KASEN INTERNATIONAL HOLDINGS LIMITED
（卡森國際控股有限公司）

(An exempted company incorporated in the Cayman Islands with limited liability)
(Stock Code: 496)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED DECEMBER 31, 2005

The board of directors of Kasen International Holdings Limited (the "Company") is pleased to announce the audited results of the Company and its subsidiaries (the "Group") for the year ended December 31, 2005, together with the comparative figures for 2004, as follows:

CONSOLIDATED INCOME STATEMENT
For the year ended December 31, 2005

	Notes	2005 RMB'000	2004 RMB'000
Turnover	3	**3,475,457**	2,852,391
Cost of sales		**(2,927,194)**	(2,408,719)
Gross profit		**548,263**	443,672
Other income		**62,285**	189,895
Distribution costs		**(81,524)**	(56,487)
Administrative expenses		**(113,180)**	(93,902)
Other expenses		**(23,145)**	(133,596)
Share of loss of an associate		**(1,114)**	–
(Loss) gain on disposals of subsidiaries		**(1,380)**	3,013
Finance costs	4	**(111,540)**	(95,419)
Profit before taxation	5	**278,665**	257,176
Taxation	6	**(18,311)**	(22,646)
Profit for the year		**260,354**	234,530
Attributable to:			
Equity holders of the Company		**265,699**	225,701
Minority interests		**(5,345)**	8,829
		260,354	234,530
Earnings per share	7		
Basic		**41 cents**	47 cents
Diluted		**34 cents**	35 cents

The directors have recommended the payment of a final dividend of approximately RMB7.86 cents (equivalent to US0.98 cents or HK7.58 cents) per ordinary share (2004: Nil) for the year ended December 31, 2005 amounting to approximately RMB79,704,000, subject to approval by the shareholders of the Company at the annual general meeting to be held on May 30, 2006.

CONSOLIDATED BALANCE SHEET
At 31 December 2005

	Notes	2005 RMB'000	2004 RMB'000
NON-CURRENT ASSETS			
Goodwill		**181,006**	181,006
Negative goodwill		**–**	(4,395)
Property, plant and equipment		**1,281,230**	1,146,912
Prepaid lease payment – non-current portion		**142,812**	140,801
Intangible assets		**1,077**	905
Interest in an associate		**9,127**	5,173
Interest in a jointly controlled entity		**811**	–
Available-for-sale investments		**310**	2,410
		1,616,373	1,472,812
CURRENT ASSETS			
Inventories		**1,378,842**	1,392,738
Trade and other receivables	*8*	**795,665**	529,466
Prepaid lease payment – current portion		**3,543**	3,436
Held for trading investments		**–**	3,505
Amounts due from related companies	*10*	**21,253**	173,795
Taxes recoverable		**13,624**	8,549
Pledged bank deposits		**240,112**	239,185
Bank balances and cash		**372,278**	213,458
		2,825,317	2,564,132
TOTAL ASSETS		**4,441,690**	4,036,944
CURRENT LIABILITIES			
Trade, bills and other payables	*9*	**783,992**	873,382
Amounts due to related companies	*10*	**60,287**	74,289
Bank and other borrowings – due within one year		**1,191,246**	1,472,825
Convertible loan notes		**–**	304,934
Taxes payable		**7,807**	7,646
		2,043,332	2,733,076
NET CURRENT ASSETS (LIABILITIES)		**781,985**	(168,944)
TOTAL ASSETS LESS CURRENT LIABILITIES		**2,398,358**	1,303,868
NON-CURRENT LIABILITIES			
Bank and other borrowings – due after one year		**100,492**	102,492
		100,492	102,492
NET ASSETS		**2,297,866**	1,201,376
CAPITAL AND RESERVES			
Share capital		**1,256**	689
Reserves		**2,198,304**	1,090,415
Equity attributable to equity holders of the Company		**2,199,560**	1,091,104
Minority interests		**98,306**	110,272
Total equity		**2,297,866**	1,201,376

Notes:

1. GENERAL

The Company is a public limited company incorporated in the Cayman Islands and its shares are listed on the Stock Exchange of Hong Kong Limited ("Stock Exchange") since October 20, 2005.

