UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of
The Securities Exchange Act of 1934

For the fiscal year ended JUNE 30, 1998 Commission file number 0-15701

NATURAL ALTERNATIVES INTERNATIONAL, INC.

Incorporated in Delaware	84-1007839
1185 Linda Vista Drive, San Marcos, California 92069	(I.R.S. Employer
(760) 744-7340	Identification No.)

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

Common Stock - $.01 par value   Nasdaq Stock Market

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

The aggregate market value of 4,499,485 shares of voting stock held by non-affiliates (assuming for this purpose that all officers and directors, and affiliates of directors, are affiliates) of the Registrant was approximately $62,151,000 based on the closing sale price as of September 25, 1998.

At September 25, 1998, the Registrant had outstanding 5,887,375 shares of Common Stock, $.01 par value.

Documents Incorporated by Reference

NONE

PART I

ITEM 1. BUSINESS

Natural Alternatives International, Inc. (referred to herein as the "Company") is engaged in the formulation and production of encapsulated vitamins and nutrients and provides sports affiliations, assistance with foreign registration of products, graphic design, brochures, formulations and a host of other marketing related services for its clients. The Company narrowly focuses its marketing activity on attracting and retaining a select number of large, financially sound companies with global, growth-oriented objectives. The Company seeks to further its customers' objectives by assisting them in expanding their market share through a variety of special programs and services. There are no fees charged or revenues generated from these marketing related services, which are generally provided before orders for product are obtained. Therefore, these costs are treated as period costs.

In 1995, the Company expanded and enhanced its laboratory and quality control capabilities. Management believes its technically advanced facilities are a major factor in solidifying existing customer relationships and adding new customers. Newly recognized standards for manufacturing nutritional products should, in the opinion of management, assist the Company in serving its present and future customers. The newly revised United States Pharmacopeia compendia (USP) contain, for the first time, specifications for vitamin and mineral supplements. This USP monograph has long been the basis for determining the strength, quality, purity, packaging and labeling of drugs and related articles. The Company believes it currently has the technical and quality control expertise to conform to all aspects of USP specifications. Conformance with USP specifications will allow the Company to use the USP designation on all products manufactured for its customers, which have the USP designation.

During 1997, the Company expanded its product-delivery system mix with the addition of a tablet manufacturing facility that nearly doubled the Company's overall manufacturing capacity. Tablets and chewable wafers are more readily accepted than capsules by consumers in overseas markets, such as Asia. The Company's proprietary and sophisticated flavoring laboratory formulates chewable wafers in a wide variety of tasty flavors.

The Company has several proprietary lines of products, which were sold by two of its wholly owned subsidiaries, Millennium Health Products, Inc. (formerly Pro-Lean, Inc. and before that Sonergy, Inc.), and CellLife International, Inc. The operations of its two primary subsidiaries were transferred to the Company during fiscal 1997. The Company believes such specialty proprietary products typically generate higher profit margins and assist in product diversification and less reliance on contract manufacturing.

RESEARCH AND DEVELOPMENT

The Company continuously produces pilot or sample runs of products to ensure stability or efficacy and to determine ingredient interaction and prospective customer acceptance. Research of this type, and the associated costs, are part of the operating expenses incurred by the Company. Such research and development has not been significant and is not expected to be significant in the future.

COMPETITION AND BUSINESS RISKS

The vitamin and nutritional supplement industry is highly competitive, and competition is expected to increase in the future. Competition for the sale of vitamins and supplements comes from many sources, including companies which sell vitamins to supermarkets, large chain discount retailers, drug store chains and independent drug stores, health food stores, pharmaceutical companies and others which sell to wholesalers, mail order vendors and network marketing companies. The Company does not believe it is possible to accurately estimate the number or size of its many competitors since the vitamin industry is largely privately held.

ITEM 1. BUSINESS (continued)

The Company believes that competition among vitamin and supplement products is based, among other things, on price, timely delivery, product quality, safety, availability, product innovation and assistance in marketing and customer service. The competitive position of the Company will also depend upon continued acceptance of its hard gel capsules, its ability to attract and retain qualified personnel, future governmental regulations affecting vitamins and nutritional supplements, and publication of vitamin product safety and efficacy studies by the government and authoritative health and medical authorities.

The Company's operations are subject to the risks normally associated with manufacturing vitamins and nutritional products, including shortage of certain raw materials and damage to property or injury to persons.

RAW MATERIALS

Raw materials used by the Company consist of nutrient powders, empty gelatin capsules, and necessary components for packaging and distribution of finished vitamin and nutritional supplement products. The nutrient powders and the empty gelatin capsules are purchased from manufacturers in the United States, including foreign-owned entities operating in the United States.

MAJOR CUSTOMERS

Nu Skin International and NSA International together represented 54% of the Company's sales for the year ended June 30, 1998. Loss of either of these customers could have an adverse impact on the Company's revenues and earnings until the Company could replace these sales. If the Company was unable to replace the sales to any of these customers, it would have a material adverse impact on the business and operations of the Company. No other customer represented 10% or more of the Company's sales for the year ended June 30, 1998.

EMPLOYEES

The Company employs 128 individuals, with three employed in executive or other professional positions, eight in the area of research, laboratory and quality control, eleven in sales and marketing, while the remaining employees are engaged in production and administration. The Company has never experienced a work stoppage, and none of its employees are currently represented by a union or any other form of collective bargaining unit. The Company believes its relations with its employees are excellent.

GOVERNMENT REGULATION

The processing, formulation, packaging, labeling and advertising of the Company's products are subject to regulation by one or more federal agencies, including the Federal Drug Administration (FDA), the Federal Trade Commission (FTC), the Consumer Product Safety Commission, the United States Department of Agriculture and the Environmental Protection Agency. These activities are also regulated by various agencies of the states and localities in which the Company's products are sold, including without limitation the California Department of Health Services, Food and Drug branch. The FDA in particular regulates the advertising, labeling and sales of vitamin and mineral supplements and may take regulatory action concerning medical claims, misleading or untruthful advertising, and product safety issues. While the Company is subject to the FDA's Good Manufacturing Practices for foods, and complies with them as a quality control practice, it also adheres to many of the FDA's more stringent standards for pharmaceutical manufacturing.

ITEM 2. PROPERTIES

The Company's corporate and manufacturing facilities consist of approximately 54,000 square feet and are located in San Marcos, California. Of this space, the Company owns approximately 36,000 square feet and leases the remaining space. In June 1996, the Company acquired certain suites within a building occupied by certain of its offices and production facilities which, up to that time, were being leased from its two principal stockholders, Marie A. LeDoux and Mark A. LeDoux. The lease provided for rent payable in the amount of $60,000 per year. Purchase price of the building was $545,000 which, in the opinion of management and an independent certified appraiser who evaluated the property in April 1996, represented fair market value.

In August 1997, the Company entered into a 15-year lease agreement under which the lessor is to construct a build-to-suit 82,000 square foot office and manufacturing facility in Carlsbad, California. The Company plans to move its administrative offices and expand its manufacturing capacity into these premises when the building is ready for occupancy in early 1999. Also, in August 1998, the Company entered into a 5-year lease agreement for the rental of a 54,000 warehousing facility located in Vista, California. The Company will continue to utilize its building in San Marcos for production.

ITEM 3. LEGAL PROCEEDINGS

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, based in part on the advice of counsel, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

On January 13, 1997, the Company's common stock began trading on the Nasdaq National Market tier of The Nasdaq Stock Market under the Symbol: NAII. The common stock of the Company had previously been traded on the American Stock Exchange (AMEX) since November 17, 1992, under the stock symbol NAI. The table below sets forth the high and low sales prices, which are derived from the Monthly Market Statistics issued by the American Stock Exchange and the Summary of Activity issued by The Nasdaq Stock Market for the respective periods.

	High	Low
First Quarter Ended September 30, 1997	$ 9.750	$ 7.000
Second Quarter Ended December 31, 1997	$ 10.813	$ 7.250
Third Quarter Ended March 31, 1998	$ 22.500	$ 17.625
Fourth Quarter Ended June 30, 1998	$ 24.500	$ 16.000
First Quarter Ended September 30, 1996	$ 10.375	$ 7.625
Second Quarter Ended December 31, 1996	$ 9.500	$ 7.125
Third Quarter Ended March 31, 1997	$ 10.500	$ 8.125
Fourth Quarter Ended June 30, 1997	$ 9.000	$ 6.875

As of June 30, 1998, the approximate number of holders of common stock was 4,000.

The Company has never paid a dividend on its common stock. It is the Company's present policy to retain all earnings to provide funds for the future growth of the Company.

PART II

ITEM 6. SELECTED FINANCIAL DATA

Five-Year Summary
(Not Covered by Independent Auditors' Report)

	YEAR ENDED JUNE 30				
	1998	1997	1996	1995	1994
Net sales	$67,894,305	$49,444,221	$47,621,804	$37,388,254	$34,334,062
Income from Operations	$ 9,622,478	$ 1,815,072	$ 5,263,376	$ 3,637,522	$ 3,592,951
Net Earnings	$ 5,871,765	$ 1,119,920	$ 3,222,317	$ 2,028,059	$ 1,887,367
Net Earnings Per Common Share(1):					

Basic	$ 1.06	$ 0.21	$ 0.61	$ 0.39	$ 0.39
Diluted	$ 1.00	$ 0.20	$ 0.58	$ 0.37	$ 0.35
Current Assets	$31,496,121	$18,857,979	$15,710,135	$14,722,929	$11,883,140
Total Assets	$42,987,279	$28,108,756	$23,561,191	$21,193,780	$17,514,511
Long-Term Debt and Capital Lease Obligations, less current installments	$ 977,375	$ 1,123,898	$ 1,324,920	$ 1,114,828	$ 958,415
Stockholders' Equity	$27,659,141	$18,699,487	$17,159,586	$13,278,255	$11,216,465

(1) amounts have been restated in accordance with SFAS 128.

