卡森國際控股有限公司

KASEN INTERNATIONAL HOLDINGS LIMITED

(an exempted company incorporated in the Cayman Islands with limited liability)

stock code : 496

ANNUAL REPORT 2007

Contents

Corporate Information

BOARD OF DIRECTORS

Executive Directors

ZHU Zhangjin, Kasen
(Chairman & Chief Executive Officer)
ZHOU Xiaosong
ZHU Jianqi

Non-Executive Director

LI Hui, David

Independent Non-Executive Directors

LU Yungang, Ken
CHOW Joseph
ZHANG Huaqiao, Joe

COMPANY SECRETARY AND QUALIFIED ACCOUNTANT

YIU Hoi Yan, Kate

STOCK CODE

0496.HK

REGISTERED OFFICE

Cricket Square
Hutchins Drive
P.O. Box 2681
Grand Cayman KY1-1111
Cayman Islands

HEAD OFFICE AND PRINCIPAL PLACE OF BUSINESS

259 Qianjiang Road West
Haining City
Zhejiang Province 314400
China

PLACE OF BUSINESS IN HONG KONG

Room 1605
Tai Tung Building
8 Fleming Road
Wanchai
Hong Kong

PRINCIPAL BANKERS

Industrial and Commercial Bank of China,
Zhejiang Province Branch
China Construction Bank, Haining Sub branch
Bank of China, Haining Sub branch
Agricultural Bank of China, Haining Sub branch
Communication Bank of China, Haining Sub branch
Agricultural Development Bank of China,
Haining Sub branch
Hongkong and Shanghai Banking Corporation Limited
Standard Chartered Bank (Hong Kong) Limited

LEGAL ADVISORS

As to Hong Kong law
Sidley Austin

As to Cayman Islands law
Conyers Dill & Pearman

PRINCIPAL SHARE REGISTRAR

Butterfield Fund Services (Cayman) Limited
Butterfield House
68 Fort Street
P.O.Box 705
Grand Cayman KY1-1107
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR

Computershare Hong Kong Investor Services Limited
Shops 1712-16, 17th Floor
Hopewell Centre
183 Queen's Road East
Wanchai
Hong Kong

AUDITORS

Deloitte Touche Tohmatsu
35th Floor, One Pacific Place
88 Queensway
Hong Kong

AUTHORISED REPRESENTATIVES

ZHU Jianqi
YIU Hoi Yan, Kate

COMPANY WEBSITE

http://www.kasen.com.cn
http://www.irasia.com/listco/hk/kasen/index.htm

Financial Highlights

RESULTS

	For the year ended December 31,				
	2007	2006	2005	2004	2003
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Turnover	**3,310,727**	3,916,513	3,475,457	2,852,391	2,135,498
(Loss) profit before taxation	**(175,440)**	105,134	278,665	257,176	281,934
(Loss) profit attributable to equity holders of the Company	**(194,149)**	64,143	265,699	225,701	199,323

FINANCIAL POSITION

	At December 31,				
	2007	2006	2005	2004	2003
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Cash and cash equivalents	**508,850**	380,973	372,278	213,458	410,293
Total borrowings	**1,580,864**	1,257,089	1,291,738	1,880,251	1,338,681
Total assets	**4,139,450**	4,074,528	4,441,690	4,036,944	2,634,285
Total liabilities	**2,169,604**	1,891,551	2,143,824	2,835,568	1,917,225
Equity attributable to equity holders of the Company	**1,917,154**	2,108,865	2,199,560	1,091,104	557,247

FINANCIAL AND OPERATING RATIOS

	At December 31,				
	2007	2006	2005	2004	2003
Dividend payout ratio (%)[1]	**–**	54.5%	30%	–	–
Debt to equity ratio (%)[2]	**80.3%**	57.6%	56.2%	156.5%	186.7%
Net debt to equity ratio (%)[3]	**54.4%**	40.1%	40.0%	138.7%	129.5%
Trade receivable turnover days[4]	**43**	46	54	35	38
Inventory turnover days[5]	**146**	139	172	211	134
Current ratio[6]	**118.7%**	135.4%	138.3%	93.7%	101.9%
(Loss) earning per share (RMB)					
Basic	**(0.20)**	0.06	0.41	0.47	0.46
Diluted	**(0.20)**	0.06	0.34	0.35	0.40

Notes:

1. The dividend per ordinary share divided by the profit (loss) attributable to equity holders of the Company per ordinary share.
2. Interest-bearing debt divided by total equity as at the end of the year.
3. Interest-bearing debt minus bank balances and cash divided by the total equity as at the end of each year.
4. Trade receivables as at the end of the year divided by turnover and multiplied by 365 days.
5. Inventories as at the end of the year divided by cost of sales and multiplied by 365 days.
6. Current assets divided by current liabilities as at the end of each year.
7. The adoption of new accounting standards in 2007 has no material impact to the Group.

Directors and Management Profiles

EXECUTIVE DIRECTORS

ZHU Zhangjin, Kasen (朱張金), aged 42, is our founding Chairman and Chief Executive Officer. Before founding our Company in 1995, Mr. Zhu was involved in several business ventures in the areas of textile, leather processing, garment, trading, etc. With over 20 years of experience in the leather manufacturing industry, Mr. Zhu has extensive knowledge in the upholstered furniture industry in the PRC and has been a successful entrepreneur in leather manufacturing related businesses. Mr. Zhu is also the vice chairman of the China Leather Association. In recognition of his contribution to promote the development of the leather manufacturing industry, Mr. Zhu was awarded the "Top Ten Businessmen in Zhejiang" in 2004. In 2006, Mr. Zhu was one of the 10 recipients of the prestigious "National May 4th Youth Award (全國五四青年獎)". In 2007, Mr. Zhu received the National May Day Award.

ZHOU Xiaosong (周小松), aged 52, joined our Company on June 12, 1995 and is an executive Director, vice president, and general manager of our Leather Manufacturing Division. Mr. Zhou has spent more than 18 years in the leather manufacturing industry. He is now the director of our research and development center. Mr. Zhou obtained a diploma in Economics and Management from the Adult College of Hangzhou University in 1999. In 2005, Mr. Zhou was appointed as an arbitrator by the China International Economic and Trade Arbitration Commission (CIETAC).

ZHU Jianqi (祝建其), aged 47, joined our Company on May 1, 1996 and is an executive Director, vice president, and general manager of our Treasury and Finance Departments. Prior to joining our Company, he served as the deputy director and deputy manager of the Qingyun Town Industrial Office. He has more than 22 years of experience in the accounting and financial fields. Mr. Zhu graduated from the business management master program of the Zhejiang University of Technology in 2002. In 2003, he received a diploma in Economics from the China University of Geosciences.

NON-EXECUTIVE DIRECTOR

LI Hui, David (黎輝), aged 39, joined our Company as a non-executive Director on May 30, 2006. Mr. Li is currently a managing director of Warburg Pincus Asia LLC, a leading private equity and venture capital firm. Mr. Li has been with Warburg Pincus since 2002. Before joining Warburg Pincus, Mr. Li was an executive director of the investment banking division of Goldman Sachs (Asia) LLC and a vice president and an associate of Morgan Stanley's investment banking division in Hong Kong and New York. Mr. Li obtained his Bachelor of Science degree in Economics from Renmin University of China and a Master of Business Administration ("MBA") from Yale University's School of Management.

INDEPENDENT NON-EXECUTIVE DIRECTORS

LU Yungang, Ken (陸運剛), aged 45, joined our Company as an independent non-executive Director on June 17, 2005. Mr. Lu is currently founder and managing director of APAC Capital Advisors Limited ("APAC"), a Hong Kong based investment management company that specializes in Greater China equities, as well as a director of AsiaInfo Holdings, Inc. Prior to setting up APAC, Mr. Lu has worked with financial institutions including Credit Suisse First Boston, JP Morgan Securities Asia Inc. and Schroders Asia Limited, holding various posts including Head of China Research when he was with Credit Suisse First Boston. Mr. Lu obtained his Bachelor of Science degree from the Beijing University in July 1985 and his Master of Science degree from the Brigham Young University, Provo, Utah in 1991. He obtained a Ph.D. in Management from the University of California in September 1998.

CHOW Joseph (周凡), aged 45, joined our Company as an independent non-executive Director on July 11, 2005. Mr. Chow is currently a consultant in the fields of finance, accounting and investment, and has held senior managerial positions in various companies, including as Chief Financial Officer of Harbour Networks Limited, Chief Financial Officer with China Netcom (Holdings) Company Limited, director of strategic planning with Bombardier Capital Inc., vice president of international operations with Citigroup and corporate auditor at GE Capital. Mr. Chow obtained a Bachelor of Arts degree in Political Science from Nanjing Institute of International Relations in 1984 and a MBA from the University of Maryland at College Park in 1993.

