

Directors' Report

The directors present their annual report and the audited consolidated financial statements of the Company for the year ended December 31, 2005.

The shares of the Company were listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange") with effect from October 20, 2005.

PRINCIPAL ACTIVITIES

The Company acts as an investment holding company. Its subsidiaries are principally engaged in the processing of raw cowhides and wet blues into finished leather or fully assembled leather products.

RESULTS

The results of the Group for the year ended December 31, 2005 are set out in the consolidated income statement on page 35.

DIVIDENDS

The directors recommend 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 will be 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 are on the registers of members of the Company on May 30, 2006.

TRADING RESULT AND PUBLISHED FORECAST

The consolidated profit attributable to the equity holders of the Company for the year amounted to approximately RMB266 million, represents an excess of 2.3% of the profit forecast of approximately RMB260 million included in the Company's prospectus dated October 10, 2005. The difference is principally attributable to favourable sales variances in the fourth quarter of 2005.

DISTRIBUTABLE RESERVES OF THE COMPANY

The amount of the Company's reserves available for distribution to shareholders as at December 31, 2005, calculated in accordance with International Financial Reporting Standards, was approximately RMB1,004 million.

FINANCIAL SUMMARY

A summary of the results, assets and liabilities of the Group for the past financial periods is set out on page 3.

PROPERTY, PLANT AND EQUIPMENT

During the year, the Group acquired property, plant and equipment of approximately RMB231 million for the purpose of expanding its production capacity.

Details of these and other movements in the property, plant and equipment of the Group during the year are set out in note 15 to the financial statements.

Directors' Report (cont'd)

VALUATION OF PROPERTIES

In the prospectus dated October 10, 2005, the Company disclosed based on a valuation report, the valuation of its properties as of August 31, 2005 of approximately RMB1,044 million. The revalued amount of the properties has not been incorporated in the financial statements for the year ended December 31, 2005. These properties have been included in the consolidated balance sheet at December 31, 2005 at RMB758 million, being their historical cost less accumulated depreciation and accumulated impairment losses. Had the properties been stated at their revalued amount in the financial statements, additional depreciation of approximately RMB3 million would have been charged against the consolidated income statement.

SHARE CAPITAL

Details of the Company's share capital are set out in note 29 to the financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

During the year, the aggregate sales attributable to the Group's five largest customers comprised approximately 38.22% of the Group's total sales and the sales attributable to the Group's largest customer were approximately 10.72% of the Group's total sales.

The aggregate purchase during the year attributable to the Group's five largest suppliers was less than 30% of the Group's total purchases.

Two of the top five largest suppliers, Yili Horgos Leather Co., Ltd. and Baiyin Kasen Leather Co., Ltd are companies in which Mr. Zhu, Zhangjin, Chairman of the Group has beneficial interests. Yili Horgos Leather Co., Ltd. and Baiyin Kasen Leather Co., Ltd. are 45% and 90% owned by Zhejiang Sunbridge Industrial (Group) Co., Ltd., a company which Mr. Zhu indirectly controls over 30% of the voting power at general meeting.

Other than as disclosed above, none of the directors, their associates or any shareholders which, to the knowledge of the directors, owned more than 5% of the Company's issued share capital had any interest in the share capital of any of the five largest customers and suppliers of the Group.

DIRECTORS

The directors of the Company during the year and up to the date of this report are:

Executive directors

ZHU Zhangjin (*Chairman*)

ZHOU Xiaosong

ZHU Jianqi

JIANG Jianzhong

(resigned on June 17, 2005)

Non-executive director

SUN Qiang Chang

Directors' Report (cont'd)

Independent non-executive directors

HAN Ying	(appointed on June 17, 2005 and resigned on July 11, 2005)
LU Yungang	(appointed on June 17, 2005)
SHI Zhengfu	(appointed on June 17, 2005)
CHOW Joseph	(appointed on July 11, 2005)

In accordance with provision 87 of the Articles, Messrs. Zhou Xiaosong and Zhu Jianqi will retire from office of executive directors by rotation and, being eligible, will offer themselves for re-election at the forthcoming annual general meeting. Mr. Sun Qiang Chang will retire from office of non-executive director and will not offer himself for re-election at the forthcoming annual general meeting.