PART II

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

FISCAL 1998 COMPARED TO FISCAL 1997

Net sales increased 37.3% or $18.5 million to $67.9 million in fiscal 1998. The Company added several new customers in the latter part of fiscal 1997 and sales to these and other new customers was the primary reason for the increase. A decrease in sales to certain existing customers was offset by increases in international sales to other existing customers through their international distribution channels.

Sales of products into international markets increased to $14.9 million in 1998 from $1.9 million in 1997. The increase is primarily the result of existing customers expanding into Asian and European markets.

Income from operations increased 430% to $9.6 million in 1998. This was due to a $8.3 million increase in gross profit offset by a $.5 million increase in selling, general and administrative expenses.

Gross profit margins were 27.6% and 21.1% in fiscal 1998 and 1997, respectively. The 1997 gross profit margin was substantially below historical margins because of factors that are discussed in the comparison of fiscal 1997 to 1996. The 1998 gross profit margin was slightly higher than historical margins experienced before 1997. The increase is principally due to negotiated raw material savings and improved manufacturing cost efficiencies.

Selling, general and administrative expenses decreased as a percentage of sales to 13.4% in 1998 from 17.4% in 1997, while increasing in absolute dollars to approximately $9.1 million in fiscal 1998 from $8.6 million in 1997. The majority of this increase in selling, general and administrative expenses is due to an increase in employee benefits expense which increased because the defined benefit pension plan adopted as of January 1, 1997 was in effect for a full year in 1998. Additionally, professional fees increased because of increased activity in the registration of foreign products. These increases in selling, general and administrative expenses were partially offset by a decline in bad debt expense, which was attributable to a related party customer write-off in fiscal 1997, and a decline in royalty expense because the Company's agreement with the United States Olympic Committee expired in March 1997.

Other income (expense) contributed to net other income approximately $44,000 in fiscal 1998 compared to a net other income contribution of approximately $25,000 in fiscal 1997.

Net earnings increased by 424% or $4.8 million to $5.9 million in fiscal 1998.

This increase was due primarily to the reasons given above and was partially offset by a higher effective income tax rate. The higher effective income tax rate, from 39.1% in 1997 to 39.3% in 1998, is the result of a smaller investment credit applicable to California franchise taxes.

Diluted earnings per share increased 400% to $1.00 per share in 1998 from $.20 per share in 1997.

The Company's backlog position amounted to $24,000,000 as of September 17, 1998, compared to $18,114,000 as of September 12, 1997. This increase is attributable to continued customer expansion into foreign markets and increased orders from existing customers.

PART II

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)

FISCAL 1997 COMPARED TO FISCAL 1996

Net sales increased 3.8% or $1.8 million to $49.4 million in fiscal 1997, primarily due to increased sales to existing customers. The Company added several new customers in the latter part of the year, however the sales to these new customers were not significant in fiscal 1997.

Sales to international customers declined from $4.3 million in 1996 to $1.9 million in 1997. The decrease is the result of a major client restructuring its European operations coupled with a declining demand for the same client's products in Europe.

Income from operations decreased 65.5% to $1.8 million. This was due to a $2.0 million decline in gross profit and a $1.4 million increase in selling, general and administrative expenses.

Gross profit margins were 21.1% and 26.1% in fiscal 1997 and 1996, respectively. The decline in gross margins is due to several factors. Shifts in product sales mix toward lower profit margin products, rising costs of certain raw materials, and increased costs for subcontracted packaging were the major contributing factors. To a lesser extent, the change in ownership of one of the Company's customers resulted in a substantial write-off of packaging materials. In addition, the Company wrote off raw materials that became obsolete because of customer discontinuance of certain products.

Selling, general and administrative expenses increased as a percentage of sales from 15.1% in 1996 to 17.4% in 1997. Selling, general and administrative expenses increased to $8.6 million in fiscal 1997 from $7.2 million in 1996. The increase in expenses was due to several factors: a specific provision for doubtful accounts was made for the balance due from a related party customer; the Company underwrote several clinical studies to show the efficacy of certain customer products; marketing fixtures related to certain unprofitable products were written off; and finally, the Company incurred startup expenses for its new tablet manufacturing facility.

Other income (expense) amounted to net other income of approximately $25,000 in fiscal 1997 compared to a net expense of approximately $56,000 in fiscal 1996. The net increase was primarily the result of increased interest income on investments.

Net earnings decreased 65.2% or $2.1 million to $1.1 million in fiscal 1997. This decrease was due, primarily, to the reasons given above. The higher effective income tax rate, from 38.1% in 1996 to 39.1% in 1997, is primarily the result of a smaller investment credit applicable to California franchise taxes.

Diluted earnings per common share decreased 65.5% to $.20 per share in 1997 from $.58 per share in 1996.

The Company's backlog position amounted to $18,114,000 as of September 12, 1997, compared to $12,465,000 as of September 16, 1996. This increase is attributable to successful customer expansion into foreign markets and increased orders from existing customers.

YEAR 2000 ISSUES

Most computer databases, as well as embedded microprocessors in computer systems and industrial equipment, have been programmed to use a two-digit number to represent the year. Computer programs that recognize a date using "00" as the year 1900 rather than the year 2000 could result in errors or system failures. Accordingly, all companies must analyze their systems and make the necessary changes to ensure that automated processes will correctly distinguish between years before and after the year 2000.

In the second quarter of its 1998 fiscal year, the Company decided to replace its financial and manufacturing software systems because these systems were not, in management's judgment, able to support the Company's continued growth and expansion. At this time, the Company also began to address its Year 2000 issues. The Company expects to implement its new computer systems by March 31, 1999 and the Company has begun an assessment of the potential for Year 2000 problems with embedded microprocessors in its production equipment.

The Company has received some preliminary information concerning the Year 2000 readiness of some of its vendors of goods and services. It expects to engage in discussions with its most significant vendors during the balance of 1998 and 1999 in an attempt to determine the extent to which the Company is vulnerable to those vendors' possible failure to become Year 2000 ready. If the Company's most significant vendors of goods and services, or the suppliers of the Company's necessary energy, telecommunications and transportation needs, fail to provide the Company with the materials and services which are necessary to produce, distribute and sell its products, such failure could have a material adverse effect on the results of operations, liquidity and financial condition of the Company.

The Company estimates that it will have incurred approximately $1 million in costs, of which approximately $100,000 will be charged to expense, by the end of its 1999 fiscal year to replace its financial and manufacturing software systems and to remediate or replace embedded microprocessors in its production equipment. This amount will be funded from internally generated cash flows.

If some or all of the Company's remediated or replaced internal computer systems fail to correctly distinguish between years before and after the year 2000, or if any software applications or embedded microprocessors critical to the Company's operations are overlooked in the assessment or implementation phases, there could be a material adverse effect on the Company's results of operations, liquidity and financial condition of a magnitude which the Company has not yet fully analyzed.

The Company has not yet established a contingency plan to address unavoided or unavoidable Year 2000 risks, but it expects to create such a plan during the balance of 1998 and 1999.

LIQUIDITY AND CAPITAL RESOURCES

Since its inception, the Company has satisfied its liquidity requirements through a combination of equity financing, net cash provided by operating activities, revolving lines of credit, equipment financing and leases. Management believes the Company's financial condition remains strong, and management also believes the Company will be able to obtain additional financing to provide the resources necessary to meet currently anticipated funding requirements.

At June 30, 1998, the Company had working capital of $18,308,000 and borrowings available under revolving lines of credit of $3,000,000. As of June 30, 1998, there were no borrowings under these lines.

In 1998, net cash provided by operating activities was $3,196,000 compared to $3,802,000 for 1997. This decrease of $606,000 was due primarily to increases in accounts receivable and inventories that was partially offset by increases in net earnings, tax benefit on option exercise, accounts payable and a decrease in tax refund receivable. Current maturities of long-term debt and capital leases amounted to $70,000 which the Company expects to pay out of working capital.

The Company has revolving lines of credit permitting borrowings up to $3,000,000, which are secured by the Company's receivables, inventory, equipment, and vehicles and bear interest at the bank's prime rate. The present loan agreement with the bank contains financial covenants concerning limitations on maintenance of debt, certain financial ratio's and other matters, for all of which the Company is in full compliance as of September 25, 1998. The lines of credit expire on January 19, 1999; management expects such lines to be renewed in the normal course of business.

Capital expenditures for 1998 amounted to $3,475,000 primarily in connection with the building improvements in progress at the Company's new headquarters building and the purchases of additional encapsulation and tablet compression equipment to expand the Company's output capacity. The Company anticipates capital expenditures of approximately $12,000,000 during fiscal 1999. These planned expenditures relate primarily to building improvements for the Company's new headquarters building, which is expected to be occupied in early 1999, and a warehouse and blending facility, which was leased in August 1998. These expenditures are expected to be paid from a combination of cash holdings, net cash provided by operating activities in fiscal 1999, borrowings under the Company's lines of credit with its bank, and anticipated long term debt or equity financing.

NEW ACCOUNTING PRONOUNCEMENTS

In February 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits." This Statement standardizes the disclosure requirements for pensions and other postretirement benefits, requires additional information on changes in the benefit obligations and fair values of plan assets and eliminates certain disclosures. Restatement of disclosures for earlier periods is required. The Company will adopt this Statement in its financial statements for the year ending June 30, 1999.

In June 1997, the FASB issued Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130") and No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131"). SFAS 130 establishes standards for the reporting and display of comprehensive income and its components in the financial statements. SFAS 131 establishes standards for the manner in which public business enterprises report information about operating segments and also establishes standards for related disclosures about products and services, geographic areas, and major customers. These statements are effective for years beginning after December 15, 1997. The Company does not expect that the adoption of SFAS Nos. 130, 131 and 132 will result in disclosures that will be materially different from those presently included in its financial statements.

PART II

ITEM 7a. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to risks relating to changes in interest rates and stock market fluctuations.