ZHANG Huaqiao, Joe (張化橋), aged 45, joined our Company as an independent non-executive Director on July 3, 2006. Mr. Zhang is currently an executive Director and Chief Operating Officer at Shenzhen Investment Limited, a company listed on The Stock Exchange of Hong Kong Limited (the "Stock Exchange"). He is also a non-executive Director of Shenzhen International Holdings Limited, Hong Long Holdings, Coastal Greenland Limited, Concepta Investment Limited and Tak Sing Alliance Holdings, all of which companies are listed on the Stock Exchange. Mr. Zhang holds a Master of Economics degree from the Australian National University, a Master of Economics in Banking and Finance degree from the Graduate School of the People's Bank of China and a Bachelor of Economics (Finance) degree from Hubei Institute of Finance and Economics. Mr. Zhang's most recent position was a managing director and co-head of China Research at UBS Securities Asia Limited where he worked for seven years.

SENIOR MANAGEMENT

ZHONG Jian (鍾劍), aged 37, joined our Company as vice president on August 1, 2007 and took up the position of Chief Financial Officer on September 30, 2007. Mr. Zhong received a Bachelor of Finance degree from the Central University of Finance and Economics in 1992 and a Master of International Finance from Renmin University of China in 2002. Mr. Zhong's most recent position was vice president and Chief Financial Officer at Zhejiang Sunbridge Industrial Group Company Limited where he worked from July 2004 to July 2007. He also worked as director of corporate finance department in Export and Import Bank of China.

YU Guanlin (余關林), aged 45, joined our Company in 1995 and has held positions as production manager and deputy general manager. He is currently the general manager for our Cut-and-sew Operations. Before joining our Company, Mr. Yu founded a garment company and was responsible for its design and production. Mr. Yu has extensive knowledge and experience in upholstered furniture manufacturing.

ZHANG Mingfa, Michael (張明發), aged 47, joined our Company on October 1, 1997 as vice president of our Import and Export Division. With more than 27 years of experience in the leather manufacturing industry, Mr. Zhang is currently the Company's Director of Logistics. Mr. Zhang qualifies as an international business engineer based on a qualification certificate approved by the Ministry of Commerce of the PRC in 1995. In 1984, Mr. Zhang obtained a diploma from Chengdu University of Technology. In 1989, Mr. Zhang obtained a diploma in Business Administration from Zhejiang University of Technology.

ZHANG Guming (張顧明), aged 42, joined our Company in 2003 and has held positions as general manager of our sofa manufacturing subsidiaries. He is currently the Director of Human Resources. Before joining our Company, Mr. Zhang was the executive deputy general manager at Haining Dunnu Fashion Co., Ltd from May 2000 to February 2003. Prior to that, Mr. Zhang had been responsible for production management in several local companies that manufactured leather, footwear and textile. Mr. Zhang has extensive knowledge and experience in corporate management and the leather industry. In 2001, he received a MBA from a joint program organized by the Shanghai University of Finance and Economics and the Webster University of the US.

JIN Xuejiang (金雪江), aged 44, joined our Company in 2001 and has held positions as plant manager and deputy general manager. He is currently the assistant general manager of Sofa Business Division. Before joining our Company, Mr. Jin founded a footwear company and was responsible for its production and sales. Mr. Jin obtained a diploma in Management from Haining Television University in 2005 and has been on a part-time Master of Business Administration course at the Management School of Zhejiang University since September 2005. Mr. Jin has extensive knowledge and experience in upholstered furniture manufacturing.

COMPANY SECRETARY AND QUALIFIED ACCOUNTANT

YIU Hoi Yan, Kate (姚凱欣), aged 35, joined our Company as an accountant on April 29, 2004 and was later promoted to be our Company Secretary, Qualified Accountant and finance and administrative manager. She has over 12 years of experience in auditing and accounting. She is a member of the ACCA and the Hong Kong Institute of Certified Public Accountants. Ms. Yiu obtained a Bachelor of Arts (Honors) in Accountancy from the City University of Hong Kong in 1995.

Chairman's Statement

Dear Shareholders,

On behalf of the Board of Directors (the "Board"), I would like to present the annual results of the Company and its subsidiaries (the "Group") for the year ended December 31, 2007.

For the year ended December 31, 2007, the Group's turnover amounted to RMB3,310.7 million, representing a decrease of 15.5% as compared to RMB3,916.5 million for the previous year. The Group suffered a loss attributable to equity holders of RMB194.1 million. The Board did not recommend the payment of a final dividend.

2007 has been a tough year for the Group. As a major original equipment manufacturer ("OEM") partner for the US upholstered furniture industry, our sales were adversely impacted by the slow down in the US housing market and subprime loan crises. The steady appreciation of RMB against US dollar, along with the acceleration of raw material and labor costs, had also led to a further squeeze on our gross profit margin. Anticipating these adverse impacts will likely deteriorate in 2008, the Group decided to write off its goodwill and make a provision for the impairment of machinery equipment and inventory.

Despite unfavorable market conditions, the Group remains committed to improve its business performance and to increase shareholders' value. Going forward, the Group will make every effort to strengthen its position as China's leading manufacturer of leather products and upholstered furniture. In the meantime, the Group will be actively seeking business opportunities in other sectors to diversify its revenue resources.

The Group is entering into the commercial real estate sector through the development of specialized leather product and furniture retail malls in major cities in China. The Group is also looking into opportunities in residential housing development to leverage its land resources. The Group is well aware of the risks and will ensure that these new property development projects would bring more value to its shareholders.

I would like to express my gratitude to my fellow directors, management team and employees for their contribution and dedication to the Group and deep thanks to our shareholders, customers, suppliers and business partners for their continuing support during these difficult times.

ZHU Zhangjin, Kasen
Chairman

The PRC, April 15, 2008

Management Discussion and Analysis

All financial figures and ratios in the following discussion include the financial figures of the assets/liabilities held for sale. For more details about this assets/liabilities held for sale, please refer to note 13 to the consolidated financial statements.

RESULTS OVERVIEW

For the year ended December 31, 2007, the Group recorded a consolidated turnover of RMB3,310.7 million, representing a decrease of 15.5% compared with RMB3,916.5 million of year 2006.

The Group's gross profit margin in 2007 was 9.0%, representing a decrease of 1.9 percentage point as compared to 2006.

For the year ended December 31, 2007, the Group recorded a loss of RMB190.0 million (2006: profit of RMB83.4 million); loss attributable to equity holders of the Company was RMB194.1 million (2006: profit attributable to equity holders of the Company of RMB64.1 million). During the year under review, the Group assessed the recoverable amounts of goodwill from previous acquisitions. Due to the anticipated deterioration of its business environment and further reduction in forecasted furniture sales, the Group determined that goodwill associated with the Group's upholstered furniture operation subsidiaries were impaired by an aggregate of RMB158.0 million in 2007 (2006: RMB23.0 million). In addition, the Group increased its impairment provision for inventory from RMB11.4 million in 2006 to RMB99.6 million in 2007 as the net realisable value of certain types of leather was reduced due to the reduction in market demand.

SALES ANALYSIS BY PRODUCTS

The table below shows the total turnover by product category for the year ended December 31, 2007:

	2007		2006		**Y-O-Y Change**
	RMB'Million	**%**	RMB'Million	%	%
Upholstered Furniture					
Leather Sofa	**1,653.3**	**49.9%**	1,841.5	47.0%	-10.2%
Fabric Sofa	**313.2**	**9.5%**	408.1	10.4%	-23.3%
Leather Cut-and-Sew	**428.7**	**12.9%**	626.2	16.0%	-31.5%
Fabric Cut-and-Sew	**178.7**	**5.4%**	247.1	6.3%	-27.7%
Furniture Leather	**461.3**	**13.9%**	615.1	15.7%	-25.0%
Automotive Leather	**217.9**	**6.6%**	150.1	3.8%	45.2%
Others	**57.6**	**1.8%**	28.4	0.8%	103.5%
Total	**3,310.7**	**100%**	3,916.5	100%	-15.5%

Upholstered Furniture

Sales of upholstered furniture including finished sofa and sofa cut-and-sew accounted for 77.7% of the Group's total revenue for the year ended December 31, 2007 (2006: 79.7%). The subprime crises and downturn in the US housing market severely affected the sales of home furnishing and furniture products. Most of the Group's major US customers have experienced difficulties in their business. This has in turn affected the Group's sales.