In preparation for listing of the Company's shares on the Stock Exchange, the Company underwent a group reorganization (the "Reorganization"). The Reorganization principally involved (1) the shareholders (the "Founding Shareholder Group") of Zhejiang Kasen Industrial Co,. Ltd. ("Zhejiang Kasen"), the then principal operating company and a holding company of certain subsidiaries of the Company, subscribed for a total of 231,095,052 ordinary shares of US$0.0001 each of the Company on January 14, 2003 and February 14, 2003 respectively, so as to set up a holding company; and (2) a transfer of the entire ownership interest in Zhejiang Kasen to the Company, Zhejiang Kasen and the Company were controlled by the Founding Shareholder Group throughout the Reorganization. The Founding Shareholder Group, as a result of contractual agreements, was regarded as a single entity controlling the Group and governed the financial and operating policies of the Group. In respect of step (2) of the Reorganization above, such contractual agreements include (i) a declaration of trust signed by Mr. Zhu Zhangjin ("Mr. Zhu"), a director and a shareholder of the Company, on February 26, 2003 which declared that 11.00% of the equity interest Mr. Zhu held in the Company was held on trust for two of the shareholders of Zhejiang Kasen ("Township Shareholders") and gave Mr. Zhu the full power to vote in his discretion on behalf of the Township Shareholders; and (ii) a voting agreement dated February 26, 2003 whereby the 21 individual shareholders of Zhejiang Kasen granted Mr. Zhu full power to vote on their behalf all shares owned by them. The declaration of trust and the voting agreement were terminated on September 16, 2004 and October 9, 2005, respectively; and (3) in return for the ownership interest in Zhejiang Kasen transferred by the Founding Shareholder Group, the Founding Shareholder Group subscribed for 421,078,856 further ordinary shares of US$0.0001 each in the Company on September 16, 2004 and the Reorganization was completed on the same date.

Accordingly, for the purpose of the preparation of the financial statements of the Group, the Group accounted for Zhejiang Kasen as a wholly-owned subsidiary on the basis that the Company has been considered as the holding company of Zhejiang Kasen and its subsidiaries throughout the period using the principles of common control except for those subsidiaries which were established or acquired during the period.

2. CHANGE IN ACCOUNTING POLICIES AND SUMMARY OF THE EFFECTS

In the current year, the Group has applied, the new and revised International Financial Reporting Standards ("IFRS"), International Accounting Standards ("IASs") and Interpretations ("IFRIC") (hereinafter collectively referred to as "new IFRSs") issued by International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretation Committee of the IASB that are effective for accounting periods beginning on or after January 1, 2005. The adoption of the new IFRSs has resulted in changes of the Group's accounting policies in the following areas that have an effect on the results for the current or prior accounting periods are prepared and presented.

Business Combinations

IFRS 3 Business Combinations is effective for business combinations for which the agreement date is on or after March 31, 2004 and from the beginning of its first annual period beginning on or after March 31, 2004 (i.e. the financial year beginning on January 1, 2005). The principal effects upon application of the transitional provisions of IFRS 3 on January 1, 2005 to negative goodwill arising from business combinations are summarized below:

Excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over cost (previously known as "negative goodwill")

In accordance with IFRS 3, any excess of the Group's interest in the net fair value of acquiree's identifiable assets, liabilities and contingent liabilities over the cost of acquisition ("discount on acquisition") is recognized immediately in profit or loss in the period in which the acquisition takes place. In previous periods, negative goodwill arising on acquisitions was presented as a deduction from assets and released to income based on an analysis of the circumstances from which the balance resulted. In accordance with the relevant transitional provisions in IFRS 3, the Group derecognized all negative goodwill on January 1, 2005. A corresponding adjustment to the Group's retained earnings of approximately RMB4,395,000 has been made.

The impact of the change in accounting policy for the year is an increase in other operating income of approximately RMB4,252,000 and an increase in net assets at January 1, 2005 of approximately RMB4,395,000.

Share-based Payments

In the current year, the Group has applied IFRS 2 Share-based Payment which requires an expense to be recognized where the Group buys goods or obtains services in exchange for shares or rights over shares ("equity-settled transactions"), or in exchange for other assets equivalent in value to a given number of shares or rights over shares ("cash-settled transactions"). The principal impact of IFRS 2 on the Group is in relation to the expensing of the fair value of share options granted to directors and employees of the Company, determined at the date of grant of the share options, over the vesting period. Prior to the application of IFRS 2, the Group did not recognize the financial effect of these share options until they were exercised. The Group has applied IFRS 2 to share options granted on or after January 1, 2005. Because there were no unvested share options at January 1, 2005, comparative figures for last year need not to be restated. During the year, no share options have been granted by the Company.