At June 30, 1998, the Company maintains a portion of its cash and cash equivalents in financial instruments with original maturities of three months or less. These financial instruments, principally comprised of government backed money market funds, are subject to interest rate risk and will decline in value if interest rates increase. The Company also maintains a short-term investment portfolio containing common stocks that are subject to market risk. The Company has not used derivative financial instruments in its investment portfolio.

PART II

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements and supplementary data as required by this item are set forth on pages 26 through 47.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The directors and executive officers of the Company (Registrant) are as follows:

Name and Position	Age as of June 30, 1998	Year of First Election	Family Relationship
Mark A. LeDoux Chief Executive Officer, Director	44	1986	Son to Chairperson of the Board, Marie A. LeDoux
William P. Spencer President, Treasurer, Chief Operating Officer, Chief Financial Officer, Chief Accounting Officer and Director	45	1986	None
Marie A. LeDoux Secretary, Chairperson of the Board	81	1986	Mother to Chief Executive Officer, Mark A. LeDoux
William R. Kellas Director	47	1988	None
Lee G. Weldon Director	59	1992	None

MARK A. LEDOUX was a director, the President and Chief Executive Officer of Natural Alternatives, Inc., the predecessor corporation, from its formation in 1981 until the 1986 merger into the Company. Mr. LeDoux has been a director and Chief Executive Officer of the Company since the August 1986 merger of the predecessor corporation into the Company, which continued the business and operations of Natural Alternatives, Inc. From August 1986 to December 1996, he also served as President of the Company. From 1976 to 1980, Mr. LeDoux held the position of Executive Vice President and Chief Operating Officer of Kovac Laboratories, a company, which was engaged in the business of manufacturing nutritional supplements. He attended the University of Oklahoma and graduated Cum Laude with a Bachelor of Arts in Letters in 1975. Mr. LeDoux graduated from Western State University, College of Law in 1979, with a Juris Doctorate.

WILLIAM P. SPENCER has been a director, Chief Operating Officer and Chief Financial Officer of the Company since August 1986. He also served as Executive Vice President until December 1996 when he became President of the Company. Prior to joining the Company, he was with San Diego Trust and Savings Bank for ten years, the last four as Vice President. Mr. Spencer received a Bachelor of Science in Finance in 1974, and a Masters in Business Administration, also in the area of Finance, in 1979 from San Diego State University.

(continued)

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT (continued)

MARIE A. LEDOUX has been a director of the Company since August 1986, and has also been Chairperson and Secretary since that time. Mrs. LeDoux was also the Chairperson/Advisor of the Company's predecessor from its formation until 1986. She has thirty-nine years of experience in the area of nutrition. In 1978, Mrs. LeDoux was awarded an Honorary Fellowship in the International Academy of Preventive Medicine. In 1981, she received an Honorary Ph.D. in Humanities from the Heritage Institute. Marie A. LeDoux is the mother of Mark A. LeDoux. For the last eighteen years, Mrs. LeDoux has been the President of Play N' Talk International, a company which is in the business of preparing instructional materials for children's reading programs.

WILLIAM R. KELLAS, Ph.D. became a director of the Company in October 1987. Mr. Kellas graduated from the University of Southern California earning a Bachelor of Science in Business with a Minor in Physics. He earned his Ph.D. in Health Sciences from the Doctors University of Natural Health Sciences in 1985. Dr. Kellas also graduated from Harvard University's Financial and Management Program. From 1974 to 1984, Dr. Kellas was employed by IBM as the firm's Western Regional Marketing Manager. From 1984 to 1985, Dr. Kellas was a District Manager for Wang Laboratories. In 1985, Dr. Kellas founded Comprehensive Health Centers, a medical clinic offering integrated medical, dental, chiropractic, and natural therapeutic services. In addition, Dr. Kellas is the President of Professional Preference, a biochemical firm that sells computerized regimens of protocols that are designed to regenerate an individual's immune system and fight related degenerative diseases.

LEE G. WELDON has been a director of the Company since June of 1992. He was the Chairman and Chief Executive Officer of Kal Healthway, Inc., a food supplement distributor, until it was acquired by another company during the past year. In 1963, Mr. Weldon graduated from UCLA and obtained a Bachelor of Science in Business Administration. In 1982, Mr. Weldon became a member of Young President's Organization (YPO), and since 1990 he has been a graduate member of YPO.

BOARD MEMBERS

Members of the Board of Directors are elected in three classes (Class I, Class II, and Class III) to serve initially until the 2000, 1998, and 1999 annual meetings of stockholders, respectively, and until the election and qualification of their successors. After the initial term of directors of each class terminates, at each regularly scheduled annual meeting of stockholders held to elect directors of that class, the number of directors equal to the number of directors of the class whose term expires at the time of such meeting shall be elected to hold office until the third succeeding annual meeting of stockholders. Directors receive $500 for each Directors' meeting attended in person. Mark A. LeDoux is the son of Marie A. LeDoux. Executive officers serve at the discretion of the Board of Directors. The classes of directors are as follows:

Director	Class
Mark A. LeDoux	I
Marie A. LeDoux, Lee G. Weldon	II
William R. Kellas, William P. Spencer	III

COMMITTEES

The Company currently has a Compensation Committee, composed of William R. Kellas and Lee G. Weldon. The Company's Audit Committee is comprised of William R. Kellas, Lee G. Weldon and William P. Spencer.

(continued)

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT (continued)

COMPLIANCE WITH SECTION 16(a) OF THE EXCHANGE ACT

Based solely on its review of the copies of Form 4's received by the Company, the Company believes that during its most recent fiscal year ended June 30, 1998, that its officers and directors complied with the filing requirements under Section 16(a).

ITEM 11. EXECUTIVE COMPENSATION

SUMMARY OF CASH AND OTHER COMPENSATION

The following table sets forth compensation for services rendered in all capacities to the Company during the years ended June 30, by each of the executive officers.

SUMMARY COMPENSATION TABLE

		Annual Compensation			
Name and Principal Position	Year	Salary	Bonus	Other(1)	All Other Compensation(2)
Mark A. LeDoux, Chief Executive Officer and Director	1998	208,000	304	40,270	27,842
	1997	201,579	50,345	28,422	18,703
	1996	213,520	45,300	8,592	21,987
William P. Spencer, President, Chief Financial Officer, and Director	1998	182,000	304	779,409	39,838
	1997	178,830	72,304	166,178	37,438
	1996	169,275	40,300	113,656	35,005

(1) Amounts do not exceed the lesser of $50,000 or 10% of salary and bonus combined for named executive, except as set forth in the following table.

(2) See following table.

(continued)

ITEM 11. EXECUTIVE COMPENSATION (continued)

SUMMARY OF CASH AND OTHER COMPENSATION (continued)

	Mark A. LeDoux	William P. Spencer
Other Annual Compensation-1998		
Gain from exercise and sale of stock options	$ --	$730,084
Personal Transportation	18,000	18,000
Other Personal Expenses	22,270	31,325
Totals	$40,270	$779,409
Other Annual Compensation-1997		
Gain from exercise and sale of stock options	$ --	$ 92,799
Personal Transportation	18,600	13,800
Other Personal Expenses	9,822	59,579

Totals	$28,422	$166,178
Other Annual Compensation-1996		
Gain from exercise and sale of stock options	$ --	$ 53,078
Personal Transportation	--	7,284
Other Personal Expenses	--	40,600
Tax Payment Reimbursements	--	12,694
Totals	$ 8,592	$113,656
All Other Compensation-1998		
401(k) Employer Contributions	$ 5,675	$ 7,647
Life Insurance and Disability Premiums	4,621	15,446
Medical, Dental and Vision	15,046	14,245
Board of Director Meetings	2,500	2,500
Totals	$27,842	$ 39,838
All Other Compensation-1997		
401(k) Employer Contributions	$ 5,550	$ 6,698
Life Insurance Premiums	1,920	13,990
Medical, Dental and Vision	10,233	15,750
Board of Director Meetings	1,000	1,000
Totals	$18,703	$ 37,438
All Other Compensation-1996		
401(k) Employer Contributions	$ 8,759	$ 10,974
Life Insurance Premiums	1,819	13,998
Medical, Dental and Vision	9,909	8,533
Board of Director Meetings	1,500	1,500
Totals	$21,987	$ 35,005

(continued)

PART III

ITEM 11. EXECUTIVE COMPENSATION (continued)

OPTION GRANTS

The following table contains information concerning the stock option grants to the Company's Chief Executive Officer and each of the other named executive officers that were made for the fiscal year ended June 30, 1998:

POTENTIAL VALUE OF OPTIONS GRANTED IN FISCAL 1998

	Shares Granted	% of Total options	Exercise Price	Expire Date	Potential at 5%	Potential at 10%
Mark A. LeDoux	30,000	10.00%	$10.50	January 21, 2003	$ 67,884	$146,192
William P. Spencer	110,000	36.67%	$10.50	January 21, 2003	$248,910	$536,036
All other	160,000	53.33%				
Total	300,000	100.00%				

(1) There is no assurance provided to any executive officer or any other holder of the Company's securities that the actual stock price appreciation over the five-year option term will be at the assumed 5% and 10% levels or at any other defined level. Unless the market price of the Company's common stock does in fact appreciate over the option term, no value will be realized from the option grants made to the executive

officers.

(2) The options granted to the named executives were granted under the Company's 1992 Incentive Stock Option Plan on January 21, 1998 at the fair market value price of $10.50. The following restrictions apply to the options granted: (a) The recipient must be employed with the Corporation on the date of exercise, (b) fifty percent of the granted options are exercisable on the date of grant, (c) the remaining fifty percent will become exercisable on January 21, 1999.