In order to consolidate its manufacturing facilities and to increase the utilization rates of its facilities, the Group disposed of its interests in two sofa manufacturing subsidiaries in Haining, Zhejiang province, and suspended another factory in Shanghai. This has further impacted the Group's sales.

As a result of the above, the Group's upholstered furniture sales experienced a decrease of 17.6%, from RMB3,122.9 million in 2006 to RMB2,573.9 million in 2007.

Furniture Leather

The Group's priority in furniture leather production is to meet the internal leather requirement of its upholstered furniture division. Due to the increase in manufacturing costs and the slow down in export-oriented upholstered furniture industry, the Group's external sales of furniture leather decreased by 25.0%, from RMB615.1 million in 2006 to RMB461.3 million in 2007.

Automotive Leather

The automotive leather operation achieved a 45.2% increase in turnover for the year ended December 31, 2007. Due to the reduction in tax rebates in 2007 for finished leather exports from 8% to nil, the Group's automotive leather export was severely affected. However, the Group's efforts in domestic market expansion over the years have started to take effect, as domestic sales recorded a 224.4% increase, from RMB28.8 million in 2006 to RMB93.4 million in 2007.

SALES ANALYSIS BY REGION

The table below shows the total turnover by geographic market for the year ended December 31, 2007:

	2007		2006		**Y-O-Y Change**
	RMB'Million	**%**	RMB'Million	%	%
USA	**2,041.1**	**61.7%**	2,825.8	72.2%	-27.8%
Europe	**293.5**	**8.9%**	160.3	4.1%	83.1%
Australia	**100.5**	**3.0%**	122.3	3.1%	-17.8%
PRC, including HK	**792.3**	**23.9%**	736.1	18.8%	7.6%
Others	**83.3**	**2.5%**	72.0	1.8%	15.6%
Total	**3,310.7**	**100%**	3,916.5	100.0%	-15.5%

For the year ended December 31, 2007, the Group's sales to the US market declined by 27.8%, and the percentage of US sales to total turnover reduced to 61.7%, representing a 10.5 percentage points drop as compared to the year of 2006. This decrease was mainly due to the US housing market downturn which had led to slower residential furniture sales.

The Group's expansion into the European market is still ongoing. In 2007, the Group was able to grow its upholstered furniture business in Europe by 83.1%, and this segment accounted for 8.9% of the Group's total turnover as compared to 4.1% in 2006.

The Group's sales to Australia market decreased by 17.8%, from RMB122.3 million in 2006 to RMB100.5 million in 2007.

In 2007, the Group's sales to the PRC domestic market mainly involved furniture leather, automotive leather and upholstered furniture, the turnover of which represented 23.9% of its total sales.

GROSS MARGIN ANALYSIS

The Group's gross profit margin in 2007 was 9.0%, representing a decrease of 1.9 percentage point as compared to 2006.

The Group's gross profit margin has continuously been under pressure as a result of the following factors: (1) the continued appreciation of RMB has been a major adverse factor for the Group's profitability as more than 80% of the Group's sales is denominated in US dollar; (2) although the price of raw cowhides and wet-blues, which accounts for about 45% of the Group's cost of sales, have stabilized during the year of 2007, it was still well above its historical average by 20%; (3) with the inflation of commodities prices, costs of chemicals, foam, timber and labor, experienced increases; (4) export tax rebates were reduced as part of China government's initiative in reducing its massive trade surplus; (5) the government further tightened its environmental protection policies, resulting an increase in the Group's waste treatment costs; and (6) the Group increased its impairment provision for inventory from RMB11.4 million in 2006 to RMB99.6 million in 2007 as the net realisable value of certain types of leather was reduced due to the reduction in market demand.

However, the Group has taken several steps to mitigate the negative impact of the above factors to its gross profit margin. Those steps included price increases for some finished products, the termination of loss-making items, and improved cost management for the production processes.

OPERATING EXPENSE, TAXATION AND LOSS ATTRIBUTABLE TO EQUITY HOLDERS

The Group's selling and distribution costs in 2007 increased to RMB116.7 million, compared to RMB107.9 million in 2006, due mainly to an increase of RMB7.5 million in operating lease rentals for the Kasen Home Furnishing Stores in Shanghai and Hangzhou. As a result, the percentage of selling and distribution costs to turnover rose from 2.8% in 2006 to 3.5% in 2007.

The administrative costs were RMB168.8 million in 2007, with a small decrease of 1.4% as compared to RMB171.1 million in 2006. The decrease was resulted from a decrease of RMB13.0 million in share option related expenses and a decrease of RMB7.3 million in bad debt provision, offset by an increase of RMB8.9 million in the net foreign exchange losses.

The other expenses were RMB168.9 million in 2007, an increase of RMB138.9 million as compared to RMB30.0 million in 2006. The increase was mainly attributable to RMB158.0 million goodwill impairment and RMB7.0 million property, plant and equipment impairment. During the year under review, the Group assessed the recoverable amount of goodwill arising from previous acquisitions. Due to the anticipated deterioration of its business environment and further reduction in forecasted furniture sales, the Group determined that goodwill associated with the Group's upholstered furniture operation subsidiaries were impaired by an aggregate of RMB158.0 million in 2007 (2006: RMB23.0 million). For details, please refer to note 16 to the Consolidated Financial Statements.

The Group's finance cost in 2007 increased by RMB6.2 million or 7.2% compared to year 2006 as (1) the Chinese central bank gradually raised the basic lending rate from 6.12% at the beginning of 2007 to 7.47% at the end of 2007; (2) the Group increased its bank borrowings.

The Group's income tax in 2007 decreased by RMB7.1 million or 32.8% compared to year 2006, due to the decrease in the Group's profit at subsidiary level. Goodwill impairment, fixed assets impairment, provision for inventory and bad debts have not been deducted for PRC tax computation.

For reasons mentioned above, the loss attributable to equity holders of the Company was RMB194.1 million in 2007, compared to profit attributable to equity holders of RMB64.1 million in 2006.

CAPITAL EXPENDITURES

Capital expenditure in 2007 decreased by 4.6% to RMB102.3 million (2006: RMB107.3 million), which was mainly comprised of a deposit of RMB19.3 million paid for the acquisition of office in Hangzhou, and an amount of RMB40.0 million spent on the purchase of property, plant and equipment for operational purposes. In addition, the Group spent RMB43.0 million to acquire 4.92% equity interests in Haining Leather Market.

PROPERTIES FOR DEVELOPMENT

As at December 31, 2007, the Group held the land use right of two parcels of land in the PRC, which were to be utilized for property development. The land in Boao, Hainan Province, with a total of site area of approximately 139,669 square metres, which acquired in 2006 and incurred total cost of RMB45,329,000 as at December 31, 2007. The land in Changsha, Hunan Province, with a total site area of approximately 145,078 square metres, was acquired in 2007 at a total cost of RMB263,781,000. The Group revalued these two parcels of land at the end of the year under review. The appreciated value in the amount of RMB5,671,000 was recorded as properties for development as at December 31, 2007.

FINANCIAL RESOURCES AND LIQUIDITY

Bank borrowings

As at December 31, 2007, the Group's bank borrowings amounted to RMB1,570.5 million, representing an increase of 26.0% from RMB1,246.7 million as at December 31, 2006. For details, please refer to note 31 to the Consolidated Financial Statements.

Turnover Period, Liquidity and Gearing

The Group's inventory primarily composed of raw cowhides and wet blues used for production, accounting for approximately 47.8% of the total inventory of RMB1,205.8 million (2006: RMB1,326.2 million). Due to the decrease in sales, the Group's inventory turnover period in 2007 increased to 146 days (2006: 139 days).

In 2007, the Group continued to maintain a strict credit policy, resulting in a decrease in account receivables turnover days to 43 days (2006: 46 days).

The accounts payable turnover days had a slight increase to 52 days in 2007 (2006: 51 days).

As at December 31, 2007, the Group's current ratio and quick ratio decreased to 1.19 (December 31, 2006: 1.35) and 0.63 (December 31, 2006: 0.65), respectively. The Group's cash and cash equivalent balance was RMB508.9 million (December 31, 2006: RMB381.0 million). This represents a gearing ratio of 79.7% (December 31, 2006: 57.1%) and a net debt-to-equity ratio of 53.9% (December 31, 2006: 39.7%). The increase in gearing ratio was resulted from increased bank borrowings for the purchase of lands for property developments. The Group intends to fund its property development projects with cash generated from operations and external financing. The gearing ratio is based on bank borrowings to shareholders' equity and the net debt-to-equity ratio is based on bank borrowings net of cash and cash equivalent to shareholders' equity.

