



INTRODUCTION

2005 has been a challenging year for the Group. Entering into the first year of “quota-free” environment, the Group has experienced, along with other industry players, all the chaos brought about by the uncertainties due to trade disputes between China and its major markets. Luen Thai, nonetheless, managed to sustain its revenue growth in 2005.

As the Group strives to develop and maintain long-term partnership with our customers, we make sure that our customers’ demands are met especially during times of uncertainties like what we experienced in 2005. In order to cope with the frequent and last-minute changes in production orders in 2005, we had to reshuffle our production planning, which affected not only our production efficiency but also the effective use of our facilities, thereby, causing an increase in our operating costs plus airfreight. However, with our intense efforts to minimize unfavorable impact of the uncertainties in quota and trade regulations, the Group still managed to record a profit in 2005.

Luen Thai considers the market chaos only temporary and we expect our business to increase in 2006 as order flows stabilize following the enforcement of trade agreements with the USA/EU along with implementation of China’s quota allocation system.

With our state-of-the-art supply chain and manufacturing platform, the Group continues to grow by gaining new customers and striving to develop stronger relationships with our key customers as we capitalize further on business opportunities with them. Operationally, the Group has taken a number of initiatives to sustain and further improve operational efficiency, and effectively control costs.

RESULT REVIEW

Turnover of the Group was approximately US\$590,234,000 for the year ended 31 December 2005, representing an increase of 6.6% as compared to that recorded in 2004.

The Group’s overall gross profit for 2005 was approximately US\$110,789,000 as compared to US\$125,799,000 in 2004. The overall gross profit margin in 2005 is 18.8% as compared to 22.7% in 2004. The Group’s operating profit for 2005 was approximately US\$23,055,000, representing a decrease of 39.9% over 2004. These reductions are the results of higher operating costs primarily due to uncertainties brought about by trade disputes between China and the USA/EU, and the reinstatement of quota on certain product categories. The Group also incurred additional start-up costs on its expansion into the production of pants and its development of OPA facilities. The average selling price of the Group in 2005, however, remained relatively stable when compared to 2004.

Mariana Express Lines Ltd. ("MELL"), an associated company engaged in ocean cargo service in Asia which was disposed on 3 September 2005, recorded a loss of approximately US\$1,895,000 for the eight months ended 31 August 2005, due to high oil prices and increase in charter hire costs.

The profit attributable to equity holders of the Company for the year ended 31 December 2005 therefore suffered a decline of 56.4% to approximately US\$13,240,000 when compared to that recorded in prior year.

The freight forwarding & logistics services recorded a turnover amounting to US\$11,872,000 in 2005, representing a decrease of 1.7% over 2004.

OPERATIONAL REVIEW

The Group accomplished a number of initiatives and the following are some of the highlights:

Co-location Strategy

Our Dongguan Supply Chain City represents the Group's long-term partnership strategy with our key customers with design support, product development, logistics and distribution, laboratory testing and production all housed in one site to continuously improve efficiencies and reduce lead time of our customers, suppliers and the Group. The Group signed up another key customer on such co-location partnership in 2005.

In addition, GJM Division opened its dedicated development center for one of its key customers in Panyu, China, which is also considered as the first vendor-partner in the greater China region to pioneer the development center exclusively for its sleepwear product.

Fabric & Trims Innovation Center

The Group opened Fabric & Trims Innovation Center at the Dongguan Supply Chain City, which is the first of its kind in the global apparel industry. This was created to cut sourcing lead time by bringing a wide selection of the latest materials development closer to our customers.



CEO REPORT

Expansion of Tomwell

Tomwell Limited was acquired by the Group in 2004 and it is engaged in the production of ladies career wear. In consideration of its growing business, we facilitated its expansion in our Dongguan Supply Chain City in 2005 and it started to operate in February 2006.

Outward Processing Arrangements

In line with the Group's multi-country and multi-product strategy and as a measure to counter uncertainties, our Outward Processing Arrangements ("OPAs") are in full swing on its first year of operations. These new facilities have allowed us to steadily grow our knit and woven production capability while our facilities in China, Saipan and the Philippines continue to complement Luen Thai's global production network. We shall continue to identify opportunities for us to expand our production capability through these OPAs and make adjustments accordingly in keeping with regulatory changes in the apparel industry.

Logistics and Distribution

CTSI Logistics, the Group's logistics division, has been upgrading its operations and facilities in anticipation of closer partnership with our customers in the logistics area. In 2005, CTSI Logistics inaugurated its Philippine Supply Chain Center (the "Center"), which houses office and warehouse spaces. The Center is an integral part of the Logistics Division's vision of becoming a total logistics solution provider – from warehousing, inventory management, freight forwarding, distribution to logistics consultancy – a full range of logistics services, which are all available under one roof.