OPTION EXERCISES AND HOLDINGS

The following table sets forth information for the year ended June 30, 1998, concerning option exercises and option holdings under the 1992 Incentive Stock Option Plan, the 1992 Nonqualified Stock Option Plan, and the 1994 Nonqualified Stock Option Plan with respect to the Company's executive officers:

AGGREGATED OPTIONS/SAR EXERCISES IN LAST FISCAL YEAR
AND FISCAL YEAR-END OPTION/SAR VALUES

	Shares Acquired	Value Realized Market Price at Exercise less Exercise Price	Number of Unexercised Options/SAR's at Fiscal Year-End(#)		Value of Unexercised In-The Money Options/SAR's at Fiscal Year End(1)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
1992 Plans-						
Mark A. LeDoux	0	$ 0	90,000	0	$1,192,500	$0
William P. Spencer	68,000	$730,084	137,000	0	$1,453,375	$0
1994 Plan-						
Mark A. LeDoux	0	$ 0	100,000	0	$1,537,500	$0
William P. Spencer	0	$ 0	125,000	0	$1,921,875	$0

(1) The closing price of the Company's common stock at June 30, 1998, as quoted on the Nasdaq Exchange, was $20.00.

PART III

ITEM 11. EXECUTIVE COMPENSATION (continued)

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The members of the Company's Compensation Committee for fiscal 1998 were William R. Kellas and Lee G. Weldon. No current member of the Compensation Committee is a current or former officer or employee of the Company or its subsidiaries.

EMPLOYMENT AGREEMENTS

There were no employment agreements in effect at June 30, 1998.

BONUS PLAN

There were no bonus plans in effect at June 30, 1998.

401(k) PLAN

The NATURAL ALTERNATIVES Partnership for Profits Plan (Plan) is considered a qualified plan under Section 401(k) of the Internal Revenue Code. All employees of the Company with twelve (12) months and at least one thousand hours of service during the twelve month period are eligible to participate in the Plan. The Plan provides for employee contributions of up to 15% of compensation. Employer contributions are determined by the Board of Directors at their discretion. The Company may match up to 100% of each employee's contribution, which does not exceed 5% of the employee's total compensation. Employee contributions in the Plan are 100% vested. Participants become vested in employer contributions at the rate of 34% the first year, 67% the second year and 100% after three years. The Company contributed and expensed $146,277, $114,206, and $101,161 in 1998, 1997 and 1996, respectively.

STOCK OPTION PLANS

The Company maintains three stock option plans: the 1992 Incentive Stock Option Plan (Incentive Plan) and the 1992 Nonqualified Stock Option Plan (1992 Nonqualified Plan), both of which were approved by the shareholders of the Company at its Annual Meeting of Shareholders on June 5, 1992, and the 1994 Nonqualified Stock Option Plan (1994 Nonqualified Plan) which was approved by the Board of Directors on December 9, 1994, and by the shareholders of the Company at its Annual Meeting of Shareholders on May 10, 1996.

The Incentive Plan provides for the granting of "incentive stock options" as described in Section 422 of the Internal Revenue Code (Code). The 1992 and 1994 Nonqualified Plans provide for the granting of nonqualified stock options which are not intended to qualify under any provision of the Code.

On September 9, 1993, all options then authorized under the Incentive Plan and 1992 Nonqualified Plan were granted with exercise prices equal to the fair market value price of $4.875 per share. On December 9, 1994, the Shareholders approved an amendment to the Incentive Plan, increasing the number of common shares that may be granted from 200,000 to 500,000. On January 24, 1995, options for 500,000 shares under the 1994 Plan were granted at the fair market value of $4.625 per share. On January 21, 1998, options for 300,000 shares under the Incentive Plan were granted at the fair market value of $10.50 per share.

(continued)

PART III

ITEM 11. EXECUTIVE COMPENSATION (continued)

STOCK OPTION PLANS (continued)

Incentive Plan

The purpose of the Incentive Plan is to promote the interests of the Company by providing a method whereby key management personnel of the Company and its subsidiaries responsible for the management, growth and financial success of the Company may be offered incentives to encourage them to acquire a proprietary interest or to increase their proprietary interest in the Company, and to remain in the employ of the Company and its subsidiaries. The total number of shares issuable under the Incentive Plan may not exceed 500,000 shares, subject to certain adjustments.

The Incentive Plan is to be administered by either the Board of Directors (Board) or the Company's Compensation Committee. Subject to the express provisions of the Incentive Plan, the Board or the Compensation Committee will have complete authority to determine the employees to whom, and the times at which options are to be granted, the number of shares to be subject to each option, the option term, and all other terms and conditions of an option. The Board or the Compensation Committee will also have the authority to interpret the provisions in the Incentive Plan and to prescribe rules and regulations for its orderly administration.

The exercise price of incentive stock options granted under the Incentive Plan may not be less than 100% of the fair market value of the Common Stock on the date of the option grant. With respect to any key employee who owns stock representing more than 10% of the voting power of the outstanding capital stock of the Company, the exercise price of any incentive stock option may not be less than 110% of the fair market value of such shares at the time of grant and the term of such option may not exceed five years. Each option granted under the Incentive Plan will be exercisable at such time or times, during such period, and for such number of shares as is determined by the Board or the Compensation Committee and set forth in the instrument evidencing the option. No option granted under the Incentive Plan shall have a term in excess of ten years from the date of grant.

During the lifetime of the optionee, the option will be exercisable only by the optionee and may not be assigned or transferred by the optionee other than by will or the laws of descent or distribution. Should an optionee cease to be an employee of the Company or its subsidiaries for any reason other than death, then any outstanding option granted under the Incentive Plan will be exercisable by the optionee only during the three month period following cessation of employee status, and only to the extent of the number of shares for which the option is exercisable at the time of such cessation of employee status.

If the Company or its shareholders enter into an agreement to dispose of all or substantially all of the assets or outstanding capital stock of the Company by sale, merger, reorganization or liquidation, each option outstanding will become exercisable during the 15 days immediately prior to the scheduled consummation of such sale, merger, reorganization or liquidation with respect to the full number of shares of the Company's Common Stock purchasable under such option, unless the successor corporation or parent assumes or replaces the outstanding options.

In the event any change is made to the outstanding shares of the Company's Common Stock without the receipt of consideration by the Company, then unless such change results in the termination of all outstanding options, appropriate adjustments will be made to the maximum number of shares issuable under the Incentive Plan and to the number of shares and the option price per share of the stock subject to each outstanding option.

(continued)

PART III

ITEM 11. EXECUTIVE COMPENSATION (continued)

STOCK OPTION PLANS (continued)

1992 and 1994 Nonqualified Plans

The purpose of the 1992 and 1994 Nonqualified Plans (the Nonqualified Plans) is to provide an incentive to eligible employees, consultants and officers whose present and potential contributions are important to the continued success of the Company, to afford those individuals the opportunity to acquire a proprietary interest in the Company and to enable the Company to enlist and retain in its employment qualified personnel for the successful conduct of its business. Officers, consultants and other employees of the Company and its subsidiaries whom the administrators deem to have the potential to contribute to the success of the Company shall be eligible to receive options under the Nonqualified Plans.

The administrators of the Nonqualified Plans shall be either the Board of the Company or a committee designated by the Board. The administrators have full power to select, from among the officers, employees and consultants of the Company eligible for options, the individuals to whom options will be granted, and to determine the specific terms of each grant, subject to the provisions of the Nonqualified Plans.

The exercise price for each share covered by the Nonqualified Plans will be determined by the administrators, but will not be less than 60% and 100% for the 1992 Nonqualified Plan and the 1994 Nonqualified Plan, respectively, of the fair market value of a share of Common Stock of the Company on the date of grant of such option. The term of each option will be fixed by the administrators of the Nonqualified Plans. In addition, the administrators will determine the time or times each option may be exercised. Options may be exercisable in installments, and the exercisability of options may be accelerated by the administrators.

Options granted pursuant to the Nonqualified Plans are nontransferable by their participants, other than by will or by the laws of descent or distribution, and may be exercised during the lifetime of the participant only by the participant. In the event of an optionee's termination of employment or consulting relationship for any reason other than death or total and permanent disability, an option may be thereafter exercised, to the extent it was exercisable at the date of such termination, for such period of time as the administrator shall determine at the time of grant, but only to the extent that the term of the option has not expired.

Subject to the Nonqualified Plans' change in control provisions, in the event of the sale of substantially all of the assets of the Company or the merger of the Company with or into another corporation, each outstanding option shall be assumed or substituted by such successor corporation or parent or subsidiary of such successor corporation. The Nonqualified Plans also provide that in the event of a change of control of the Company, certain acceleration and valuation provisions shall apply, except as otherwise determined by the Board at its discretion prior to the change of control.

In the event of any change in capitalization in the Company which results in an increase or decrease in the number of outstanding shares of Common Stock without receipt of consideration by the Company, an appropriate adjustment shall be made in the number of shares which have been reserved for issuance under the Nonqualified Plans and the price per share covered by each outstanding option.

DEFINED BENEFIT PENSION PLAN

Effective January 1, 1997, the Company adopted a defined benefit pension plan (the "Plan") covering substantially all of its employees. The benefits are based on years of service and the employee's compensation during the five years before retirement. The Company expects to make annual contributions to the Plan equal to the maximum amount that can be deducted for income tax purposes. For the year ended June 30, 1998, the estimated current service cost (normal cost) and the amortized portion of the unfunded estimated accrued liability for prior service cost, using a 30-year funding period, amounted to $404,614. This amount has been accrued in the current period.

PART III

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth, as far as is known to the Board of Directors or management of the Company, as of September 24, 1998, the stock ownership of each person known by the Company to be the beneficial owner of 5% or more of the Company's Common Stock, all Directors individually, all Directors and Officers as a group and by the individuals listed under the summary compensation table.