3. TURNOVER AND SEGMENT INFORMATION

For management purposes, the Group is currently organized into four operating divisions. These divisions are the basis on which the Group reports its primary segment information.

Business segment

During the year, the Group has presented its business by the following segments:

- Upholstered furniture, comprising leather and fabric upholstered furniture and furniture covers;
- Furniture leather;
- Automotive leather;
- Leather garments; and
- Others (including sale of wooden frame and others)

Segment information about these business is presented below:

	2005					
	Upholstered furniture *RMB'000*	**Furniture leather** *RMB'000*	**Automotive leather** *RMB'000*	**Leather garments** *RMB'000*	**Others** *RMB'000*	**Total** *RMB'000*
Consolidated Income statement						
Turnover	**2,755,003**	**593,121**	**126,907**	**–**	**426**	**3,475,457**
Segment result	**317,237**	**41,993**	**9,200**	**–**	**(2,477)**	**365,953**
Unallocated corporate income						**49,891**
Unallocated corporate expenses						**(23,145)**
Loss on disposals of subsidiaries						**(1,380)**
Share of loss of an associate						**(1,114)**
Finance costs						**(111,540)**
Profit before taxation						**278,665**

Inter-segment sales are charged at prevailing market prices.

	2004					
	Upholstered furniture *RMB'000*	Furniture leather *RMB'000*	Automotive leather *RMB'000*	Leather garments *RMB'000*	Others *RMB'000*	Total *RMB'000*
Consolidated Income statement						
Turnover	2,033,173	491,839	127,451	130,811	69,117	2,852,391
Segment result	255,551	47,263	11,005	13,044	10,141	337,004
Unallocated corporate income						24,634
Unallocated corporate expenses						(12,056)
Gain on disposals of subsidiaries						3,013
Finance costs						(95,419)
Profit before taxation						257,176

Inter-segment sales are charged at prevailing market prices.

Geographical segments

The following table provides an analysis of the Group's sales by geographical market:

	2005	2004
	RMB'000	*RMB'000*
United States	**2,383,797**	1,915,701
PRC, including Hong Kong	**727,001**	637,763
Russia	**563**	131,742
Europe	**119,709**	89,659
Australia	**187,543**	70,427
Others	**56,844**	7,099
	3,475,457	2,852,391

4. FINANCE COSTS

	2005	2004
	RMB'000	*RMB'000*
Interest on:		
Bank borrowings wholly repayable within five years	**94,245**	77,340
Other borrowings wholly repayable within five years	**3,536**	2,975
Other borrowings not wholly repayable within five years	**510**	205
Convertible loan notes	**13,249**	14,899
	111,540	95,419

5. PROFIT BEFORE TAXATION

Profit before taxation has been arrived at after charging:

	2005	2004
	RMB'000	*RMB'000*
Amortization of intangible assets (included in administrative expenses)	**225**	113
Depreciation of property, plant and equipment	**87,474**	61,155
Total depreciation and amortization	**87,699**	61,268
Cost of sales of raw materials (included in other expenses)	**18,230**	128,163
Total employee benefit expenses	**237,063**	190,221

6. TAXATION

	2005	2004
	RMB'000	*RMB'000*
Hong Kong Profits Tax		
– current year	**718**	–
– under-provision in previous year	**425**	–
PRC enterprise income tax		
– current year	**19,504**	22,646
– over-provision of income tax	**(2,336)**	–
	18,311	22,646

Hong Kong Profits Tax is calculated at 17.5% of estimated assessable profit for the year.

PRC enterprise income tax is calculated at the applicable rates to the PRC subsidiaries. Certain subsidiaries of the Company operating in the PRC are eligible for certain tax holidays and concessions and were exempted from PRC income taxes for the year ("Tax Holidays").

In the opinion of the directors of the Company, no deferred tax asset has been recognized in 2005 and 2004 as the effect to the Group's financial statement was immaterial.

7. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to the equity holders of the Company is based on the following data:

Earnings

	2005 *RMB'000*	2004 *RMB'000*
Earnings for the purposes of basic earnings per share, being profit attributable to equity holders of the Company	**265,699**	225,701
Effect of dilutive potential ordinary shares: Interest on convertible loan notes	**13,249**	14,899
Earnings for the purposes of diluted earnings per share	**278,948**	240,600

Number of shares

	2005	2004
Weighted average number of ordinary shares for the purposes of basic earnings per share	**645,419,597**	476,675,977
Effect of dilutive potential ordinary shares: Convertible loan notes	**179,512,056**	207,951,216
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**824,931,653**	684,627,193

The weighted average number of ordinary shares for the purpose of calculating basic and diluted earnings per share attributable to the equity holders of the Company for the year has been retrospectively adjusted for the effect of the share consolidation completed during the year.