None of the directors being proposed for re-election at the forthcoming annual general meeting has a service contract with the Company or any of its subsidiaries which is not determinable by the Group within one year without payment of compensation (other than statutory compensation).

BRIEF DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Brief details of directors and senior management are set out on pages 5 to 8.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at December 31, 2005, the interests of the directors and chief executives of the Company in the shares of the Company (within the meaning of Part XV of the Securities and Futures Ordinance ("SFO")) as recorded in the register required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Companies (the "Model Code") are as follows:

Name of director	Capacity	Number of issued ordinary shares held	Percentage of the Company's issued share capital
Zhu Zhangjin	Beneficial owner	328,867,019	32.43%
Zhou Xiaosong	Beneficial owner	8,173,912	0.81%
Zhu Jianqi	Beneficial owner	7,478,260	0.74%

All the interests disclosed above represent long positions in the shares of the Company.

Save as disclosed herein, none of the directors nor the chief executives of the Company has any interests or short positions in any shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code as at December 31, 2005.

Directors' Report (cont'd)

SHARE OPTIONS

Particulars of the Company's share option scheme are set out in note 30 to the financial statements.

Subsequent to the balance sheet date, the board of directors of the Company granted 30,200,000 share options to certain directors and employees of the Company and the exercisable price of the share options was HK\$2.38 per share. The closing price of the Company's shares immediately before the date of grant was HK\$2.30 per share.

SUBSTANTIAL SHAREHOLDERS

As at December 31, 2005, the following persons (other than directors or chief executives of the Company stated in "Directors' and Chief Executives' Interests and Short Positions in Shares, Underlying Shares and Debentures") had interests or short positions in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO:

Name of Shareholder	Capacity	Short position	Long position	Number of issued shares held	Percentage
					of the Company's issued share capital
Warburg Pincus & Co. ¹	Interest of controlled corporation	–	186,989,966	186,989,966	18.44%
UBS AG	Beneficial owner	10,141,412	78,529,412	88,670,824	8.74%
Warburg Pincus Private Equity VIII L. P. ¹	Beneficial owner	–	90,605,988	90,605,988	8.94%
Griffin John Anthony	Beneficial owner	–	71,022,000	71,022,000	7.00%
Warburg Pincus Partners LLC ¹	Beneficial owner	–	186,989,966	186,989,966	18.44%
Warburg Pincus International Partners L.P. ¹	Beneficial owner	–	89,616,811	89,616,811	8.84%

Note 1: Warburg Pincus International Partners, L.P., and Warburg Pincus Private Equity VIII L.P. are part of the Warburg Pincus Funds. The general partner of the Warburg Pincus Funds is Warburg Pincus Partners LLC, which is a subsidiary of Warburg Pincus & Co. Each of Warburg Pincus Partners LLC and Warburg Pincus & Co. is therefore deemed to be interested in the shares held by the Warburg Pincus Funds, which includes Warburg Pincus International Partners, L.P. and Warburg Pincus Private Equity VIII L.P. as well as four other funds consisted in the Warburg Pincus Funds.

Save as disclosed herein, the Company has not been notified of any other person (other than a director or a chief executive of the Company) who had an interest or a short position in the shares and underlying shares of the Company as recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO as at December 31, 2005.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES

Other than the share option scheme disclosed in note 30 to the financial statements, at no time during the year was the Company or any of its subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares in, or debt securities (including debentures) of, the Company or any other body corporate.

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CONNECTED TRANSACTIONS

During the year ended December 31, 2005, the Group entered into the following transactions with its connected persons. The transactions are defined by the Listing Rules as "continuing connected transactions". Waivers from strict compliance with the announcement requirements, or the announcement and independent shareholders' approval requirements, had been received from the Stock Exchange. The transactions are subject to the reporting requirements set out in Chapter 14A of the Listing Rules.