MATERIAL ACQUISITION AND DISPOSAL

The Group had disposed of its interests in two subsidiaries in 2007 in order to increase its sofa production facility capacity utilization and acquired 4.92% equity interests in Haining Leather Market as a strategic expansion into domestic leather market. For details, please refer to notes 23, 35 and 36 to the Consolidated Financial Statements.

CONTINGENT LIABILITIES

As at December 31, 2007, the Group had certain contingent liabilities. For details, please refer to note 42 to the Consolidated Financial Statements.

PLEDGE OF ASSETS

Certain assets of the Group have been pledged to secure the bank borrowings of the Group. For details, please refer to note 38 to the Consolidated Financial Statements.

FOREIGN EXCHANGE EXPOSURE

RMB appreciated approximately 3.4% and 6.5%, respectively against US dollar in 2006 and 2007. The Group is principally engaged in export-related business and transactions (including sales and procurements) entered into by the Group were mainly denominated in US dollar, and most of its trade receivables was exposed to fluctuation in 2007. The Group used forward contract and some other financial instruments to hedge foreign exchange risk, and recorded a gain of RMB18.1 million.

EMPLOYEES AND EMOLUMENTS POLICIES

As at December 31, 2007, the Group employed a total of approximately 11,000 full time employees (2006: 14,800) including management staff, technicians, salespersons and workers. For the year ended December 31, 2007, the Group's total expenses on the remuneration of employees is RMB270.2 million (2006: RMB286.7 million) and represents 8.16% (2006: 7.32%) of the turnover of the Group. The Group's emolument policies for employees are formulated on the performance of individual employees, which will be reviewed regularly every year. Apart from the provident fund scheme (according to 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.

The emolument policy of the employees of the Group is formulated by the Board with reference to their respective qualification and experience, responsibilities undertaken, contribution to the Group, and the prevailing market level of remuneration of similar position. The emoluments of the Directors are decided by the Board and the Remuneration Committee, who are authorized by the shareholders in the annual general meeting, having regard to the Group's operating results, individual performance and comparable market statistics.

KEY RISK FACTORS

Exchange Risk

As the Group is principally engaged in export-related business and transactions entered into by the Group are primarily denominated in US dollar (approximately 80%), management considers the Group is exposed to foreign exchange fluctuation risks. Although a substantial portion of the Group's procurements is denominated in US dollar and currency risks can be partly reduced, the Group is still subject to great effects of exchange rate fluctuations. The Group monitors its foreign exchange exposure and utilized appropriate financial instruments for hedging purposes.

Commodities Risk

Raw cowhides and wet-blues are the principal raw materials of the Group's business, accounting for approximately 45% of the Group's cost of sales. As such, the Group is exposed to the fluctuations in the price of cattle raw hides. During the past 24 months, the increase of raw cowhides prices in the global market has adversely affected the Group's profitability. Although the cowhide prices have stabilized, they are still well above its historical average. The Group remains cautious about the future trend of cowhide prices.

Cyclical Demand for Furniture

Historically, the furniture industry was cyclical in nature, fluctuating with economic cycles, and was sensitive to general economic conditions, home buying, interest rate levels, etc. The downturn in the US housing market has adversely impacted the Group's sales to this major market. The current financial uncertainties in the US may prolong and can further depress the market conditions for residential furniture.

Export VAT Rebates

In order to reduce its massive trade surplus, the Chinese government has gradually reduced its export VAT rebates for many business sectors. Started from July 1, 2007, export VAT rebates for all of the Group's product segments were reduced, from 8% to nil for finished leather, from 13% to 5% for leather cut-and-sew, and from 13% to 11% for finished sofa. These reductions had affected the Group's profitability. There may be further reductions that will continue to affect the Group's profitability.

Processing Trade Policy Change

Since 2006, the Chinese government has been introducing changes to the processing trade ("加工貿易") policy – such as moving certain widely used materials to the prohibited category – aimed at restricting the production and export of high pollution, high energy consumption and resource consuming products. Pursuant to the latest policy implemented by the PRC government in July 2007, enterprises engaged in the processing trade industry in the prohibited category are required to pay a mandatory duty deposit for imported raw materials. As the Group's products fall into the category of prohibited industry, it will be required to pay a substantial amount of duty deposit to the PRC customs. This will cause adverse impact to the Group's cash flow and will incur increased financial costs.

Environmental Risk

The production of leather is pollutive. As the Chinese government is tightening the environmental protection policies, the Group's production activities will be put under close scrutiny. The Group has at all time adhered to high standard of social and environmental duties, and welcomes the government's new initiatives. However, it is possible that further investment will need to be made by the Group to upgrade waste treatment facilities and this will in turn increases the Group's waste treatment costs.

FUTURE PLANS AND PROSPECTS

The export-oriented manufacturers for household products in China will continue to face challenges as US economy will not see any turnaround in the foreseeable future and the RMB is expected to accelerate its appreciation. As China inflation rate escalates and the New Labor Contract Law enacted in 2008, the Group has to focus on cost saving programs to go through the rest of 2008.

Maintaining and strengthening position as a major player in upholstered furniture industry

Compared with other competitors, the Group has a unique advantage in its vertically integrated production and large scale manufacturing capabilities. The Group will leverage on this advantage to work with its major customers and to strengthen its reputation as a quality OEM partner not only with US customers but also with European and Australian customers.

The Group's aggressive expansion prior to 2006 has resulted in relatively low level capacity utilization. As the industry wide over capacity is unlikely to abate soon, the Group has taken initiatives to consolidate its production capabilities while realizing returns arising from asset value appreciation. In 2007, the Group disposed of its interests in two manufacturing subsidiaries and leased the facility of La Kassa Furniture Co., Ltd in Shanghai to a third party. The Group is considering further consolidation of its assets and cash generated from this initiative will be used to finance new business development projects.

The Group recognises the importance of business process efficiency, and will continue improving its raw material procurement and its supply chain management. The Group also implemented a new incentive schemes to motivate its business units. These will lead to the strengthening of the Group's competitiveness.

Establishing domestic presence to tap into China's growth potentials for consumption goods

Kasen Home Furnishing Stores

The residential furniture market in China is currently very fragmented. The Group believes that, with its fast growing economy, China's residential furniture market will go through major changes in the next few years. The Group plans to tap into China's growth potentials for mid to high end residential furniture by opening large furniture malls in major cities in China. The first 6,000 square meters flagship store in Shanghai was opened in October 2007, and the second store will be opened in Hangzhou in the middle of 2008. The Group believes that it will take two to three years to build a strong brand in furniture retail business.

Retail Mall Project

To further diversify its revenue sources and implement its domestic marketing plans, the Group has acquired 4.92% equity interests in Haining Leather Market, a well-known and experienced developer and operator of large leather product shopping malls in China, and formed a joint venture with Haining Leather Market. The joint venture, in which the Group holds 60% equity interests, will look for new sites in major cities in the PRC to develop large specialized leather product shopping malls. The joint venture company has successfully tendered for a land of approximately 145,078 square meters in Changsha, Hunan province at a total cost of RMB263.78 million. The land will be used to build a leather and furniture retail mall. Most of the shop floors will be sold or leased out to retailers, while the Group intends to retain part of the mall for its Kasen Home Furnishing Stores. Development of the Changsha land is expected to begin in 2008.

Real estate development

In addition to the Changsha land, the Group had acquired a parcel of land with a site area of approximately 139,669 square meters in Boao, Hainan province in 2006. In December 2007, the Group acquired Qionghai Bodi Real Estate Co., Ltd. that held a parcel of land with a site area of approximately 450,497 square meters, adjacent to the Group's existing land in Boao. After this acquisition, the Group owns a total site area of 590,166 square metres of lands in Boao which will be used for residential property development projects beginning in late 2008. The Group believes these projects will provide the Group with good opportunity to diversify its business and will contribute to the Group's profitability in the long run.

Directors' Report

The directors present their annual report and the audited consolidated financial statements for the year ended December 31, 2007.

The shares of the Company were listed on 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 AND APPROPRIATIONS

The results of the Group for the year ended December 31, 2007 are set out in the consolidated income statement on page 33.

The directors do not recommend the payment of any final dividend for the year ended December 31, 2007.

DISTRIBUTABLE RESERVES OF THE COMPANY

The amount of the Company's reserves available for distribution to shareholders as at December 31, 2007, calculated in accordance with International Financial Reporting Standards, was approximately RMB803.4 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 of 2007, the Group had acquired property, plant and equipment of approximately RMB40.0 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 of 2007 are set out in note 17 to the financial statements.