8. TRADE RECEIVABLES

The Group grants a credit period predominantly ranging from 30 days to 90 days to their trade customers. The aging analysis of trade receivables is as follows:

	2005 *RMB'000*	2004 *RMB'000*
Aged:		
Within 60 days	**355,407**	226,629
60 - 90 days	**51,342**	12,903
91 - 180 days	**63,429**	18,189
181 - 365 days	**43,139**	11,344
1 - 2 years	**1,116**	1,483
Total trade receivables, net of impairment loss	**514,433**	270,548

9. TRADE AND BILLS PAYABLES

The aging analysis of trade payables and bills payable are as follows:

	2005	2004
	RMB'000	*RMB'000*
Aged:		
Within 60 days	**321,512**	339,688
60 - 90 days	**33,685**	61,320
91 - 180 days	**49,869**	40,140
181 - 365 days	**15,974**	12,032
1 - 2 years	**6,643**	6,160
Over 2 years	**3,206**	630
Total trade payables	**430,889**	459,970
Aged:		
Within 60 days	**81,026**	214,838
60 - 90 days	**58,959**	–
91 - 180 days	**43,418**	–
Total bills payable	**183,403**	214,838

10. AMOUNTS DUE FROM (TO) RELATED PARTIES

Aging of amounts due from (to) related companies in operating nature is as follows:

	2005		2004	
	Amounts due from related companies	**Amounts due to related companies**	Amounts due from related companies	Amounts due to related companies
	RMB'000	***RMB'000***	*RMB'000*	*RMB'000*
Aged:				
Within 60 days	**4,588**	**(14,484)**	24,310	(12,661)
60 - 90 days	**3,900**	**(544)**	1,084	(10,680)
91 - 180 days	**12,100**	**(45,259)**	3,944	(18,138)
181 - 365 days	**80**	**–**	2,460	(5,610)
	20,668	**(60,287)**	31,798	(47,089)

11. PLEDGE OF ASSETS

At the balance sheet date, certain of the Group's assets have been pledged to secure the borrowings of the Group. The aggregate carrying amount of the assets of the Group at the balance sheet date is as follows:

	2005	2004
	RMB'000	*RMB'000*
Prepaid lease payment	**87,144**	27,575
Buildings	**486,878**	209,150
Bank deposits	**240,112**	239,185
	814,134	475,910

12. CAPITAL COMMITMENTS

At the balance sheet date, the Group had capital commitments as follows:

	2005 *RMB'000*	2004 *RMB'000*
Capital expenditure contracted for but not provided in the financial statements in respect of acquisition of property, plant and the equipment	**6,656**	108,365
Capital expenditure contracted for but not provided in the financial statements in respect of construction of certain infrastructure and public facilities in the PRC on behalf of the government	**20,991**	33,200
	27,647	141,565

13. CONTINGENT LIABILITIES

At the balance sheet date, the Group had the following contingent liabilities:

	2005 *RMB'000*	2004 *RMB'000*
Guarantees given to banks in respect of banking facilities extended to		
– Independent third parties	**67,897**	261,663
– Related parties	**–**	113,000
	67,897	374,663

14. SYNDICATED LOAN

In late December 2005, the Group obtained a syndicated loan in aggregate of HK$125,000,000 arranged by CITIC Capital Markets Limited, with a term of three years, which will be principally used for general working capital of the Group. The three-year-term syndicated loan, drawn down in January 2006, bears interest at 2.00% over 12-month Hong Kong Interbank Offered Rate per annum.

MANAGEMENT DISCUSSION AND ANALYSIS

Overview

During the year under review, there was significant increase in the Group's turnover and profit, mainly attributable to active market expansion, continuous capacity uplift and rigorous cost control.

For the year ended December 31, 2005, the Group's turnover increased 21.8% to RMB3,475,457,000 (2004: RMB2,852,391,000), while its profit for the year rose 11% to RMB260,354,000 (2004: RMB234,530,000). The profit attributable to equity holders of the Company for 2005 was RMB265,699,000 as compared to RMB225,701,000 in 2004.