(1) Agreement for purchase of sofa fabrics from Wansheng Silk

On January 1, 2005, Haining Wansheng Silk Waving Co., Ltd. ("Wansheng Silk") entered into an agreement with Haining Wansheng Furniture Co., Ltd. ("Wansheng Furniture") and Haining Kasen Leather Co., Ltd. ("Haining Kasen") which will expire on December 31, 2007 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for 3 year terms thereafter. Wansheng Silk is an associate of Mr. Sun Jianxin, the non-executive director of the Company, and therefore Wansheng Silk is a connected person of the Company. The pricing under this agreement is determined by reference to the prevailing market price. Details of this agreement have been set out in the prospectus of the Company dated October 10, 2005 ("the Prospectus").

Pursuant to this agreement, Wansheng Furniture and Haining Kasen purchase sofa fabrics for use in making upholstered furniture from Wansheng Silk. Wansheng Silk is a manufacturer of silk and other fabrics, suitable for use in sofas. During the year, the aggregate value of the transaction under this agreement was RMB9,895,000, within the estimate of RMB10,000,000 as disclosed in the Prospectus.

(2) Agreement for sale of production wastes to Yujie

On January 1, 2005, Haining Yujie Material Recycling Co., Ltd. ("Yujie") entered into an agreement with Zhejiang Kasen Industrial Co., Ltd. ("Zhejiang Kasen") which will expire on December 31, 2007 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for 3 year terms thereafter. Yujie is an 80% owned subsidiary of Zhejiang Sunbridge Industrial (Group) Co., Ltd. ("Sunbridge") and Sunbridge is a company in which Mr. Zhu Zhangjin indirectly controls more than 30% of the voting power at general meetings. The pricing under this agreement is determined by reference to the prevailing market price. Details of this agreement have been set out in the Prospectus.

Pursuant to this agreement, Yujie will purchase wastes (including residue leather, used tubs, hair and fat) from the Company's subsidiaries (including Zhejiang Kasen, Haining Kasen, Haining Home Impression Furniture Co., Ltd., Haining Schinder Tanning Co., Ltd., Haining Gaosheng Leather Co., Ltd. and Haining Kareno Furniture Co., Ltd.). Yujie is one of the largest recycling companies in Haining and is located near many of the Group's production facilities (all within approximately 10 km). The Company believes that by selling wastes to Yujie, the Group will achieve an efficient management of disposal logistics and an effective supervision of its employees in the sale of wastes. During the year, the aggregate value of the transaction under this agreement was RMB11,369,000, within the estimate of RMB16,000,000 as disclosed in the Prospectus.

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(3) Agreement for sale of upholstered furniture to Starcorp

On January 1, 2005, Starcorp Corporation Pty. Ltd. ("Starcorp") entered into an agreement with Zhejiang Kasen which will expire on December 31, 2007 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for 3 year terms thereafter. Starcorp is a 70% owned subsidiary of Sunbridge and Sunbridge is a company in which Mr. Zhu Zhangjin indirectly controls more than 30% of the voting power at general meetings. The pricing under this agreement is determined by reference to the prevailing market price. Details of this agreement have been set out in the Prospectus.

Pursuant to this agreement, Zhejiang Kasen will through its subsidiaries (including Haining Kareno Furniture Co., Ltd., Haining Home Impression Furniture Co., Ltd. and Haining Home Point Furniture Co., Ltd.) sell upholstered furniture to Starcorp. Starcorp's core business is retail sales of wooden and other upholstered furniture in Australia and the Company considers that this provides a good opportunity for the Group to increase its sales of the upholstered furniture in the Australian market. During the year, the aggregate value of the transaction under this agreement was RMB57,443,000, within the revised estimate of RMB58,000,000 as disclosed in the announcement dated December 22, 2005.

(4) Agreement for purchase of wet blues from Kezilesu Xinrong, Yili Horgos and Baiyin Kasen

On January 1, 2005, Kezilesu Xinrong Leather Co., Ltd. ("Kezilesu Xinrong"), Yili Horgos Leather Co., Ltd. ("Yili Horgos") and Baiyin Kasen Leather Co., Ltd. ("Baiyin Kasen") entered into an agreement with Zhejiang Kasen which will expire on December 31, 2007 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for 3 year terms thereafter. Kezilesu Xinrong, Yili Horgos and Baiyin Kasen are each a subsidiary of Sunbridge and Sunbridge is a company in which Mr. Zhu Zhangjin indirectly controls more than 30% of the voting power at general meetings. The pricing under this agreement is determined by reference to the prevailing market price. Details of this agreement have been set out in the Prospectus.