Directors and Officers

Title of Class	Name and Address of Beneficial Owner	Amounts and Nature of Beneficial Ownership (1)(2)	Percent of Class(2)
Common Stock	Marie A. LeDoux (3) 1185 Linda Vista Drive San Marcos CA 92069	1,012,301	15.96%
Common Stock	Mark A. LeDoux (4) 1185 Linda Vista Drive San Marcos CA 92069	412,417	6.50%
Common Stock	William R. Kellas (5) 1185 Linda Vista Drive San Marcos CA 92069	29,500	.47%
Common Stock	William P. Spencer (6) 1185 Linda Vista Drive San Marcos CA 92069	139,792	2.20%
Common Stock	Lee G. Weldon 1185 Linda Vista Drive San Marcos CA 92069	43,880	.69%
Common Stock	All Directors and Officers as a Group (5 persons)	1,637,890	25.82%

(continued)

PART III

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT (continued)

(1) Except as indicated in the footnotes to this table and pursuant to applicable community property laws, to the Company's knowledge, the persons named in the table have sole voting and investment power with respect to all shares of Common Stock.

(2) Shares of common stock which were not outstanding but which could be acquired upon exercise of an option within 60 days from the date of this filing are considered outstanding for the purpose of computing the percentage of outstanding shares beneficially owned. However, such shares are not considered to be outstanding for any other purpose.

(3) Includes 10,000 shares, which Mrs. LeDoux has the right to acquire upon exercise of options exercisable within 60 days of the date of this filing.

(4) Includes 800 shares of common stock held in the name of Mr. LeDoux's wife, Julie LeDoux, and 8,000 shares of common stock held as custodian for his children and a niece. Also includes 100,000 shares, which Mr. LeDoux has the right to acquire upon exercise of options exercisable within 60 days of the date of this filing.

(5) Includes 1,500 shares of common stock held in the name of Mr. Kellas' wife.

(6) Includes 2,400 shares of common stock held as custodian for Mr. Spencer's children and 125,000 shares, which he has the right to acquire upon exercise of options exercisable within 60 days of the date of this filing.

There is no arrangement known to the Company, the operation of which may at a subsequent date, result in a change of control of the Company.

PART III

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

In June 1996, the Company acquired a portion of a building occupied by certain of its offices and production facilities which, up to that time, were being leased from its two principal stockholders, Marie A. LeDoux and Mark A. LeDoux. The lease provided for rent payable in the amount of $60,000 per year. The purchase price of the building was $545,000 which, in the opinion of management and an independent certified appraiser who evaluated the property in April 1996, represented fair market value.

The Company entered into an agreement with the father-in-law and mother-in-law of the Chief Executive Officer of the Company in December 1991, which provides commissions on sales to a particular customer. The term of the agreement is ten years and will expire in December 2001. The commission equals 5% of sales, with earnings capped at $25,000 per calendar quarter. Amounts paid under this agreement were $100,000 for each of the years ending June 30, 1998, 1997 and 1996. There were no amounts owed under the agreement at June 30, 1998 or 1997.

Included in notes receivable are notes from the Company's Chief Executive Officer and President. The balance of the notes, including accrued interest, was $79,036 and $95,365, respectively, as of June 30, 1998 and $74,444 and $89,824, respectively, at June 30, 1997.

Additionally, during the year ended June 30, 1998, the Company made noninterest-bearing loans to the Chairman of the Board and the President in the amount of $50,000 and $13,803, respectively, bringing the aggregate amount of such loans to $282,815. Amounts owed on these loans, which are secured by proceeds from life insurance policies on their respective lives, were $200,000 and $150,000 for the Chairman of the Board and $82,815 and $69,012 for the President at June 30, 1998 and 1997, respectively.

The Company paid commissions during the year ended June 30, 1996 in the amount of $6,916 to the Chairman of the Board.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

(a) 1. FINANCIAL STATEMENTS

The financial statements listed in the accompanying index to consolidated financial statements are filed as part of this report.

2. FINANCIAL STATEMENT SCHEDULES

The financial statement schedule listed in the accompanying index to the consolidated financial statements is filed as part of this annual report. Schedules not included have been omitted because they are not applicable or the information required is included in the financial statements and notes thereto.

(b) EXHIBITS

Exhibit 23 Re: Consent of KPMG Peat Marwick LLP
Exhibit 27 Financial Data Schedule

(c) REPORTS FORM 8-K

Not Applicable

NATURAL ALTERNATIVES INTERNATIONAL, INC. AND SUBSIDIARIES
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULE
JUNE 30, 1998

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Stockholders
NATURAL ALTERNATIVES INTERNATIONAL, INC.:

We have audited the consolidated financial statements of Natural Alternatives International, Inc. and subsidiaries as listed in the accompanying index. In connection with our audits of the consolidated financial statements, we have also audited the financial statement schedule as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Natural Alternatives International, Inc. and subsidiaries as of June 30, 1998 and 1997, and the results of their operations and their cash flows for each of the years in the three-year period ended June 30, 1998, in conformity with generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG Peat Marwick LLP

San Diego, California
September 8, 1998

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS
JUNE 30, 1998 AND 1997

ASSETS

	1998	1997
Current Assets:		
Cash and cash equivalents	$ 4,714,212	$ 3,469,739
Accounts receivable - less allowance for doubtful accounts of $1,073,000 at June 30, 1998 and $1,006,000 at June 30, 1997 (Notes E, F, and L)	12,558,731	6,990,121
Inventories (Notes B, E, and F)	11,504,936	5,690,850
Tax refund receivable	--	842,209
Notes receivable - current portion (Note K)	399,307	235,613
Prepaid expenses	594,054	404,899
Deferred income taxes (Note H)	854,000	851,000
Deposits	641,573	322,269
Other current assets	229,308	51,279
Total Current Assets	31,496,121	18,857,979
Property and equipment, net (Notes C, E, F, G, and K)	10,531,865	8,259,705
Other Assets:		
Investments (Note D)	61,971	58,862
Notes receivable, less current portion (Note K)	160,273	261,697
Other noncurrent assets, net	737,049	670,513
Total Other Assets	959,293	991,072
TOTAL ASSETS	$42,987,279	$28,108,756

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS (continued)

JUNE 30, 1998 AND 1997

LIABILITIES AND STOCKHOLDERS' EQUITY

	1998	1997
Current Liabilities:		
Accounts payable	$ 12,301,859	$ 6,824,198
Current installments of long-term debt (Note F)	46,501	164,266
Current installments of capital lease obligation (Note G)	23,542	25,189
Income taxes payable (Note H)	378,055	--
Accrued compensation and employee benefits	438,242	321,337
Total Current Liabilities	13,188,199	7,334,990
Deferred income taxes (Note H)	500,000	487,000
Long-term debt, less current installments (Note F)	977,375	1,100,285
Long-term pension liability (Note I)	662,564	463,381
Capital lease obligations, less current installments (Note G)	--	23,613
Total Liabilities	$ 15,328,138	$ 9,409,269
Stockholders' Equity (Note J):		
Preferred stock; $.01 par value; 500,000 shares authorized; none issued or outstanding		
Common stock; $.01 par value; 8,000,000 shares authorized; issued and outstanding 5,768,209 at June 30, 1998 and 5,429,764 at June 30, 1997	57,682	54,298
Additional paid-in capital	9,756,822	6,675,426
Retained earnings	17,892,778	12,021,013
Net unrealized losses on investments (Note D)	(48,141)	(51,250)
Total Stockholders' Equity	$ 27,659,141	$ 18,699,487
Commitments and contingencies (Notes K, L and M)		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 42,987,279	$ 28,108,756

See accompanying notes to consolidated financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF EARNINGS
FOR THE YEARS ENDED JUNE 30, 1998, 1997, AND 1996

	1998	1997	1996
Net sales	$ 67,894,305	$ 49,444,221	$ 47,621,804
Cost of goods sold	49,157,717	39,019,224	35,182,059
GROSS PROFIT	18,736,588	10,424,997	12,439,745
Selling, general & administrative expenses	9,114,110	8,609,925	7,176,369
INCOME FROM OPERATIONS	9,622,478	1,815,072	5,263,376
Other income (expense):			
Interest income	194,781	163,368	92,926
Interest expense	(110,337)	(147,373)	(190,850)
Other, net	(40,157)	8,853	41,865
	44,287	24,848	(56,059)

EARNINGS BEFORE INCOME TAXES	9,666,765	1,839,920	5,207,317
Income taxes (Note H)	3,795,000	720,000	1,985,000
NET EARNINGS	$ 5,871,765	$ 1,119,920	$ 3,222,317
NET EARNINGS PER COMMON SHARE:			
Basic	$ 1.06	$ 0.21	$ 0.61
Diluted	$ 1.00	$ 0.20	$ 0.58

See accompanying notes to consolidated financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED JUNE 30, 1998, 1997, AND 1996

	COMMON STOCK		ADDITIONAL		NET UNREALIZED GAINS	
	SHARES	AMOUNT	PAID-IN CAPITAL	RETAINED EARNINGS	(LOSSES) ON INVESTMENTS	TOTAL
Balance, June 30,1995	5,257,875	$52,579	$5,586,759	$ 7,678,776	$(39,859)	$ 13,278,255
Issuance of common stock upon exercise of employee stock options	94,000	940	454,662	--	--	455,602
Income tax benefit from stock options exercised	--	--	178,775	--	--	178,775
Net unrealized gains on investments	--	--	--	--	24,637	24,637
Net earnings	--	--	--	3,222,317	--	3,222,317
Balance, June 30, 1996	5,351,875	53,519	6,220,196	10,901,093	(15,222)	17,159,586
Issuance of common stock upon exercise of employee stock options	77,889	779	369,630	--	--	370,409
Income tax benefit from stock options exercised	--	--	85,600	--	--	85,600
Net unrealized loss on investments	--	--	--	--	(36,028)	(36,028)
Net earnings	--	--	--	1,119,920	--	1,119,920
Balance, June 30, 1997	5,429,764	54,298	6,675,426	12,021,013	(51,250)	18,699,487
Issuance of common stock upon exercise of employee stock options	338,445	3,384	1,646,202	--	--	1,649,586
Income tax benefit from stock options exercised	--	--	1,435,194	--	--	1,435,194
Net unrealized gains on investments	--	--	--	--	3,109	3,109
Net earnings	--	--	--	5,871,765	--	5,871,765
Balance, June 30, 1998	5,768,209	$57,682	$9,756,822	$17,892,778	$(48,141)	$ 27,659,141