SHARE CAPITAL

Details of the Company's share capital are set out in note 32 to the financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

During the year of 2007, the aggregate sales attributable to the Group's five largest customers comprised approximately 39.6% of the Group's total sales and the sales attributable to the Group's largest customer were approximately 11.1% of the Group's total sales.

The aggregate purchases during the year of 2007 attributable to the Group's five largest suppliers were approximately 23.4% of the Group's total purchases.

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 of 2007 and up to the date of this report are:

Executive directors

ZHU Zhangjin, Kasen *(Chairman)*
ZHOU Xiaosong
ZHU Jianqi

Non-executive director

LI Hui, David

Independent non-executive directors

LU Yungang, Ken
CHOW Joseph
ZHANG Huaqiao, Joe

In accordance with provision 87 of the Articles, Messrs., Zhu Jianqi, Zhou Xiaosong and Chow Joseph will retire from office of directors by rotation and, being eligible, will offer themselves 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 4 to 6.

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

As at December 31, 2007, the interests of the directors and chief executives and their associates 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") as contained in Appendix 10 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules") are as follows:

(1) Long positions in shares of the Company

	Number of shares held, capacity and nature of interest			
Name of Director	**Directly beneficially owned**	**Through controlled corporation**	**Total number of shares interested**	**Percentage of the Company's issued share capital**
Zhu Zhangjin	–	328,867,019 (Note)	328,867,019	33.22%
Zhou Xiaosong	8,173,912	–	8,173,912	0.83%
Zhu Jianqi	7,478,260	–	7,478,260	0.76%

Note: 328,867,019 shares are beneficially owned by Joyview Enterprises Limited, a company wholly-owned by Mr. Zhu Zhangjin.

(2) Long positions in underlying shares of the Company

Long positions in underlying shares of the Company are separately disclosed in the section "Share Option Scheme" below.

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, 2007.

SHARE OPTION SCHEME

Particulars of the Company's share option scheme are set out in note 33 to the financial statements.

A share option scheme was adopted by the Company pursuant to a board resolution passed on September 26, 2005 (the "Scheme") for the primary purpose of providing incentives to Directors and eligible employees. The Scheme became effective on October 20, 2005 and the options issued pursuant to the Scheme will expire no later than 10 years from the date of grant of the option. Under the Scheme, the Board may grant options to any employees of the Company or any of its subsidiaries to subscribe shares of the Company.

For any options granted to directors, chief executives or substantial shareholders of the Company, options to be granted shall be approved by the independent non-executive Directors of the Company (excluding any independent non-executive Director who is the proposed grantee of options).

The total number of shares in respect of which options may be granted under the Scheme is not permitted to exceed 10% of the shares of the Company on October 20, 2005 (representing 101,404,536 shares of the Company) without prior approval from the Company's shareholders. The number of shares issued and to be issued in respect of options granted and may be granted to any individual in any one year is not permitted to exceed 1% of the total shares of the Company in issue at any point in time, without prior approval from the Company's shareholders.

The amount payable on acceptance of an option is HK$1.00. In relation to any options granted under the Scheme, the exercise price is determined by the directors of the Company, and will not be less than the higher of (i) the closing price of the Company's shares on the date of grant; (ii) the average closing price of the shares for the five business days immediately preceding the date of grant; and (iii) the nominal value of the Company's share.

The Scheme does not contain any minimum period(s) for which an option must be held before it can be exercised. However, at the time of granting of the options, the Company may specify any such minimum period(s).

Unless otherwise terminated by the Board or the shareholders of the Company in general meeting in accordance with the terms of the Scheme, the Scheme shall be valid and effective for a period of 10 years from the date on which it becomes unconditional which was October 10, 2005, after which no further options will be granted or offered but the provisions of the Scheme shall remain in full force and effect to the extent necessary to give effect to the exercise of any subsisting options granted prior to the expiry of the 10-years period or otherwise as may be required in accordance with the provisions of the Scheme.

Details of the share options granted under the 2006 Share Option Scheme during the year ended December 31, 2007 were as follows:

		Number of share options						
Name or category of participant	Exercise price HK$	Outstanding as at January 1, 2007	Granted from January 1, 2007 to December 31, 2007	Cancelled from January 1, 2007 to December 31, 2007	Outstanding as at December 31, 2007	Percentage of total issued share capital	Exercisable period	Notes
Directors								
Zhu Zhangjin	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2007 to 8/3/2016	1,3,4
	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2008 to 8/3/2016	2,3,4
Zhou Xiaosong	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2007 to 8/3/2016	1,3,4
	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2008 to 8/3/2016	2,3,4
Zhu Jianqi	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2007 to 8/3/2016	1,3,4
	2.38	1,000,000	–	–	1,000,000	0.10%	1/1/2008 to 8/3/2016	2,3,4
Lu Yungang, Ken	2.38	200,000	–	–	200,000	0.02%	1/1/2007 to 8/3/2016	1,3,4
	2.38	200,000	–	–	200,000	0.02%	1/1/2008 to 8/3/2016	2,3,4
Chow Joseph	2.38	200,000	–	–	200,000	0.02%	1/1/2007 to 8/3/2016	1,3,4
	2.38	200,000	–	–	200,000	0.02%	1/1/2008 to 8/3/2016	2,3,4
		6,800,000	–	–	6,800,000	0.68%		
Other employees in aggregate	2.38	11,500,000	–	(2,250,000)	9,250,000	0.94%	1/1/2007 to 8/3/2016	1,3,4
	2.38	11,500,000	–	(2,250,000)	9,250,000	0.94%	1/1/2008 to 8/3/2016	2,3,4
		29,800,000	–	(4,500,000)	25,300,000	2.56%		

Notes:

1. Pursuant to the Scheme adopted by a resolution of the Shareholders on September 24, 2005 and adopted by a resolution of the Board on September 26, 2005, these share options were granted on March 9, 2006 and are exercisable at HK$2.38 per Share from January 1, 2007 to March 8, 2016.

2. These share options were granted pursuant to the Scheme on March 9, 2006 and are exercisable at HK$2.38 per Share from January 1, 2008 to March 8, 2016.

3. These share options represent personal interest held by the relevant participants as beneficial owner.

4. Except the cancelled share option stated above, up to December 31, 2007, none of these share options were exercised nor lapsed.

SUBSTANTIAL SHAREHOLDERS

As at December 31, 2007, the following persons (other than directors or chief executives of the Company stated in "Directors' and Chief Executive's 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
Joyview Enterprises Limited[2]	Beneficial owner	-	328,867,019	328,867,019	33.22%
Warburg Pincus & Co.[1]	Interest of controlled corporation	-	186,989,966	186,989,966	18.88%
Warburg Pincus Partners LLC[1]	Beneficial owner	-	186,989,966	186,989,966	18.88%
Warburg Pincus Private Equity VIII L.P.[1]	Beneficial owner	-	90,605,988	90,605,988	9.15%
Warburg Pincus International Partners L.P.[1]	Beneficial owner	-	89,616,811	89,616,811	9.05%

Notes:

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.

2. Joyview Enterprises Limited is a company beneficially owned as to 100% by Mr. Zhu Zhangjin. Mr. Zhu Zhangjin is the director of Joyview Enterprises Limited.

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, 2007.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBT SECURITIES

Other than the share option scheme disclosed in note 33 to the financial statements, at no time during the year of 2007 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.

CONNECTED TRANSACTION

During the year ended December 31, 2007, the Group entered into the following transaction with its connected persons.

Acquisition of 4.92% equity interests in Haining Leather Market

On September 30, 2007, pursuant to an auction for strategic investment in Haining Leather Market, Zhejiang Kasen, a wholly owned subsidiary of the Company, succeeded in its bidding in such auction and entered into the Capital Increase Agreement to acquire 4.92% equity interests in Haining Leather Market (the "Acquisition") upon increase of its registered capital. The total consideration payable in cash under the Capital Increase Agreement is RMB43,000,000.

The Acquisition constitutes a connected transaction for the Company under Chapter 14A of the Listing Rules and is subject to reporting and announcement requirements as well as independent shareholders' approval requirements under the Listing Rules.

CONTINUING CONNECTED TRANSACTIONS

During the year ended December 31, 2007, the Group entered into the following continuing 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"), a wholly-owned subsidiary of the Company, which will expire on December 31, 2007 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for a term of 3 years thereafter. Pursuant to the agreement, Wansheng Furniture and Haining Kasen agreed to purchase sofa fabrics from Wansheng Silk. Wansheng Silk is an associate of Mr. Sun Jianxin, an executive director of Wansheng Furniture, 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 between Wansheng Silk, Wansheng Furniture and Haining Kasen have been set out in the prospectus of the Company dated October 10, 2005 (the "Prospectus").