Overall Gross Profit Margin

The Group's gross profit margin in 2005 was 15.8%, representing an improvement as compared to 15.6% in 2004.

The Group's principal raw materials are raw cowhides and wet blues, which accounted for 46.5% of the total cost of sales in 2005. The prices for raw cowhides in international market remained comparatively stable in 2005, which was the major contribution to the Group's steady gross profit margin.

However, RMB's further appreciation and costs rising in China brought challenge to the manufacturing and export industries that operate in the country. The Group was able to offset the negative impact of rising labour costs in China by improving its operation efficiency. By importing its principal raw material for production, the Group partially offset the impact of RMB's appreciation.

Operating Expenses, Taxation and Profit Attributable to Equity Holders

Rising oil price had little influence on the Group's distribution costs, as the marine freight charges of almost all the exporting business of the Group were borne by the customers. However, the percentage of distribution costs to turnover rose slightly to 2.3% (2004: 2.0%) of the turnover, as the share of finished upholstered furniture export to the total turnover of the Group increased and land transportation cost from factory to port also climbed up.

In regard of administrative expenses, though the remuneration of the management increased in 2005, the percentage of administrative expenses to turnover remained unchanged at 3.3%, for the operating efficiency was improved after productivity of the Group increased.

In 2005, interest-bearing loans continued to be one of the major funding sources of the Group, and finance costs increased to RMB111,540,000 (2004: RMB95,419,000), of which the interest incurred by the Convertible Loans granted to the Group by Warburg Pincus amounted to RMB13,249,000 (2004: RMB14,899,000). After the initial public offering of the Group's shares, the above Convertible Loans were converted into the Group's equity, and the accumulated interests not yet paid during the past years in total of RMB32,823,000 were fully transferred into shareholders' equity.

Most of the Group's operations are carried out in the economic and technological development zones and coastal open areas of the PRC where allow income tax relieves in accordance with relevant income tax laws and regulations, so the overall effective tax rate of the Group remains approximately 6.6% (2004: 8.8%).

In September 2004, the Group redeemed the equity interests held by minority shareholders in most of its subsidiaries, except five joint ventures located in the Higher Point Sofa Industrial Park, so in 2005 minority shareholders continued to be interested in the five joint ventures located in the Higher Point Sofa Industrial Park. Profit attributable to minority shareholders represented -2.1% (2004: 3.8%) of profit after taxation .

For reasons mentioned above, profit attributable to equity holders of the Company increased by approximately 17.7% to RMB265,699,000.

Sales Analysis by Products

Upholstered Furniture

Upholstered furniture remained the core products of the Group, and its sales accounted for 79.3% of the total turnover in 2005. As the upholstered furniture industry in the Group's principal export regions increasingly outsourced its production, the Group's upholstered furniture operation was able to increase by 35.5% in 2005, among which, the fabric upholstered furniture operation grew especially fast, up by 54.0% and took up 13.7% of the total turnover (2004: 10.9%).

Furniture Leather

Furniture leather produced by the Group continued to be well received by overseas and domestic furniture producers, which contributed to a rapid growth in this operation in 2005. Although the Group gave priority to meet its internal requirement of the fast growing leather upholstered furniture division, the external sales of the furniture leather operation still managed to grow by 20.6% in 2005.

Automotive Leather

In contrast, the automotive leather operation did not achieve the expected growth in 2005, with its turnover at the same level as 2004. It was principally due to that the operation commenced in 2003 and it usually takes quite a long time to obtain product certificates from the auto makers.

Sales Analysis by Regions

In 2005, the Group continued to expand its markets in the US, Europe and Australia. In line with the ongoing outsourcing trend of consumption products in the regions, the Group's sale increased strongly in these markets. The Group's sales in the US, Europe and Australia increased by 24.4%, 33.5% and 166.3% respectively; and, as a percentage to the total sales, the turnovers in the US, Europe and Australia accounted for 68.6%, 3.4% and 5.4% respectively.

The Group's sales to the PRC domestic market mainly involved furniture leather and automotive leather, the turnover of which represented 20.9% of its total sales. Business in this segment increased by 14.0% in 2005.

The Higher Point Project

The Group commenced to establish Higher Point Sofa Industrial Park in Haining city, Zhejiang province, in 2004 to expand its production capacity. It was planned to include eight upholstered furniture factories after completion, with three factories to be wholly owned by the Group and other five factories to be run in the form of joint-ventures.

