Board or Directors and Established Committees

Board of Directors							Internal Controls Committee ●		Compensation Committee ◆	
Role	**Name**	**Executive**	**Non Executive**	**Indepen-dent**	**(****)**	**Number of other positions (**)**	**(***)**	**(****)**	**(***)**	**(****)**
Chairman	Salvatore Orlando	x			100	4				
Deputy Chairman	Vincenzo Manes	x			100	5				
Managing Director	Vincenzo Cannatelli	x			100	2				
Director	Mario d'Urso		x	x	66	//	x	100	x	100
Director	Marcello Gallo		x		77	7	x	100		
Director	Giuseppe Lignana		x	x	88	//			x	100
Director	Diva Moriani	x			100	3				
Director	Alberto Pecci			x	77	3	x	100		
Director	Alberto Pirelli			x	66	6			x	100

● **Summary of grounds for possible absences of the Committee for Internal Control or composition other than that recommended by the Code:**
The Committee is exclusively composed of non-executive Directors including two independent Directors instead of the three required for adequacy.

◆ **Summary of grounds for possible absences of the Compensation Committee or composition other than that recommended by the Code:**
The composition of the Committee adheres to the requirements of the Code of Conduct.

Summary of grounds for absences of the Executive Committee:
The Committee was not established due to the appointment of a Managing Director.

Summary of grounds for absences of the Appointment Committee:
The Committee was not established due to one shareholder having control of the Company's voting capital.

Number of meetings held during period	**Board of Directors: nine**	**Internal Control Committee: two**	**Compensation Committee: three**

NOTES

(*) The asterisks (*) indicate the Directors that were appointed by lists presented by minority shareholders.

(**) This column indicates the number of Director or Auditor positions held by individuals in other companies listed in regulated markets, foreign or domestic, in financial services companies, banks, insurance companies, or companies of significant size.

(***) This column indicates ("X") which Committee the member of the Board of Directors participates in.

(****) This column indicates the attendance percentages of Directors in Board of Directors' and Committee meetings.

TABLE 2

Board of Statutory Auditors

Role	Name	Attendance percentages at meetings of the Board of Statutory Auditors	No. of other positions (**)
Chairman	Fazzini Marcello	100	7
Standing Auditor	Pace Pasquale	100	7
Standing Auditor	Trotter Alessandro	100	27
Alternate Auditor	Garcea Angelo	///	5
Alternate Auditor	Lombardi Marco	///	14
Number of meetings held during the calendar year:			
Quorum required for the presentation of minority shareholder lists for the election of one or more standing members (according to article 148 TUF): 3%.			

NOTES

(*) The asterisks (*) indicate the Auditors that were appointed by lists presented by minority shareholders.

(**) This column indicates the number of Director or Auditor positions held by individuals in other companies listed in regulated markets, foreign or domestic, in financial services companies, banks, insurance companies, or companies of significant size.

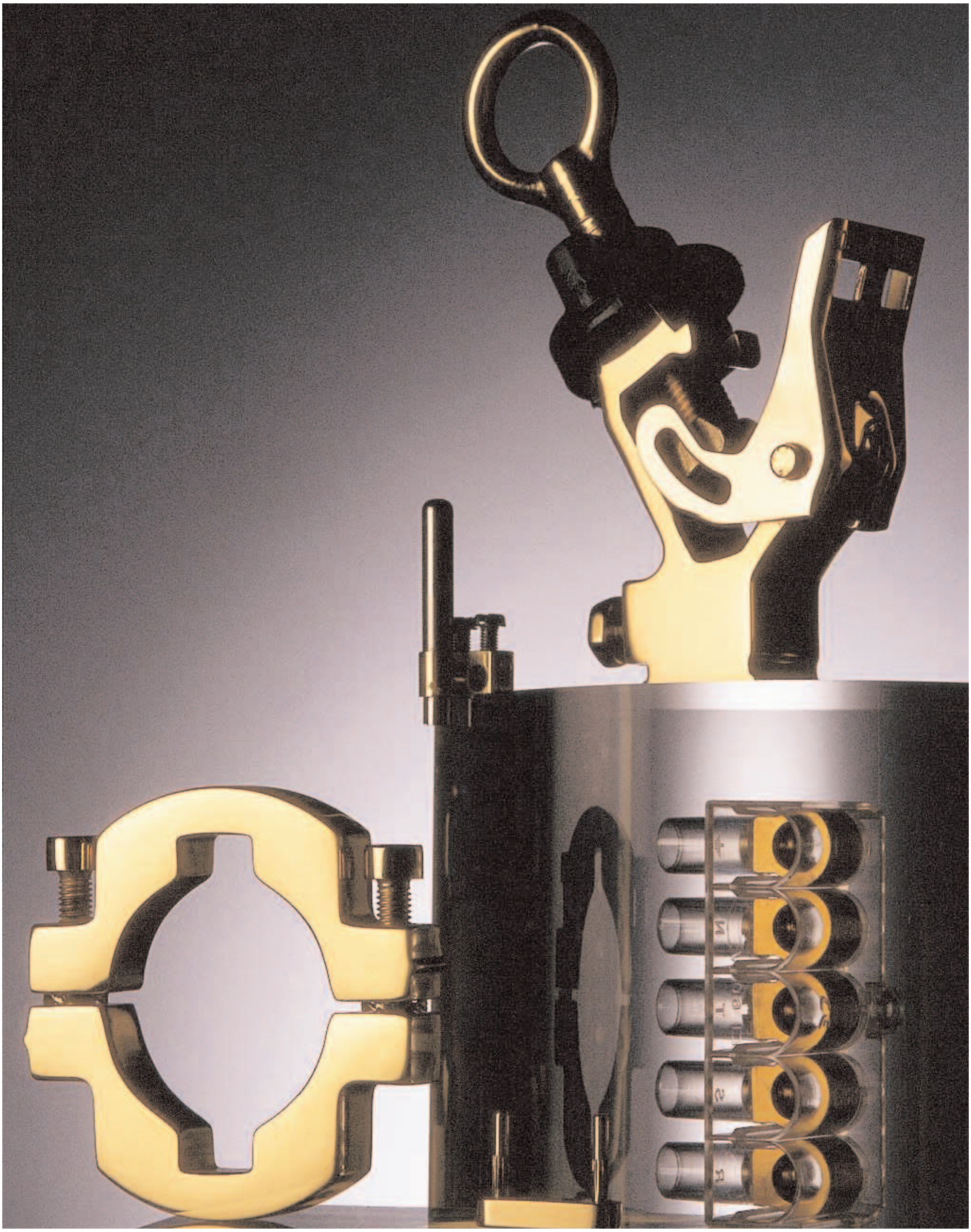
TABLE 3

Other Code of Conduct provisions

	YES	NO	Summary of the grounds for any discrepancy with recommendations in the Code
Delegation system and related party transactions			
On delegating, has the Board of Directors defined the following:			
a) limits	X		
b) means of execution	X		
c) frequency of reporting?	X		
Has the Board reserved for itself the examination and approval of transactions having certain economic or financial importance (including related party transactions)?	X		
Has the Board defined guidelines and criteria which can be used to identify "significant" transactions?	X		
Are these guidelines and criteria described in the Report?	X		
Has the Board established appropriate procedures to examine and approve related party transactions?	X		
Are the procedures for the approval of related party transactions described in the report?	X		Available in full on the company website
Procedures followed for the most recent appointments of Directors or Statutory Auditors			
Were the proposal details of the candidate for directorship filed at least ten days in advance?		X	They were presented at the Shareholders' Meeting
Did the proposal of the candidate for directorship include all of the appropriate documents?	X		
Did the proposal of the candidate for directorship include a statement by the candidate of his or her suitability as an independent director?		X	This is indicated in the Report of the Board of Directors
Were the proposal details of the statutory auditor candidate filed at least ten days in advance?		X	Article 22 of the bylaws sets a two-day period
Did the proposal for the statutory auditor candidate include all of the appropriate documents?	X		
Shareholders' meetings			
Has the company approved regulations governing shareholders' meetings?		X	These regulations are contained in the bylaws
Are the regulations attached to the report (or is there a description as to where these may be obtained or downloaded)?	X		Refer to Charter III of the bylaws, available in full on the website
Internal Control			
Has the company appointed an internal control officer/s?	X		
Is/are the officer/s hierarchically independent from the heads of the operating areas?	X		
Organisational unit in charge of internal control (pursuant to article 9.3 of the Code)	X		Internal Control Officer
Investor relations			
Has the company appointed a head of investor relations?	X		This role is temporarily held by the Managing Director The typical activities of this role are performed with the support of the various heads of business functions
Business dept. and contact details of head of investor relations (address/telephone no./fax no./email)	X		Please see the Report of the Board of Directors and the company website

Legislation on Protection of Personal Data

Pursuant to article 26 Attachment B (Technical regulations regarding minimum security levels) of Legislative Decree no. 196 of 30 June 2003 (the “Personal Data Protection Code”), the required “Data Security Planning Program” has been adopted through a dated, certified document.



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CONSOLIDATED FINANCIAL STATEMENTS AT 31 DECEMBER 2006

Consolidated Balance Sheet

KME Group S.p.A. consolidated financial statements at 31 December 2006

BALANCE SHEET **Distinction made between current/non-current items** (Thousands of Euros)	**Ref. in notes**	**At 31.12.2006**	**At 31.12.2005**
Property, plant and equipment	4.1	619,923	624,305
Investment in property	4.2	10,591	9,272
Goodwill	4.3	109,840	109,840
Other intangible assets	4.4	955	1,631
Investments in subsidiaries and associates	4.5	4,906	5,564
Other equity investments	4.5	245	245
Equity investments at equity method	4.5	2,634	2,573
Other non-current assets	4.6	29,143	28,960
Deferred tax assets	4.19	44,710	40,651
Non-current assets		**822,947**	**823,041**
Inventories	4.7	683,627	444,361
Trade receivables	4.8	230,693	358,270
Other current assets and receivables	4.9	67,791	50,141
Current financial assets	4.10	75,347	14,404
Cash and cash equivalents	4.11	162,098	151,992
Current assets		**1,219,556**	**1,019,168**
TOTAL ASSETS		**2,042,503**	**1,842,209**
Share capital		319,643	189,775
Other reserves		(4)	–
Treasury shares	2.10	(37)	(37)
Retained earnings (loss carried forward)		5,176	5,165
Consolidation reserves		25,044	22,292
Reserve for first adoption of IAS/IFRS	2.10	93,658	93,658
Profit (loss) for the year		51,785	4,343
Group interest in shareholders' equity		**495,265**	**315,196**
Minority interest in shareholders' equity		–	–
Total shareholders' equity		**495,265**	**315,196**
Employee benefits	4.13	166,904	166,663
Deferred tax liabilities	4.19	160,289	128,977
Long-term borrowings and other financial liabilities	4.14	487,353	589,379
Other non-current liabilities	4.15	7,721	7,257
Provisions for risks and charges	4.16	143,137	128,668
Non-current liabilities		**965,404**	**1,020,944**
Short-term borrowings and other financial liabilities	4.17	279,175	260,924
Trade payables	4.18	164,575	122,575
Other current liabilities	4.18	108,080	94,767
Provisions for risks and charges	4.16	30,004	27,803
Current liabilities		**581,834**	**506,069**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**2,042,503**	**1,842,209**

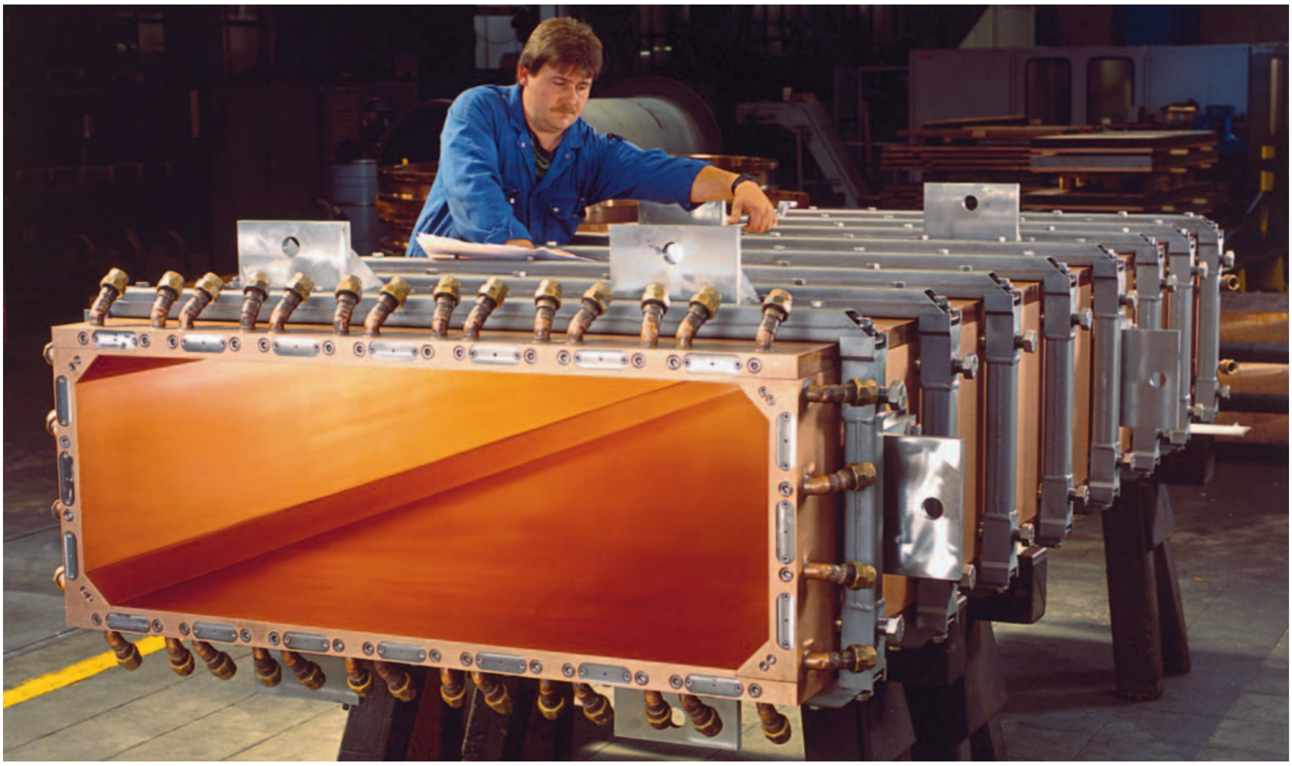
In the balance sheet, the income statement and the cash flow statement, the totals relating to positions in or transactions with related parties are not shown separately as they were not deemed significant for comprehension of the Group's financial, equity and cash flow situation.

KME Group S.p.A. consolidated financial statement at 31 December 2006

CONSOLIDATED INCOME STATEMENT **Costs classification per nature** (Thousands of Euros)	**Ref. in notes**	**FY 2006**	**FY 2005**
Sales revenues	5.1	3,556,833	2,176,063
Change in inventory of finished and semi-finished goods		10,883	(8,860)
Capitalization of Company-produced assets		2,601	2,564
Other operating revenues		16,027	38,281
Purchases and change in inventory of raw materials		(2,751,587)	(1,448,477)
Labour costs	5.2	(347,350)	(341,768)
Depreciation, amortisation, impairment losses and write-downs	5.3	(51,394)	(71,482)
Other operating expenses	5.4	(307,440)	(301,506)
Operating profit (EBIT)		**128,573**	**44,815**
Financial income	5.5	6,081	5,882
Financial (expense)	5.5	(50,738)	(43,653)
Interest in result of associates valued using equity method		216	317
Profit (loss) before taxation		**84,132**	**7,361**
Current taxes	5.6	(4,938)	(3,771)
Deferred taxes	5.6	(27,409)	753
Total income tax		**(32,347)**	**(3,018)**
Profit (loss) from continuing operations		**51,785**	**4,343**
Profit (loss) from discontinued operations		–	–
Profit (loss)		**51,785**	**4,343**
Minority interest in (profit) loss		**–**	**–**
Group interest in profit (loss)		**51,785**	**4,343**

Profits per share (figures in Euros):	**2006**	**2005**
Basic profits per share	0.0917	0.0071
Diluted profits per share	0.0753	0.0071

In the balance sheet, the income statement and the cash flow statement, the totals relating to positions in or transactions with related parties are not shown separately as they were not deemed significant for comprehension of the Group's financial, equity and cash flow situation.



Crucibles for the iron and steel industry.

Consolidated cash flow statement KME Group S.p.A. at 31 December 2006

CONSOLIDATED CASH FLOW STATEMENT **Indirect method** (Thousands of Euros)	**December 2006**	**December 2005**
(A) Cash and cash equivalents at beginning of year	**151,992**	**74,035**
Profit before taxes	84,133	7,362
Depreciation and amortisation of property, plants and equipment and intangibles	53,421	55,030
Write-downs of current assets	1,439	1,538
Write-downs (revaluations) of non-current assets other than financial assets	(2,027)	16,452
Write-downs (revaluations) of current/non-current financial assets	1,149	183
Net accrued interest	33,452	29,617
Losses (gains) on non-current assets	(789)	(5,292)
Interest in results of associates measured at equity	(216)	(317)
Changes in pension funds and employees' indemnity fund	681	(3,125)
Changes in provisions for risks and charges	14,653	9,148
Decrease (increase) in inventories	(238,887)	(56,352)
(Increase) decrease in current receivables	108,694	(24,829)
Increase (decrease) in current payables	55,512	(2,568)
Changes in foreign currency conversions	96	113
Net interest paid in the year	(33,366)	(29,529)
Current taxes paid and tax refunds during the year	(5,004)	(5,182)
(B) Cash flows from operating activities	**72,941**	**(7,751)**
(Increase) in non-current property, plants and equipment and intangibles	(50,242)	(44,818)
Decrease in non-current property, plants and equipment and intangibles	3,512	15,105
(Increase) decrease in equity investments	(479)	–
(Increase) decrease in financial assets available for sale	–	–
Increase/decrease in other non-current assets/liabilities	16	(4,106)
Dividends received	1,750	426
(C) Cash flow from investment activities	**(45,443)**	**(33,393)**
Contributory increase in shareholders' equity	128,835	–
Increase (decrease) in current and non-current indebtedness	(84,036)	124,217
(Increase) decrease in current and non-current loans receivables	(60,877)	(5,116)
Dividends paid	(1,314)	–
(D) Cash flow from financing activities	**(17,392)**	**119,101**
(E) Change in cash and cash equivalents (B + C + D)	**10,106**	**77,957**
(F) Cash and cash equivalents at end of period (A + E)	**162,098**	**151,992**

In the balance sheet, the income statement and the cash flow statement, the totals relating to positions in or transactions with related parties are not shown separately as they were not deemed significant for comprehension of the Group's financial, equity and cash flow situation.

Reconciliation between the net profit of Parent Company KME Group S.p.A. and Group interest of consolidated net profit at 31 December 2006 (Thousands of Euros)		
Profits from separate financial statements of KME Group S.p.A.		**7,206**
Interest of profits of consolidated companies (1) (2)		44,579
Consolidation adjustments (3)		0
Consolidated net profits		**51,785**
Subsidiary profits 1.1.2006-31.12.2006		
(1) Profits from KM Europa Metal AG (consolidated)	44,866	
(2) Immobiliare Agricola Limestre S.r.l. profits	(287)	
(3) Consolidation adjustments	0	
Total	**44,579**	

Schedule of Reconciliations of Consolidated Shareholders' Equity KME Group S.p.A. at 31 December 2006 (Thousands of Euros)	Share capital	Addition. paid-in capital	Treasury shares	Ret. Earn. (loss carry-fwd.)	Consolidation reserve	Reserve for 1st adoption IAS/IFRS	Profit (loss) for the year	Total shareholders' equity
Shareholders' Equity at 31.12.2005 IAS/IFRS	**189,775**	**0**	**(37)**	**5,165**	**22,292**	**93,658**	**4,343**	**315,196**
Appropriation of previous year's profits		70		11	4,262		(4,343)	0
Dividends distribution					(1,314)			(1,314)
Share capital increase net of expenses	129,868	(1,033)						128,835
Stock option bonuses		959						959
Change in technical consolidation reserves					(196)			(196)
Profit (loss) for the year							51,785	51,785
Shareholders' Equity at 31.12.2006 IAS/IFRS	**319,643**	**(4)**	**(37)**	**5,176**	**25,044**	**93,658**	**51,785**	**495,265**
IAS reclassification treasury shares	(37)	0	37	0	0	0	0	0
Shareholders' Equity at 31.12.2006 IAS/IFRS	**319,606**	**(4)**	**0**	**5,176**	**25,044**	**93,658**	**51,785**	**495,265**

At 31 December 2006, the Parent Company directly held 65,000 savings shares not having a nominal value. These shares were all reclassified in reduction of Company share capital.

The item "consolidation reserves" mainly involves the conversion into Euros of the items of the financial statements expressed in foreign currencies.

Cuprotherm – Coated copper pipes for heating systems.

ACCOUNTING PRINCIPLES AND NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. General Information

KME Group S.p.A. (or "KME") and its industrial subsidiaries (which together make up the "Group") operate in the sector of semi-finished products in copper and copper-based alloys.
The Group owns manufacturing plants in various European countries, and markets its products in all the major countries of the world.
KME is a joint stock corporation (*Società per Azioni*) registered in Italy at the Florence Chamber of Commerce under no. 00931330583, and its shares are listed on the electronic stock market managed by Borsa Italiana S.p.A..
The consolidated financial statements at 31 December 2006 were approved by the Board of Directors on 20 March 2007.