Wansheng Silk has ceased to be part of the Group since June 2006 because of the disposal of one subsidiary by the Group.

(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 a term of 3 years 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 agreed to purchase wastes (including reside 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 amount of the transactions under this agreement was RMB11,040,000 and the waiver granted by the Stock Exchange was RMB21,000,000.

(3) 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 a term of 3 years 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 agreed to 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 they 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 amount of the transactions under this agreement was RMB119,577,000 and the waiver granted by the Stock Exchange was RMB560,000,000.

(4) Agreement for sale of upholstered furniture to Starcorp

On February 22, 2006, Starcorp Corporation Pty. Ltd. ("Starcorp") entered into an agreement with the Group which will expire on December 31, 2008 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for a term of 3 years 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 was determined by reference to the prevailing market price. Details of this agreement have been set out in the circular dated March 16, 2006. Pursuant to this agreement, the Group agreed to 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 RMB53,065,000 and the waiver granted by the Stock Exchange was RMB150,000,000.

(5) Agreement for sales of outdoor leisure products to North Pole

On February 22, 2006, the Group entered into several agreements with North Pole Ltd. and North Pole (China) Ltd. (collectively the "North Pole Agreements"), which will expire on December 31, 2008 and, subject to compliance with Listing Rules requirements regarding connected transactions, automatically renewable for 3 year terms thereafter. North Pole Ltd. and North Pole (China) Ltd. are subsidiaries of a shareholder of the Company for the continuing sales transactions. North Pole Ltd., is owned, among others, as to approximately 46.1% by North Pole Holdings Ltd. and approximately 46.1% by North Pole International Holdings Ltd., both of which are in turn wholly-owned by Warburg Pincus Funds. North Pole (China) Ltd. is a wholly-owned subsidiary of North Pole Ltd. 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. The pricing under this agreement was determined by reference to the prevailing market price. Details of this agreement have been set out in the circular dated March 16, 2006.

On February 12, 2007, the Group announced that the Company had decided to cease the sales of outdoor leisure products under the North Pole Agreements from March 1, 2007. The Board considers that the cessation of its sales of outdoor leisure products under the North Pole Agreements is a commercial decision for the benefit of the Group.

(6) Transactions with Haining Haipai

On March 6, 2008, the Group announced the sales of wooden frames and scrapped leather (the "Wooden Frames and Scrapped leather Transactions") and sub-contracted the manufacturing of leather sofa cover service (the "Sub-contract Transactions") to Haining Haipai during the year ended December 31, 2007. Haining Haipai is the subsidiary of Haining Ounuoya Import & Export Co., Ltd which is the major shareholder of one subsidiary, Haining Oyi May, of the Group. The pricing under these transactions was determined by reference to the prevailing market price. Details of these transactions have been set out in the announcement dated March 6, 2008. During the year, the aggregate amount of the Wooden Frames and Scrapped leather Transactions and the Sub-contract Transactions was RMB7,608,000 and RMB1,956,000, respectively and the waiver granted by the Stock Exchange was RMB7,608,000 and RMB1,956,000, respectively.

As Haining Oyi May is no longer part of the Group, any transactions entered or to be entered into between the Company's subsidiaries and Haining Haipai after January 2008 will no longer constitute connected transactions for the Company under Chapter 14A of the Listing Rules.

Pursuant to Rule 14A.38 of the Listing Rules, the Board 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. Based on the work performed, the auditors of the Company have provided a letter and confirmed that the aforesaid continuing connected transactions (1) have been approved by the Board of the Company; (2) are in accordance with the pricing policies of the Group; (3) have been entered into in accordance with the terms of the relevant agreements governing the transactions; and (4) have not exceeded the caps allowed by the Stock Exchange in the previous waiver.

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 and in note 41 to the financial statements, there were no other transactions which need to be disclosed as connected transactions in accordance with the requirements of the Listing Rules during the year ended December 31, 2007.

DIRECTORS' INTEREST IN CONTRACTS OF SIGNIFICANCE

Save as disclosed under the headings "Connected Transaction" and "Continuing 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 throughout the year ended December 31, 2007.

DIRECTOR'S 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, 2007.

PRE-EMPTIVE RIGHTS

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

INDEPENDENT NON-EXECUTIVE DIRECTORS' CONFIRMATION OF INDEPENDENCE

The Company has received, from each of the independent non-executive directors, Messrs. LU Yungang, Ken, CHOW Joseph, ZHANG Huaqiao, Joe, 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.

POST BALANCE SHEET EVENTS

Pursuant to an equity transfer agreement dated February 19, 2008, a wholly owned subsidiary of the Company agreed to purchase from an independent third party 49.5% equity interest in Chengdu Longteng Shoes Market Investment and Development Co., Ltd. (成都隆騰鞋城投資開發有限公司) for a consideration of RMB29.7 million. This transaction has been approved by local authority on March 7, 2008. Chengdu Longteng Shoes Market Investment and Development Co., Ltd. becomes the associate of the Group since then.

AUDIT COMMITTEE

An Audit Committee was established by the Company 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 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. Li Hui, David 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, Kasen
Director

The PRC, April 15, 2008

Corporate Governance Report

The Board and the Management are committed to maintain a high standard of corporate governance, holding the beliefs of transparency, independence, honesty and accountability. We believe that effective corporate governance is an essential factor to create more value to shareholders. Therefore we continuously review and improve our corporate governance standards to ensure maximum compliance with relevant laws and codes.

The Company has complied with the "Code on Corporate Governance Practices" (the "CG Code") as set out in Appendix 14 of the Listing Rules throughout the year ended December 31, 2007, except for the following deviations:

CODE PROVISION A.2.1

Under CG Code Provision A.2.1, the roles of chairman and Chief Executive Officer should be separated and should not be performed by the same individual. The Company does not at present separate the roles of Chairman and Chief Executive Officer. 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 appointing 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 is required for the position of Chief Executive Officer, the Company is unable to determine as to when the appointment of a Chief Executive Officer for the Company can be effected.

CODE PROVISION A.4.1

Under CG Code Provision A.4.1, non-executive directors should be appointed for a specific term, subject to re-election. The current non-executive director of the Company, Mr. Li Hui, David and independent non-executive directors of the Company, Mr. Chow Joseph, Mr. Lu Yungang, Ken and Mr. Zhang Huaqiao, Joe are not appointed for specific terms, but are subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Company's articles of association which has provided that at every annual general meeting, one-third of the directors for the time being or, if their number is not a multiple of three, the number nearest to but not less than one-third, shall retire from office by rotation. Given that the provisions stipulated under the articles of association of the Company, the Company considers that appropriate measures have been taken by the Company regarding its corporate governance practices. The Board will keep these matters under review and will continue to monitor and revise the Company's corporate governance policies in order to ensure that such policies can meet the general rules and standards required by the Stock Exchange.

The Board will keep these matters under review. Following sustained development and growth of the Company, we will continue to monitor and revise the Company's corporate governance policies in order to ensure that such policies can meet the general rules and standards required by the Stock Exchange.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") set out in Appendix 10 to the Listing Rules as its own code of conduct regarding directors' securities transactions. Specific enquiries have been made with all directors, who have confirmed that, during the period under review, they were in compliance with the provisions of the Model Code. All directors of the Company declared that they have complied with the Model Code for the year ended December 31, 2007.

BOARD OF DIRECTORS

The primary responsibilities of the Board are to establish long term strategies, administrate and oversee the operations and financial policies and set up and regularly review the Company's performance. The Board comprises of seven members, including three executive directors, one non-executive director and three independent non-executive directors. The Board members for the year ended December 31, 2007 were:

Executive directors

Mr. Zhu Zhangjin, Kasen *(Chairman)*
Mr. Zhu Jianqi
Mr. Zhou Xiaosong

Non-executive director

Mr. Li Hui, David

Independent non-executive directors

Mr. Chow Joseph
Mr. Lu Yungang, Ken
Mr. Zhang Huaqiao, Joe

The Biographical details of all directors and the relationships between them are set out in the "Directors and Management Profiles" section on pages 4 to 6 of this annual report, the Company's website: http://www.kasen.com.cn, and http://www.irasia.com/listco/hk/kasen/index.htm. None of the directors of the Company have any financial, business, family or other material or relevant relationships among members of the Board.

The Company has received an annual confirmation of independence from each of the three independent non-executive directors pursuant to Rule 3.13 of the Listing Rules. Based on the contents of such confirmation, the Company considers that the three independent non-executive directors are independent and that they all meet the specific independence guidelines as set out in Rule 3.13 of the Listing Rules.