For the year ended December 31, 2005, one of the Group's wholly-owned subsidiaries and other five joint-ventures (collectively referred to as the "Higher Point Enterprises") in Higher Point Sofa Industrial Park formally commenced operation. The total sales amounted to RMB925,916,000 in 2005 (2004: RMB265,722,000), representing an increase of 248.5%. The Higher Point Enterprises recorded remarkable achievement in developing customers, which was reflected in the successful expansion of the Group's customer base and revenue sources, and currently became an important part of Group's operation.

As Higher Point Project was still in its preliminary stage, most workers were not well trained which resulted in a lower production efficiency. For the year ended December 31, 2005, the overall gross profit margin of the Higher Point Enterprises was 10.2%, which was lower than the average level of the Group, while the net profit was just at breakeven point. Along with the improvement of the workers' skills and the continuous rapid growth in operations, it is anticipated that the performance of the Higher Point Enterprises will be improved substantially in near future.

Capital Expenditure

As most investments by the Group to increase production capacity completed in previous years up to 2004, the capital expenditure in 2005 was reduced significantly to RMB231,468,000 (2004: RMB739,558,000). The capital expenditure in 2005 was mainly used in (1) construction of additional production facilities required for normal operation by Higher Point Project; (2) replacement of old furniture leather equipment with new ones; and (3) purchase of new equipment for producing automotive leather. The principal expenditure for these items were approximately RMB99,193,000, RMB66,600,000 and RMB23,339,000 respectively.

Financial Resources and Liquidity

Total Borrowings

As at December 31, 2005, the Group's total borrowings amounted to RMB1,291,738,000 (2004: RMB1,880,251,000). Such decrease in total borrowing was primarily because (1) the Group utilised proceeds raised through its initial public offering to repay part of its loans; (2) Warburg Pincus's Convertible loans granted to the Group were converted into equity; and (3) cash flow from operation of the Group was significantly improved.

As at December 31, 2005, the Group's total borrowings primarily comprise of (1) short-term borrowings of RMB1,191,246,000 provided by local banks, bearing an interest rate ranging from 4.0% to 8.1% per annum; and (2) long-term borrowings of RMB90,092,000 provided by local banks, bearing an interest rate ranging from 5.1% to 6.0% per annum; and (3) government debt of RMB10,400,000, bearing an interest rate of 2.55%.

Turnover Period, Liquidity and Gearing

The Group's inventory primarily represented raw cowhides and wet blues used for production, accounting for approximately 44.4% of the total inventory. In 2005, the Group endeavoured to control inventory level and managed to decrease its inventory turnover period to 172 days (2004: 211 days).

In 2005, the Group maintained export credit insurances and appropriately extended the credit terms to certain substantial customers, resulting in an increase in accounts receivable turnover days to 54 days (2004: 35 days).

The Group attempted to shorten the accounts payable credit term so as to cut the purchase costs. As a result, the accounts payable turnover days decreased to 77 days (2004: 102 days).

As the Group's operating cashflow continuously improved in 2005, as at December 31, 2005, its current ratio and quick ratio increased to 1.38 (2004: 0.94) and 0.71 (2004: 0.43), respectively. The Group's cash and cash equivalents balance was RMB372,278,000 (2004: RMB213,458,000).

Mainly due to the completion of its initial public offering in the year, the Group's gearing was significantly improved. Such ratios included: (1) bank borrowings to total assets, (2) bank borrowings to equity and (3) net debts (i.e. net balance between bank borrowings and cash and cash equivalents) to equity, dropped from 38.8%, 130.3% and 112.5% as at December 31, 2004 to 28.8%, 55.8% and 39.6% as at December 31, 2005, respectively. Interest rate coverage (i.e. the ratio of profit from operating activities over finance costs) was approximately 3.5 times (2004 : 3.7 times). A high interest rate coverage reflected that the leverage level of the Group remained healthy.

Foreign Exchange Exposure

As the Group's businesses are principally export-related and transactions are primarily denominated in US dollars, the Directors consider the Group is exposed to foreign exchange fluctuation risks. However, as a substantial portion of procurements of the Group is denominated in US dollars, such risks can be reduced partly through natural hedges. Therefore, the Group neither used any financial instrument for hedging purposes during the year, nor had any hedging instrument outstanding as at December 31, 2005.