2. Accounting Principles

2.1 Basis of Preparation

The financial statements at 31 December 2005 have been prepared following the indications provided by CONSOB in its Regulations for Issuers and observing international accounting standards.
The consolidated financial statements have been prepared in accordance with the valuation and measurement criteria established in the ***International Financial Reporting Standards*** (IFRS) issued by the ***International Accounting Standards Board*** (IASB) and adopted by the European Commission pursuant to article 6 of EC Regulation no. 1606/2002 of the European Parliament and of the Council of 19 July 2002. In preparing the consolidated financial statements, the directors have taken account of the accrual principle, going concerns, understandability, materiality, relevance, reliability, neutrality, prudence and comparability. These financial statements were also prepared in accordance with CONSOB regulation no. 15519 from 27 July 2006 (enforced by article 9, paragraph 3; of Legislative Decree no. 38/2005) regarding the preparation of financial statements, and CONSOB memo no. 6064293 dated 28 July 2006 regarding the type of information that must be given in the notes to the financial statements and in the Report of the Board of Directors.

The Group has not yet adopted those accounting standards which, although issued by the IASB, become effective after the balance sheet date of these financial statements. However, we estimate that the future adoption of these standards will not have a significant impact on the Group's equity, financial position or income situation.
The events and company operations were reported and represented according to their actual economic reality, and not only according to their legal form.
The balance sheet date of the consolidated financial statements is that of the accounting period of the Parent Company.
The information and reconciliation statements outlined in paragraphs 39 and 40 of IFRS 1 *First adoption of IFRS* and the CONSOB memo no. 6064313 from 28 July 2006 were not included in these financial statements, as the Parent Company adopted new accounting principles on 1 December 2004, both on a consolidated level as well as on an individual level. Prospectuses and figures involving this can be found in the half year report to 30 June 2005 and in the financial statements to 31 December 2005.
KME gave the appointment for the full audit and review of the IFRS reconciliation statements to 1 January 2004 and 31 December 2004 to the Deloitte & Touche S.p.A. auditing company; their report is available on the company website www.kmegroup.it.

2.2 Basis of Consolidation

(a) Subsidiaries

Subsidiaries are companies over which KME has the power to direct and control their financial and operating policies. Generally, this power is accompanied by the right to cast more than 50% of the votes at meetings of corporate governance bodies.
Assets and liabilities and income and expenses of subsidiaries that are consolidated on a line-by-line basis are reflected in their full amount in the consolidated financial statements. The value of the respective equity investments is eliminated against the corresponding interests in the shareholders' equities of the investee companies, with the individual assets

and liabilities recognized at their value on the date when control was acquired. Any residual difference is booked as goodwill, if positive, or recognized in earnings, if negative. The interest of minority shareholders in shareholders' equity and earnings is reflected on separate lines in the financial statements. Following initial recognition, "goodwill" is valued at cost, net of impairment losses accumulated in accordance with the provisions of IAS 36 *Impairment of Assets*.
On the IFRS transition date, there was no change in the scope of consolidation, which does not include subsidiaries that are not significant nor companies the consolidation of which would not have a material impact. These are mainly companies that are engaged in distribution activities. The impact of the above-mentioned exclusions is not material and, consequently, these omissions have no impact on the financial decisions of the users of these financial statements.
Unrealized earnings of a material amount that have been generated by intra-Group transactions have been eliminated. Receivables, payables, income, expenses, guarantees, commitments and risks arising from transactions between consolidated companies have also been eliminated. Intercompany losses were not eliminated because they are indicative of a reduction in the value of the goods being sold. The financial statements of all consolidated subsidiaries have been restated to make them consistent with the accounting principles and policies adopted by the Group.
The table below lists the subsidiaries that are consolidated line by line.

Subsidiaries consolidated at equity

Name	Reg. Offices	Currency	Share cap.	Type of business	% held	
					Directly	Indirectly
KME Group S.p.A.	Italy	Euro	319,643,223	Financial co.	Parent Company	
KM Europa Metal A.G.	Germany	Euro	142,743,879	Copper and alloys proc.	100.00%	
Europa Metalli S.p.A.	Italy	Euro	100,000,000	Copper and alloys proc.		100.00%
Tréfimétaux S.A.	France	Euro	53,000,000	Copper and alloys proc.		100.00%
KME Iberica S.A. (*)	Spain	Euro	1,943,980	Holding		100.00%
LOCSA SA	Spain	Euro	10,040,000	Copper and alloys proc.		100.00%
KME Verwaltungs und Dienst. mit beschr.	Germany	Euro	10,225,838	Copper and alloys proc.		100.00%
Fricke GmbH	Germany	Euro	25,564	Holding		100.00%
Kabelmetal Messing Beteiligungsges mbH Berlin	Germany	Euro	15,338,756	Real estate		100.00%
Fricke GmbH & Co. KG	Germany	Euro	1,329,359	Copper and alloys proc.		100.00%
Cuprum S.A.	Spain	Euro	60,910	Distribution		100.00%
Bertram Gmbh	Germany	Euro	300,000	Services		100.00%
KME Ibertubos S.A.	Spain	Euro	332,100	Copper and alloys proc.		100.00%
KME Yorkshire Ltd.	England	GBP	10,014,603	Copper and alloys proc.		100.00%
Yorkshire Copper Tube	England	GBP	3,261,000	Non-operating		100.00%
Yorkshire Copper Tube (Exports) Ltd.	England	GBP	100	Non-operating		100.00%
KME Brass Gmbh	Germany	Euro	50,000	Copper and alloys proc.		100.00%
TMX Brass S.A.S.	France	Euro	7,800,000	Copper and alloys proc.		100.00%
Immobiliare Agricola Limestre S.r.l.	Italy	Euro	7,735,000	Real estate	100.00%	
EM Brass S.r.l.	Italy	Euro	15,025,000	Copper and alloys proc.		100.00%

(*) During the year the subsidiary S.I.A. - Santa Barbàra S.A. incorporated KME Iberica SL, changing its corporate name to KME Iberica S.A. Since these are companies under regular control of the Parent Company, the transaction did not have any equity, financial or income effects on the consolidated financial statement, pursuant to paragraph 3 point (b) of IFRS 3.

At 31 December 2006, there were no changes in the scope of consolidation.

(b) Associates

Associate companies are those companies over which KME GR exercises significant influence, but not control. Significant influence is deemed to exist when GIM controls, either directly or indirectly through subsidiaries, 20% or more of the votes that can be cast at a Shareholders' Meeting of the investee company. Investments in associates are consolidated by the equity method.

Under the equity method, an investment is initially recognized at cost, which is later adjusted to reflect the controlling company's interest in profits or losses generated after acquisition. Dividends received reduce the carrying amount of the investment.

The table below lists the associates that are consolidated by the equity method.

Subsidiaries consolidated at equity

Name	HQ	Activity	% owned by KME	
			Directly	Indirectly
Dalian Dashan Chrystallizer Co. Ltd	China	Manufacturing		30.00%
Dalian ETDZ Dashan Surface Machinery Ltd	China	Manufacturing		30.00%

On 19 December 2006, KME announced that it had signed an agreement to increase its shareholding in Dalian Dashan Christallizer Co. Ltd and in Dalian ETDZ Dashan Surface Machinery Ltd simultaneous to the acquisition of 70% of the company Dalian Dashan Machinery Co. Ltd. The directors believe that this agreement will allow them to acquire the financial control of the three companies involved within the first half of 2007.

(c) Joint ventures

A joint venture is a contractual agreement whereby two or more parties carry out business operations that they control jointly. Joint control is the shared control, in accordance with contractual provisions, of the company's business activity.
Joint ventures are consolidated by the proportional method, as defined in Paragraphs 30 to 37 of IAS 31.
As of the date of this report, the Group was not a party to any joint venture, as defined under IAS 31.

2.3 Transactions in Foreign Currencies

(a) Functional and Presentation Currency

All amounts are expressed in euros, which is also the functional currency of the Parent Company.

(b) Conversion of the Financial Statements in Currencies other than the Euro

Financial statements expressed in foreign currencies were converted into euros by applying the average exchange rates for the period to individual income statement items, and the current exchange rates at the closing date of these statements to individual balance sheet items.

The exchange rates used to convert foreign currencies are listed below:

1 Euro	0.6853 GBP	31.12.2005 used to convert opening balances
1 Euro	0.6716 GBP	31.12.2006 used to convert balance sheet figures
1 Euro	0.6817 GBP	average for 2006 used to convert income statement figures
1 Euro	9,5204 RMB	31.12.2005 used to convert opening balances
1 Euro	10.2793 RMB	31.12.2006 used to convert balance sheet figures
1 Euro	not applicable	average for 2006 used to convert income statement figures

The portions of the difference between the earnings amounts converted by using the average exchange rates for the period and those obtained by applying end-of-December exchange rates attributable to the Group and to minority shareholders were posted to the technical consolidation reserves and to minority interest in shareholders' equity, respectively. If the investment in an associate is divested, these differences are recognized in earnings as part of the gain or loss generated by the sale of the investment.

2.4 Property, Plants and Equipment

Property, plants and equipment is recognized at purchase or production cost, including directly attributable incidental expenses.
Property, plants and equipment is valued at cost, net of depreciation and accumulated impairment losses, except for land, which is not depreciated and is valued at cost, less accumulated impairment losses.
Depreciation is taken starting in the month when an asset is available for use or has the potential for providing the economic benefits associated with it. Depreciation is booked monthly on a straight-line basis until the end of an asset's useful life or, in the event of disposals, until the last month of use.
Depreciation rates are based on the useful lives of the different facilities, as determined by the findings of a survey carried out by *American Appraisal*. As of January 1, 2004, these new useful lives were applied to components of Property, plants and equipment to which the fair value criterion had been applied in lieu of cost. The new useful lives were applied to the other components of Property, plants and equipment as of January 1, 2005.
Financial expense incurred to acquire Property, plants and equipment is charged to income, unless it can be directly attributed to the acquisition, construction or production of an asset and its capitalization is justified.
Replacement parts of significant value are capitalized and depreciated over the useful lives of the assets to which they belong. Other replacement parts are charged to income when the expense is incurred.
Assets acquired under finance leases are booked as Property, plants and equipment as an offset to the corresponding liability. Lease payments are broken down into their components: financial expense, which is charged to income, and principal repayment, which is deducted from indebtedness. Assets owned in financial leasing are recognised at either their cost or the current value of the minimum leasing payments due at the starting date of the contract, whichever is lower.
If there is an indication of impairment losses, Property, plants and equipment is subjected to an impairment test. The test consists of estimating an asset's recoverable value, which is defined as the greatest out of the net sale price and the use value, and comparing it with the corresponding carrying amount. If the recoverable amount is less than the carrying amount, the latter is written down to the recoverable amount. The amount of the write-down is charged to income or to a revaluation provision, if such a provision existed when the same assets were revalued in the past. If subsequent revaluations become necessary, the reverse process is applied.

2.5 Intangible Assets

(a) Goodwill

Goodwill represents the difference between the cost incurred to acquire the investment in KME Europa Metal A.G. and the value of its shareholders' equity at the time of acquisition. Goodwill and other intangible assets with an indefinite useful life are not amortized. The recoverability of their carrying amounts is checked annually and whenever events indicate that an impairment loss may have occurred. Write-downs may not be reversed.

(b) Other Intangible Assets with a Finite Useful Life

These are intangible assets that are identifiable, are controlled by the Company and are capable of producing future economic benefits.

A company may acquire intangible assets in any of the following ways:
- purchase from a third party;
- as a result of a business combination;
- internal development.

In the first two cases, intangible assets are measured initially and respectively at cost and at fair value, including any directly attributable incidental charges. They are then amortised on a straight line over their useful lives, which corresponds to an estimate of the period during which the assets are used by the company, usually a length of time between 3 to five years. These assets are shown net of possible write-downs for impairments losses, which are determined the same way as for "property, plants and equipment". It is assumed that at the end of their useful lives, their residual value will be zero.

Assets developed internally are only capitalised when they meet the requirements detailed in Paragraph 57 of IAS 38.

2.6 Investment Property

This account includes land and buildings that are held for the purpose of earning rental income, or for capital appreciation, or both. These assets are carried at fair value, and are therefore not depreciated on a straight-line basis.

2.7 Financial Assets

In the financial statements of the individual subsidiaries, all equity investments in unconsolidated subsidiaries, associates and joint ventures are carried at cost.

Consistent with the guidelines provided in Paragraph 2.2 above, equity investments in unconsolidated subsidiaries are carried at cost, adjusted for impairment losses.

Any other equity investments are carried at fair value, with the resulting gains or losses recognised in equity. When the fair value can not be determined reliably, equity investments are carried at cost, adjusted for impairment losses.

Non-derivative financial assets with fixed or determinable payments and fixed maturities that the company plans to hold to maturity are classified as assets held to maturity. The assets in this category are carried at the amortised cost method, using the effective interest criterion, as defined in IAS 39.

Financial assets that are acquired or held mainly for sale or short-term repurchase agreements and the derivatives not designated as hedging instruments are classified as fair value assets recognised in the income statement, i.e. designated assets. These assets are carried at fair value, with the resulting gains or losses recognised in earnings.

With the exception of financial instruments that represent equity capital, non-derivative financial assets with fixed or determinable payments that are not traded on an active market, and cannot be included in one of the categories above, are classified as "*loans and other receivables*", and are carried at amortised cost using the effective interest method. For current *loans and receivables* and in general for all short term receivables and payables for which time value has little relevance, we assume that their amortised expense coincides with their carrying amount.

All other non-derivative financial assets that cannot be classified in one of the three categories above are classified as "*financial instruments available for sale*" and carried at fair value. Their gains or losses are recognised at equity, except for impairment losses.

All financial assets, except for "*fair value financial assets recognised to the income statement*", are tested for impairment losses as required by Paragraphs 58-70 of IAS 39.

Treasury shares are carried at historical cost and booked as a deduction from consolidated shareholders' equity.

The Group uses derivatives to hedge against changes in the price of raw materials, interest rates and exchange rates. The use of derivatives — mainly London Metal Exchange (LME) contracts, Interest Rate Swaps (IRS) and forward contracts — is regulated by specific risk management strategies, approved by the Board of Directors. The Group does not use derivative financial instruments for speculative purposes.

2.8 Inventories

Inventories are carried at the lower of cost and net realisable value. Cost is determined through the application of the weighted average cost method on a quarterly basis, and includes all direct charges and a share of the other costs sustained to bring the inventories to their current place in their current conditions. The manufacturing costs incurred for work in process and finished goods include directly attributable incidental expenses and a pro-rata share of indirect manufacturing costs that can be reasonably allocated to the products in question. Completed portions of contract work in progress are carried based on their corresponding contractual consideration that can be accrued with reasonable certainty, less distribution costs.

2.9 Cash and Cash Equivalents

This account includes cash on hand, sight deposits and highly liquid short-term financial investments that may be readily convertible into cash, and are not subject to a significant change in value (as per IAS 7, Paragraph 45).

2.10 Shareholders' Equity

The Company's share capital is equal to the nominal value of ordinary and savings shares, subscribed and paid in as of the reference date for these statements, less any stock subscription arrears owed to shareholders. As required by IAS 32, the nominal value of repurchased treasury shares is deducted from issue share capital. This presentation is however only provided in the Notes to the financial statements. On the balance sheet, the historical cost of treasury shares is shown separately as a deduction from shareholders' equity.

Reserves for treasury shares is no longer shown due to the different method of presentation required under IAS. The existing reserve balance was reclassified to the individual reserves that had been originally used to establish it. The Parent Company's Notes to the financial statements state indications regarding the individual reserves established according to the civil code.

Costs incurred for shareholders' equity transactions are posted as a direct deduction from equity reserves, using the additional paid-in capital account for this purpose.

The balance of adjustments made for the transition to IAS is booked to a separate equity reserve called the "reserve for initial adoption to IAS/IFRS".

2.11 Liabilities

Liabilities are shown at their amortised cost. When the gains and losses for this are insignificant — as for short-term trade payables — these are shown at nominal value.

2.12 Current and Deferred Taxes

Current and deferred income taxes are calculated based on the estimate of taxable income, according to the tax rates and laws that are in force or have effectively been approved at the closing date of the period.

Deferred and prepaid taxes are calculated on the temporary differences between the amounts assigned to the assets and liabilities on the financial statements and those used for tax purposes according to the balance sheet liability method. Deferred-tax assets are recognised when their recovery is highly probable. The book value of deferred-tax assets is reviewed at the reference date of each financial year to verify that their future recovery is probable.

Deferred-tax items are booked as non-current assets or liabilities and can be offset by each individual subsidiary if the requirements of IAS 12 can be met.

Current income tax and deferred taxes are shown in the income statement, except for current and deferred taxes deriving from transactions that are paid directly to shareholders' equity.

2.13 Employee Benefits

Benefits are provided to employees at the end of the employment relationship in accordance with plans that, based on their characteristics, can be classified as "defined contribution" or "defined benefit" plans. Under defined contribution plans, a company's obligation, which is limited to the payment of contributions to a separate legal entity (which can be the Government or a fund), is represented by the contributions that are due on the reference date of the financial statements. As is the case for the provision for employee severance indemnities, which is governed by article 2120 of the Italian Civil Code, the liability for a defined benefit plan, which is computed net of any assets earmarked for the plan, is determined on the basis of actuarial assumptions and is recognized on an accrual basis, taking into account the length of service necessary to receive the benefits. Actuarial gains or losses on defined benefit plans that arise from changes in actuarial assumptions or the terms of a plan are recognized in earnings on a pro rata basis using the so-called "corridor method", i.e., they are recognized when the net value or actuarial gains and losses that were not recognized at the end of the previous accounting period is greater than 10% of the present value of the obligation or 10% of the fair value of any asset earmarked for the plan, whichever is larger.

All liability evaluations are provided by independent actuaries.

2.14 Provisions

Provisions reflect liabilities the due date or amount of which is uncertain. Provisions are recognized only when:

1. the Group is currently subject to an obligation (legal or contingent) as a result of a past event;
2. it is likely that, in order to discharge this obligation, the Group will have to use resources that could otherwise produce financial benefits;
3. a reliable estimate can be made of the amount of the obligation.

The amounts set aside as provisions represent the best estimate of the charge that will be incurred to discharge an obligation or transfer it to a third party. When the computation of the present value of money is a significant factor, the amount of a provision should be equal to the present value of the charges that the Group expects to incur to discharge the obligation.

Provisions for restructuring costs are recognised only when the Group has a detailed formal plan to do so, which identifies at least: the assets and the main operations units involved, the costs to be sustained, the approximate number of employees involved and when the third parties involved may reasonably expect that the company will implement the said restructuring, either because it is under way or it has been publicly announced.

2.15 Revenue Recognition

Sales and service revenues are recognized when the risks and benefits inherent in the ownership of an asset or the performance of a service have effectively been transferred.

2.16 Leases

A lease is a contract whereby the lessor transfers to the lessee the right to use an asset for a pre-set period of time in exchange for payment or a series of payments. Contracts that effectively transfer all the risks and benefits inherent in the ownership of an asset are called finance leases, even when ownership is not transferred at the end of the lease. Finance leases are recognised in accordance with IAS 17 Paragraphs 20 to 32.

Leases that cannot be defined as finance leases are called operating leases.

2.17 Dividends

Dividends are recognised as a liability only during the period after the general meeting of shareholders has declared them.

2.18 Stock Options

Starting from the financial statements at 31 December 2006, labour costs include the stock options given to executive members of the KME Group S.p.A. Board of Directors, and some Group Managers, since their nature is basically one of remuneration. The fair value of stock options was set according to the value of the option when it was assigned, applying the *Black & Scholes* model that keeps account of their exercise rights, the current value of the underlying share, the exercise price, the maturity, dividends, expected volatility and the risk-free rate. The stock options expense is recognised an offset in shareholders' equity in the item "reserve for stock options". The fair value of rights given to managers of KME Group S.p.A. subsidiaries is deducted from the companies where the managers hold their positions, in early accordance with IFRIC 11 as provided for in Paragraph 12 of this regulation.

2.19 Earnings per Share

The following criteria were used in the calculation of basic and diluted earnings per share:

1) the numerator is determined as the result for the year attributable to the Parent Company adjusted by the result attributable for the current year to savings shares outstanding during the year, excluding those savings shares held as treasury shares either directly or indirectly through subsidiaries;
2) the denominator of "basic earnings per share" is determined as the weighted average of ordinary shares outstanding during the year, excluding any ordinary shares held as treasury shares;
3) the denominator of "diluted earnings per share" is determined as the weighted average of ordinary shares adjusted for the number of new ordinary shares:
    - at the conversion of all warrants in circulation;
    - at the exercise of all stock options.

For this calculation it has been assumed that the conversion of warrants and the exercise of stock options take place at the beginning of the year, and that no additional income or lower costs result from their conversion.

2.20 Use of Estimates

The preparation of these financial statements and the accompanying Notes in accordance with IFRS required that the Directors make estimates and assumptions which affect the carrying value of the assets and liabilities in those statements.
Estimates have been primarily made to determine the useful lives of fixed assets, to make provisions for credit risk, to determine impairment, to calculate for employee benefits, taxation and restructuring provisions, to determine intangible assets having indeterminate lives, and in the measurement of other accruals and provisions.
These estimates and assumptions will be periodically reviewed and any resulting effects will be immediately recognised in the income statement. At the reference date for these statements, the Directors believe, however, that the estimates and assumptions made reflect the best assessment possible given the information available. Moreover, the Directors believe that the estimates and assumptions made will not result in material adjustments to the carrying values of assets and liabilities during the following year.