In addition, CTSI Logistics in Guam moved to the new Guam Distribution Center of 23,800 square feet, which is dubbed as the "Hub of Micronesia" and is set to become a point of convergence for business growth in Guam and in the Micronesian region.

ACQUISITIONS AND JOINT VENTURES

It is the Group's strategy in expanding into other apparel product categories by way of selective acquisitions and joint ventures. With an established experience of acquiring and managing entities in different segments such as GJM for sleepwear (from Warnaco Inc. in 2002), Tomwell for ladies career wear (from Kasper Holdings Inc./Jones Apparel Group, Inc. in 2004) and the joint venture with Yue Yuen in 2004 for activewear, the Group has again expanded its product line through the acquisition of the 71% equity interest in Partner Joy Group Limited ("Partner Joy") in May 2005. Partner Joy, through its



three wholly owned subsidiaries in Hong Kong – Tien-Hu Knitters Limited, Tien-Hu Knitting Factory (Hong Kong) Limited and Tien-Hu Trading (Hong Kong) Limited (collectively referred to as “Tien-Hu”) – is principally engaged in the manufacturing and trading of sweaters. Tien-Hu has been in operation since the 1980s and its major customers include many renowned US brands. The acquisition gives Luen Thai a significant presence in the sweater segment and further consolidates the Group’s leading positions in the apparel industry.

In our effort to maximize growth from activewear, we have also recently acquired a production facility in Cebu, the Philippines through a joint venture with athletic footwear giant Yue Yuen Industrial (Holdings) Ltd. The acquired facility has already been renovated and has started operations in March this year.

In January 2006, Luen Thai entered into a 50%-50% joint venture agreement with Guangdong Foreign Trade Group Co., Ltd., the largest foreign trade group in Guangdong, China, to establish Shenzhen Guangthai International Co. Ltd. (“SGTI”). SGTI is expected to give Luen Thai a strong outsourcing platform in various products in China.

Moreover, Luen Thai entered into an agreement to acquire 50% stake in On Time International Limited and its subsidiaries (collectively, the “On Time Group”) on 10 March 2006 (the “Acquisition”), which is more particularly described in the Company’s announcement dated 16 March 2006. On Time Group is principally engaged in the design, sourcing and distribution on a worldwide basis of garments and other textile products. Established in the early 1990s, its headquarter is located in Hong Kong with offices in Asia Pacific. The Acquisition is expected to further enhance Luen Thai’s design capabilities, which along with its production scale, will speed up turnaround times and bring in more European business to the Group.



Acquisitions and joint ventures are one of Luen Thai’s core competencies considering our scale, management and strong customer relationships. We will continue to capitalize on these to become one of the major consolidators and beneficiaries in the “quota-free” era in the apparel industry.

CORPORATE GOVERNANCE

The Group acknowledges the need and importance of corporate governance as one of the key elements in creating shareholders’ value. The Group continuously improves its corporate governance policies in accordance with international best practices. As at the date of this report, the Company has formed the following committees at the Board level:

CEO REPORT

Audit Committee: The Audit Committee was set up to provide advice and recommendations to the Board. All Committee members are independent non-executive Directors namely: Mr. Chan Henry, Mr. Cheung Siu Kee and Mr. Seing Nea Yie as the Committee Chairman. Each Committee member possesses appropriate finance and/or industry expertise to advise the Board. The Audit Committee met three times in 2005 with 100% attendance rate.

Remuneration Committee: The Remuneration Committee was set up with the responsibility of recommending to the Board the remuneration policy of all Directors and the senior management. Mr. Tan Henry and the three independent non-executive Directors of the Company namely: Mr. Chan Henry, Mr. Cheung Siu Kee, and Mr. Seing Nea Yie as the Committee Chairman, comprise the Remuneration Committee.

Bank Facility Committee: The Bank Facility Committee was set up in December 2005 to review and approve any bank facility of the Group, to ensure that each facility is in the best commercial interest of the Group as a whole. Mr. Tan Siu Lin, Mr. Tan Henry and Mr. Tan Sunny comprise the Bank Facility Committee.

INVESTOR RELATIONS AND COMMUNICATION

The Group acknowledges the importance of communication with our shareholders. The Group has proactive policy of promoting investor relations through meetings with analysts and investors, and participation of international roadshows, investors' conferences, company interviews and manufacturing plant visits. All shareholders have no fewer than 21 days notice of the Annual General Meeting at which Directors shall be available to answer questions on the business.

The Group has established various forms of communication channels to improve the transparency of the Group including proactive and timely issuance of press releases so as to inform investors of our latest corporate development. The Group maintains a website (www.luenthai.com) in English and Chinese to disseminate information electronically on a timely basis to all concerned parties.