FUTURE PLANS AND PROSPECTS

The Group aims to become one of the world's leading manufacturers of leather products and upholstered furniture. To achieve this goal, the Group continues its effort in expanding its market share, strengthening product portfolios, further reducing production costs and forming strategic alliances with globally reputable leading manufacturers, so as to strengthen the Group's competitive edges in product development.

Upholstered Furniture Business

The US is currently the largest market for the Group's upholstered furniture products. Although statistics show that there is a slowdown in real estate industry in the US, the Group does not consider that it will have impact on further expansion of the Group's business in the US. This is primarily due to the fact that US brand name furniture companies will continue to save costs through manufacture outsourcing, while export from countries with low production costs (including the PRC) to the US will maintain its strong growth.

At present, the percentage of upholstered furniture imported from the PRC to the US total consumption remains at a comparatively low level, thus the US market still promises a great potential. The Group will continue to explore the US market by taking advantage of the established business relationship with leading upholstered furniture companies in the US. The Group will consider a realignment of the logistics arrangement for export to the US so as to assist its customers to reduce their logistics costs and to strengthen the Group's competitive edges.

The year 2005 witnessed a fast growth in the Group's sale of fabric upholstered furniture to the US market, representing an increase of 54%. As fabric upholstered furniture accounted for more than 70% of the total consumption of upholstered furniture in the US, and the import share in this section is comparatively low, accordingly, the Group will continue to develop more new lines of fabric upholstered furniture products.

European countries, Australia and other countries will also increase manufacture outsourcing to the PRC, which is evidenced by the fast growth in the Group's Europe and Australia businesses in 2005. The Group will put more efforts in these markets for faster growth.

In 2005, the Group's Higher Point Project achieved significant progress in turnover and gained several key customers. The Group anticipates that the sales from Higher Point Enterprises will continue to grow rapidly in future and their profitability will improve significantly.

Furniture Leather Business

The Group purchases raw cowhides, wet blues and other raw materials and processes them into finished leather for the production of leather products and upholstered furniture. The Group is currently the largest finished leather producer in the PRC.

As a vertically integrated producer, the Group's leading position in the furniture leather industry allows it to win upholstered furniture customers' confidence through low costs, high quality and fast delivery schedule. The Group will continue to develop new lines of leather products with constantly improved textures, appearances and styles to cater its customers' needs. Meanwhile, the Group will continue to seek for alternative materials to ensure a competitive edge supported by low costs.

Automotive Leather Business

Although the development of its automotive leather operation in 2005 was disappointing, the Group remains optimistic in the outlook for the automotive leather market. At present, the Group is carrying out tests on automotive leather required for new automotive models by several automotive manufacturers at home and abroad and has obtained various product certifications. The Group anticipates that its automotive leather operation will experience a fast growth in future, but its contribution to the Group's overall turnover will be insignificant in near future.

In 2005, a joint venture was established by the Group and MELX, a leading leather producer in Japan, to develop various businesses including automotive leather products. The joint venture will increase the sales of automotive leather products to Japanese automakers.

Other Operations

To make full use of cowhides resources to enhance its profitability, the Group has carried out trial production of footwear leather since 2005, but its contribution to the Group's overall turnover will be insignificant in near future.

In order to make full use of its advantages in cutting and sewing and to improve the utilization of production facilities, from the beginning of 2006, the Group has expanded its business into the field of outdoor leisure products, mainly including tents, sleeping bags, outdoor furniture, etc. In February 2006, a supply agreement was entered into between the Group and North Pole Limited, an associate of the Group, with a term of three years. The transaction was approved at the Extraordinary General Meeting held on March 31, 2006.

USE OF PROCEEDS

In late October 2005, the Shares were listed on the Stock Exchange by way of public offering and placing. Out of a total of 304,220,000 Shares at initial offer price HK$2.55 per share under the public offering and placing, we were offering 202,809,074 Shares and the selling shareholders were offering 101,410,926 Shares. The Company successfully raised HK$517,163,000, equivalent to RMB539,246,000, through its initial public offering. Of the total proceeds, approximately HK$40 million was paid for underwriting commission and expenses. At the end of 2005, the Group had used approximately RMB251 million and RMB32 million from the proceeds to repay short-term bank loans and to fund its capital expenditure respectively. The remaining amounts were deposited in short term demand bank deposits. The actual use of proceeds is in line with the plans as set out in the prospectus of the Company relating to the initial public offering.