3. Risk Management

The Group is subject to various operating and financial risks in carrying out its activities. The policy of the Group is to eliminate or at least minimise those risks via hedging strategies established and approved by the Board of Directors. As a result, the Group has formal procedures at its disposal to define the objectives and procedures for hedging risks: credit risk, liquidity risk, foreign exchange risk, interest rate risk and, above all, fluctuations in the price of raw materials.

Credit risk is managed chiefly by selecting the customer portfolio on the basis of past experience, obtaining guarantees and insuring the majority of trade receivables.

Liquidity risk may arise from the difficulty in obtaining loans or advances to support operations within the necessary period of time. Cash inflows and outflows and the Group's cash situation are monitored and coordinated centrally under the control of Group Treasury.

The Group is exposed to the risk of fluctuations of foreign exchange rates and interest rates as it operates in an international context in which transactions are carried out in various currencies and at different interest rates. Foreign exchange risk is primarily the result of the fact that the Group's production activities are carried out in different geographical locations, and that the markets in which the Group sells its products are situated throughout the world. The Group's policy is to hedge against all of these risks by using derivative financial instruments such as cross-currency swaps and forward contracts.

The management of the risk of fluctuations in raw materials prices (copper above all) is, however, the most important and the most strategic. In order to do this, the Group uses physical transactions or forward contracts on the London Metal Exchange (LME), aiming at hedging 100% of the risk.

4. Explanatory Notes to the Consolidated Financial Statements

4.1 Property, Plants and Equipment

(Thousands of Euros)	Land	Buildings	Plant & mach.	Other assets	Constr. in prog.	Total
At 31 December 2005						
Historic cost	56,934	181,076	871,083	149,205	27,008	1,285,306
Accum. depreciation	80	89,223	465,620	106,078	0	661,001
Net book value	**56,854**	**91,853**	**405,463**	**43,127**	**27,008**	**624,305**
At 31 December 2006						
Historic opening balance	56,934	181,076	871,083	149,205	27,008	1,285,306
Foreign exchange diff.	113	81	1,387	45	15	1,641
Change in consolidation perimeter	0	0	0	0	0	
Increases	0	640	12,648	2,219	30,068	45,575
Reclassifications	1,069	6,218	20,626	2,305	(27,334)	2,884
Decreases	(146)	(133)	(23,191)	(2,207)	0	(25,677)
Historic closing balance	**57,970**	**187,882**	**882,553**	**151,567**	**29,757**	**1,309,729**
At 31 December 2006						
Accum. depreciation	80	89,223	465,620	106,078	0	661,001
Foreign exchange diff.	0	4	1,199	42	0	1,245
Change in consolidation perimeter	0	0	0	0	0	0
Amortisation and depreciation	0	5,449	38,332	8,499	0	52,280
Impairment losses	0	0	(2,027)		0	(2,027)
Reclassifications	0	0	0	0	0	0
Decreases	0	(284)	(20,665)	(1,744)	0	(22,693)
Accum. depreciation	**80**	**94,392**	**482,459**	**112,875**	**0**	**689,806**
At 31 December 2006						
Historic closing balance	57,970	187,882	882,553	151,567	29,757	1,309,729
Accum. depreciation	80	94,392	482,459	112,875	0	689,806
Net closing balance	**57,890**	**93,490**	**400,094**	**38,692**	**29,757**	**619,923**
of which finance leases:	**1,300**	**3,872**		**308**		**5,480**

Part of the assets above (Euro 272 million) were lodged to guarantee the new refinancing contract that was signed during the year.

The largest investments during the year are detailed in the relevant Report contained within these statements.

During the fiscal year, the Directors recognised depreciations for Euro 2.3 million relating to activities of the subsidiary TMX S.A. Depreciations are carried net of impairment losses for the year.

Reclassifications (Euro 2.9 million) include the reclassification of a property of the subsidiary Immobiliare Agricola Limestre S.r.l. pursuant to IAS 40 Par. 57 paragraph (a), which was previously classified as a real estate investment and is now classified as property under use of owner.

Assets held in financial leasing involve the property in the Novoli district of Florence that is the Group's headquarters (for Euro 5.2 million), and some equipment and telecoms facilities (for Euro 0.3 million). The leasing contract for this piece of real estate includes two purchase options on the dates of 30 September 2009 or 30 September 2016.

The following table shows details of the minimum future payments for finance leases at financial statement reference dates and their current value:

(Thousands of Euros)	Within 1 year	From 1 to 5 year	Over 5 year	Total 31.12.2006
Minimum payments due	508	1,841	3,896	6,245
Interest	10	256	1,443	1,709
Current value	498	1,585	2,453	4,536

4.2 *Investment Property*

(Thousands of Euros)	Investment property at fair value
Net book value at 1st January 2006	**9,272**
Increases for acquisitions	0
Increases for capitalised expenses	2,653
Increases for company aggregations	0
Disposals	0
Change in fair value	1,550
Change of classification	(2,884)
Other changes	0
Net book value at 31 December 2006	**10,591**

The item “Investment property” is composed of the investments of Immobiliare Agricola Limestre S.r.l. in plots of land and buildings (Euro 7.8 million) and buildings owned by the Parent Company (Euro 2.8 million). Investment property consists of land and buildings held to earn rentals or for capital appreciation, and is carried at fair value. During the fiscal year, no revenues from rental fees or operating costs directly connected to the said real estate investments were recognised to the income statement.
Increases during the year of Euro 4.2 million are imputed to the increase in the fair value of items, and to improvements made on some investment property of the subsidiary Immobiliare Agricola Limestre S.r.l..
The reclassifications from investment property to property under use by owner pursuant to IAS 40 Par. 57 (a) regard the subsidiary Immobiliare Agricola Limestre S.r.l..

4.3 *Goodwill and Consolidation Differences*

During the year the value of consolidation differences did not record any changes. The said value inherent to the cost of the investment in KME AG was compared with the recoverable value determined with an estimate of its use value. The use value of this asset is estimated by using financing flow projections based on reasonable and sustainable hypotheses contained in the most recent forecasts approved by company bodies. The discounting back of cash flows, net of fiscal and financial charges, was obtained by using the rate that results from sum of the return of a risk-free investment and an equity risk premium multiplied by the volatility index of its specific sector relative to that of the market (i.e. the *Weighted Average Cost of Capital approach*).
Financing flows include a constant growth rate not higher than the average long term growth rate of the industrial sector in which the Group operates.

4.4 *Other Intangible Assets*

	Other assets	Work in progress	Total
At 31 December 2005			
Opening balance	14,539	13	14,552
Accumulated amortisation	12,921	0	12,921
Net opening balance	**1,618**	**13**	**1,631**
At 31 December 2006			
Opening balance	14,539	13	14,552
Foreign exchange diff.	0	0	0
Change in consolidation perimeter	0	0	0
Increases	453	11	464
Reclassifications	13	(13)	0
Decreases	(29)	0	(29)
Closing balance	**14,976**	**11**	**14,987**
At 31 December 2006			
Opening accumulated amortisation	12,921	0	12,921
Foreign exchange diff.	0	0	0
Change in consolidation perimeter	0	0	0
Increases	1,140	0	1,140
Reclassifications	0	0	0
Decreases	(29)	0	(29)
Closing accumulated amortisation	**14,032**	**0**	**14,032**
At 31 December 2006			
Closing balance	14,976	11	14,987
Closing accumulated amortisation	14,032	0	14,032
Net closing balance	944	11	955

There were no significant changes to this account during 2005.

4.5 Investments in Subsidiaries and Associates, Other Equity Investments and Equity Investments Carried at Equity

A list of the Group's equity investments is provided below:

Name	Registered office	Type of business	% held by KME		December 2006	December 2005
			Directly	Indirectly	(Thousand of Euro)	
Subsidiaries and associates measured at cost						
Accumold AG	Switzerland	Services		100.00%	0	0
Europa Metalli Tréfimétaux Deutschland GmbH	Germany	Services		100.00%	0	0
Europa Metalli Tréfimétaux UK Ltd.	England	Services		100.00%	595	583
Evidal Schmole Verwaltungsges mbH	Germany	Services		50.00%	0	0
KME Austria Vertriebgesellschaft mbH	Austria	Distribution		100.00%	168	168
KM - Hungaria Szinesfem Kft.	Hungary	Distribution		100.00%	8	8
KME Metal GmbH	Portugal	Services		100.00%	511	511
KME Polska Sp.zo.o.	Poland	Distribution		100.00%	64	64
KME (Suisse) S.A.	Switzerland	Distribution		100.00%	1,000	1,000
KME America Inc,	United States	Distribution		100.00%	7	7
KME Asia Pte Ltd.	Singapore	Distribution		100.00%	99	99
KME Chile Lda	Chile	Distribution		100.00%	18	18
KME China Limited	China	Distribution		100.00%	657	1,149
KME Czech Republic	Czech Rep.	Distribution		100.00%	3	3
KME Danmark A/S	Denmark	Distribution		100.00%	134	134
KME Messing Beteiligungs GmbH	Germany	Services		100.00%	511	511
KME Portugal Metais Lda	Portugal	Distribution		100.00%	0	177
Irish Metal Industrial Ltd.	Ireland	Distribution		100.00%	0	0
YIM Scandinavia A.B.	Sweden	Distribution		100.00%	0	0
KME Moulds Mexico SA de CV	Mexico	Distribution		100.00%	6	6
Luebke GmbH	Germany	In liquidation		100.00%	102	102
N.V. KME Benelux SA	Belgium	Distribution		100.00%	885	885
Societe Haillane de Partecipations	France	Financial co.		99.99%	40	40
TMX Components sas	France	Financial co.		65.00%	99	99
XT Limited	England	Distribution		100.00%	0	0
KME Metals (Dongguan) Ltd.	China	Distribution		100.00%	0	0
Informatica Y Organizacion SA	Spain	Services		100.00%	0	0
Total					**4,907**	**5,564**
Other investments stated at cost						
Consorzio Italmun	Italy	In liquidation	50.00%		129	129
Other Tréfimétaux S.A. equity interests	France	Various	n.a.	n.a.	116	116
Total					**245**	**245**
Interest in result of associates valued at equity						
Dalian Dashan Chrystallizer Co. Ltd.	China	Manufacturing		30.00%	1,813	1,780
Dalian ETDZ Dashan Surface Machinery Ltd.	China	Manufacturing		30.00%	822	793
Total					**2,635**	**2,573**

The main changes in the item "investments in subsidiaries and associates" are reviewed below:

- the investment held in Europa Metalli Tréfimétaux UK Ltd increased by Euro 12,000 due to foreign exchange fluctuations;
- the decrease of Euro 177,000 is due to the disposal of the interest in the subsidiary KME Portugal Metais Lda;
- the decrease of Euro 1,149,000 was due to an impairment loss, and there was a related increase in share capital of Euro 657,000 of the equity investment in KME China Ltd..

The item "other interests of Tréfimétaux S.A." includes small equity investments (usually of less than 1%) in companies that operate in the building sector. The French companies must pay a certain percentage of their labour costs as contributions, loans and investments to help their employees pay for their real estate properties. The value of these investments remained unchanged.

Associated companies were consolidated with the equity method.

The value of these investments includes Euro 486,000 in goodwill.

The table below shows some basic financial information regarding the following associated companies:

Name (Thousands of Euros)	Country	Assets	Liabilities	Revenues	Profit for period	% held
Dalian Dashan Chrystallizer Co. Ltd.	China	6,294	929	981	528	30%
Dalian ETDZ Dashan Surface Machinery Co. Ltd.	China	1,441	85	900	191	30%

4.6 Other Non-current Assets

This item is mostly composed of security deposits of EM (Euro 1 million), receivables to insurance companies of KME AG (Euro 2.3 million), loans to employees, provided mostly by the Tréfimétaux S.A. (TMX) subsidiary pursuant to a law that entitles employees to receive loans from their employer to purchase a home (Euro 4.2 million), and amounts held by credit institutions (Euro 17.5 million, including accrued interest to 31 December 2006) as interest-bearing security deposits to ensure partial funding for the fines levied by the European Commission for violations of Article 81 of the EC Treaty. The unfunded balance is covered by bank guarantees.

No portion of the abovementioned receivables is due within one year.

4.7 Inventories

(Thousands of Euros)	Beginning inventory	Changes in the period	Ending inventory
1) Raw materials, auxiliaries and supplies	377,011	228,338	605,349
2) Work in progr. and semi-finished goods	30,819	3,790	34,609
3) Contract work in process	982	(283)	699
4) Finished goods and merchandise	35,549	7,421	42,970
Total	**444,361**	**239,266**	**683,627**

Inventories are carried at either cost or their realisable value, the lower of the two.

At 31 December 2006, a write-down for Euro 82.3 million was included in the income statement to keep account of the lower realisable price compared to the cost price calculated according to the average cost weighted on a quarterly basis.
The net realisable value, which is the estimated sales price under normal business conditions, was calculated net of manufacturing and sales costs.
During the next financial years, should the circumstances that caused this write-down cease to exist, this adjustment will be reversed in such a way that the book value of inventories are always carried at the lower price between the cost price and the net realisable value.

The increase in the value of inventories is largely due to the price increase for raw materials that was recorded during the year. The increase in inventory quantities only weighed on the increase in value of inventories for Euro 37.6 million.

Quantities comparison schedule			
Company owned inventory	**31.12.2005**	**31.12.2006**	**Change %**
Total tonnes	**114,206**	**123,751**	***8.4%***

118,600,000 tonnes of owned stock were pledged to guarantee lines of credit made available to the Group.

4.8 Trade Receivables

(Thousands of Euros)	Balance at 31.12.2005	Change during period	Balance at 31.12.2006
1) Receivables from customers	361,277	(128,932)	232,345
(Allowance for doubtful accounts)	(7,653)	(13)	(7,666)
Net amount	**353,624**		**224,679**
2) Receivables from subsidiaries	4,534	1,419	5,953
3) Receivables from associates	62	(25)	37
4) Receivables from Parent Co.	50	(26)	24
Total	**358,270**	**(127,577)**	**230,693**

The book value of trade receivables approximates their fair value.

The decrease in trade receivables is mainly due to the increased use of factoring transactions without recourse, and their subsequent derecognition.

4.9 Other Receivables and Current Assets

(Thousands of Euros)	Balance at 31.12.2005	Change during period	Balance at 31.12.2006
1) Tax credits	21,939	(7,878)	14,061
2) Pre-payments to suppliers	9,152	6,935	16,087
3) Accrued income and pre-paid expenses	3,458	(1,214)	2,244
4) Receivables from factoring companies	7,971	14,400	22,371
5) Other receivables	7,621	5,407	13,028
Total other current assets	**50,141**	**17,650**	**67,791**

The book value of other receivables approximates their fair value.

4.10 Current Financial Assets

(Thousands of Euros)	Balance at 31.12.2005	Change during period	Balance at 31.12.2006
Financial assets available for sale	557	(557)	0
Financial assets held for trading	4,621	622	5,243
LME contracts	8,248	7,084	15,332
Interest Rate Swaps (IRS)/forward contracts	58	374	432
Receivables from factoring companies	0	53,425	53,425
Financial receivables from subsidiaries	920	(5)	915
Total	**14,404**	**60,943**	**75,347**

Financial assets held for trading include 5,242,497 G.M.I. S.p.A. savings shares held by the Parent Company. The increase for the period involves the adjustment of these shares with a unit value of Euro 1 each, net of the sale of 461,947 shares. The unit value of Euro 1 is the exercise price of a call option for the credit institutions made as part of the previous banking agreement that was signed in February 2005 and is no longer valid.

LME contracts represent the value of the potential gains that resulted from the fair value measurement of contracts outstanding at 31 December 2006.

Receivables from factoring companies mostly include the value of receivables given and not yet collected at 31 December 2006.

4.11 Cash and Cash Equivalents

(Thousands of Euros)	Balance at 31.12.2005	Change during period	Balance at 31.12.2006
Bank and postal deposits	151,194	8,264	159,458
Cash float	798	1,842	2,640
Total	**151,992**	**10,106**	**162,098**

Cash and cash equivalents are composed of bank and postal deposits, and cash floats.

4.12 Shareholders' Equity

An analysis of the changes in shareholders' equity is provided elsewhere in this publication.

4.13 Provisions for Employee Benefits

(Thousands of Euros)	Balance at 31.12.2005	Increases	Decreases	Balance at 31.12.2006
Defined benefits pension fund	143,426	11,323	(9,363)	145,386
Employee Sev. Fund	23,237	2,546	(4,265)	21,518
Total	**166,663**	**13,869**	**(13,628)**	**166,904**

The amount shown under defined benefit pension funds is net of the value of any assets earmarked for the benefit of the plans. Defined-benefit pension plans include Euro 119.2 million for the German subsidiaries and Euro 26.2 million for the KME Yorkshire Ltd. subsidiaries.

General Criteria Used:

	31.12.2005	31.12.2006
Discount rate	4.0%-4.9%	4.5%-5.3%
Rate of return on assets	7.0%	6.9%
Increase in future compensation	2.2%-3.0%	2.3%-3.0%
Increase in future productivity	1.5%-3.0%	1.75%-3.0%
Average residual working life	15 years	14 years

Net value of liabilities:

	31.12.2005	31.12.2006
Present value of partly or fully funded obligations	76,173	75,289
Fair value of assets earmarked for defined benefit plans	(59,010)	(65,499)
Shortfall	**17,163**	**9,790**
Present value of unfunded obligations	161,954	162,966
Unrecognised actuarial gains or losses	(12,454)	(5,852)
Cost of benefits provided and not yet recognised	0	0
Amount not recognised as an asset, pursuant to IAS 19 Par. 58 (b)	0	0
Net liability recognised on the balance sheet	**166,663**	**166,904**

Changes in Income Statement (Thousands of Euros)	**2005**	**2006**
Estimated cost relative to current service performance	6,337	6,583
Interest liabilities	10,872	10,323
Expected yield of assets servicing the plan	(3,152)	(3,570)
Recognised actuary profits (losses)	58	455
Estimated cost relative to past service performance	0	22
Effects of any reductions or extinctions	0	56
Total cost recognised in the income statement	**14,115**	**13,869**

All amounts recognised to the income statement are included in the item "labour costs".

Other information:

Current value of bonds (Thousands of Euros)	**2006**
Opening balance	238,127
Cost relative to current service performance	6,583
Interest on bonds	10,323
Contributions from participants in the plan	290
Recognised actuary (profits) losses	(5,861)
Extinct or reduced liabilities	0
Foreign exchange differences on non-domestic plan	1,533
Paid and distributed benefits	(12,762)
Cost relative to current service performance	22
Closing balance	**238,255**

Fair value of assets servicing the stock options plans (Thousands of Euros)	**2006**
Opening balance	59,010
Expected yield of assets servicing the plan	3,570
Recognised actuary profits (losses)	1,234
Foreign exchange difference on plans not in Euros	1,175
Employer contribution	1,861
Contributions from participants in the plan	290
Extinctions	0
Paid and distributed benefits	(1,641)
Final balance of assets servicing the plan	**65,499**

Current value of defined benefits plans and adjustments based on experience (Thousands of Euros)	**2006**
Current value of defined benefits obligations	238,255
Assets servicing the plan	(65,499)
Surplus (deficit)	172,756
Experience-based adjustments to liabilities in the plan	2,714
Experience-based adjustments to liabilities in the plan	70

4.14 Long-term Borrowings and Financial Liabilities

(Thousands of Euros)	Balance **at 31.12.2005**	Changes **for the period**	Balance **at 31.12.2006**
1) Bank borrowings	453,395	28,661	482,056
2) Amounts owed to Parent Co.	130,000	(130,000)	0
3) Amounts owed to leasing co.	4,471	(264)	4,207
4) Amounts owed to others	1,513	(423)	1,090
Total	**589,379**	**(102,026)**	**487,353**

During the year, KME Group S.p.A. signed two new refinancing contracts worth a total of Euro 1.65 billion. These agreements were made with GE Commercial Finance (GE Corporate Finance Bank S.A.) and Deutsche Bank each for their own facility.

The first agreement, signed with GE Commercial Finance, is a line of credit for a maximum of Euro 800 million, which can be used to factor without recourse trade receivables. It has a duration of five years.

The second agreement, signed with Deutsche Bank as Initial Mandated Lead Arranger, Agent and co-ordinating bank, and with seven other large Mandated Lead Arrangers (BNL, UniCredit, Capitalia, Mediobanca, Commerzbank, Dresdner Bank and HSH Nordbank), involves two blocks of financing:

- a three-year line of revolving credit of a maximum of Euro 650 million to cover Group company working capital requirements, specifically regarding inventory stocks, which may be extended a further two years;
- a five-year loan of Euro 200 million to cover the Group's other financial requirements (with a three-year grace period and straight-line depreciation over the next two years), guaranteed by the real estate properties of the Group's German industrial companies.

These new financing deals have replaced those made under the banking agreement made in February 2005, and allow more flexibility in terms of their amount and their use, specifically their use against the changes in working capital requirements that is strictly linked to raw materials prices (mainly copper). Furthermore, the Group was able to eliminate the commitments undertaken according to the previous banking agreement which allowed dividends to be distributed only under certain pre-arranged conditions.