See accompanying notes to consolidated financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 1998, 1997, AND 1996

	1998	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net earnings	$ 5,871,765	$ 1,119,920	$ 3,222,317
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Bad debt provision	360,000	725,000	391,162
Tax benefit on option exercise	1,435,194	85,600	178,775
Depreciation and amortization	1,515,402	1,276,355	1,069,460
Provision for deferred income taxes	10,000	(296,000)	(27,000)
Pension expense, net of contributions	88,839	158,560	--
Loss on disposal of assets	54,727	3,601	11,038
Gain on investments	--	--	(48,020)
Other	(36,808)	(18,105)	(32,005)
Changes in operating assets and liabilities:			
(Increase) decrease in:			
Accounts receivable	(6,028,610)	(1,747,544)	(686,338)
Inventories	(5,814,086)	708,742	(1,170,007)
Prepaid expenses	(189,155)	107,812	(50,002)
Deposits	(319,304)	(221,756)	25,710
Tax refund receivable	842,209	(842,209)	--
Other assets	(134,221)	438,037	37,329
(Decrease) increase in:			
Accounts payable	5,044,941	2,785,720	(1,325,016)
Accrued compensation and employee benefits	116,905	40,997	(248,364)
Income taxes payable	378,055	(520,246)	(217,829)
Customer deposits	--	(2,606)	(27,801)
Net Cash Provided by Operating Activities	3,195,853	3,801,878	1,103,409

(continued)

NATURAL ALTERNATIVES INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
FOR THE YEARS ENDED JUNE 30, 1998, 1997, AND 1996

	1998	1997	1996
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of property and equipment	$ 65,000	$ 10,000	$ 55,337
Proceeds from sale of investments	--	--	64,108
Capital expenditures	(3,474,569)	(2,236,165)	(2,064,524)
Capital expenditure-related party	--	--	(545,000)
Investment purchases	--	(20,000)	(16,088)
Issuance of notes receivable	(4,625)	(183,909)	(60,605)
Repayment of notes receivable	79,163	109,262	135,259
Net Cash Used in Investing Activities	(3,335,031)	(2,320,812)	(2,431,513)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Borrowings on lines of credit	--	443,959	--
Payments on lines of credit	--	(443,959)	--
Payments on long-term debt and capital leases	(265,935)	(269,163)	(311,910)
Proceeds from long-term debt financing	--	--	545,000
Issuance of common stock	1,649,586	370,409	455,602
Net Cash Provided by Financing Activities	1,383,651	101,246	688,692
Net Increase (Decrease) in Cash and Cash Equivalents	1,244,473	1,582,312	(639,412)
Cash and Cash Equivalents at Beginning of Period	3,469,739	1,887,427	2,526,839
Cash and Cash Equivalents at End of Period	$ 4,714,212	$ 3,469,739	$ 1,887,427
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Interest	$ 99,602	$ 147,373	$ 190,850
Income Taxes	1,494,000	2,289,959	2,052,000
Disclosure of non-cash activities:			
Notes payable refinanced with new debt	$ 0	$ 0	$ 565,000
Net unrealized gains (losses) on investments	3,109	(36,028)	24,637
Fixed asset purchases in accounts payable	432,720	--	--
Issuance of note receivable for payment of account receivable	100,000	--	--
Write-off of notes receivable through the allowance for doubtful accounts	--	15,504	62,790

See accompanying notes to consolidated financial statements.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Natural Alternatives International, Inc., (the Company) manufactures vitamins, micronutrients and related nutritional supplements, and provides innovative private-label products for specialized corporate, institutional and commercial accounts worldwide. The Company operates as a single business segment.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries: Millennium Health International, Inc. (formerly Pro-Lean, Inc. and prior to that Sonergy, Inc.), CellLife International, Inc. and CellLife Pharmaceuticals International, Inc., all of which had been administered and operated out of the Company's facilities. During fiscal 1997, the assets and liabilities of each of the subsidiaries were transferred to the Company and their operations were assumed by the Company. All significant intercompany accounts and transactions through the date of transfer have been eliminated.

Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and cash equivalents include highly liquid investments purchased with an original maturity of three months or less.

Inventories

Inventories are recorded at the lower of cost (first-in, first-out) or market (net realizable value). Such costs include raw materials, labor and production overhead.

Property and Equipment

Property and equipment are stated at cost. Property and equipment under capital leases are recorded at the lower of fair market value or the present value of future minimum lease payments and are amortized using the straight-line method over the shorter of the estimated useful life of the asset or the lease term. Depreciation of property and equipment is provided using the straight-line method over their estimated useful lives, generally ranging from 3 to 39 years. Leasehold improvements are amortized using the straight-line method over the shorter of the life of the improvement or the remaining term of the lease.

Impairment of Long-Lived Assets

The Company accounts for its long-lived assets in accordance with SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of. This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceed the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(continued)

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments

The Company accounts for its investments in accordance with Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities." The Company's investments, which consist of equity securities, are classified as available for sale and are carried at fair value, with unrealized gains and losses excluded from earnings and reported as a separate component of stockholders' equity.

Revenue Recognition

Revenue is recognized when products are shipped and title has transferred.

Marketing Costs

In order to attract and retain its customer base, the Company provides a wide range of marketing services to its customers. The Company does not generate fees or revenues from these services and the related costs are expensed as incurred.

Income Taxes

The Company accounts for income taxes using the asset and liability method in accordance with Statement of Financial Accounting Standards No. 109 "Accounting for Income Taxes." Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Stock Option Plans

Prior to July 1, 1996, the Company accounted for its stock option plans in accordance with the provisions of Accounting Principles Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. As such, compensation expense would be recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. On July 1, 1996, the Company adopted SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), which permits entities to recognize as expense over the vesting period the fair value of all stock-based awards on the date of grant. Alternatively, SFAS No. 123 also allows entities to continue to apply the provisions of APB Opinion No. 25 and provide pro forma net earnings and pro forma net earnings per share disclosures for employee stock option grants made in fiscal 1996 and future years as if the fair-value-based method defined in SFAS No. 123 had been applied. The Company has elected to continue to apply the provisions of APB Opinion No. 25 and provide the pro forma disclosures required by SFAS No. 123.

Fair Value of Financial Instruments

Because of their short maturities, the carrying amounts for cash and cash equivalents, accounts receivable, notes receivable, investments, accounts payable, and accrued compensation and employee benefits approximate fair value. The carrying amounts for long-term debt approximate fair value as the interest rates and terms are substantially similar to rates and terms that could be obtained currently for similar instruments.

(continued)

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of Estimates

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities, revenue and expenses, and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

Net Earnings per Share

In 1998, the Company adopted Statement of Financial Accounting Standards No. 128, "Earnings Per Share" ("SFAS 128"). SFAS 128 requires the presentation of basic earnings per share, computed using the weighted average number of shares outstanding during the period, and diluted earning per share, computed using the additional dilutive effect of all dilutive securities. The dilutive impact of stock options and warrants account for the additional weighted average shares of common stock outstanding for the Company's diluted earnings per share computation. All prior periods have been restated to conform with the provisions of SFAS 128. Basic and diluted earnings per share have been calculated as follows:

For the Years Ended June 30, 1998, 1997, and 1996

	1998	1997	1996
NUMERATOR:			
Net earnings - Numerator for basic and diluted earnings per share income available to common shareholders	$5,871,765	$1,119,920	$3,222,317
DENOMINATOR:			
Denominator for basic earnings per share - weighted average shares	5,544,337	5,395,438	5,290,187
Effect of dilutive securities - employee stock options	322,303	197,638	310,595
Denominator for diluted earnings per share - adjusted weighted average shares and assumed conversions	5,866,640	5,593,076	5,600,782
Basic earnings per share	$ 1.06	$ 0.21	$ 0.61
Diluted earnings per share	$ 1.00	$ 0.20	$ 0.58

(continued)

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Concentrations of Credit Risk

Financial instruments that subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company places its cash and cash equivalent investments with high credit qualified financial institutions. Credit risk with respect to receivables is concentrated with the Company's two largest customers (see Note L). These two customers' receivable balances collectively represent 34% and 31% of total accounts receivable at June 30, 1998 and 1997, respectively. Concentrations of credit risk related to the remaining accounts receivable balance are limited due to the large number of customers comprising the Company's remaining customer base and their dispersion across many different industries and geographies.

Reclassifications

Certain amounts in prior years' consolidated financial statements have been reclassified to conform to the 1998 presentation.

B. INVENTORIES

Inventories are comprised of the following at June 30:

	1998	1997
Raw materials	$ 7,049,954	$2,747,451
Work in progress	3,971,315	2,598,430
Finished goods	483,667	344,969
	$11,504,936	$5,690,850

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

C. PROPERTY AND EQUIPMENT

The following is a summary of property and equipment at June 30:

	Life Used For Depreciation	1998	1997
Land	NA	$392,600	$392,600
Building and building improvements	5 - 39 years	3,140,655	3,124,691
Machinery and equipment	3 - 15 years	10,077,375	7,649,609
Office equipment and furniture	5 to 7 years	2,304,243	2,103,479
Equipment under capital leases	5 Years	516,362	516,362
Vehicles	3 years	42,684	49,534
Leasehold improvements	5 to 39 years	1,274,076	268,968
Total property and equipment		17,747,995	14,105,243
Less accumulated depreciation and amortization		(7,216,130)	(5,845,538)
Property and equipment, net		$10,531,865	$ 8,259,705

At June 30, 1998 and 1997, accumulated depreciation and amortization includes $477,532 and $452,343, respectively, of amortization of equipment under capital leases.