FINAL DIVIDENDS

The directors have recommended the payment of a final dividend of approximately RMB7.86 cents (equivalent to US0.98 cents or HK7.58 cents) per ordinary share for the year ended December 31, 2005, subject to approval by the shareholders of the Company at the annual general meeting to be held on May 30, 2006. The translation of RMB into Hong Kong dollars is made at the exchange rate of HK$1.00=RMB1.0363 as at April 19, 2006. The actual translation rate for the purpose of dividend payment in Hong Kong dollars will be based on the official exchange rate of RMB against Hong Kong dollars as quoted by the People's Bank of China on May 30, 2006, being the date of the annual general meeting on which the final dividend is proposed to the shareholders of the Company for the approval. Subject to the approval by the shareholders, the proposed final dividend is expected to be paid on or about June 29, 2006 to the shareholders whose names appear on the registers of members of the Company on May 30, 2006.

CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed from May 26, 2006 to May 30, 2006 (both days inclusive), during which period no transfer of shares in the Company will be effected. In order to qualify for the proposed final dividend and the entitlement to attend and vote at the forthcoming annual general meeting, all transfers documents, accompanied by the relevant share certificates, must be lodged with the Company's Hong Kong branch registrar, Computershare Hong Kong Investor Services Limited, Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, not later than 4:00 p.m. on May 25, 2006.

PURCHASE, SALE OR REDEMPTION OF SHARES

At no time during the year, did the Company nor any of its subsidiaries purchase, sell or redeem any of the Company's listed securities.

EMPLOYEES AND EMOLUMENTS

As at December 31, 2005, the Group employs a total of approximately 15,000 full time employees (2004: 14,827) which included management staff, technicians, salespersons and workers. For the year ended December 31, 2005, the Group's total expenses on the remuneration of employees is RMB237,063,000 and represents 6.82% of the turnover of the Group. The Group's emolument policies are formulated on the performance of individual employees, which will be reviewed regularly every year. Apart from provident fund scheme (in accordance with the provisions of the Mandatory Provident Fund Schemes Ordinance for Hong Kong employees) or state-managed retirement pension scheme (for the PRC employees) and medical insurance, discretionary bonuses and employee share options are also awarded to employees according to the assessment of individual performance.

CODE ON CORPORATE GOVERNANCE PRACTICES

In the opinion of the Directors, the Company has complied with the code provisions set out in the Code on Corporate Governance Practices ("Code") contained in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules") since our IPO date being October 20, 2005 to December 31, 2005 (the "Period"), except for Mr. Zhu Zhangjin who had served as both the Chairman of the Board and the Chief Executive Officer of the Company.

Mr. Zhu Zhangjin is the Chairman and Chief Executive Officer of the Company responsible for overseeing the operations of the Group. The Company is currently considering to appoint a new Chief Executive Officer to replace Mr. Zhu if candidate with suitable leadership, knowledge, skills and experience can be identified within or outside the Group. However, due to the nature and extent of the Group's operations, in particular in Mainland China and the in-depth knowledge and experience in the leather and upholstery furniture market required for the position of Chief Executive Officer, it is not possible to determine as to when the appointment of a new Chief Executive Officer of the Company can be effected. However, the Board believes that the appointment of Mr. Zhu as the Chairman and Chief Executive Officer of the Company will not impair the balance of power and authority between the Board and the management of the Company, and is most beneficial to the Company's interest at present.

AUDIT COMMITTEE

An Audit Committee was established by the Company in September 2005 to review and supervise the Company's financial reporting process and internal controls. The Audit Committee comprises the three independent non-executive directors of the Company. Mr. CHOW Joseph is the chairman of the Audit Committee.

The annual results of the Company have been reviewed by the Audit Committee.

REMUNERATION COMMITTEE

A Remuneration Committee was established by the Company in September 2005 to establish policies, review and determine the remuneration of the directors and the senior management. The Remuneration Committee, comprises the two independent non-executive directors and a non-executive director of the Company. Mr. SUN Qiang Chang is the chairman of the Remuneration Committee.

By Order of the Board
Kasen International Holdings Limited
Yiu Hoi Yan
Company Secretary

Hong Kong, April 19, 2006

As at the date hereof, the Executive Directors are Mr. Zhu Zhangjin, Mr. Zhou Xiaosong and Mr. Zhu Jianqi. The Non-executive Director is Mr. Sun Qiang Chang. The Independent Non-executive Directors are Mr. Lu Yungang, Mr. Chow Joseph and Mr. Shi Zhengfu.