To guarantee repayment of these lines of credit, the following was arranged:

- the shares, with voting rights, of the subsidiaries Europa Metalli S.p.A., Europa Metalli Brass S.p.A., Tréfimétaux S.A. and TMX Brass S.a.s. were lodged as collateral;
- a first-tier mortgage was made on KM Europa Metal A.G.'s real estate property and other fixed assets;
- the warehouse inventory of the industrial companies, excluding the Spanish ones, was lodged as collateral;
- a lien was made on factoring and insurance contracts.

Furthermore, all economic and financial covenants regarding shareholder equity, indebtedness and consolidated EBITDA, as well as the EBITDA/consolidated net interest ratio, were respected in the agreements.

Bank loans have been negotiated at a variable rate with a spread on the Euribor. Figures shown in the statements are measured at amortised cost using the effective interest rate. This total includes commissions and margins that are a basic part of interest rates and transaction costs.

At 31 December 2006, all covenants had been respected.

The amount owed to leasing companies refers to the finance lease for a building in Florence where the Group's headquarters are located, which has been recognized in accordance with the provisions of IAS 17.

All long-term debts and liabilities have a maturity of more than 12 months and less than 5 years, except for Euro 6.4 million in debt to credit institutions and Euro 3.2 million in debt to leasing companies, the maturities of which exceed the five financial years.

4.15 Other Non-current Liabilities

These primarily relate to debts to employees of German subsidiaries (Euro 7.7 million).

4.16 *Provisions for Risks and Charges*

The table below summarises the changes that occurred in provisions for risks and charges:

(Thousands of Euros)	Balance at 31.12.2005	Forex diff.	Increases	Decreases	Current components	Balance at 31.12.2006
Provision for restructuring	19,089	2	18,972	(12,664)	(19,960)	5,439
Provision for EU fines	110,304	0	3,279	0	0	113,583
Other provisions for risks and charges	22,216	20	10,353	(2,531)	(10,044)	20,014
Provisions of Parent Co.	4,862	0	0	(761)	0	4,101
Total	**156,471**	**22**	**32,604**	**(15,956)**	**(30,004)**	**143,137**

“Reclassifications” refers to the transfer of the short-term component, which was moved to the provisions for risks and charges account shown under current liabilities.

The increase in the provision for restructuring refers to staff downsizing programs of businesses in the sheeting sector. After having concentrated sheeting production in the factories in Osnabruck and Fornaci di Barga, and closing factories in Stolberg and Campo Tizzoro in Germany and Italy, a restructuring programme was launched in France at the Sérifontaine manufacturing plant, which will involve staff downsizing of 225 employees.

The increase in “EU sanctions provisions” relates to the accrual of liability interest on the nominal amount of European Commission sanctions.

The changes in Parent Company provisions are shown in the Notes to the separate financial statements included in this publication.

4.17 *Short-term Borrowings and Other Financial Liabilities*

(Thousands of Euros)	Balance at 31.12.2005	Change for the period	Balance at 31.12.2006
1) Due to banks	165,292	(2,786)	162,506
2) Due to Parent Co.	15,440	40,576	56,016
3) Due to subsidiaries	2,589	65	2,654
4) Due to leasing co.	252	13	265
5) Due to factoring companies	60,136	(30,843)	29,293
6) Interest Rate Swaps (IRS)/forward currency contracts	2,390	(1,683)	707
7) LME contracts	14,634	(8,918)	5,716
8) Due to others	191	21,827	22,018
Totale	**260,924**	**18,251**	**279,175**

LME contracts reflect the value of the potential charges resulting from the measurement at fair value of contracts outstanding at 31 December 2006.

Interest rate swaps are executed to hedge interest rate risks on a portion of the outstanding bank debt. This is accomplished by buying a fixed interest rate and selling a variable interest rate tied to the six-month Euribor.

Payables to banks include part (Euro 143 million) of the revolving line of credit of Euro 650 million with a minimum maturity of three years that the Directors believe is prudent to classify under current liabilities. Based on information available at 31 December 2006, this portion might in fact be due by the following year according to contractual agreements that are aligned with price trends of raw materials.

Payables to factoring companies are the total of loans with recourse at 31 December 2006.

The following are included in the item payables to others:

- Euro 14.3 million for the invoices received from clients factored without recourse that must be transferred to the factoring company that bought the debt;
- Euro 6.9 million for forward contracts on raw materials made by the subsidiary KME AG.

The table below shows the notional amounts and maturities of the derivatives outstanding at 31 December 2005.

Description (Thousands of Euros)	**Description**			**Total at**	
	Within 1 year	**From 1 to 5 years**	**Over 5 years**	**31.12.2006**	**31.12.2005**
LME commodity contracts	150,581	0	0	**150,581**	**186,354**
Forward currency contracts	140,891	0	0	**140,891**	**120,568**
Cross-currency swaps	2,548	0	0	**2,548**	**3,385**
Interest Rate Swaps	0	45,000	0	**45,000**	**70,000**
Total	**294,020**	**45,000**	**0**	**339,020**	**380,307**

The net financial position and its main items pursuant to CONSOB memo no. 6064293 and the CESR guidelines from 10 February 2005 entitled *Recommendations for the Uniform Implementation of European Commission Regulations on Financial Reporting* is shown in the Report of the Board of Directors instead of in these notes.

4.18 Trade Payables and Other Current Liabilities

(Thousands of Euros)	**Balance at 31.12.2005**	**Changes for the period**	**Balance at 31.12.2006**
1) Due to suppliers	121,621	41,327	162,948
2) Due to subsidiaries	951	676	1,627
2) Due to Parent Co.	3	(3)	0
Total trade payables	**122,575**	**42,000**	**164,575**

The accounting value of trade payables approximates their fair value.

(Thousands of Euros)	**Balance at 31.12.2005**	**Changes for the period**	**Balance at 31.12.2006**
3) Due to employees	40,486	1,703	42,189
4) Due to insurance companies	16,303	(3,979)	12,324
5) Tax liabilities	15,578	5,902	21,480
6) Accrued and deferred liabilities	1,149	(390)	759
6) Other payables	21,251	10,077	31,328
Total other current liabilities	**94,767**	**13,313**	**108,080**

Payables to employees includes bonds that had matured but not been liquidated at 31 December 2006.

Tax payables refer to VAT payments of Euro 11.2 million still due.

Other payables include Euro 25 million in payables to clients for prepayments and credit notes.

4.19 Deferred Tax Assets and Liabilities

(Thousands of Euros)	Balance at 31.12.2005	Changes for the period	Balance at 31.12.2006
1) Deferred tax assets	40,651	4,059	44,710
1) Deferred tax liabilities	(128,977)	(31,312)	(160,289)
Difference	**(88,326)**	**(27,253)**	**(115,579)**

Deferred and prepaid taxes are calculated on the temporary differences between the amounts assigned to assets and liabilities on the financial statements and those used for tax purposes.
Deferred tax assets are booked when their recoverability is highly probable.
Deferred tax items are booked to non-current assets or liabilities, and are offset by individual subsidiaries if the requirements of IAS 12 can be met.
At 31 December 2006, the Group did not recognise deferred tax assets on past tax losses of Euro 118.5 million.

The following shows in detail the past tax losses to 31 December 2006 that were recognised or not recognised in order to ascertain the deferred tax assets divided per company:

(Thousands of Euros)	31.12.2006
a) Past fiscal losses carried foward	
KME AG	28,030
KME Verwaltungs- u. Dienstleistungs-GmbH	4,164
KME Yorkshire Ltd	3,716
Total (1)	**35,910**
b) Past fiscal losses not recognised	
KME Group S.p.A.	42,600
TMX S.A.	42,355
SIA SA	11,762
Locsa SA	21,818
Other companies	0
Total (2)	**118,535**
Total (1 + 2)	**154,445**

The following shows in detail the deferred tax assets and liabilities by item.

(Thousands of Euros)	Deferred tax assets		Deferred tax liabilities	
	31.12.2005	31.12.2006	31.12.2005	31.12.2006
Property, plants and equipment		222	90,038	86,964
Intangible fixed assets	831	653	4	0
Property investments				0
Other non-current assets	215	2	1,464	1,190
Inventories		2,707	31,846	61,778
Trade receivables		389	1,134	985
Other current assets and receivables	125	0	74	97
Current financial assets		2,374	1,444	4,460
Employee benefits	15,564	14,729	301	599
Non-current financial liabilities	1,826	1,544		248
Other non-current liabilities	875	1,750		
Provisions for risks and charges	7,483	6,510	188	2,470
Current financial liabilities	4,425	1,651	1,741	1,449
Trade payables		38	105	49
Other current liabilities	2,496	956	638	
Deferred taxes on past tax losses	6,811	11,185		
Total	**40,651**	**44,710**	**128,977**	**160,289**

No current or deferred taxes were booked to shareholders' equity.

4.20 Information on Operations Between Related Companies

During the year, the Group initiated commercial transactions with related companies not contained within the consolidation perimeter which resulted in insignificant amounts, except for the following transactions:

- KME Group S.p.A. transferred Euro 5.2 million to the Parent Company G.I.M. S.p.A. as interest on a loan of Euro 130 million, which was then fully repaid or transformed into share capital during 2006, as included in the statement of the current account held with the Parent Company;
- the Group made insurance premium payments to RAS S.p.A. of Euro 1.6 million;
- the Group obtained a loan from Mediobanca S.p.A. within the same conventions of a previous loan (Euro 46.1 million) and a new loan (Euro 106.3 million), paying about Euro 2.3 million in interest;
- the subsidiary Europa Metalli S.p.A. made an indemnity payment of Euro 1.1 million to the widow of the deceased Chairman Luigi Orlando, due for past business regarding a residence that was in 1995 conceded to the deceased, which is presently part of the corporate real estate located in Florence. This asset was therefore disposed for a sum of Euro 2.8 million, which is the market value of the asset according to the assessment made by an independent surveyor.

All aforementioned transactions were in any case executed at market values and prices. Given their non-significant amounts, information regarding the weight of these transactions on the asset, income and equity figures have been the Group have been omitted, in accordance to CONSOB memo no. 6064293.

The following shows information regarding the remuneration of managers with strategic positions:

(Thousands of Euros)	2006	2005
Short-term benefits	7,059	4,673
Post-employment benefits	30	980
Long-term benefits	283	16
Employee severance indemnity	–	1,566
Payment in shares	738	–
Total for the year	**8,110**	**7,235**

5. Income Statement

Pursuant to CONSOB memo no. 6064293/06, please note that the Group did not make any "atypical and/or unusual transactions", while for the details of "non-recurring significant events and transactions", please see the notes contained in the "Report of the Board of Directors".

5.1 Sales Revenues

The table below provides a breakdown of sales revenues by geographic region:

Division by geographic area (Figures in millions of Euros)	FY 2006	%	FY 2005	%
Italy	715	*20.1*	455	*20.9*
France	368	*10.3*	255	*11.7*
Germany	875	*24.6*	527	*24.2*
Spain	184	*5.2*	115	*5.3*
Other European countries	1,148	*32.3*	654	*30.1*
Total	**3,290**	***92.5***	**2,006**	***92.2***
Rest of world	267	*7.5*	170	*7.8*
Total	**3,557**	***100.0***	**2,176**	***100.0***

Sales revenues show an increase of Euro 89.2 million, going from Euro 758.1 million (for the 2005 calendar year) to Euro 847.3 million (for the 2006 calendar year), net of the impact of raw material price increases.

5.2 Labour Costs

(Thousands of Euros)	FY 2006	FY 2005	Change %
Wages and salaries	259,084	254,884	*1.65%*
Social security	69,294	71,154	*–2.61%*
Other labour costs	18,013	15,730	*14.51%*
Stock option plan charges	959	–	*n.a.*
Total	**347,350**	**341,768**	***1.63%***

"*Other labour costs*" include additions to the "defined benefit pension funds", which includes provision for employee severance indemnities (Euro 13.8 million).

Stock options expenses involve incentive plans reserved for executive members of the Board of Directors and for Group managers that have positions that are directly responsible for operational results. These include rights for bonus KME Group S.p.A. shares at a ratio of 1:1 starting from 1 September 2007, which can be executed until 28 February 2011. The strike price of these options has been set at Euro 0.343 per share based on official average market prices which were recorded in the month before the date they were given (31 July 2006). Their expense for this financial year and therefore the fair value of the services received was calculated indirectly according to the fair value of the financial instruments that represent the amount of capital set aside.
The fair value of these stock options (Euro 0.10) was calculated by an independent actuary when they were given by applying the *Black & Scholes* model, which takes into account conditions under which the rights are exercised, current value of the underlying shares, expected volatility (estimated according to the historical volatility of the underlying asset at one year), the European area risk-free rate, the expected dividend rate (estimated at zero) and the probability that the rights have the conditions to be executed at the end of their vesting period.

The following table shows the situation of the stock option plan at 31 December 2006:

	2006 no. Shares
Rights existing at 1 January	**0**
New rights given	43,731,776
Rights exercised during the year	0
Rights expired during the year	0
Rights existing at 31 December	**43,731,776**
exercisable	

The first block of rights will be exercisable starting from September 2007.

5.3 Depreciation, Amortisation, Impairment Losses and Write-downs

(Thousands of Euros)	FY 2006	FY 2005	Change %
Intangible fixed assets amortisation	1,140	2,002	*–43.06%*
Property, plants and equipment depreciation	52,281	53,028	*–1.41%*
Impairment losses (gains)	(2,027)	16,452	*n.a.*
Total	**51,394**	**71,482**	***–28.10%***

During the fiscal year, the Directors recognised impairment losses of Euro 2.3 million relating to assets of the subsidiary TMX S.A. This amount is net of "impairment losses" for the year.

5.4 *Other Operating Expenses*

(Thousands of Euros)	FY 2006	FY 2005	Change %
Power supply	65,481	55,893	*17.15%*
Maintenance and repairs	32,817	28,341	*15.79%*
Insurance premiums	14,659	10,579	*38.57%*
Rent and industrial equipment leasing	7,050	8,748	*–19.41%*
Differential on LME transactions	(2,731)	27,242	*n.a.*
Fair value of LME contracts	(16,001)	7,847	*n.a.*
Other production costs	21,800	21,692	*0.50%*
Third-party processing	22,487	21,367	*5.24%*
Transport on sales	46,843	41,222	*13.64%*
Commissions	18,060	16,330	*10.59%*
Other operational expenses	96,975	62,245	*55.80%*
Total	**307,440**	**301,506**	***1.97%***

The increase in the item "insurance premiums" includes the higher level of factoring transactions, and therefore the higher expenses for the insurance of receivables factored.

The item "differential on LME transactions" shows the difference between the notional amounts of buy and sell transactions executed during the period.

"Other operating expenses" also include the following:

- provisions for "funds for risks and charges" of Euro 30.2 million, net of any possible usages;
- banking service charges relating to without recourse factoring transactions of Euro 9.9 million;

The table below shows the minimum non-cancellable payments due for operating leases as of 31 December 2006:

(Thousands of Euros)	31.12.2006	31.12.2005
Within 1 year	3,787	2,554
From 1 to 5 years	6,897	5,449
Over 5 years	312	258
	10,996	**8,261**

5.5 *Financial Income and Expense*

(Thousands of Euros)	FY 2006	FY 2005	Change %
Interest assets	1,819	606	*n.a.*
Dividends	1,750	426	*n.a.*
Other financial income	2,512	4,850	*–48.21%*
Total other financial income	**6,081**	**5,882**	***3.38%***
Interest liabilities	(35,221)	(33,043)	*6.59%*
Profits (loss) on currencies	(1,797)	(3,395)	*–47.07%*
Impairment losses on financial assets	(1,149)	0	*n.a.*
Other financial charges	(12,571)	(7,215)	*n.a.*
Total financial charges	**(50,738)**	**(43,653)**	***16.23%***
Total net financial charges	**(44,657)**	**(37,771)**	***18.23%***

The item interest liabilities includes Euro 5.2 million in interest to the Parent Company G.I.M. S.p.A..

5.6 *Current and Deferred Taxes*

(Thousands of Euros)	31 December 2006	31 December 2005	Change %
Current taxes	(4,938)	(3,771)	*30.95%*
Deferred taxes	(27,409)	753	*n.a.*
Total	**(32,347)**	**(3,018)**	***971.80%***

Starting from the 2004 financial year, G.I.M. S.p.A., KME Group S.p.A. and their Italian subsidiaries which exercised the option to be included in the "national fiscal consolidation scheme" calculated their corporate tax rates as the sum of the positive and negative tax amounts of the individual companies within the group. Business relations between parent companies and their subsidiaries, which include contractual obligations and various responsibilities, are defined in the agreement and regulations regarding the national fiscal consolidation, according to which the parent companies and/or the subsidiaries having negative taxable income receive a tax credit equal to the tax savings made by the parent company and/or subsidiaries having positive taxable incomes.
During the year, tax benefits of Euro 10.5 million were recognised, deriving from the use of KME Group S.p.A. past tax losses which were previously not recognised as deferred tax assets and used to reduce current taxes.

Deferred and pre-paid tax assets are calculated on the temporary differences between the value of the assets and liabilities according to the civil tax code, and their corresponding tax values. These temporary differences arise from consolidation adjustments that change the book values in the consolidated financial statements from their tax values.

Correlation Between Tax Charges and Accounting Profits

	31.12.2006	31.12.2005
Pre-tax profit	84,132	7,361
Theoretical tax burden (tax rate used 37.25%)	31,339	2,742
Reconciliation:		
Different tax rate effect	223	(1,166)
Other effects:		
Non-deductible expenses	18,226	8,608
Non-taxable income	(3,793)	(1,647)
Effect of past fiscal losses	(13,659)	(5,910)
Other effects	11	391
Effective tax burden carried in income statement	**32,347**	**3,018**

Coating in Tecu® Oxid – Motorway tollgate at Lucca.

REPORT OF THE BOARD OF STATUTORY AUDITORS' FOR THE CONSOLIDATED FINANCIAL STATEMENTS AT 31 DECEMBER 2006

The Board of Statutory Auditors here presents its brief report on the consolidated financial statements at 31 December 2006, both in observance of the law and the constitutional act to which it is generally held (article 149), and in observance of company principles which require the matters or documents presented by the Directors at the meeting to be — by rule — subject to examination by the Board of Statutory Auditors who report at the meeting itself.

The Board of Directors, in observance of Leg. Dec. no. 127/1991, prepared the financial statements at 31 December 2006, the same date of closing as those of the Parent Company and its subsidiaries.

Regarding the consolidation perimeter, please see the events and grounds reported in the supplementary notes to these statements which, in short, show that the interests in subsidiaries have been consolidated on a line-by-line basis; those in associated companies have been consolidated at equity. Those not having considerable influence on the Group and having little business activity regarding the main Group companies were excluded from the consolidation perimeter without any effect on the overall process, as specifically underlined in the notes regarding the accounting principles adopted by the Group.

As resulting from the linking statement shown in the attachments to the statements, the consolidated net profits for 2006 amount to Euro 51,785,000, of which Euro 7,206,000 is the net profit from the KME Group S.p.A., and the remaining Euro 44,579,000 is the net profit from the consolidated subsidiaries. This total is almost exclusively from the subsidiaries under KM Europa Metal AG, having deducted the negative result of Euro 287,000 from the real estate company I.A.L. S.r.l..

Not shown in the notes to the financial statements are the figures and reconciliation statements regarding the application of the new IAS/IFRS accounting principles as from the moment the Parent Company adopted them on the transition date (1 January 2004) and at 31 December 2004, regarding both its consolidated and the individual financial statements. These figures and statements are contained in the half year report at 30 June 2005 and the annual statements at 31 December 2005.

The balance sheet items may be aggregated according to their nature as follows (figures in millions of Euros):

ASSETS	2006	2005
– Tangible, intangible, financial fixed assets	823	823
– Warehouse inventory	684	444
– Other assets	535	575
TOTAL ASSETS	**2,042**	**1,842**

LIABILITIES	2006	2005
– Shareholders' equity of which net profit for the year: Euro 51.8 million in 2006 Euro 4.3 million in 2005	495	315
– Employee severance funds and other employee benefits	167	167
– Long-term payables and financial liabilities	487	589
– Provisions for risks and charges	173	157
– Other non-current liabilities	168	136
– Short-term payables and financial liabilities	279	261
– Other current liabilities	273	217
TOTAL LIABILITIES	**2,042**	**1,842**

The independent auditors, who communicated regularly with the Board of Auditors, confirmed that they had checked the regularity and the coherence of the balance sheet and income statements situation deriving from consolidation with the accounting results of the Parent Company, and with information transmitted from the subsidiaries, included in consolidation. They also confirmed that they had established the consistency between that information and the clarifications contained in the supplementary notes, as well as the management report and the contents of the financial statements.

In particular, we note that the following principles have been applied:

- Goodwill and other intangible fixed assets having an indeterminate useful life are not amortised; they are subject to an annual verification for the recovery of their value, without being amortised. Intangible assets with defined useful lives are depreciated on a line-by-line basis according to their use, which is generally a period of time ranging from three to five years;
- the employee severance indemnity and pension provisions of foreign subsidiaries are also recognized on an actuarial basis when required by national law, and are entered based on their maturity to 31 December 2006, with adjustments based on their forecasted increase after the closing of the fiscal year, as required by international accounting principles. Starting from these financial statements, labour expenses include the stock options given to executive members of KME Group's Board of Directors and some Group Managers in light of the fact that these options are basically given as salary bonuses. The notes to the statements clearly show the principles adopted for the calculation of the fair value of these stock options, the expense for which is offset by an item in shareholders' equity called "reserve for stock options";
- inventories are carried as the lower amount between the average weighted cost on a quarterly basis, and the net realisable value;
- EU sanctions, which were already booked to the 2003 income statement for the full ascertainable or ascertained amount of Euro 119.8 million, were then calculated based on the amount that was definitively given by EU authorities, and which are now booked at Euro 113.6 million, an amount that includes the interest liabilities, matured at 31 December 2006 on their nominal amount.