D. INVESTMENTS

Investments consist of marketable securities. Securities held at June 30, 1998 and 1997 are considered "available for sale securities." Securities are valued at $61,971 and $58,862 as of June 30, 1998 and 1997. The security portfolio includes gross unrealized losses, net of tax, of $48,141 and $51,250 at June 30, 1998 and 1997.

E. LINE OF CREDIT AGREEMENTS

The Company has revolving lines of credit agreements permitting borrowings up to $3,000,000, which are secured by the Company's receivables, inventories, equipment, and vehicles and bear interest at the bank's prime rate, which was 8.50% at June 30, 1998. Advances against the revolving lines of credit cannot exceed 70% of eligible receivables. These agreements contain financial covenants concerning limitations on maintenance of debt, certain financial ratios and other matters. The lines of credit expire on January 19, 1999; management expects such lines to be renewed in the normal course of business. There were no amounts outstanding under these credit agreements at June 30, 1998 and 1997, respectively.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

F. LONG-TERM DEBT

Long-term debt consisted of the following as of June 30:

	1998	1997
Note payable to bank, secured by building, interest at 8.25%, principal and interest payments of $10,769 monthly, due 2011	$ 1,023,876	$ 1,066,644
Note payable to bank, repaid in November 1997	--	197,907
	1,023,876	1,264,551
Less current installments	(46,501)	(164,266)
Long-term debt, less current installments	$ 977,375	$ 1,100,285

Aggregate amounts of long-term debt maturities as of June 30, 1998 are as follows:

1999	$ 46,501
2000	50,531
2001	54,812
2002	59,509
2003	64,608
Thereafter	747,915
	$1,023,876

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

G. CAPITAL LEASE OBLIGATION

The Company leases certain equipment under a capital lease, which expires in fiscal year 1999. The present value of the future minimum capital lease payments as of June 30 are as follows:

	1998	1997
Capital lease payable to AT&T Credit Corporation, secured by phone system, interest at 13%, principal and interest in monthly installments of $2,504 through May 1999	$ 24,964	$ 55,078

Less amount representing interest	(1,422)	(6,276)
Present value of net minimum lease payments	23,542	48,802
Less current installments	(23,542)	(25,189)
Capital lease obligations - less current installments	$ --	$ 23,613

H. INCOME TAXES

Income taxes for the year ended June 30 consist of the following:

	1998	1997	1996
Current:			
Federal	$ 3,104,000	$ 850,000	$ 1,712,000
State	681,000	166,000	300,000
	3,785,000	1,016,000	2,012,000
Deferred:			
Federal	8,500	(215,000)	(15,000)
State	1,500	(81,000)	(12,000)
	10,000	(296,000)	(27,000)
Income taxes	$ 3,795,000	$ 720,000	$ 1,985,000

The provision (benefits) for deferred income taxes for the year ended June 30 consists of the following:

	1998	1997	1996
Accelerated depreciation and amortization for tax purposes	13,000	95,000	78,000
Increase in valuation allowance	--	2,000	--
Accrued compensation	--	--	108,000
Inventory valuation reserve	(24,000)	(131,000)	(202,000)
Bad debt expense	238,000	(309,000)	(41,000)
Accrued vacation expense	1,000	(15,000)	(6,000)
Customer deposits	--	(1,000)	11,000
State income taxes	(207,000)	63,000	48,000
Other, net	(11,000)	--	(23,000)
	10,000	(296,000)	(27,000)

H. INCOME TAXES (continued)

Net deferred tax assets and deferred tax liabilities as of June 30 are as follows:

	1998	1997
Deferred tax assets:		
Allowance for doubtful accounts	198,000	436,000
Accrued vacation expense	53,000	54,000
Investment loss carryforward	36,000	36,000
State income taxes	232,000	25,000
Allowance for inventory valuation	357,000	333,000
Other, net	14,000	3,000
Total gross deferred tax assets	890,000	887,000
Less valuation allowance	36,000	36,000
Net deferred tax assets	854,000	851,000
Deferred tax liabilities:		
Accumulated depreciation and amortization	500,000	487,000
Net deferred tax asset	354,000	364,000

The valuation allowance for deferred tax assets was $36,000 at June 30, 1998 and 1997. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Management considers, among other things, the scheduled reversal of deferred tax liabilities, projected future taxable income, and other planning strategies. In making this assessment, management believes it is more likely than not that the Company will realize the benefit of the deferred tax asset, net of the existing valuation allowance, at June 30, 1998.

(continued)

H. INCOME TAXES (continued)

A reconciliation of income taxes computed by applying the statutory federal income tax rate of 34% to earnings before income taxes for the year ended June 30 is as follows:

	1998	1997	1996
Income taxes computed at statutory federal income tax rate	$3,286,700	$626,000	$1,770,000
State income taxes, net of federal income tax benefit	451,000	56,000	190,000
Increase in valuation allowance	--	2,000	--
Expenses not deductible for tax purposes	35,000	31,000	22,000
Other	22,300	5,000	3,000
Income taxes as reported	$3,795,000	$720,000	$1,985,000
Effective tax rate	39.3%	39.1%	38.1%

I. EMPLOYEE BENEFIT PLANS

The Company has a profit sharing plan pursuant to Section 401(k) of the Internal Revenue Code, whereby participants may contribute a percentage of compensation, but not in excess of the maximum allowed under the Code. All employees with twelve months and at least one thousand hours of service during the twelve-month period are eligible to participate in the plan. The Company may make contributions at the discretion of its Board of Directors. The Company contributed and expensed $146,277, $114,206 and $100,161 in 1998, 1997 and 1996, respectively.

The Company has a "Cafeteria Plan" pursuant to Section 125 of the Internal Revenue Code, whereby health care benefits are provided for active employees through insurance companies. Substantially all active full-time employees are eligible for these benefits. The Company recognizes the cost of providing these benefits by expensing the annual premiums, which are based on benefits paid during the year. The premiums expensed for these benefits totaled $241,815, $228,805 and $217,375 for 1998, 1997 and 1996, respectively.

Effective January 1, 1997, the Company adopted a defined benefit pension plan (the "Plan") covering substantially all of its employees. The benefits are based on years of service and the employee's compensation during the five years before retirement. The Company expects to make annual contributions to the Plan equal to the maximum amount that can be deducted for income tax purposes.

(continued)

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

I. EMPLOYEE BENEFIT PLANS (continued)

The following table sets forth the plan's funded status and amount recognized in the Company's consolidated balance sheets at June 30:

	1998	1997
Actuarial present value of benefit obligations:		
Vested	$ 887,697	$ 417,236
Non-vested	88,617	120,905
	$ 976,314	$ 538,141
Projected benefit obligation	$ 2,084,109	$ 1,207,944
Plan assets at fair value	(313,750)	--
Projected benefit obligation (in excess of) plan assets	1,770,359	1,207,944
Unrecognized net (loss) gain	(529,132)	3,753
Prior service cost not yet recognized in net periodic pension cost	(993,828)	(1,053,137)
Increase in accrued pension cost	247,399	158,560
Adjustment to recognize minimum liability	415,165	304,821
Accrued pension cost at end of year	$ 662,564	$ 463,381
Net pension cost includes the following components:		
Service cost - benefits earned during the period	$ 268,815	$ 91,934
Interest cost on projected benefit obligation	84,171	37,172
Actual return on plan assets	(5,368)	--
Net amortization and deferral	56,996	29,454
Net pension cost	$ 404,614	$ 158,560

Assumptions used in accounting for the pension plan as of June 30 are as follows:

Discount rate	6.00%	7.00%
Rates of increase in compensation levels	5.90%	5.76%
Expected long-term rate of return on plan assets	7.50%	7.50%

NATURAL ALTERNATIVES INTERNATIONAL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

J. STOCKHOLDERS' EQUITY

Employee Stock Option Plans

Effective June 5, 1992, the Company adopted the 1992 Incentive Stock Option Plan for which 500,000 common shares have been reserved for issuance to officers, directors, and key employees of the Company. The plan provides that no option may be granted at an exercise price less than the fair market value of the common stock of the Company on the date of grant. On September 9, 1993, 200,000 options were granted with an exercise price equal to the fair market value price of $4.875 per share. On March 10, 1998, 300,000 options were granted with an exercise price equal to the fair market value price of $10.50 per share.

Also effective June 5, 1992, the Company adopted the 1992 Nonqualified Stock Option Plan and reserved a total of 250,000 common shares for issuance to officers, employees, and consultants of the Company. On September 9, 1993, 250,000 options were granted with an exercise price equal to the fair market value price of $4.875 per share.

Effective December 9, 1994, the Board of Directors approved the 1994 Nonqualified Stock Option Plan for which 500,000 common shares were reserved for issuance to officers, employees, and consultants of the Company. On January 24, 1995, 500,000 options were granted with an exercise price equal to the fair market value price of $4.625 per share.

All stock options under each of the plans have five-year terms and all options became fully vested within two years of their grant date.

Stock option activity during the periods indicated is summarized below:

	1992 Incentive Plan	1992 Nonqualified Plan	1994 Nonqualified Plan
Outstanding at June 30, 1995	198,362	242,138	500,000
Exercised	74,360	8,640	11,000
Outstanding at June 30, 1996	124,002	233,498	489,000
Exercised	27,833	12,556	37,500
Outstanding and exercisable at June 30, 1997	96,169	220,942	451,500
Exercised	57,778	159,333	121,334
Granted	300,000	--	--
Outstanding and exercisable at June 30, 1998	338,391	61,609	330,166
Weighted-average exercise price:			
June 30, 1998	$ 9.86	$ 4.88	$ 4.63
June 30, 1997	$ 4.88	$ 4.88	$ 4.63
Weighted-average remaining contractual life in years	5.00	0.17	1.50
Available for grant at June 30, 1998	--	--	--

(continued)

J. STOCKHOLDERS' EQUITY (continued)

The fair value of the option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions: risk-free interest rate equal to 5.33% at the grant date; dividend yield of zero; expected life of three years; and volatility of 53.4%. The weighted average fair value of options granted during fiscal year 1998 was $4.27.