FINANCIAL RESULTS AND LIQUIDITY

As at 31 December 2005, the total amount of cash and bank balances of the Group was approximately US\$148,038,000, representing an increase of approximately US\$36,980,000 when compared to 31 December 2004. The total bank borrowings at 31 December 2005 was US\$83,687,000, representing a 14.1% decrease when compared to US\$97,392,000 at 31 December 2004.

As at 31 December 2005, the maturity profile of the Group's bank borrowings spread over two years with US\$83,301,000 repayable within one year or on demand and US\$386,000 in the second year.

The gearing ratio is defined as net debt (represented by bank borrowings net of cash and bank balances) divided by the capital and reserves attributable to the equity holders of the Company. As at 31 December 2005, the Group is in a net cash position. Hence, no gearing ratio is presented.

FOREIGN EXCHANGE RISK MANAGEMENT

The Group adopts a prudent policy to hedge the fluctuation of exchange rates. Most of the Group's operating activities are denominated in US dollars and Hong Kong dollars. For those activities denominated in other currencies, the Group may enter into forward contracts to hedge its receivable and payable denominated in foreign currencies against the exchange rate fluctuation.

CONTINGENT LIABILITIES AND OFF-BALANCE SHEET OBLIGATIONS

The Group is involved in various labour lawsuits and claims arising from the normal course of business. The Directors believe that the Group has substantial legal and factual bases for their position and are of the opinion that losses arising from these lawsuits, if any, will not have a material adverse impact on the results of the operations or the financial position of the Group. Accordingly, no provision for such liabilities has been made in the financial statements.

HUMAN RESOURCES, SOCIAL RESPONSIBILITIES, AND CORPORATE CITIZENSHIP

Luen Thai is becoming recognized by professionals in the industry as the company of choice to work for. As a business leader in people management, Luen Thai has developed well-planned work environments for its geographically diverse and multi-cultural workforce of about 23,000. The Group's operations are managed by a professional and multicultural management team whose specialties have been honed in the industry. This executive and management team is aligned to the Group's strategic objectives, business model and corporate values.

We promote customer-focused practices and wellness amenities so each employee can be treated with utmost care. We generate advancement opportunities across the organization through a wide array of technical training and leadership development programs. These help our teams develop their talent so they can contribute to the advancement of the Group and grow as leaders in their own right. In addition, the Group offers its staff competitive remuneration schemes. In addition, share options are granted to eligible employees as incentive for their contribution to the Group.



Luen Thai's pioneering of supply chain initiatives, quality assurance and employee care programs in the industry have been acknowledged by well recognized organizations and government bodies in the region.

CEO REPORT



This symbolizes our efforts in ensuring that our customers, employees, partners and stakeholders receive only the best products and services from us. In 2005, we received the Excellent Manufacturing Enterprise Award from the Trans-Century Dongguan & Hong Kong Association for our contributions to the development of Hong Kong, Dongguan and the Pearl River Delta industries.

Our corporate values help shape our social relationships and daily business decisions. In all our undertakings, we do our best to meet the expectations of the people in the community where we operate. At Luen Thai, we believe that service to the community is a core social responsibility.

We are honored to have contributed to broad-reaching community programs that support the environment, the families, and the education of the youth. Last year, Luen Thai key executives and employees worldwide raised over US\$111,000 for the victims of the tsunami that hit in 2004. Apart from this, we have supported numerous education, cultural, and social welfare activities of the Quanzhou Normal University in China, Po Leung Kuk, the Community Chest of Hong Kong, and the President's Relief Fund of Pakistan.

PROSPECTS

Looking forward to 2006, we expect our business to increase as order flows start to stabilize, with the enforcement of trade agreements between China and the USA/EU, and with the implementation of China's quota allocation system. Furthermore, we expect to gain on the current developments in the apparel industry on the strength of our product innovation capabilities and value-added services from design support, fabric development and logistics services. Along with our organic growth, the Group will continue to expand through acquisitions and joint ventures where we would strike a balance portfolio globally on customers/markets, product categories and countries of production. With newly acquired companies such as Partner Joy, SGTI and On Time Group, Luen Thai will further expand through outsourcing, in addition to internal capacity expansion. We believe that these would enable the Group to continue to sustain its growth in the coming years and will ultimately allow us to emerge as one of the major consolidators and beneficiaries in the "quota-free" era in the apparel industry, as we also continue to grow our market share with selected key customers through closer partnership based on multi-product and co-location strategies.

Operation of diversified manufacturing base in different countries is still important in servicing our customers in view of possible regulatory measures against China. However, as we recognize the importance of quality and lead-time to our customers, we expect our China operations to continue to play an important role in providing customer satisfaction. We believe that it has the required efficiency that will continue to aid Luen Thai's global competitiveness.

We expect the Group to benefit from its post-acquisition synergies, which are consistent with the Group's multi-country and multi-product strategy. The Group is currently in different stages of negotiation on acquisitions and joint ventures opportunities.