The meeting must note that these financial statements and related figures are only given for information purposes, since by law they do not need to approve them.

Florence, 31 March 2007

The Board of Statutory Auditors

REPORT OF THE INDEPENDENT AUDITORS

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**AUDITORS' REPORT PURSUANT TO ART. 156
OF LEGISLATIVE DECREE No. 58 OF FEBRUARY 24, 1998**

**To the Shareholders of
KME GROUP S.p.A.**

1. We have audited the consolidated financial statements of KME GROUP S.p.A. (and subsidiaries) (the KME GROUP Group), which comprise the balance sheet as at December 31, 2006, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. These consolidated financial statements are the responsibility of the Company's Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

2. We conducted our audit in accordance with the Auditing Standards recommended by CONSOB, the Italian Commission for listed Companies and the Stock Exchange. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Directors, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

   For the opinion on the prior year consolidated financial statements, the balances of which are presented for comparative purposes, reference should be made to our auditors' report issued on April 11, 2006.

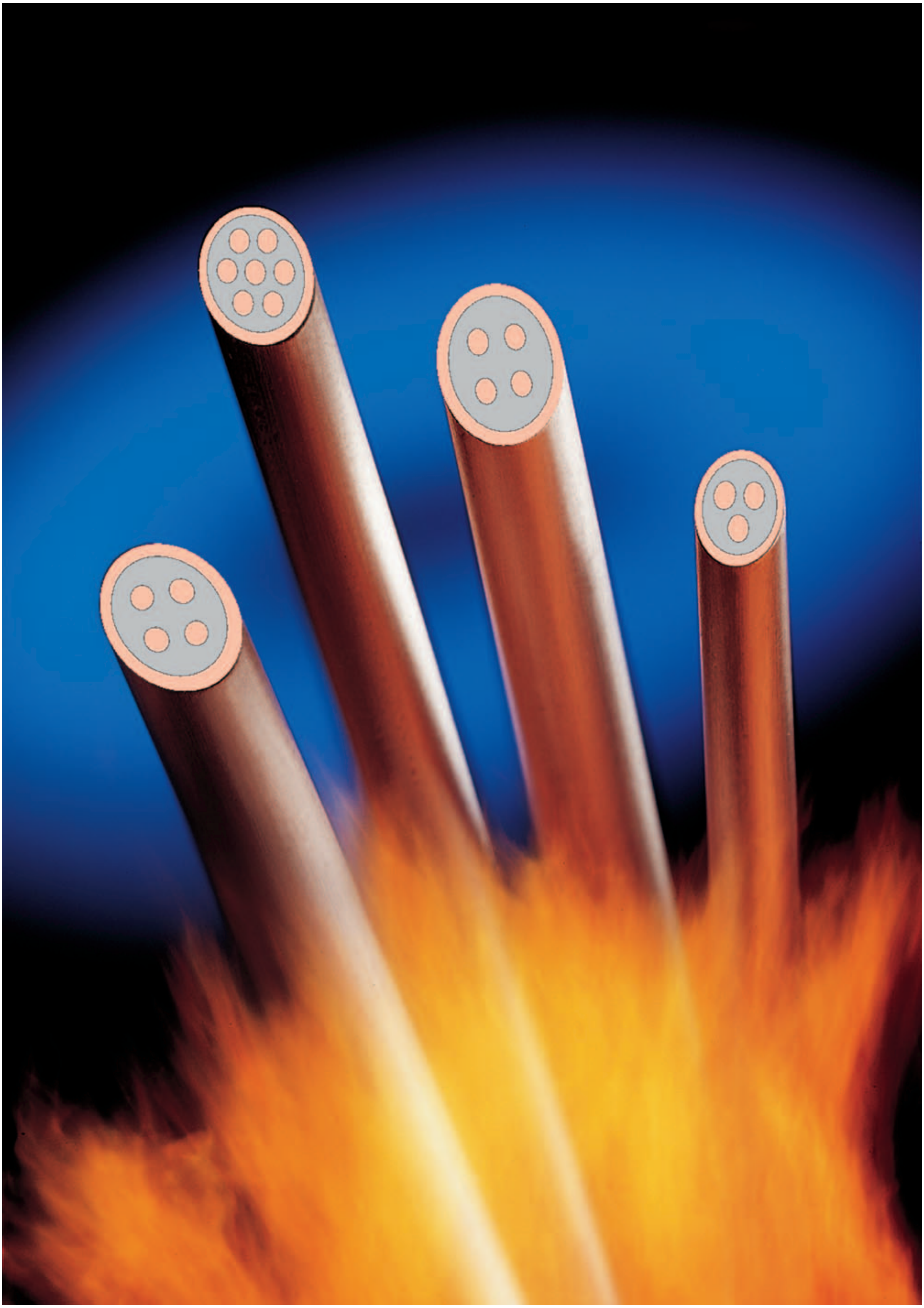
3. In our opinion, the consolidated financial statements present fairly the financial position of KME GROUP S.p.A. (the KME GROUP Group) as of December 31, 2006, and the results of its operations and its cash flows for the year then ended in accordance with IFRS as adopted by the European Union and the requirements of national regulations issued pursuant to art. 9 of Italian Legislative Decree n. 38/2005.

DELOITTE & TOUCHE S.p.A.

Signed:
Paolo Guglielmetti
Partner

Florence, April 11, 2007

This report has been translated into the English language solely for the convenience of international readers.



MICO – Cables with mineral insulation.

PARENT COMPANY FINANCIAL STATEMENTS

Separate financial statement of KME Group S.p.A. at 31 December 2006

BALANCE SHEET (figures in Euros)	**Ref. in notes**	**At 31.12.2006**	**At 31.12.2005**
Property, plants and equipment	4.1	–	–
Investments in property	4.2	2,800,000	1,250,000
Investments	4.3	310,890,540	310,404,881
Other investments	4.4	129,114	129,114
Other financial assets	4.5	22,180	13,923
Deferred tax assets	4.6	–	33,144
Non-current assets		**313,841,834**	**311,831,062**
Trade receivables	4.7	10,539,502	139,832
Other current assets and receivables	4.8	5,821,521	9,916,420
Current financial assets	4.9	67,718,529	21,474,496
Cash and cash equivalents	4.10	376,938	9,378,448
Current assets		**84,456,490**	**40,909,196**
TOTAL ASSETS		**398,298,324**	**352,740,258**
Share capital	4.11	319,643,223	189,775,023
Other reserves	4.11	(963,499)	
Treasury shares	4.11	(37,161)	(37,161)
Retained earnings (loss carried forward)	4.11	5,178,100	5,167,157
Reserve for first adoption of IAS/IFRS	4.11	2,784,099	2,784,099
Reserve for stock options	4.11	958,537	
Profit (loss) for the year	4.11	7,205,770	1,395,184
Shareholders' equity		**334,769,069**	**199,084,302**
GIM subordinated loan	4.12	–	130,000,000
Provisions for employee benefits	4.13	347,436	373,887
Deferred tax liabilities	4.14	–	–
Short-term borrowings and other financial liabilities	4.15	581,551	684,456
Other liabilities	4.16	–	–
Provisions for risks and charges	4.17	4,101,180	4,861,353
Non-current liabilities		**5,030,167**	**135,919,696**
Short-term borrowings and other financial liabilities	4.18	56,119,342	15,918,350
Trade payables	4.19	436,819	1,116,709
Other current liabilities	4.20	1,942,927	701,201
Current liabilities		**58,499,088**	**17,736,260**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**398,298,324**	**352,740,258**

The figures relating to positions or transactions with associates are not included in the balance sheet, income statements or cash flow statements because they were not deemed significant for comprehension of the income, asset and cash flow situation of the Group.

Separate financial statements KME Group S.p.A. at 31 December 2006

INCOME STATEMENT (Thousands of Euros)	**Ref. in notes**	**FY 2006**	**FY 2005**
Sales and Services revenues	6.1	2,913,550	1,289,257
Other income	6.2	1,842,496	396,207
Labour costs	6.3	(1,348,410)	(1,591,420)
Depreciation, amortisation and write-downs	6.4	–	(143,075)
Other operating expenses			
– Non-financial services	6.5	(4,788,556)	(2,378,834)
– Rent, leases, and similar	6.6	(175,391)	(248,456)
– Various operating costs	6.7	(218,236)	(260,218)
Non-recurring income (charges)	6.8	–	6,701,401
Operating result		**(1,774,547)**	**3,764,862**
Financial income	6.9	3,727,194	2,740,201
Financial charges	6.10	(5,311,966)	(6,065,465)
Pre-tax profit		**(3,359,319)**	**439,598**
Current taxes	6.11	10,598,233	(307,000)
Deferred taxes	6.12	(33,144)	1,262,586
Total income tax		**10,565,089**	**955,586**
NET PROFIT (LOSS)		**7,205,770**	**1,395,184**

The figures relating to positions or transactions with associates are not included in the balance sheet, income statements or cash flow statements because they were not deemed significant for comprehension of the income, asset and cash flow situation of the Group.

KME Group S.p.A.

CASH FLOW STATEMENT (figures in thousands of Euros)		FY 2006	FY 2005
(A)	**Cash and cash equivalents at beginning of year**	**9,379**	**8,434**
	Pre-tax profit	(3,359)	439
	Depreciation and amortisation of property, plants and equipment and intangibles	–	143
	Net accrued interest	3,186	1,926
	Losses (gains) on non-current assets	(43)	–
	Provisions for pension funds and similar	446	(131)
	Allocation to provisions and other funds	(934)	2,348
	(Increase) decrease in current receivables	(7,337)	51,335
	Increase (decrease) in current payables	463	(3,954)
	Net interest paid in the year	(3,100)	(1,838)
	Current taxes (paid) and refunded during the year	10,532	–
(B)	**Cash flows from operating activities**	**(146)**	**50,268**
	(Increase) decrease in non-current tangible fixed assets and intangible assets	(1,507)	7,710
	Increase/decrease in other non-current assets/liabilities	(8)	(2)
	(Increase) decrease in equity investments	–	(119,563)
	Dividends received	415	–
(C)	**Cash flow from investment activities**	**(1,100)**	**(111,855)**
	Contributory increase in shareholders' equity	128,835	
	Increase (decrease) in current and non-current indebtedness	(89,655)	79,386
	(Increase) decrease in current and non-current loans receivables	(45,622)	(16,854)
	Dividends paid	(1,314)	–
(D)	**Cash flow from financing activities**	**(7,756)**	**62,532**
(E)	**Net result of cash and cash equivalents (B + C + D)**	**(9,002)**	**945**
(F)	**Cash and cash equivalents and end of year (A + E)**	**377**	**9,379**

The figures relating to positions or transactions with associates are not included in the balance sheet, income statements or cash flow statements because they were not deemed significant for comprehension of the income, asset and cash flow situation of the Group.

ACCOUNTING PRINCIPLES AND NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. General information

KME Group S.p.A. (or “KME”) and its industrial subsidiaries (which together make up the “Group”) operate in the sector of semi-finished products in copper and copper-based alloys.

The Group owns manufacturing plants in various European countries, and markets its products in all of the major countries of the world.

KME is a joint stock corporation (*Società per Azioni*) registered in Italy at the Florence Chamber of Commerce under no. 00931330583, and its shares are listed on the electronic stock market managed by Borsa Italiana S.p.A..

The consolidated financial statements at 31 December 2006 were approved by the Board of Directors on 20 March 2007.

2.1 Basis of Preparation

The financial statements at 31 December 2006 were prepared following CONSOB’s Regulations for Issuers, and in accordance with international accounting principles.

The financial statements were prepared in conformance with the accounting principles established in the ***International Financial Report Standards*** (IFRS) issued by the ***International Accounting Standards Board*** (IASB), and endorsed by the European Commission through article 6 of EU Regulation no. 1606/2002 of the European Parliament and Council on 19 July 2002. In preparing the consolidated financial statements, the Directors have taken account of the accrual principle, going concern, understandability, materiality, relevance, reliability, neutrality, prudence and comparability.

KME has not yet adopted those accounting standards which, although issued by the IASB, become effective after the balance sheet date of these financial statements. It has nevertheless been estimated that the future adoption of these standards will not have a significant impact on the Group’s balance sheet, financial position or economic situation.

Events and business operations are recognised and represented on the basis of their substance and economic reality and not only in accordance with their legal form.

The reference date of the separate financial statements coincides with the calendar year.

Not shown in the financial statements are the figures and reconciliation statements pursuant to Paragraphs 39 and 40 of IFRS 1 *First adoption of IFRS*, and CONSOB memo no. 6064313 dated 28 July 2006 as from the moment the Parent Company adopted them on 1 December 2004 for both its consolidated and separate financial statements. These figures and statements are contained in the half year report at 30 June 2006 and the annual statements at 31 December 2005.

KME mandated the Deloitte & Touche S.p.A. auditing company with the full audit of its IFRS reconciliation statements at 1 January 2004 and 31 December 2004. This company’s report can be see on the company’s website at www.kmegroup.it.

2.2 Property, Plants and Equipment

Property, plants and equipment are recorded at purchase cost, including any additional charges directly imputed to them.

Tangible assets are measured at cost, net of depreciations and impairment losses, with the exception of land that is not amortisable and that is measured at cost, net of impairment losses.

Depreciations are carried starting from the month in which the asset is available for use or is potentially able to supply economic benefits. Depreciation is booked monthly on a straight-line basis until the end of an asset’s useful life or, in the event of disposals, until the last month of use.

The financial charges relative to the purchase of fixed assets are charged to the income statement unless they are directly attributed to the acquisition, construction, or production of an asset that justified the capitalisation thereof.

Replacement parts of significant value are capitalised and amortised based on the useful life of their related asset; others are expensed to the income statement when their cost has been sustained.

Assets acquired under finance leases are booked as Property, plants and equipment as an offset to the corresponding liability. Lease payments are broken down into their components: financial expense, which is charged to income, and principal repayment, which is deducted from indebtedness. Assets owned in financial leasing are recognised at either their cost or the current value of the minimum leasing payments due at the starting date of the contract, whichever is lower.
If there is an indication of impairment losses, Property, plants and equipment is subjected to an "impairment test". The test consists of estimating an asset's recoverable value, defined as the greater of the net sale price and its useful value, and comparing it with the corresponding carrying amount. If the recoverable amount is less than the carrying amount, the latter is written down to the recoverable amount. The amount of the write-down is charged to income or to a revaluation provision, if such a provision existed when the same assets were revalued in the past. If subsequent revaluations become necessary, the reverse process is applied.

2.3 Intangible Assets

These are intangible assets that are identifiable, are controlled by the Company and are capable of producing future economic benefits.
A company may acquire intangible assets in any of the following ways:

- purchase from a third party;
- as a result of a business combination;
- internal development.

In the first two cases, intangible assets are measurement initially at cost and at fair value, including any directly attributable incidental charges, respectively. They are then amortised on a straight line over their useful lives, which corresponds to an estimate of the period during which the assets are used by the company, usually a length of time between 3 to 5 years. These assets are shown net of possible write-downs for impairments losses, which are determined the same way as for "property, plants and equipment". It is assumed that at the end of their useful lives, their residual value will be zero.
Assets developed internally are only capitalised when they meet the requirements detailed in Paragraph 57 of IAS 38.

2.4 Investment Property

This account includes land and buildings that are held for the purpose of earning rental income, or for capital appreciation, or both. These assets are carried at fair value, and are therefore not depreciated on a straight-line basis.

2.5 Financial Assets

All equity investments in unconsolidated subsidiaries, associates and joint ventures are carried at cost.
Any other equity investments are carried at fair value, with the resulting gains or losses recognised in equity. When the fair value can not be determined reliably, equity investments are carried at cost, adjusted for impairment losses.
Non-derivative financial assets with fixed or determinable payments and fixed maturities that the company plans to hold to maturity are classified as "*assets held to maturity*". The assets in this category carried at the amortised cost method, using the effective interest criterion, as defined in IAS 39.
Financial assets that are acquired or held mainly for sale or short-term repurchase agreements and the derivatives not designated as hedging instruments are classified as "*fair value assets recognised to the income statement*", i.e. designated assets. These assets are carried at fair value, with the resulting gains or losses recognised in earnings.
With the exception of financial instruments that represent equity capital, non-derivative financial assets with fixed or determinable payments that are not traded on an active market, and cannot be included in one of the categories above, are classified as "loans and other receivables", and are carried at amortised cost using the effective interest method. For current loans and receivables and in general for all short term receivables and payables for which time value has little relevance, we assume that their amortised expense coincides with their carrying amount.

All other non-derivative financial assets that cannot be classified one of the three categories above are classified as "*financial instruments available for sale*" and carried at fair value. Their gains or losses are recognised at equity, except for impairment losses.
All financial assets, except for "*fair value financial assets recognised to the income statement*", are tested for impairment losses as required by Paragraphs 58-70 of IAS 39.
Treasury shares are carried at historical cost and booked as a deduction from consolidated shareholders' equity.

2.6 Inventories

Inventories are carried at the lower of cost and net realisable value. Cost is determined through the application of the weighted average cost method on a quarterly basis, and includes all direct charges and a share of the other costs sustained to bring the inventories to their current place in their current conditions. The manufacturing costs incurred for work in process and finished goods include directly attributable incidental expenses and a pro-rata share of indirect manufacturing costs that can be reasonably allocated to the products in question. Completed portions of contract work in progress are carried based on the corresponding contractual consideration which can be accrued with reasonable certainty, less distribution costs.

2.7 Cash and Cash Equivalents

This account includes cash on hand, sight deposits and highly liquid short-term financial investments that may be readily convertible into cash, and are not subject to a significant change in value (as per IAS 7, Paragraph 45).

2.8 Shareholders' Equity

The Company's share capital is equal to the nominal value of ordinary and savings shares, subscribed and paid in as of the reference date for these statements, less any stock subscription arrears own by shareholders. As required by IAS 32, the nominal value of repurchased treasury shares is deducted from issue share capital. This presentation is however only provided in the Notes to the financial statements. On the balance sheet, the historical cost of treasury shares is shown separately as a deduction from shareholders' equity.
Reserve for treasury shares is no longer shown due to the different method of presentation required under IAS. The existing reserve balance was reclassified to the individual reserves that had been originally used to establish it.
The balance of adjustments made for the transition to IAS is booked to a separate equity reserve called "reserve for initial adoption to IAS/IFRS".

2.9 Liabilities

Liabilities are shown at their amortised cost. When the gains and losses for this are insignificant — as for short-term trade payables — these are shown at nominal value.

2.10 Current and Deferred Taxes

Current income taxes are calculated based on the estimate of taxable income, according to the tax rates and laws that are in force or have effectively been approved at the closing date of the period.
Deferred and prepaid taxes are calculated on the temporary differences between the amounts assigned to the assets and liabilities on the financial statements and those used for tax purposes according to the "*balance sheet liability method*".
Deferred-tax assets are recognised when their recovery is highly probable. The book value of deferred-tax assets is reviewed at the reference date of each financial year to verify that their future recovery is "probable".

Deferred-tax items are booked as non-current assets or liabilities and can be offset by each individual subsidiary if the requirements of IAS 12 can be met. Current income tax and deferred taxes are shown in the income statement, except for current and deferred taxes deriving from transactions that are paid directly to shareholders' equity.

2.11 Employee Benefits

Benefits are provided to employees at the end of the employment relationship in accordance with plans that, based on their characteristics, can be classified as "defined contribution" or "defined benefit" plans. Under defined contribution plans, a company's obligation, which is limited to the payment of contributions to a separate legal entity (which can be the Government or a fund), is represented by the contributions that are due on the reference date of the financial statements. As is the case for the provision for employee severance indemnities, which is governed by article 2120 of the Civil Code, the liability for a defined benefit plan, which is computed net of any assets earmarked for the plan, is determined on the basis of actuarial assumptions and is recognized on an accrual basis, taking into account the length of service necessary to receive the benefits. Actuarial gains or losses on defined benefit plans that arise from changes in actuarial assumptions or the terms of a plan are recognized in earnings on a pro rata basis using the so-called "corridor method", i.e., they are recognized when the net value or actuarial gains and losses that were not recognized at the end of the previous accounting period is greater than 10% of the present value of the obligation or 10% of the fair value of any asset earmarked for the plan, whichever is larger.
All liability evaluations are provided by independent actuaries.

2.12 Provisions

Provisions reflect liabilities the due date or amount of which is uncertain. Provisions are recognized only when:

1. The Group is currently subject to an obligation (legal or contingent) as a result of a past event;
2. It is likely that, in order to discharge this obligation, the Group will have to use resources that could otherwise produce financial benefits;
3. A reliable estimate can be made of the amount of the obligation.

The amounts set aside as provisions represent the best estimates, on the reference date of the 34 financial statements, of the charge that will be incurred to discharge an obligation or transfer it to a third party. When the computation of the present value of money is a significant factor, the amount of a provision should be equal to the present value of the charges that the Group expects to incur to discharge the obligation.
Provisions for restructuring costs are recognised only when the Group has a detailed formal plan to do so, that identifies at least: the assets and the main operations units involved, the costs to be sustained, the approximate number of employees involved and when the third parties involved may validly expect that the company will implement the said restructuring, either because it is under way or it has been publicly announced.

2.13 Revenue Recognition

Sales and service revenues are recognized when the risks and benefits inherent in the ownership of an asset or the performance of a service have effectively been transferred.