The independent non-executive directors bring a wide range of business and financial expertise, experiences and independent judgement to the Board. Through active participation in Board meetings and serving on various Board committees, all independent non-executive directors make various contributions to the effective direction of the Company.

The Company has purchased Directors & Officers Liability and Company Reimbursement Insurance for all directors and some senior management.

CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Mr. Zhu Zhangjin is the Chairman and Chief Executive Officer of the Company responsible for overseeing the operations of the Group. The Board believes that the appointment of Mr. Zhu Zhangjin 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.

NON-EXECUTIVE DIRECTOR

The current non-executive director of the Company is not appointed for specific terms, but is subject to retirement by rotation and re-election at the annual general meeting of the Company in accordance with the Company's articles of association.

BOARD COMMITTEES

As an integral part of good corporate governance, the following committees have been set up:

Audit Committee

The audit committee comprises three independent non-executive directors of the Company:

Mr. Chow Joseph *(Chairman of the Audit Committee)*
Mr. Lu Yungang, Ken
Mr. Zhang Huaqiao, Joe

The audit committee was set up with written terms of reference prepared based on "A Guide for Effective Audit Committees" published by the Hong Kong Institute of Certified Public Accountants and the CG Code. The primary duties of the audit committee are to review the Company's annual reports and accounts and interim reports and results announcements and to provide advice and comments thereon to the directors. The members meet regularly with the external auditors and the Company's senior management for the review and supervision of the Company's financial reporting and internal control procedures.

During the year ended December 31, 2007, the Audit Committee held three meetings to review the annual and interim results, and to make recommendations to improve the Company's internal control. The chief financial officer, internal audit officer and representatives of the external auditors attended the meetings.

Remuneration Committee

The remuneration committee comprises three members, the majority of which are independent non-executive directors:

Mr. Li Hui, David *(Chairman of the Remuneration Committee)*
Mr. Lu Yungang, Ken
Mr. Zhang Huaqiao, Joe

The remuneration committee has adopted written terms of reference prepared by reference to the suggested terms of reference stated under the CG Code Provision B.1.3.

The remuneration committee has been delegated with the powers and authorities to implement the share option scheme of the Company and to deal with all compensation matters regarding the directors and senior management of the Company in accordance with the terms and conditions of their respective agreement/contract with the relevant member of the Group.

During the year ended December 31, 2007, the Remuneration Committee held one meeting to review the remuneration package of the Board members and the senior management.

NUMBER OF MEETINGS AND DIRECTORS' ATTENDANCE

The individual attendance record of each director at the meetings of the Board, Remuneration Committee and Audit Committee during the year ended December 31, 2007 is set out below:

	Attendance/Number of Meetings		
Name of Directors	**Board**	**Remuneration Committee**	**Audit Committee**
Executive Directors			
Mr. ZHU Zhangjin, Kasen *(Chairman)*	4/4	N/A	N/A
Mr. ZHOU Xiaosong	3/4	N/A	N/A
Mr. ZHU Jianqi	3/4	N/A	N/A
Non-executive Director			
Mr. LI Hui, David *(Chairman of Remuneration Committee)*	4/4	1/1	N/A
Independent Non-executive Directors			
Mr. CHOW Joseph *(Chairman of Audit Committee)*	3/4	N/A	3/3
Mr. LU Yungang, Ken *(Member of Audit Committee and Remuneration Committee)*	3/4	1/1	2/3
Mr. ZHANG Huaqiao, Joe *(Member of Audit Committee and Remuneration Committee)*	3/4	1/1	3/3

NOMINATION OF DIRECTORS

The Company believes that it is not necessary to establish a separate Nomination Committee to nominate directors. The task of nominating directors is vested with the Board of the Company. The Board reviews the structure and the composition of the Board regularly, then identifies and nominates qualified individuals to be appointed as new directors of the Company.

RESPONSIBILITIES IN RESPECT OF THE FINANCIAL STATEMENTS

The Board is responsible for presenting a balanced, clear and understandable assessment of annual and interim reports, price sensitive information announcements and other disclosures required under the Listing Rules and other regulatory requirements.

The directors acknowledge their responsibility for preparing the financial statements of the Company for the year ended December 31, 2007.

The statement of the external auditors of the Company about their reporting responsibilities on the financial statements is set out in the "Independent Auditor's Report".

AUDITORS' REMUNERATION

The remuneration paid to the external auditors of the Company in respect of audit services for the year ended December 31, 2007 amounted to approximately RMB5.1 million.

INTERNAL CONTROL

The Company endeavors to implement a sound risk management and internal control system. The Board is responsible for maintaining an adequate internal control system to safeguard shareholder investments and Company assets, and reviewing the effectiveness of such on an annual basis through the Audit Committee. The Audit Committee reports to the Board on any material issues and makes recommendations to the Board.

SHAREHOLDER RIGHTS AND INVESTOR RELATIONS

The rights of shareholders and the procedures for them to demand a poll on resolutions at shareholders' meetings are contained in the Company's Articles of Association. Details of such rights to demand a poll and the poll procedures are included in all circulars to shareholders and will be explained during the proceedings of meetings. Poll results, if any, will be posted on both the website of the Stock Exchange and the website of the Company on the business day of the shareholders' meeting.

The general meetings of the Company provide a platform for communication between the shareholders and the Board. The Chairman of the Board as well as chairman of the Remuneration Committee and Audit Committee or if, in their absence, other members of the respective committees, and where applicable, the independent Board committee, are available to answer questions at the shareholders' meetings. The Company continues to enhance communications and relationships with its investors. Enquiries from investors are dealt with in an informative and timely manner.

Taking advantages of various resources, the Company keeps communicating with shareholders regularly and properly to ensure that shareholders are adequately aware of any important issues during the course of the Company's operation, and then exercise their rights as shareholders with sufficient knowledge. In addition, the Company regularly meets with institutional investors, financial analysts and financial media, and promptly releases information related to any significant progress of the Company, so as to promote the development of the Company through mutual and efficient communications. Investors are welcome to write directly to the Company at its Hong Kong registered office for any inquiries.

Independent Auditor's Report

Deloitte.
德勤

TO THE SHAREHOLDERS OF KASEN INTERNATIONAL HOLDINGS LIMITED
(incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of Kasen International Holdings Limited (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 33 to 88, which comprise the consolidated balance sheet as at December 31, 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Group as at December 31, 2007 and of the Group's loss and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

Deloitte Touche Tohmatsu
Certified Public Accountants
Hong Kong
April 15, 2008

Consolidated Income Statement

For the year ended December 31, 2007

	Notes	**2007** **RMB'000**	2006 RMB'000
Turnover	6	**3,310,727**	3,916,513
Cost of sales		**(3,011,190)**	(3,489,136)
Gross profit		**299,537**	427,377
Other income	7	**70,921**	71,230
Distribution costs		**(116,721)**	(107,908)
Administrative expenses		**(168,788)**	(171,115)
Other expenses	8	**(168,913)**	(29,997)
Share of profit of associates	21	**103**	937
Finance costs	9	**(91,579)**	(85,390)
(Loss) profit before taxation	10	**(175,440)**	105,134
Taxation	12	**(14,584)**	(21,707)
(Loss) profit for the year		**(190,024)**	83,427
Attributable to:			
Equity holders of the Company		**(194,149)**	64,143
Minority interests		**4,125**	19,284
		(190,024)	83,427
Dividend	14	**–**	114,258
(Loss) earning per share	15		
Basic		**(20) cents**	6 cents
Diluted		**(20) cents**	6 cents

Consolidated Balance Sheet

As at December 31, 2007

	Notes	2007 RMB'000	2006 RMB'000
NON-CURRENT ASSETS			
Goodwill	16	–	157,958
Property, plant and equipment	17	952,492	1,173,599
Prepaid lease payment – non-current portion	18	102,265	131,860
Properties for development	19	314,781	–
Investment properties	19	–	32,901
Intangible assets	20	1,321	1,485
Investments in associates	21	15,833	26,728
Investment in a jointly controlled entity	22	2,614	2,614
Available-for-sale investments	23	43,278	310
Other long term assets	24	143,360	–
		1,575,944	1,527,455
CURRENT ASSETS			
Inventories	25	1,142,720	1,326,216
Trade and other receivables	26	549,588	633,848
Prepaid lease payment – current portion	18	2,311	2,904
Amounts due from related companies	27	24,372	36,596
Taxes recoverable		6,682	3,315
Derivative financial instruments	28	16,151	–
Pledged bank deposits	29	85,743	163,221
Bank balances and cash	29	504,549	380,973
		2,332,116	2,547,073
Assets classified as held for sale	13	231,390	–
TOTAL ASSETS		4,139,450	4,074,528
CURRENT LIABILITIES			
Trade, bills and other payables	30	429,576	604,036
Amounts due to related companies	27	81	19,467
Bank and other borrowings – due within one year	31	1,546,812	1,246,689
Taxes payable		7,722	10,959
		1,984,191	1,881,151
Liabilities classified as held for sale	13	175,013	–
NET CURRENT ASSETS		404,302	665,922
TOTAL ASSETS LESS CURRENT LIABILITIES		1,980,246	2,193,377
NON-CURRENT LIABILITIES			
Bank and other borrowings – due after one year	31	10,400	10,400
		10,400	10,400
NET ASSETS		1,969,846	2,182,977