Pursuant to this agreement, the Company will purchase wet blues from Kezilesu Xinrong, Yili Horgos and Baiyin Kasen. Kezilesu Xinrong, Yili Horgos and Baiyin Kasen are the largest importer of raw cowhides in Southern Xinjiang, Northern Xinjiang and Gansu Provinces respectively, and process such raw cowhides into wet blues. The Group needs to source wet blues externally from time to time and it would also be an advantage in saving transportation and handling costs for the Group if the processing and enhancement of raw cowhides into wet blues were performed near the place of origin of the raw cowhides. During the year, the aggregate value under this agreement for the purchases of wet blues from Kezilesu Xinrong, Yili Horgos and Baiyin Kasen were RMB35,981,000, RMB108,522,000 and RMB148,680,000 respectively. The aggregate of these purchases are within the estimate of RMB460,000,000 as disclosed in the Prospectus.

Pursuant to Rule 14A.38 of the Rules Governing the Listing Securities on the Stock Exchange of Hong Kong, the board of directors engaged the auditors of the Company to perform certain agreed upon procedures in respect of the continuing connected transactions of the Group. The auditors have reported their factual findings on these procedures to the board of directors.

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In the opinion of the independent non-executive directors, the continuing connected transactions entered into by the Group were:

- (i) in the ordinary and usual course of business of the Group;
- (ii) either (a) on normal commercial terms; or (b) where there is no available comparison, on terms that are no less favorable to the Group than terms to or from independent third parties; and
- (iii) in accordance with the agreements governing the transactions on terms that are fair and reasonable so far as the shareholders of the Company.

Save as disclosed above, there were no other transactions which need to be disclosed as connected transactions in accordance with the requirements of the Listing Rules from October 20, 2005 to December 31, 2005.

On December 22, 2005, the Group revised its annual cap in respect of continuing sales transactions with Starcorp Corporation Pty. Ltd, a company in which Mr. Zhu Zhangjin has beneficial interests through Zhejiang Sunbridge Industrial (Group) Co., Ltd, for the year ended December 31, 2005. On February 22, 2006, the Group entered into agreements with North Pole Ltd. and North Pole (China) Ltd., which are subsidiaries of a shareholder of the Company for the continuing sales transactions. The annual cap in respect of the continuing transactions for the three years ending December 31, 2008 are RMB250 million, RMB500 million, and RMB800 million respectively.

DIRECTORS' INTEREST IN CONTRACTS

Save as disclosed under the heading "Connected Transactions", there were no contracts of significance to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly and indirectly, subsisted at the end of the year or at any time during the year.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

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.

SUFFICIENCY OF PUBLIC FLOAT

Based on information that is available to the Company and within the knowledge of its directors, the Company has maintained sufficient public float as required under the Listing Rules from October 20, 2005 to December 31, 2005.

DIRECTORS' INTERESTS IN COMPETING BUSINESS

None of the Directors hold any interests in any competing business against the Company or any of its jointly-controlled entities and subsidiaries for the year ended December 31, 2005.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's Article of Association, or the laws of the Caymans Islands, which would oblige the Company to offer new shares on a pro-rata basis to existing shareholders.

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INDEPENDENT NON-EXECUTIVE DIRECTORS' CONFIRMATION OF INDEPENDENCE

The Company has received, from each of the independent non-executive directors, Messrs. LU Yungang, CHOW Joseph, SHI Zhengfu, a confirmation of his independence pursuant to Rule 3.13 of the Listing Rules. The Company considers all of the independent non-executive directors are independent.

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 two independent non-executive directors and a non-executive director of the Company. Mr. SUN Qiang Chang is the chairman of the Remuneration Committee.

AUDITORS

A resolution will be submitted to the annual general meeting of the Company to re-appoint Messrs. Deloitte Touche Tohmatsu as auditors of the Company.

On behalf of the Board

ZHU Zhangjin

Director

Hong Kong, April 19, 2006