2.14 Leasing

A lease is a contract whereby the lessor transfers to the lessee the right to use an asset for a pre-set period of time in exchange for payment or a series of payments. Contracts that effectively transfer all the risks and benefits inherent in the ownership of an asset are called "finance leases", even when ownership is not transferred at the end of the lease. Finance leases are recognised in accordance with IAS 17 Paragraphs 20 through 32.
Leases that cannot be defined as finance leases are called "operating leases".

2.15 Dividends

Dividends are recognised as a liability only during the period after the general meeting of shareholders has declared them.

2.16 Stock Options

Starting from the financial statements at 31 December 2006, personnel expenses include the stock options given to executive members of the KME Group S.p.A. Board of Directors, and some Group Managers, since their nature is basically one of remuneration. The fair value of stock options was set according to the value of the option when it was assigned, applying the Black & Scholes model that keeps account of their exercise rights, the current value of the underlying share, the exercise price, the maturity, dividends, expected volatility and the risk-free rate. The stock options expense is recognised and offset in shareholders' equity in the item "reserve for stock options". The fair value of rights given to managers of unconsolidated KME Group S.p.A. subsidiaries is deducted from the companies where the managers hold their positions, in early accordance with IFRIC 11 as provided for in Paragraph 12 of this regulation.

2.17 Earnings per Share

For information regarding the calculation of basic and diluted earnings, please see the notes to the consolidated financial statements in this document. Pursuant to IAS 33 Paragraph 4, this information must be shown only based on consolidated figures.

2.18 Use of Estimates

The preparation of these financial statements and the accompanying Notes in accordance with IFRS required that the Directors make estimates and assumptions which affect the carrying value of the assets and liabilities in those statements.
Estimates have been primarily made to determine the useful lives of fixed assets, to make provisions for credit risk, to determine impairment, to calculate for employee benefits, taxation and restructuring provisions, to determine intangible assets having indeterminate lives, and in the measurement of other accruals and provisions.
These estimates and assumptions will be periodically reviewed and any resulting effects will be immediately recognised in the income statement. However, at the reference date for these statements, the Directors believe that the estimates and assumptions made reflect the best assessment possible given the information available. Moreover, the Directors believe that the estimates and assumptions made will not result in material adjustments to the carrying values of assets and liabilities during the following year.

3. Risk Management

The Group is subject to various operating and financial risks in carrying out its activities. The policy of the Group is to eliminate or at least minimise those risks via hedging strategies established and approved by the Board of Directors. As a result, the Group has formal procedures at its disposal to define the objectives and procedures for hedging risks: credit risk, liquidity risk, foreign exchange risk, interest rate risk and, above all, fluctuations in the price of raw materials.
Credit risk is managed chiefly by selecting the customer portfolio on the basis of past experience, obtaining guarantees and insuring the majority of trade receivables.
Liquidity risk may arise from the difficulty in obtaining loans or advances to support operations within the necessary period of time. Cash inflows and outflows and the Group's cash situation are monitored and coordinated centrally under the control of Group Treasury.
The Group is exposed to the risk of fluctuations in foreign exchange rates and interest rates as it operates in an international context in which transactions are carried out in various currencies and at different interest rates. Foreign exchange risk is primarily the result of the fact that the Group's production activities are carried out in different

geographical locations, and that the markets in which the Group sells its products are situated throughout the world. The Group's policy is to hedge against all of these risks by using derivative financial instruments such as cross-currency swaps and forward contracts.

The management of the risk of fluctuations in raw materials prices (copper above all) is, however, the most important and the most strategic. In order to do this, the Group uses physical transactions or forward contracts on the London Metal Exchange (LME), aiming at hedging 100% of the risk.

4. Balance Sheet Information

4.1 Property, Plants and Equipment

(Euro)	Prop., plants and equip.	Other assets	Total
At 31 December 2005			
Historic cost	185,510	735,626	921,136
Accum. depreciation and write-downs	185,510	735,626	921,136
Net book	**–**	**–**	**–**
At 31 December 2006			
Historic opening balance	185,510	735,626	921,136
Increases	–	–	–
Reclassifications	–	–	–
Decreases	–	(46,994)	(46,994)
Closing balance	**185,510**	**688,632**	**874,142**
At 31 December 2006			
Accum. depreciation and write-downs	185,510	735,626	921,136
Depreciation	–	–	–
Reclassifications	–	–	–
Decreases	–	(46,994)	(46,994)
Accum. depreciation and write-downs	**185,510**	**688,632**	**874,142**
At 31 December 2006			
Closing balance	185,510	688,632	874,142
Accum. depreciation and write-downs	185,510	688,632	874,142
Net closing balance	**–**	**–**	**–**

Some fully amortised furniture and transportation vehicles were sold during the year, resulting in some capital gains. No amortisations were recognised during the year in that assets were fully amortised at 31 December 2005, and during 2006 no increases for new purchases were recognised.

4.2 Investment Property

(Euro)	At fair value
Net book value at 1 January 2006	**1,250,000**
Increases for acquisitions	–
Increases for capitalised expenses	–
Increases for company aggregations	–
Disposals	–
Changes in fair value	1,550,000
Changes of classification	–
Other	–
Net book value at 31 December 2006	**2,800,000**

During the year a fair value adjustment of Euro 1.55 million was recognised, based on a real estate estimate of the property used for residential purposes in Florence in Borgo San Jacopo no. 26. The property was sold, at this price, on 15 January 2007.

4.3 Investments

Below is a list of equity investments in subsidiaries carried in financial fixed assets.

Name (value in Euros)	**Registered offices**	**Share capital**	**Shareholders' equity at 31.12.2006** (1)	**Profits at 31.12.2006**	**Owned portion**	**Book value (item: interests)**
Subsidiaries						
KM Europa Metal AG	Osnabrueck	142,743,879	128,101,000	(31,436,000)	100%	303,155,540
			354,205,000 (2)	44,866,000 (2)		

(1) Including profits for the fiscal year.
(2) Consolidated shareholders' equity and profits at 31 December 2006.

(Euro)	**Investments in subsidiaries**	**Investments in associates**	**Investments in other companies**	**Total**
Historic cost	530,582,719	129,114	–	530,711,833
Revaluations	–	–	–	0
Write-downs	(220,177,838)	–	–	(220,177,838)
Previous FY balance	**310,404,881**	**129,114**	**–**	**310,533,995**
Increases	485,659	–	–	485,659
Decreases	–	–	–	0
Revaluations	–	–	–	0
Write-downs	–			0
Change in FY	**485,659**	**–**	**–**	**485,659**
Historic cost	531,068,378	129,114	–	531,197,492
Revaluations	–	–	–	0
Write-downs	(220,177,838)	–	–	(220,177,838)
Final balance	**310,890,540**	**129,114**	**–**	**311,019,654**

The item "investments in subsidiaries" includes the entire equity investment in KM Europa Metal A.G. (Euro 303,155,540) and in Immobiliare Agricola Limestre S.r.l. (Euro 7,735,000).
The item "investments in associates" refers to the 50% interest in "Consorzio Italmun 25 in liquidation" from the incorporation of Europa Metalli SEDI S.p.A..
The increase in the item "investments in subsidiaries" by Euro 486,000 is due to the value of the stock options given to the Managers of the subsidiaries, which was carried at shareholders' equity.

4.5 Other financial assets

(Euro)	**31.12.2006**	**31.12.2005**	**Absolute change**	**Change %**
Security deposits	6,900	–	6,900	*N.A.*
Prepaid taxes for TFR lg. 662/96	15,280	13,923	1,357	*9.75%*
	22,180	**13,923**	**1,357**	***9.75%***

4.6 *Deferred tax assets*

The change in this item in 2006 is due to the use of deferred tax assets for the final expiry of an Interest Rate Swap (IRS).

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Deferred tax assets	–	33,144	(33,144)	*N.A.*
	–	**33,144**	**(33,144)**	***N.A.***

4.7 *Trade Receivables*

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Due from customers	935,671	937,089	(1,418)	*–0.15%*
Provision for bad debts	(933,169)	(933,169)	–	*N.A.*
Total customers	**2,502**	**3,920**	**(1,418)**	***–36.19%***
Due from subsidiaries	10,537,000	135,912	10,401,088	*N.A.*
	10,539,502	**139,832**	**10,399,670**	***N.A.***

Receivables from customers remained essentially unchanged. Regarding litigation with a Greek client of the subsidiary Europa Metalli SE.DI S.p.A. for a receivable of Euro 933,000, which has been fully written down, please see the paragraph regarding current litigation.

At the end of 2006, receivables from subsidiaries involved a benefit deriving from the use of past tax losses of the Parent Company, used by the Italian subsidiaries, which exercised their option to take part in the "national fiscal consolidation" scheme.

4.8 *Other Receivables and Current Assets*

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Due from others:				
– various	5,821,521	9,916,420	(4,094,899)	*–41.3%*
	5,821,521	**9,916,420**	**(4,094,899)**	***–41.3%***

Various receivables refer mainly to receivables from Inland Revenue for taxes due to be reimbursed (Euro 5.7 million) and for regional tax accounts (Euro 135,000).

The following table shows receivables by maturity:

(Euro)	Maturity			
	Within next 12 months	Within 5 years	Beyond 5 years	Total
Due from customers	2,502	–	–	2,502
Due from subsidiaries	10,537,000	–	–	10,537,000
Due from others:				
– various	5,821,521	–	–	5,821,521
	16,361,023	**–**	**–**	**16,361,023**

4.9 Current Financial Assets

(Euro)	No. Shares	31.12.2006	31.12.2005	Absolute change
Financial assets held for trading:				
– GIM S.p.A. savings shares	5,242,497	5,242,497	4,620,600	621,897
Loans to subsidiaries	N.A.	62,476,032	16,853,896	45,622,136
Total		**67,718,529**	**21,474,496**	**46,244,033**

Financial assets held for trading comprise 5,242,497 G.I.M. S.p.A. savings shares. The increase for the period involves an adjustment to the value of these shares at a unit price of Euro 1.00. During the year, 461,947 shares were sold. The unit price of Euro 1.00 represents the exercise price of a call option, valid until 2012, given to banking institutions that took part in the banking agreement made with the Group signed in February 2005. The option is still valid, with a new agreement signed 30 September 2006.

The amount carried in financial receivables from subsidiaries represents the balance of current accounts held by the Parent Company with the subsidiaries KM Europa Metal A.G., Europa Metalli S.p.A., TMX S.A. and Immobiliare Agricola Limestre S.r.l..
The receivable shown matures within 12 months.

4.10 Cash and Cash Equivalents

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
1) Bank and postal deposits	373,663	9,372,498	(8,998,835)	*–96.0%*
3) Cash on hand and float	3,275	5,950	(2,675)	*–45.0%*
	376,938	**9,378,448**	**(9,001,510)**	***–96.0%***

The decrease in cash on the previous year is due to the fact that the 2005 year benefited temporarily from cash receipts from the Inland Revenue.

4.11 Shareholders' Equity

Shareholders' equity at 31 December 2006 amounted to Euro 319,643,223, divided into 693,385,714 ordinary shares and 57,216,332 savings shares without nominal value.
Pursuant to article 8 of the bylaws, in a year in which no profits were made, holders of the savings shares have the right to receive a minimum preference dividend in the subsequent two financial years. Please be reminded that for the 2004 and 2005 financial years no dividends were distributed.

The following table shows the changes in shareholders' equity:

(Euro)	Share capital	Other reserves	Treasury shares	Retained earnings (loss carried forward)	Reserve for first adoption of IAS/IFRS	Reserve for stock options	Profits for the year	Total shareholders' equity
Balance at 31.12.2004	**189,775,023**	**25,350**	**(37,161)**	**5,521,780**	**2,784,099**	**–**	**(381,973)**	**197,687,118**
Shareholders' resolution from 27.4.2005:								
Balance at 31.12.2004	189,775,023	25,350	(37,161)	5,521,780	2,784,099	–	(381,973)	197,687,118
– 2004 profits carried forward				(100,973)				(100,973)
– adoption of IAS/IFRS		(25,350)		(253,650)			381,973	102,973
Profit (loss) for FY 2005							1,395,184	1,395,184
Balance at 31.12.2005	**189,775,023**	**–**	**(37,161)**	**5,167,157**	**2,784,099**	**–**	**1,395,184**	**199,084,302**
Appropriation of previous year's profits								
Shareholders' resolution from 19.5.2006:								
– legal reserves		69,760					(69,760)	
– 2005 profits carried forward				10,943			(10,943)	
– dividends							(1,314,481)	(1,314,481)
Share capital increase	129,868,200							129,868,200
Costs for share capital increase		(1,037,925)						(1,037,925)
Revenues from unopted rights		4,666						4,666
Stock Option bonuses						958,537		958,537
– Profits for FY 2006							7,205,770	7,205,770
Balance at 31.12.2006	**319,643,223**	**(963,499)**	**(37,161)**	**5,178,100**	**2,784,099**	**958,537**	**7,205,770**	**334,769,069**
IAS reclassification own shares	(37,161)		37,161					–
Balance at 31.12.2006	**319,606,062**	**(963,499)**	**–**	**5,178,100**	**2,784,099**	**958,537**	**7,205,770**	**334,769,069**

Treasury shares amount to 65,000 savings shares, carried at a cost of Euro 37,161.
The item "other reserves" includes:

• Legal reserve of	Euro	69,760
• Costs of increasing capital by Euro 129.9 million	Euro	(1,037,925)
• Revenues from sale of unopted rights	Euro	4,666
	Euro	(963,499)

Reserves from "profits carried forward" and "first adoption IAS/IFRS", created for the transfer to the new accounting principles in 2004, are available except for amounts allocated to cover the following:

- reserves to offset 5,242,497 G.I.M. savings shares in portfolio, totalling Euro 5,242,497, pursuant to article 2359 ii of the civil code;
- reserves to offset 65,000 G.I.M. savings shares in portfolio, totalling Euro 37,161 pursuant to article 2357 iii of the civil code.

The item "stock option reserve" (carried for this financial year's tranche of Euro 958,537) derives from the value of the stock options given to executive Directors of the Company (Euro 472,878) and those given to Group Managers (Euro 485,659).

4.12 Subordinated Loan

Euro 39.7 million of the subordinated loan was repaid, while Euro 90.9 million was used by the Parent Company to underwrite a capital increase, approved on 19 May 2006.

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Payables to Parent for subordinated loan	–	130,000,000	(130,000,000)	*N.A.*
	–	**130,000,000**	**(130,000,000)**	***N.A.***

4.13 Employee Benefits

This amount was determined based on the benefits matured at the end of the year for all employees, based on legislation and labour contracts pursuant to IAS 19.

(Euro)	31.12.2006	31.12.2005	Change during year	
			Usages	Provisions
Employee severance fund	336,622	376,772	70,071	32,806
Actualisation and recognition IAS 19	10,814	(2,885)		10,814
	347,436	**373,887**	**70,071**	**43,620**

Usages are related to employees who left the Company during 2006.

4.14 Deferred tax liabilities

No deferred tax liabilities were recognised for significant past tax losses. Basically, the deferred tax liabilities were reimbursed, not their related assets.

At 31 December 2006, KME Group S.p.A. had past tax losses of Euro 42.6 million.

4.15 Payables and Financial Liabilities

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Financing as per law 46/1982	581,551	684,456	(102,905)	*–15.0%*
	581,551	**684,456**	**(102,905)**	***–15.0%***

The amount for this item refers to the portion of the loan deriving from the incorporation of Europa Metalli SE.DI S.p.A. that matures beyond the twelve months due for the loan, pursuant to law no. 46/1982.

4.16 Other Payables

No other payables were recognised.

4.17 Provisions for Risks and Charges

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Product guarantee provision	2,707,049	2,707,049	–	*N.A.*
Company reorg. provision	780,645	1,691,728	(911,083)	*–53.9%*
Legal and tax risks provision	613,486	462,576	150,910	*32.6%*
	4,101,180	**4,861,353**	**(760,173)**	***–15.6%***

The “product guarantee provision” was booked into the accounts following the merger of Europa Metalli SE.DI. S.p.A. to cover guarantees of the products that it sold in the past to the Ministry of Defence.
The decrease in the “Company reorganisation provision” is due to payments made to employees that left the Company during 2006.

4.18 Payables and Financial Liabilities

The table below shows the composition of this item.

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Bank loans	103,009	202,545	(99,536)	*–49.1%*
Payables to unconsolidated subsidiaries	–	172,630	(172,630)	*N.A.*
Payables to Parent Co.	56,016,333	15,439,886	40,576,447	*N.A.*
IRS fair value recognition	–	103,289	(103,289)	*N.A.*
	56,119,342	**15,918,350**	**40,200,992**	***N.A.***

Payables due to the Parent Company increase due to the higher level of financial support received.

4.19 Payables to Suppliers

The table below shows the composition of this item.

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Suppliers	371,729	1,116,709	(744,980)	*–66.7%*
Suppliers - Parent Co.	3,717	–	3,717	*N.A.*
Suppliers - subsidiaries	61,373	–	61,373	*N.A.*
	436,819	**1,116,709**	**(744,980)**	***–66.7%***

4.20 Other Current Liabilities

These are composed as follows.

(Euro)	31.12.2006	31.12.2005	Absolute change	Change %
Other current liabilities	1,942,927	701,201	1,241,726	*N.A.*
	1,942,927	**701,201**	**1,241,726**	***N.A.***

This item refers to debts to corporate bodies for unliquidated charges and tax and insurance debts with maturities that last beyond the closing of the financial year.

5. Guarantees and commitments

As part of the banking agreements signed last September, along with its manufacturing subsidiaries KME is bonded for up to a maximum usage amount of Euro 650 million for three years (Tranche A) and Euro 200 million for five years (Tranche B). This is amortised at monthly rates starting from the fourth year.

At the end of the year, usages of these tranches were the following:

- Euro 544.3 million of Tranche A;
- Euro 196.0 million of Tranche B.

We remind you that Tranche B also includes financing granted by the European Investment Bank of Euro 50.7 million, and guarantees given by the European Community worth Euro 97.1 million.

We also remind you that the KME Group has kept the commitment to maintain a call option on 5,704,444 G.I.M. savings shares at the disposal of participating banking institutions, exercisable at a unit price of Euro 1.00. At the end of December last year, following the exercising of this option by a bank, the number of shares was reduced to 5,242,497.

6. Income statement information

6.1 Sales and Services Revenues

(Euro)	FY 2006	FY 2005	Change %
Commissions for services to Group companies	2,913,550	1,289,257	*N.A.*
Sales and services revenues	**2,913,550**	**1,289,257**	***N.A.***

The item "commissions for services to Group companies" includes amounts invoiced for services rendered for financial, insurance and administrative assistance.

6.2 Other Income

(Euro)	FY 2006	FY 2005	Change %
Real estate income	33,739	37,264	*–9.5%*
Recovery of expenses sustained in the interest of Group companies	59,739	217,920	*–72.6%*
Various income	156,329	141,023	*10.9%*
Capital gains on property sales	42,689	–	*N.A.*
Change in fair value of investment property	1,550,000	–	*N.A.*
Other operating revenues	**1,842,496**	**396,207**	***N.A.***

Real estate income derives from the lease of real estate in Florence.
Expenses recovery relates to costs sustained in the interests of Group companies and then re-debited; the main items relate to personnel costs.
Various income involves tax credits from 1973 and other small repayments.
Capital gains on property sales involves the sale of an automobile that was no longer used, and various furniture.
The change in fair value on investment property involves the adjustment to market prices of a piece of residential property in Florence, Borgo San Jacopo no. 26, based on estimates made by an expert independent assessor, who set the base price at which the property was sold on 15 January 2007.

6.3 Labour Costs

(Euro)	FY 2006	FY 2005	Change %
Salaries	616,503	1,175,071	*–47.5%*
Social security contributions	215,409	373,359	*–42.3%*
Cost of stock options	472,878	–	*N.A.*
Staff severance provision	43,620	42,990	*1.5%*
	1,348,410	**1,591,420**	***–15.3%***

The amount for labour costs was reduced due to the lower number of employees.

In the 2006 financial statements, labour costs included the stock options given to executive members of the KME Board of Directors. For more information on this item, please see the relevant sections of this report.

6.4 Depreciation, Amortisation and Write-downs

(Euro)	FY 2006	FY 2005	Change %
Furniture	–	116,722	*N.A.*
Plants, machinery and equipment	–	10,641	*N.A.*
Automobiles	–	15,712	*N.A.*
	–	**143,075**	***N.A.***

No amortisations were booked for the year due to the fact that all assets were already fully amortised at the end of 2005.

6.5 Non-financial Services

This item is detailed in the table below.

(Euro)	FY 2006	FY 2005	Change %
Compensation to Directors and Statutory Auditors	2,911,117	914,446	*n,s*
Professional services	1,431,051	925,907	*54.6%*
Travel expenses	214,603	92,333	*N.A.*
Payments to Parent Co. for services rendered	4,132	161,908	*–97.4%*
Legal and company advertising	57,592	62,751	*–8.2%*
Electricity, heating, postage and telephone expenses	54,432	86,286	*–36.9%*
Various insurance costs	71,615	79,993	*–10.5%*
Various maintenance costs	483	18,419	*–97.4%*
Listing fees	43,531	36,791	*18.3%*
	4,788,556	**2,378,834**	***N.A.***

Compensation to executive directors was increased following changes to their number. Professional services includes a non-recurring cost of Euro 1,052,000 regarding consultancy for the Group re-organization plan.