The Company applies APB Opinion No. 25 in accounting for its Plans and, accordingly, no compensation cost has been recognized for its stock options in the financial statements. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's net earnings would have been reduced to the pro forma amounts indicated below:

	1998
Net earnings, as reported	$5,871,765
Pro forma net earnings	$5,700,965
Basic earnings per share, as reported	$ 1.06
Pro forma basic earnings per share	$ 1.03
Diluted earnings per share, as reported	$ 1.00
Pro forma diluted earnings per share	$ 0.97

Pro forma net earnings reflects only options granted in fiscal year 1998 as there were no options granted by the Company during fiscal year 1997 or 1996. Therefore, the full impact of calculating compensation cost for stock options under Statement No. 123 is not reflected in the pro forma net earnings amounts presented above because compensation cost is reflected over the options' vesting period and compensation cost for options granted prior to July 1, 1995 is not considered.

Other Stock Options

On January 24, 1995, the Board of Directors granted 100,000 options with an exercise price of $4.625 in exchange for consulting services and reserved 100,000 common shares. As of June 30, 1998, none of these options had been exercised or canceled. At June 30, 1998, the weighted-average remaining contractual life was two years.

On March 14, 1997, 45,000 options were granted pursuant to a consulting agreement at prices ranging from $9.00 to $15.00 per share. Consulting expense incurred as a result of these options was $84,000 for the year ended June 30, 1997. None of these options had been exercised as of June 30, 1998. At June 30, 1998, the weighted-average remaining contractual life was one year and the weighted-average exercise price was $12.00.

K. COMMITMENTS AND RELATED PARTY TRANSACTIONS

The Company leases part of its main facilities under leases that are classified as noncancelable operating leases. In August 1997, the Company entered into a 15-year lease agreement under which the lessor is to construct a build-to-suit office and manufacturing facility in Carlsbad, California. The Company plans to move its administrative offices and expand its manufacturing capacity into these premises when the building is ready for occupancy in early 1999. Annual lease payments, which will commence in November, 1998, are $1,222,000 and are subject to annual inflation adjustments. The Company has an option to acquire the facility during the sixth year of the lease.

Minimum rental commitments (exclusive of property tax, insurance and maintenance) under all noncancelable operating leases, including the 15-year lease agreement referred to above, (with initial or remaining lease terms in excess of one year) are set forth below.

1999	$ 887,504
2000	1,307,736
2001	1,335,640
2002	1,329,580
2003	1,359,960
Thereafter	16,673,220
	$22,893,640

Rental expense totaled $193,018, $169,079, and $193,340 for the years ended June 30, 1998, 1997 and 1996, respectively. These amounts include rental charges, pursuant to a lease agreement (the related party lease) with its two principal stockholders, Marie A. LeDoux and Mark A. LeDoux, of $55,000 for the year ended June 30, 1996. Amounts paid under this agreement were $100,000 for the year ended June 30, 1996.

In June 1996, the Company acquired certain suites within a building occupied by certain of its offices and production facilities which, up to that time, were subject to the related party lease. The lease provided for rent payable in the amount of $60,000 per year. The purchase price of the building was $545,000 which, in the opinion of management and an independent certified appraiser who evaluated the property in April 1996, represented fair market value.

During 1997 and 1996, the Company had sales of $14,812 and $1,084,290, respectively, to a company in which a key employee and beneficial owner of 1% of the stock of the Company was formerly the president and part owner. At June 30, 1997, the amount receivable from this company was $775,302, which was fully reserved because the Company had determined the account to be doubtful of collection. The Company recovered $263,400 in the year ended June 30, 1998.

The Company entered into an agreement with the father-in-law and mother-in-law of the Chief Executive Officer of the Company in December, 1991, which provides commissions on sales to a particular customer. The agreement will expire in December, 2001. The commission equals 5% of sales, and is capped at $25,000 per calendar quarter, effective January 1, 1993. Amounts paid under this agreement were $100,000 for each of the years ended June 30, 1998, 1997 and 1996. There were no amounts owed under the agreement at June 30, 1998 or 1997.

(continued)

K. COMMITMENTS AND RELATED PARTY TRANSACTIONS (continued)

During fiscal year 1993, the Company entered into an agreement that required future minimum royalty payments over the term of the contract, which expired December 31, 1996. Amounts paid under this agreement were $154,728 and $247,898 for the years ended June 30, 1997 and 1996, respectively. No amounts were owed under the agreement at June 30, 1997.

Included in notes receivable are notes from the Company's Chief Executive Officer and President. The balance of the notes, including accrued interest, was $79,036 and $95,365, respectively, as of June 30, 1998 and $74,444 and $89,824, respectively, at June 30, 1997.

Additionally, during the year ended June 30, 1998, the Company made noninterest-bearing loans to the Chairman of the Board and the President in the amount of $50,000 and $13,803, respectively, bringing the aggregate amount of such loans to $282,815. Amounts owed on these loans, which are secured by proceeds from life insurance policies on their respective lives, were $200,000 and $150,000 for the Chairman of the Board and $82,815 and $69,012 for the President at June 30, 1998 and 1997, respectively.

The Company paid commissions during the year ended June 30, 1996 in the amount of $6,916 to the Chairman of the Board.

L. ECONOMIC DEPENDENCY

The Company had substantial sales to four separate customers during one or more of the periods shown in the following table. The loss of any of these customers could have an adverse impact on the Company's revenues and earnings in the short-term. Sales by customer, representing 10% or more of the respective year's total sales, are shown below by industry segment.

	1998		1997		1996	
Industry Segment	Sales by Customer	%(a)	Sales by Customer	%(a)	Sales by Customer	%(a)
Multi-level Distribution:						
Customer 1	$24,914,144	37%	$17,934,985	36%	$13,616,835	29%
Customer 2	11,659,906	17%	6,851,560	14%	13,785,211	29%
Customer 3	(b)		5,936,477	12%	(b)	
	36,574,050	54%	30,723,022	62%	27,402,046	58%
Weight Loss:						
Customer 4	(b)		(b)		5,364,185	11%
Total	$36,574,050	54%	$30,723,022	62%	$32,766,231	69%

(a) Percent of total sales

(b) Sales for the year were less than 10% of total sales.

Accounts receivable from these customers totaled $4,271,969 and $3,108,597 at June 30, 1998 and 1997, respectively.

M. CONTINGENCIES

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, based in part on the advice of counsel, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

N. QUARTERLY DATA (unaudited)

The following is a summary of unaudited quarterly data:

	Year Ended June 30, 1998				
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Net sales	$12,032,576	$16,297,341	$18,960,255	$ 20,604,133	$67,894,305

Gross profit	3,161,354	4,442,561	5,223,250	5,909,423	18,736,588
Net earnings	598,420	1,363,023	1,823,729	2,086,593	5,871,765
Net earnings per common share:					
Basic	0.11	0.25	0.33	0.36	1.06
Diluted	0.11	0.24	0.31	0.34	1.00

	Year Ended June 30, 1997				
	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total
Net sales	$11,437,022	$12,630,234	$11,406,325	$ 13,970,640	$49,444,221
Gross profit	3,260,640	3,215,954	2,866,067	1,082,336	10,424,997
Net earnings (loss)	900,373	849,292	560,637	(1,190,382)	1,119,920
Net earnings (loss) per common share:					
Basic	0.17	0.16	0.10	(0.22)	0.21
Diluted	0.16	0.15	0.10	(0.22)	0.20

SCHEDULE II

NATURAL ALTERNATIVES INTERNATIONAL, INC.
VALUATION AND QUALIFYING ACCOUNTS
FOR THE YEARS ENDED JUNE 30, 1998, 1997, AND 1996

Allowance for doubtful accounts	Balance at beginning of period	Provision	Deductions*	Balance at end of period
Year ended June 30, 1998	$1,006,000	$360,000	$293,000	$1,073,000
Year ended June 30, 1997	$319,000	$725,000	$38,000	$1,006,000
Year ended June 30, 1996	$215,000	$391,000	$287,000	$319,000

* Accounts written off

See accompanying independent auditors report.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NATURAL ALTERNATIVES INTERNATIONAL, INC.
(Registrant)

Date: September 25, 1998 By: Mark A. LeDoux

(Mark A. LeDoux, Chief Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
Marie A. LeDoux ---------------------- (Marie A. LeDoux)	Chairperson of the Board, Secretary, and Director	September 25, 1998
Mark A. LeDoux ---------------------- (Mark A. LeDoux)	Chief Executive Officer and Director	September 25, 1998
William P. Spencer ---------------------- (William P. Spencer)	President, and Chief Operating Officer, and Treasurer, and Chief Financial Officer, and Chief Accounting Officer, and Director	September 25, 1998
William R. Kellas ---------------------- (William R. Kellas)	Director	September 25, 1998
Lee G. Weldon ---------------------- (Lee G. Weldon)	Director	September 25, 1998

EXHIBIT 23

The Board of Directors
Natural Alternatives International, Inc.:

We consent to incorporation by reference in the registration statement (No. 33-00947) on Form S-8 of Natural Alternatives International, Inc. of our report dated September 8, 1998, relating to the consolidated balance sheets of Natural Alternatives International, Inc. and subsidiaries as of June 30, 1998 and 1997, and the related consolidated statements of earnings, stockholders' equity, and cash flows for each of the years in the three-year period ended June 30, 1998, and the related schedule, which report appears in the June 30, 1998, annual report on Form 10-K of Natural Alternatives International, Inc.

KPMG Peat Marwick LLP

San Diego, California
September 25, 1998

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THE SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 1998, AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.
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