6.6 Rent, Leases and Similar

(Euro)	FY 2006	FY 2005	Change %
Real estate rent	66,352	130,190	*–49.0%*
Condominium fees	51,848	62,178	*–16.6%*
Leasing fees	57,191	56,088	*–1.9%*
	175,391	**248,456**	***–29.4%***

Rental fees decreased compared to the previous year due to the closure of the offices in Rome and the closure of a contract in Florence.

6.7 Various Operating Costs

(Euro)	FY 2006	FY 2005	Change %
Various tax charges	7,645	54,520	*–86.0%*
Non-deductible VAT	137,837	30,528	*N.A.*
Membership fees	17,292	29,542	*–41.5%*
Various costs	55,461	145,628	*–61.9%*
	218,236	**260,218**	***–16.1%***

Please note the increased non-deductible VAT costs compared to the 2005 financial statements, due to the increase of the non-deductible rate because of the higher number of transactions on overall 2006 business volume.

6.8 Non-recurring Income (Charges)

(Euro)	FY 2006	FY 2005	Change %
Income	–	9,048,650	*N.A.*
Charges	–	(2,347,249)	*N.A.*
	–	**6,701,401**	***N.A.***

In the first half of 2006, following CONSOB recommendations announced in their press release dated 28 July 2006 no. 6064293, the non-recurring items in the income statement were shown within the various accounting items as well as aggregated and described in the notes to the reclassified income statement in the general section of this report.

6.9 Financial Income

(Euro)	FY 2006	FY 2005	Change %
Interest liabilities to subsidiaries	2,006,159	617,951	*N.A.*
Bank interest assets	32,442	46,683	*–30.5%*
Dividends received	415,020	–	*N.A.*
Income on securities	87,770	1,328,995	*–93.4%*
Interest assets on other loans	–	319	*N.A.*
Interest assets on tax credits	86,440	429,308	*–79.9%*
Fair value adjustment	1,099,363	100,435	*N.A.*
Other financial income	–	216,510	*N.A.*
	3,727,194	**2,740,201**	***36.0%***

Interest assets on subsidiaries increased due to the higher amounts recognised in inter-company current accounts. These were made at market rates.
Dividends received involve the G.I.M. savings shares held in portfolio.
Income on securities involves the sale of 461,947 G.I.M. savings shares.
Fair value adjustments involve G.I.M. savings shares (Euro 996,074) and the closure of an interest rate derivative during the year (Euro 103,289).

6.10 Financial Charges

(Euro)	FY 2006	FY 2005	Change %
Interest liabilities to subsidiaries	5,198,154	4,646,246	*11.9%*
Bank interest liabilities and charges	19,195	95,172	*–79.8%*
Interest liabilities on medium/long-term loans	51,411	35,358	*45.4%*
Interest liabilities on short-term loans	–	419,070	*N.A.*
Other interest liabilities	–	97	*N.A.*
Commissions on coupon payments	43,206	36,674	*17.8%*
Other financial charges	–	832,848	*N.A.*
	5,311,966	**6,065,465**	***N.A.***

Interest liabilities due to the Parent Company involve the subordinated loan and the balance of ordinary current accounts. These were made at market rates.

6.11 Current Taxes

(Euro)	FY 2006	FY 2005	Change %
Taxes for the period	–	307,000	*N.A.*
Income from tax consolidation 2005	(61,233)	–	*N.A.*
Income from tax consolidation 2006	(10,537,000)	–	*N.A.*
	(10,598,233)	**307,000**	***N.A.***

There were no tax liabilities recognised for the year that benefited from the tax consolidation with Europa Metalli and Europa Metalli Brass.
Starting from the 2004 financial year, KME Group S.p.A. and their Italian subsidiaries which exercised the option to be included in the “national fiscal consolidation” scheme calculated their corporate tax rates as the sum of the positive and negative tax amounts of the individual companies within the group. Business relations between parent companies and their subsidiaries, which include contractual obligations and various responsibilities, are defined in the agreement and

regulations regarding the national fiscal consolidation, according to which the parent companies and/or the subsidiaries having negative taxable income receive a tax credit equal to the tax savings made by the parent company and/or subsidiaries having positive taxable incomes.
During the year, tax benefits of Euro 10.5 million were recognised, deriving from the use of KME Group S.p.A. past tax losses which were previously not recognised as deferred tax assets. They were used to reduce the current taxes of the subsidiary companies.

6.12 Deferred Taxes

(Euro)	FY 2006	FY 2005	Change %
Clearance of deferred taxes calculated on revaluation of assets conferred	–	1,262,586	*N.A.*
Clearance of deferred taxes for closure of IRS	33,144	–	*N.A.*
	33,144	**1,262,586**	***N.A.***

This item refers to the clearance of deferred tax assets calculated on the Interest Rate Swap that was closed in 2006.

7. Other information

Average number of employees

	FY 2006	FY 2005	Change %
Managers	3	5	*–40.0%*
Clerical employees	2	1	*N.A.*
Labourers	1	1	*N.A.*
	6	**7**	***–14.3%***

ATTACHMENTS TO THE NOTES

List of equity investments at 31 December 2006 and changes on figures at 31 December 2005

(pursuant to article 126 of CONSOB regulation no. 11971/99)

(figures in Euros)

Investments	Par value	Balance at 31.12.2005		Change in period (+ / –)		Adjustments	Balance at 31.12.2006				Market value B		Difference
		Quantity	Value	Quantity	Value		Quantity	%	Average Book value	Book value	Unit value	Countervalue	
Subsidiaries (booked in fixed financial assets)													
KM Europa Metal A.G.	No par value	27,918,276	302,669,881		485,659		27,918,276	100.00		303,155,540			
Immobiliare Agricola Limestre S.r.l.			7,735,000					100.00		7,735,000			
Total investments in subsidiaries		**310,404,881**			**485,659**	**0**				**310,890,540**			
Associated companies (booked in fixed financial assets)													
Consorzio Italmun		1	129,114				1	50.00	129,114.00	129,114			
Total investments in associates		**129,114**		**0**	**0**					**129,114**			
Parent companies (booked in working capital)													
GIM - saving shares	Euro 1.00	5,704,444	4,620,600	(461,947)	(374,177)	996,074	5,242,497	37.37	1.000	5,242,497	1.119	5,866,354	623,857
Total investments in parent companies			**4,620,600**		**(374,177)**	**996,074**				**5,242,497**			**623,857**
Treasury shares (booked in working capital)													
KME Group S.p.A. saving shares		65,000	37,161				65,000		0.572	37,161	0.560	36,400	(761)
Total treasury shares		**37,161**			**0**	**0**				**37,161**			**(761)**
Total		**315,191,756**			**111,482**	**996,074**				**316,299,312**			**623,096**

List of interests in indirectly controlled subsidiaries
(pursuant to articles 125 and 126 of CONSOB regulation no. 11971/99)

	Registered office	Type of business	Share capital		Direct interests at 31.12.2006		% Total direct and indirect
			Currency	Amount	%	Company name	
Europa Metalli S.p.A.	Italy	Copper and alloys proc.	Euro	100,000,000	100.00	KM Europa Metal A.G.	100.00
Kabelmetal Messing Bet. GmbH. Berlin	Germany	Real estate	Euro	4,514,200	100.00	KM Europa Metal A.G.	100.00
Kabelmetal Messing Bet. GmbH. Nbg.	Germany	Holding	DM	511,291	100.00	KM Europa Metal A.G.	100.00
KME Metal GmbH	Germany	Raw materials distribution	Euro	511,292	100.00	KM Europa Metal A.G.	100.00
KME Verwaltungs - und Dienstleistungsgesellschaft mit beschraenkter Haftung	Germany	Copper and alloys proc.	Euro	10,225,838	100.00	KM Europa Metal A.G.	100.00
Evidal Schmoele Verwautungsgesellschaft	Germany	Distribution	Euro	30,000	50.00	KM Europa Metal A.G.	50.00
Fricke GmbH	Germany	Holding	Euro	25,564	100.00	KM Europa Metal A.G.	100.00
Fricke GmbH & Co. K.G.	Germany	Non-ferrous metals processing	Euro	1,329,359	100.00	KM Europa Metal A.G.	100.00
KME Asia Pte. Ltd.	Singapore	Distribution	$SG	300,000	100.00	KM Europa Metal A.G.	100.00
KME Danmark A/S	Denmark	Distribution	DKK	1,000,000	100.00	KM Europa Metal A.G.	100.00
KME Metals (Dongguan) Ltd.	China	Distribution	RMB	41,391,200	100.00	KME China Ltd.	100.00
KME America Inc.	United States	Distribution	$US	5,000	100.00	KM Europa Metal A.G.	100.00
KME Austria Vertriebsgesellschaft mbH	Austria	Distribution	Euro	72,673	100.00	KM Europa Metal A.G.	100.00
KM - Hungaria Szinesfem Kft.	Hungary	Distribution	HUF	3,000,000	100.00	KM Europa Metal A.G.	100.00
KME (Suisse) S.A.	Switzerland	Distribution	FS	250,000	100.00	KM Europa Metal A.G.	100.00
KME Polska Sp.zo.o.	Poland	Distribution	PLZ	250,000	100.00	KM Europa Metal A.G.	100.00
KME UK Ltd.	Great Britain	Distribution	LST	10,014,603	100.00	KM Europa Metal A.G.	100.00
Yorkshire Copper Tube	Great Britain	Manufacturing	LST	3,261,000	100.00	KME UK Ltd.	100.00
EMT UK Ltd.	Great Britain	Distribution	LST	500,000	100.00	KME UK Ltd.	100.00
Irish Metal Industries Ltd.	Ireland	Distribution	Euro	127	100.00	KME UK Ltd.	100.00
Yorkshire Copper Tube (Exports) Ltd.	Great Britain	Distribution	LST	100	100.00	Yorkshire Copper Tube	100.00
YIM Scandinavia A.B.	Sweden	Distribution	SEK	100,000	100.00	KME Danmark A/S	100.00
N.V. KME Benelux	Belgium	Distribution	Euro	62,000	84.70	KM Europa Metal A.G.	100.00
					15.30	Tréfimétaux S.A.	
KME China Ltd.	China	Distribution	$HK	27,095,000	100.00	KM Europa Metal A.G.	100.00
KME Chile Lda.	Chile	Distribution	PSC	9,000,000	99.00	KM Europa Metal A.G.	100.00
					1.00	KME metal GmbH	
KME Moulds Mexico S.A. de C.V.	Mexico	Distribution	MXN	50,000	99.00	KM Europa Metal A.G.	100.00
					1.00	Kabelmetal Messing Bet. GmbH, Berlin	
KME Czech Republic S.r.O.	Czech Republic	Distribution	CZK	100,000	100.00	KM Europa Metal A.G.	100.00
Accumold A.G.	Switzerland	Services	FS	200,000	100.00	KM Europa Metal A.G.	100.00
Bertram's GmbH	Germany	Services	Euro	300,000	100.00	KM Europa Metal A.G.	100.00
Luebke GmbH	Germany	In liquidation	Euro	102,258	100.00	KM Europa Metal A.G.	100.00
KME Ibertubos S.A.	Spain	Copper and alloys proc.	Euro	332,100	100.00	KME Iberica S.A.	100.00
KME Iberica S.A.	Spain	Holding	Euro	1,943,980	99.86	Kabelmetal Messing Bet. GmbH, Berlin	99.86
Cuprum S.A.	Spain	Distribution	Euro	60,910	100.00	KME Iberica S.A.	100.00
Informatica y Organizacion S.A.	Spain	Services	Euro	276,175	100.00	KME Iberica S.A.	100.00
LOCSA - Laminados Oviedo Cordoba S.A.	Spain	Copper and alloys proc.	Euro	10,040,000	100.00	KME Iberica S.A.	100.00
Europa Metalli Tréfimétaux Deutschland GmbH	Germany	Distribution	Euro	1,043,035	100.00	KM Europa Metal A.G.	100.00
Tréfimétaux S.A.	France	Copper and alloys proc.	Euro	53,000,000	100.00	KM Europa Metal A.G.	100.00
XT Ltd.	Great Britain	Distribution	LST	430,000	100.00	KME UK Ltd.	100.00
TMX Brass S.A.S.	France	Copper and alloys proc.	Euro	7,800,000	100.00	Tréfimétaux S.A.	100
Société Haillane de Participations S.A.	France	Financial co.	Euro	40,000	99.76	Tréfimétaux S.A.	99.76
TMX Components S.A.S.	France	Financial co.	Euro	52,450	65.00	Tréfimétaux S.A.	65.00
Dalian Dashan Chrystallizer Co. Ltd.	China	Copper and alloys proc.	RMB	10,000,000	30.00	KM Europa Metal A.G.	30.00
Dalian Surface Machinery Co. Ltd.	China	Copper and alloys proc.	RMB	5,500,000	30.00	KM Europa Metal A.G.	30.00
Immobiliare Agricola Limestre S.r.l.	Italy	Real estate	Euro	7,735,000	100.00	KME Group S.p.A.	100.00
KME Brass GmbH	Germany	Copper and alloys proc.	Euro	50,000	100.00	KM Europa Metal A.G.	100.00
Europa Metalli Brass S.r.l.	Italy	Copper and alloys proc.	Euro	15,025,000	100.00	Europa Metalli S.p.A.	100.00

REPORT OF THE BOARD OF STATUTORY AUDITORS TO THE SHAREHOLDERS ADJOURNED FOR THE APPROVAL OF FINANCIAL STATEMENTS CLOSED AT 31 DECEMBER 2006

Shareholders,

The Directors have called you to assemble on 30 April-23 May 2007 to approve the financial statements closed on 31 December 2006 in accordance with article 2364 of the civil code. The Board of Statutory Auditors will report to you, as is their responsibility in accordance with article 153 of Legislative Decree 24 February 1998, no. 58.

Board of Statutory Auditors' Surveillance and Information

During the financial year closed on 31 December 2006, the Board of Statutory Auditors, as well as having attended the nine meetings of the Board of Directors in accordance with article 149, paragraph 2, of Legislative Decree 24 February 1998, no. 58, and the shareholders' meetings that were held during the year, also attended six Board of Statutory Auditors' meetings pursuant to article 2404 of the civil code. The Board kept in contact with the independent auditors and was in continuous contact with corporate management in general, and moreover with the Internal Control and Compensation Committees, in which the Chairman of the Board and other Statutory Auditors have always participated, as they did in the periodic O.C.I. (Internal Control Body) meetings (pursuant to Legislative Decree 231/01). For information regarding the composition, governing and functions of the corporate bodies please see the full description contained in the Report of the Board of Directors. This contains the criteria pursuant to article 3.C.1 of the Code of Conduct, which the Board of Statutory Auditors believes that it has followed, as four members of the Board of Directors may be considered independent. The minutes of the company board meetings are contained in the regular obligatory company books as legally required, and include any pertinent details. The Board of Statutory Auditors kept in contact with the Board of Statutory Auditors of the Parent Company G.I.M. S.p.A. and with members of the Boards of the subsidiary companies.
To fulfil its duties and for the frequent meetings mentioned above, the Board of Statutory Auditors:

a) ascertained that the legal and statutory regulations were observed. These were adjusted in accordance with new norms to protect the rights of minority shareholders contained in Legislative Decree 58/1998;

b) having been requested to do so by the Directors, ascertained that company administration was performed according to the correct principles, frequently and at proper time intervals, on activities performed, on operations, and on major events, both with reference to KME Group S.p.A., its Parent Company and its subsidiaries;

c) oversaw the internal control accounting and organisation procedures, which did not give rise to any remarks. Despite the relatively small size of the Company's administrative structure, this supervision was trustworthy, even in consideration of problems relating to administrative responsibility as described in article 5 of Legislative Decree 231/2001. The Board also ensured that control procedures were suitable to Company and Group requirements, and adhered to accounting regulations. It was not necessary for the Auditors to avail themselves of assistance from employees or auxiliaries (pursuant to article 151, paragraph 3 of Legislative Decree no. 58 of 24 February 1998);

d) ascertained that during the financial year both directly and indirectly held subsidiaries notified KME Group S.p.A. regularly and on time through the direct subsidiary KME Europa Metal AG of the necessary news so that it could fulfil the financial reporting obligations pursuant to article 114, paragraph 2; article 149, letter d of paragraph 1; article 150, paragraph 1; of Legislative Decree no. 58 of 24 February 1998;

e) did not find irregularities and did not receive notifications or complaints from shareholders. No final judgements were made by the Court of Rome regarding the questions that were raised at one point by a shareholder against Luigi Orlando, the Company's previous Chairman of the Board of Directors. After the initial judgement in favour of the defendant (which is described in the previous year's report), the plaintiff appealed. Regarding the other civil suit concerning the conditions of the right of withdrawal for the Europa Metalli - LME S.p.A. merger, please note the following: a date has been set with the Italian High Court of Appeal (27 April 2007), as the previous judgements all ruled for the Company. Lastly, the subsidiary Europa Metalli and other companies were accused of having caused environmental damage for the area around the disused company plant in Brescia, in two different court cases. This litigation is by nature complex, and therefore the Directors cannot presently make any assumption as to their outcome;

f) did not find any unusual or atypical operations with associates or third parties. Regarding transactions with other Group companies, none were unusual or atypical. For detailed information on this subject please see the Report of the Board of Directors, and the information contained below;

g) is also aware that during the 2006 financial year, Deloitte & Touche — who were assigned to audit the financial statements of the KME Group S.p.A. and its Parent Company G.I.M. S.p.A. — audited the accounts of Group subsidiaries, a service for which the subsidiaries paid separately, as in previous financial years;

h) was informed that during the 2006 financial year, the Company assigned the independent auditors with the following actions: the creation of a report involving the prospectus of the options offer for the capital increase which was resolved on 19 May 2006; the report for the issue price of the shares involved in the capital increase excluding the options rights (article 2441, paragraph IV of the civil code); and the ensuing review for the related tax declarations. This information is described in full in the Report of the Board of Directors. The Board of Statutory Auditors also:

i) took note, participating in the actions of the ruling corporate bodies, of the resolution made at the extraordinary meeting of shareholders held on 19 May 2006 in which the Company name was changed from "S.M.I. - Società Metallurgica Italiana S.p.A." to "KME Group S.p.A.". The Board shared the sentiment that this reflected the international aims of the Group in the copper and alloys sector;

j) participated in and supervised the process that saw the application of Borsa Italiana S.p.A.'s Code of Conduct to the Company in its latest, 2006 edition. This compliance programme, pursuant to TUF article 124 ii must be divulged to shareholders and the market. Therefore, the Auditors took note of these actions, not only to help shareholders but also as a base upon which the Directors could make their report. Furthermore, please note, regarding internal control, the acceleration of the activities of the O.C.I. (Internal Control Body). Starting from halfway through last year it held frequent meetings, mostly to discuss the regulation of access to "sensitive information" and related matters;

k) please note furthermore the substantial section in the Report of the Board of Directors that deals with Corporate Governance, which, besides containing detailed information on corporate bodies and its components, also contains information on the following: regulations regarding transactions with related parties; Directors' and upper management compensation, particularly regarding the stock options plan that was implemented last year; the Compensation Committee; the Internal Control Committee; and also some notes to other issues such as the Code of Conduct regarding Internal Dealing. On the whole, the information given is exhaustive, also regarding these last points.

Proposals for the 2006 Financial Statements

The financial statements at 31 December 2006 show a net profit of Euro 7,205,770 (in 2005 net profit was Euro 1,395,184).
The reasons for the improvement in the Parent Company's profits were: higher commissions for services made to Group companies; lower financial expenses due to the extinction of the subordinated loan taken out by the Parent Company G.I.M. S.p.A. for Euro 130 million in order to transfer funds resulting from the increase in share capital approved by the shareholders in the general meeting on 19 May 2006; the adjustment of G.I.M. S.p.A. saving shares to reflect fair value, of Euro 1 million; and last but not least, for the positive booking in the income statement under the item "Taxes" of Euro 10.5 million, deriving from the usage of past tax losses of the Parent Company regarding income taxes of the Italian subsidiaries of the Group (see E.M. Brass S.r.l.) which exercised their option to adhere to the national tax consolidation scheme.
The first part of this Report shows a wide ranging picture of the Group's operations in 2006, and the many and varied reasons that allowed for the attainment of consolidated profits of Euro 51.7 million, which were much higher than those in 2005, which amounted to Euro 4.3 million. Information is given regarding this general aspect, starting from the steps taken regarding unusually volatile copper prices, to an analysis of production and distribution trends for each individual compartment (in short, the sheeting compartment did not do well, while brass bars and fittings attained satisfying results, as did copper casting). At the end of 2006, the Group net financial position was Euro 534 million (Euro 559 million at the end of 2005). Please see the press releases that were widely divulged to the market regarding the new loans that were obtained by the Group's banks, based on agreements that were signed in 2006, for a total of Euro 1.6 billion.

In accordance with article 153, paragraph 2 of Legislative Decree 58/98, the Board of Statutory Auditors proposes no motions regarding the financial statements under examination. It only believes that, for fullness of information, it is opportune to make the following remarks regarding shareholders' equity, and regarding some of the accounting principles and the opinion of the independent auditors, with which the Board of Statutory Auditors — we repeat — was occasionally in contact during the year and during the preparation of the statements by the Directors.

The balance sheet items, listed according to their nature, may be summarised as follows (figures in thousands of Euros):

ASSETS	2006	2005
– Investments in property	10,535	8,985
– Equity investments in KME AG	303,156	302,670
– Other assets (GIM savings shares and various)	14,926	7,444
TOTAL ASSETS	**328,617**	**319,099**

LIABILITIES	2006	2005
– Share capital and reserves	327,563	197,689
– Net financial position	(6,152)	(9,985)
– Subordinated loan from G.I.M. S.p.A.	0	130,000
– Net profit for the year	7,206	1,395
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**328,617**	**319,099**

From meetings held with Company management and through other channels, the Board of Statutory Auditors received pertinent information regarding the accounting principles applied to the various assets and liabilities, as well as those used to calculate the components of the income statement; the decisions made were based on correct and proper reasoning. On 31 December 2006, the independent auditors had not yet issued their report regarding their opinion on the financial statements and their overall year-end reports. Furthermore please note that in the Board's meetings and discussions with the independent auditors, the Board was informed beforehand that the independent auditors did not find any facts and/or events that might have prevented the auditors from issuing a professional opinion with any major reservations.

In acknowledgment of this result, the Board of Statutory Auditors particularly notes that:

– the accounting principles applied were those set by IFRS issued by the IASB, and were clearly shown in detail for each item category in assets and liabilities;

– the balance of adjustments made for the transition to IAS is booked to a separate reserve in shareholders' equity called "Reserve for first adoption of IAS IFRS";

– the principles and procedures used to calculate deferred taxes are shown appropriately, and no issues arose in this regard;

– the completeness of information to which the Directors referred in detail regarding intra-group transactions, all of which may be classified as regular holding company operations. These specifically refer to financing relationships regulated as current accounts and service relationships for specific management areas, all of which are regulated on a normal contractual basis;

– we hereby conclude our Report for the 2006 financial year, with a proposal inviting our shareholders to approve in their entirety this report and these financial statements, which show a net profit of Euro 7,205,770; to resolve the usage of funds to the "Reserve for first adoption of IAS/IFRS", which therefore goes from Euro 2,784,099 to Euro 1,644,616, due to the cost of Euro 1,037,925 sustained for the recent share capital increase, as well as the allocation of Euro 101,558 to the "Reserve for Parent Company shares in portfolio"; and lastly, to allocate profits for the year of Euro 7,205,770, of which Euro 360,289 (5%) to Legal Reserves, Euro 6,206,637 to savings shares at a measure of one dividend of Euro 0.1086 per share including a preference dividend for the 2006 financial year and, according to the company bylaws, preference dividends for the previous 2005 and 2004 financial years; and carry forward the remaining profits of Euro 638,844.

Taking account of all of the above and the contents of the Statutory Auditors' report of the consolidated financial statements, the Board of Statutory Auditors hereby raises no objections to the approval of the statements to 31 December 2006 and the allocation of part of the IAS/IFRS reserve to the uses indicated previously, and of the profits of Euro 7,205,770 as mentioned in detail above.

Florence, 31 March 2007

The Board of Statutory Auditors

REPORT OF THE INDEPENDENT AUDITORS

Deloitte.

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AUDITORS' REPORT PURSUANT TO ART. 156 OF LEGISLATIVE DECREE No. 58 OF FEBRUARY 24, 1998

To the Shareholders of
KME GROUP S.p.A.

1. We have audited the financial statements of KME GROUP S.p.A., which comprise the balance sheet as at December 31, 2006, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. These financial statements are the responsibility of the Company's Directors. Our responsibility is to express an opinion on these financial statements based on our audit.

2. We conducted our audit in accordance with the Auditing Standards recommended by CONSOB, the Italian Commission for listed Companies and the Stock Exchange. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Directors, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

   For the opinion on the prior year financial statements, the balances of which are presented for comparative purposes, reference should be made to our auditors' report issued on April 11, 2006.

3. In our opinion, the financial statements present fairly the financial position of KME GROUP S.p.A. as of December 31, 2006, and the results of its operations and its cash flows for the year then ended in accordance with IFRS as adopted by the European Union and the requirements of national regulations issued pursuant to art. 9 of Italian Legislative Decree n. 38/2005.

DELOITTE & TOUCHE S.p.A.

Signed:
Paolo Guglielmetti
Partner

Florence, April 11, 2007

This report has been translated into the English language solely for the convenience of international readers.

APPOINTMENT OF DIRECTORS AFTER DETERMINING THE SIZE OF THE BOARD OF DIRECTORS, AND RELATED AND REQUIRED RESOLUTIONS, INCLUDING RESOLUTIONS CONCERNING THE DETERMINATION OF THE FIXED ANNUAL DIRECTOR'S FEE REFERRED TO IN ARTICLE 21 OF THE COMPANY BYLAWS

Shareholders,

The Board of Directors in office was appointed through resolutions made at the general meeting of shareholders on 19 May 2006 for the financial years 2006, 2007 and 2008; therefore their office will expire at the general meeting held to approve the financial statements at 31 December 2008.

At the same meeting, the shareholders resolved to fix their number at nine and set their compensation.

The names and the positions held by each individual, along with their curriculum vitae, are shown in the "Report of the Board of Directors".

Taking into consideration the imminent merger of the Parent Company G.I.M - Generale Industrie Metallurgiche S.p.A. ([1]) and INTEK S.p.A., we believe that the number of Directors should be increased in order to better diversify the individual personal and professional expertise of each member of the Board of Directors.

Naturally, any possible new Directors will be appointed for the same period as those currently holding positions, and therefore will expire at the same reference date as the general meeting indicated above.

Please also set their level of compensation in accordance with article 21 of the company bylaws.

Florence, 20 March 2006

The Board of Directors

(1) The merger of G.I.M. - Generale Industrie Metallurgiche S.p.A. and INTEK S.p.A. was finalised on 31 March 2007.

REPORT AND PROPOSAL MADE BY THE BOARD OF STATUTORY AUDITORS AT THE SHAREHOLDERS' GENERAL MEETING HELD ON 30 APRIL/23 MAY 2007 REGARDING AUDITING ACTIVITIES

Cancellation of the assignment to audit the statutory and consolidated financial statements for the financial year ending 31 December 2007, perform a limited audit of the semi-annual report at June 30, 2007 and perform regular checks of the accounting records, which was granted to Deloitte & Touche S.p.A. pursuant to articles 155 and following of Legislative Decree no. 58 of February 24, 1998.
Awarding the auditing role to KPMG S.p.A., pursuant to the abovementioned articles 155 and following of Legislative Decree no. 58 of 24 February 1998, regarding the annual and consolidated financial statements for the financial years closing on 31 December of the years 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015, as well as the assignment to perform a limited audit of the semi-annual report, consolidated and non-consolidated, to 30 June for the years 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015 and occasional checks of company accounting practices.
Related and required resolutions, including resolutions concerning the setting of the fee payable to the Independent Auditors

Shareholders,

Recent regulations regarding the auditing of corporate accounts have made innovations in this area, and because this matter directly involves the Board of Statutory Auditors, corporate controls bodies have been assigned a particularly relevant role regarding proposals for bestowal of the assignment as independent auditor, the eventual cancellation of this assignment, and the determination of related fees.

These regulations were introduced through Legislative Decree no. 303 dated 29 December 2006 and those specifically relating to the bestowal of the assignment were included in Law no. 262 dated 28 December 2005, called the "Savings Protection Law". The latest and prevailing version of article 159 of Legislative Decree 24 February 1998 no. 58 (the "TUF") specifically indicates the bestowal of a nine-year, non-renewable assignment, that can only be newly bestowed if an additional three years have passed following the cancellation of the previous assignment.

Regarding these regulations, please note that the shareholders of G.I.M. - Generale Industrie Metallurgiche S.p.A. ([1]) – the Parent Company of KME Group S.p.A., assembled in the general meeting, resolved on 16 January 2007 to merge with INTEK S.p.A.. This will be put forth for approval in the very near future. As of the effective date of this merger, the Company will fall under direct control of INTEK S.p.A., an event that will produce effects that include auditing activities and certification of accounts.

Please be reminded that the KME Group S.p.A. (then called S.M.I. - Società Metallurgica Italiana S.p.A.) shareholders assembled on 27 April 2005 bestowed the company Deloitte & Touche S.p.A. with the following:

a) the role of auditing the accounts pursuant to article 159 and following of the TUF for the financial statements closed on 31 December of the years 2005, 2006 and 2007;
b) a limited review of accounts of the semi-annual consolidated and non-consolidated reports at 30 June for the years 2005, 2006 and 2007;
c) periodic checks on corporate accounting practices.

A similar assignment was given to Deloitte & Touche S.p.A. by G.I.M. - Generale Industrie Metallurgiche S.p.A. at the general meeting of shareholders held on 19 May 2006 for the 2006 to 2011 period, in accordance with the regulations prevailing at that time.

Please also note that in reference to the governance prevailing at that time, the current assignment approved by the Company constitutes the second renewal of the three-year period, and therefore, when it expires with the closing of the

(1) The merger of G.I.M. - Generale Industrie Metallurgiche S.p.A. and INTEK S.p.A. was finalised on 31 March 2007.

current financial year on 31 December 2007, it will not be possible to bestow it again to Deloitte & Touche S.p.A., since this company will have carried out such activities without interruption for a total of nine financial years.

The financial statements of INTEK S.p.A. are subject to audits made by KPMG S.p.A., as resolved by shareholders of the company in the general meeting on 13 June 2006, a resolution that bestowed KPMG S.p.A. with the assignment to audit its statutory and consolidated financial statements closed on 31 December for the years 2006, 2007 and 2008, as well as a limited accounting review of the semi-annual reports at 30 June for 2006, 2007 and 2008.

Therefore, effective as of the merger date of G.I.M. - Generale Industrie Metallurgiche S.p.A. and INTEK S.p.A., since a situation would have arisen in which the audit assignments would not have allowed KPMG S.p.A. to have the status of principal auditor for INTEK S.p.A., discussions were initiated with Deloitte & Touche S.p.A. and KPMG S.p.A. in order to find a practical solution to problems that would inevitably arise.

Prevailing regulations do not allow for the auditing assignment to be cancelled by mutual consent, but rather it may only be cancelled with “just cause”, which must be approved by shareholder resolution upon a proposal made by the Board of Statutory Auditors. We believe that this situation represents just such a cause, and therefore we propose the cancellation of the assignment that was bestowed to Deloitte & Touche S.p.A. for the time remaining.

Please note articles 165 and following of the TUF, and specifically the CONSOB regulation dated 1999 (n. DAC/99023119 from 25 March 1999). These establish which situations might and might not be defined as “just cause” in cancelling an auditing assignment. The loss of status as principal Group auditor (in the case of the auditing company that previously held this position) is one of these situations.

The decision to cancel the assignment given to Deloitte & Touche S.p.A. was naturally preceded by suitable investigations in order to proceed with the substitution of the auditing company without weighing down the procedures, avoid duplication of auditing activities within Group companies and ensure auditing continuity during the course of the year.

Pursuant to article 159, Paragraph V of the TUF, the resolution to cancel the assignment of Deloitte & Touche S.p.A. is only effective if CONSOB does not express its disapproval within 20 days of receiving the necessary documentation. In this case, Paragraph 2 of this same article states that continuous accounting controls must be exercised by the company whose assignment is revoked up until the date in which the resolution takes full effect.

Furthermore, we propose that you bestow the auditing assignment to KPMG S.p.A. for a period of nine financial years closing on 31 December, for 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015 in reference to the annual and consolidated financial statements in accordance with prevailing regulations, and jointly for the limited review of the semi-annual and consolidated reports closed on 30 June for the years 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015. This company will have the status of principal auditor at Group level through current or renewable assignments. The head of the auditing and certification duties will take on this position in reference to certification made regarding shareholder equity at 30 June 2007 and the financial statements at 31 December 2007, and can hold this position for a maximum of six financial years pursuant to article 160, Paragraph I *iv* of the TUF.

KPMG S.p.A. has proposed to KME Group S.p.A. on 16 March 2007 the following annual fees for the audits of the annual and consolidated financial statements of the Parent company for the years closing at 31 December 2007/2015 pursuant to articles 155 and following of the TUF as well as for the limited accounting review of the semi-annual reports at 30 June 2007/2015 and for periodic tests of the accounting and the correct recognition of operating events in accounts:

- Euro 20,000.00 for the financial statements (for a total of 250 hours);
- Euro 26,000.00 for the consolidated financial statements (for a total of 260 hours);
- Euro 14,000.00 for the semi-annual report (for a total of 140 hours).

The total is therefore Euro 60,000.00 for 650 hours, and includes fees for accounting checks and for verification of proper recognition of operating events in corporate accounts.

These totals do not include reimbursements for expenses that will be included in the final balance for travel and lodging, secretarial fees (direct and indirect) and other expenses sustained for the Company (telephone, fax, external consultancy, etc.), the guarantee contribution due to CONSOB for its temporarily applicable provisions or VAT.

As per CONSOB regulations, the aforementioned fees may be adjusted annually, starting from 1 July 2007, at the same percentage rate of change of the ISTAT cost of living index for the previous year. Any other possible adjustments to these fees will be made in accordance to criteria set by pertinent CONSOB regulations.

The fees proposal, which is detailed in a letter of 44 pages accompanied by analytic figures and well-grounded reasoning, also includes:

- the auditing procedures and the plan for the carrying out of audits prescribed by the relevant regulations and applicable auditing principles, in accordance with the legal prescriptions and CONSOB indications;
- a list of the personnel employed for the job and the composition of the relevant team, which will be managed at the offices of the auditing company in Florence, as well as the name of the auditing manager Mr Riccardo Cecchi.

Regarding the suitability of the proposal, please note the following:

- KPMG S.p.A. in our opinion possesses the necessary characteristics to be qualified as independent from the company bestowing the assignment and its Group, as it does not carry out any other assignments for the KME Group S.p.A. nor for any other Group companies;
- the KPMG S.p.A. head of auditing has the required first-rate professional expertise, and the auditing company has a suitable office in Florence with a number of employees appropriate to meet requirements, and having the necessary level of experience;
- the auditing procedures and the established auditing plan are objectively reliable, both from a theoretical and from a practical point of view;
- auditing activities must be made in a suitable and complete manner, with the necessary investigations relating to the size and complexity of the assignment, keeping in mind particularly that KPMG S.p.A. will audit the accounting of other Group companies according to an agreement with KPMG and the previous auditing company Deloitte & Touche S.p.A.;
- for the Group companies that are not audited by KPMG S.p.A., KPMG S.p.A. will review the results of the audits for these companies made by other auditing companies;
- these fees, set in accordance to CONSOB criteria, are congruent with the activities performed and the amount which was set for the previous assignment, which came to a total of Euro 65,000.00.

It will naturally be the responsibility of the Board of Statutory Auditors to collaborate with the independent auditing company with due regularity.

Lastly, please note that this proposal was brought before the Board of Directors of KME Group S.p.A. during its meeting held on 20 March 2007.

We therefore propose the following resolutions:

The shareholders of KME Group S.p.A., meeting in ordinary session at the company's offices in Via dei Barucci, 2, Florence:

- having noted the effective merger between G.I.M. - Generale Industrie Metallurgiche S.p.A. and Intek S.p.A.;
- considering the proposal motioned by the Board of Statutory Auditors regarding the cancellation of the assignment given to Deloitte & Touche S.p.A.;
- considering the proposal motioned by the Board of Statutory Auditors regarding the bestowal of the assignment to KPMG S.p.A.;
- considering the assignment proposal made by KPMG S.p.A.;
- taking into account the Report of the Board of Directors and their conclusions made therein;
- taking into account article 159 of Legislative Decree no. 58 of 24 February 1998, which states that the assignment for auditing the statutory and consolidated financial statements may last nine financial years and therefore article 24 (Accounting Audits) of the company bylaws must be suitably updated;

RESOLVE

1. to cancel the remaining assignment made to Deloitte & Touche S.p.A. by shareholders in general assembly on 27 April 2005 for the auditing of the annual and consolidated financial statements, in accordance with article 155 and following of Legislative Decree no. 58 of 24 February 1998, to be completed with the year closing on 31 December 2007 along with the limited audit of the semi-annual report at June 30, 2007, the regular reviews of the consolidated and non-consolidated accounts, the periodic checks of the accounts and the proper recognition of operating events in corporate accounts;
2. to bestow to KPMG S.p.A. the assignment to audit the statutory and consolidated financial statements, in accordance with article 155 and following of Legislative Decree 24 February 1998 no. 58, to be completed in reference to the statutory and consolidated financial statements closing on 31 December for the years 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015, as well as the assignment for the limited review of the accounts for the semi-annual consolidated and non-consolidated reports closed at 30 June for the years 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 and 2015, the periodic checks of the accounts and the proper recognition of operating events in corporate accounts;
3. based on an estimate made according to criteria established by CONSOB — the Italian National Commission for Companies and Markets — in regulation DAC/RM/96003556 issued on 18 April 1996, to set the fees for the performance of this assignment at a total of Euro 60,000.00 annually to the aforementioned auditing company for the following duties: Euro 20,000.00 for the annual financial statements, Euro 26,000.00 for the consolidated financial statements and Euro 14,000.00 for the consolidated and non-consolidated semi-annual report. These fees also include those for periodic checks of the accounts and the proper recognition of operating events in corporate accounts, but do not include the guarantee contribution due to CONSOB — the Italian National Commission for Companies and Markets — which, in line with the temporarily applicable provisions, will be included in the final balance, sundry costs, which will be reimbursed at the same level as they were sustained, and VAT. As per CONSOB regulations, the aforementioned fees may be adjusted annually on 1 July of each year, starting from 1 July 2007, at the same percentage rate of change of the ISTAT index regarding cost of living from the previous year. If any exceptional or unforeseeable circumstances arise, these fees may be adjusted according to the criteria set by CONSOB — the Italian National Commission for Companies and Markets — regulation no. DAC/RM/96003556 issued 18 April 1996.

Florence, 20 March 2007

The Board of Statutory Auditors

REPORT OF THE BOARD OF DIRECTORS REGARDING THE PROPOSAL MADE BY THE BOARD OF STATUTORY AUDITORS TO CANCEL THE ASSIGNMENT AWARDED TO DELOITTE & TOUCH S.P.A. TO AUDIT THE ACCOUNTS, AND CONCURRENT AWARD TO KPMG S.P.A. FOR THE YEARS 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 AND 2015, AND PERFORM LIMITED AUDITS OF THE SEMI-ANNUAL REPORTS AND CONSOLIDATED FINANCIAL STATEMENTS AT JUNE 30, 2007, 2008, 2009, 2010, 2011, 2012, 2013, 2014 AND 2015

Shareholders,

The new regulations contained in the TUF have given the Board of Statutory Auditors powers and faculties that were once possessed by the Board of Directors for the selection of the company to audit the accounts, and the cancellation of its mandate.

Regarding the immanent merger of our Parent Company G.I.M. - Generale Industrie Metallurgiche S.p.A. ([1]) with INTEK S.p.A., the Board of Statutory Auditors has provided information on the issues that will arise relating to Group auditing, and therefore it proposes, with just cause, to cancel the assignment given to Deloitte & Touche S.p.A. for its remaining audit period, and give this assignment to KPMG S.p.A., pursuant to new regulations, especially those regarding the nine-year term that is currently provided for.

As is our duty, we have in turn evaluated the situation that was highlighted by the Board of Statutory Auditors and we hereby express our full agreement regarding the solutions made by them in their report and the motions proposed, and we especially agree upon the resolutions put forth to you, which we recommend for approval.

Florence, 20 March 2007

The Board of Directors

(1) The merger of G.I.M. - Generale Industrie Metallurgiche S.p.A. and INTEK S.p.A. was finalised on 31 March 2007.

RESOLUTIONS OF THE ORDINARY GENERAL MEETING ON 23 MAY 2007

The General Meeting of KME Group S.p.A. shareholders, meeting on 23 May 2007 in an ordinary session at the company's registered office in Florence,

resolved

a) to approve the Directors' Report on Operations for the financial year ended 31 December 2006, in addition to the financial accounts, the individual items and entries and the allocations and uses suggested, which showed net profit of Euro 7,205,770;

b) to take from the "reserve for first adoption of IAS/IFRS" the "charges related to the increase in capital transaction", amounting to Euro 1,037,925, and to supplement the "reserve for shares of the parent company in the portfolio" with Euro 101,558, thus reducing the "reserve for first adoption of IAS/IFRS" from Euro 2,784,099 to Euro 1,644,616;

c) to distribute net profit of Euro 7,205,770 as follows: after allocating 5% to the Legal Reserve, to saving shares with a total dividend of Euro 0.1086 per share – which includes the preference dividend relating to the 2006 financial year of Euro 0.0362 and the preference dividends for the two previous financial years 2005 and 2004 – totalling Euro 6,206,637, and allocating the remaining Euro 638,844 to retained earnings;

d) to cancel, for the remainder of the period, the assignment given to Deloitte & Touche S.p.A. to audit the consolidated and statutory annual accounts for the year ending on 31 December 2007 and to provide a limited audit of the interim statutory and consolidated reports at 30 June 2007 and an audit of compliance with accounting practices and correct registration of operating events in the accounting ledgers;

e) to give KPMG S.p.A. the assignment of auditing the consolidated and statutory annual accounts, in accordance with Article 155 et sequitur of Leg. Decree 58 of 24 February 1998, commencing from the accounts of the financial years that will end on 31 December from 2007 to 2015, in addition to the assignment for the limited audit of the interim statutory and consolidated reports at 30 June from 2007 to 2015 and audit of compliance with accounting practices and correct registration of operating events in the accounting ledgers, setting the annual fee to the independent auditors for such services at Euro 60,000.00.

Florence, 23 May 2007

The Board of Directors

KME Group S.p.A. Report and financial statements at 31 December 2006