Consolidated Balance Sheet (cont'd)

As at December 31, 2007

	Note	**2007 RMB'000**	2006 RMB'000
CAPITAL AND RESERVES			
Share capital	32	**1,227**	1,227
Reserves		**1,915,927**	2,107,638
Equity attributable to equity holders of the Company		**1,917,154**	2,108,865
Minority interests		**52,692**	74,112
Total equity		**1,969,846**	2,182,977

The consolidated financial statements on pages 33 to 88 were approved and authorized for issue by the Board of Directors on April 15, 2008 and are signed on its behalf by:

Zhu Zhangjin, Kasen	**Zhu Jianqi**
Director	*Director*

Consolidated Statement of Changes in Equity

For the year ended December 31, 2007

	Attributable to equity holders of the Company										
	Share capital RMB'000	**Share premium** RMB'000	**Exchange reserve** RMB'000	**Statutory reserve** RMB'000 (note 34)	**Special reserve** RMB'000 (note 34)	**Share option reserve** RMB'000 (note 33)	**Reserve on acquisition** RMB'000	**Retained earnings** RMB'000	**Sub-total** RMB'000	**Minority interests** RMB'000	**Total equity** RMB'000
At January 1, 2006	1,256	1,147,408	(793)	169,262	168,659	–	–	713,768	2,199,560	98,306	2,297,866
Reversal of exchange difference on translation of foreign operation	–	–	793	–	–	–	–	–	793	–	793
Profit for the year	–	–	–	–	–	–	–	64,143	64,143	19,284	83,427
Total recognised income and expense for the year	–	–	793	–	–	–	–	64,143	64,936	19,284	84,220
Acquisition of additional interests in subsidiaries from minority shareholders	–	–	–	–	–	–	(30,968)	–	(30,968)	(29,188)	(60,156)
Disposal of subsidiaries	–	–	–	–	–	–	–	–	–	(19,230)	(19,230)
Capital contribution from minority shareholders	–	–	–	–	–	–	–	–	–	5,600	5,600
Share repurchase	(29)	(25,862)	–	–	–	–	–	–	(25,891)	–	(25,891)
Dividend paid	–	–	–	–	–	–	–	(114,258)	(114,258)	(660)	(114,918)
Share based payment expense	–	–	–	–	–	15,486	–	–	15,486	–	15,486
Appropriation to statutory reserve	–	–	–	10,742	–	–	–	(10,742)	–	–	–
At December 31, 2006	1,227	1,121,546	–	180,004	168,659	15,486	(30,968)	652,911	2,108,865	74,112	2,182,977
(Loss) profit for the year	–	–	–	–	–	–	–	(194,149)	(194,149)	4,125	(190,024)
Total recognised income and expense for the year	–	–	–	–	–	–	–	(194,149)	(194,149)	4,125	(190,024)
Share based payment expense (note 33)	–	–	–	–	–	2,438	–	–	2,438	–	2,438
Acquisition of additional interests in subsidiaries from minority shareholders (note 35)	–	–	–	–	–	–	–	–	–	(3,600)	(3,600)
Dividend paid	–	–	–	–	–	–	–	–	–	(21,945)	(21,945)
Appropriation to statutory reserve	–	–	–	11,689	–	–	–	(11,689)	–	–	–
At December 31, 2007	**1,227**	**1,121,546**	**–**	**191,693**	**168,659**	**17,924**	**(30,968)**	**447,073**	**1,917,154**	**52,692**	**1,969,846**

Consolidated Cash Flow Statement

For the year ended December 31, 2007

	2007	2006
	RMB'000	RMB'000
OPERATING ACTIVITIES		
(Loss) profit before taxation	**(175,440)**	105,134
Adjustments for:		
Impairment loss recognised in respect of trade and other receivables	**10,368**	17,626
Impairment loss in respect of property, plant and equipment	**7,004**	–
Allowances for inventories	**99,639**	11,404
Amortization of intangible assets	**500**	350
Investment income	**(157)**	–
Gain on disposal of an associate	**(1,056)**	–
Amortization of prepaid lease payment	**2,707**	3,277
Depreciation of property, plant and equipment	**94,498**	95,858
Loss on disposal of property, plant and equipment	**396**	2,161
Interest expenses	**91,579**	85,390
Interest income	**(6,358)**	(8,905)
Share based payment expense	**2,438**	15,486
Adjustment of exchange reserve recognised in previous years	**–**	793
Fair value of forward contracts	**(16,151)**	–
Fair value change on investment property	**(5,671)**	–
Gain on disposals of subsidiaries	**(7,720)**	(8,838)
Goodwill impairment	**157,958**	23,048
Share of profit of associates	**(103)**	(937)
Discounts on acquisition of an additional interest in a subsidiary	**–**	(10,279)
Operating cash flows before movements in working capital	**254,431**	331,568
Decrease (increase) in inventories	**2,220**	(9,097)
(Increase) decrease in trade and other receivables	**(6,040)**	68,604
Increase in amounts due from related companies	**(22,750)**	(15,993)
Increase (decrease) in trade, bills and other payables	**13,827**	(98,713)
Decrease in amounts due to related companies	**(10,413)**	(35,225)
Cash (used in) generated from operations	**231,275**	241,144
Income taxes paid	**(29,629)**	(27,277)
Income taxes refunded	**8,975**	19,031
NET CASH (USED IN) FROM OPERATING ACTIVITIES	**210,621**	232,898

Consolidated Cash Flow Statement (cont'd)

For the year ended December 31, 2007

	Notes	2007 RMB'000	2006 RMB'000
INVESTING ACTIVITIES			
Acquisition of available for sale investment		**(42,968)**	–
Purchase of property, plant and equipment		**(39,644)**	(41,123)
Additions to properties for development		**(276,209)**	–
Additions to other long term assets		**(143,360)**	–
Increase in prepaid lease payment		**(82)**	(614)
Increase in investment properties		**–**	(32,901)
Investment in a jointly controlled entity		**–**	(1,803)
Investment in associates		**–**	(13,664)
Payment for acquisition of additional interests in subsidiaries	35	**(3,600)**	(49,877)
Decrease in pledged bank deposits		**49,532**	76,891
Purchase of intangible assets		**(394)**	(891)
Proceeds from disposals of property, plant and equipment		**95**	250
Interest received		**6,358**	8,905
Proceeds from sale of available-for-sales investments		**157**	–
Disposal of subsidiaries	36	**24,823**	(5,672)
Disposal of investment in associate	21	**12,054**	–
NET CASH USED IN INVESTING ACTIVITIES		**(413,238)**	(60,499)
FINANCING ACTIVITIES			
Bank and other borrowings raised		**2,528,008**	2,301,375
Repurchase of shares		**–**	(25,891)
Advances from related companies		**–**	8,000
Repayment of bank and other borrowings		**(2,084,233)**	(2,250,224)
Interest paid		**(85,336)**	(85,646)
Repayment to related companies		**(6,000)**	(2,000)
Dividends paid to equity shareholders		**–**	(114,258)
Dividends paid to minority shareholders		**(21,945)**	(660)
Capital contribution from minority shareholders		**–**	5,600
NET CASH FROM (USED IN) FINANCING ACTIVITIES		**330,494**	(163,704)
NET INCREASE IN CASH AND CASH EQUIVALENTS		**127,877**	8,695
CASH AND CASH EQUIVALENTS AT BEGINNING OF THE YEAR		**380,973**	372,278
CASH AND CASH EQUIVALENTS AT END OF THE YEAR, represented by bank balances and cash		**508,850**	380,973

Notes to the Consolidated Financial Statements

For the year ended December 31, 2007

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. Its parent and ultimate holding company is Joyview Enterprises Ltd. (incorporated in the British Virgin Islands). The addresses of the registered office and principal place of business of the Company are disclosed in the corporate information attached to the annual report.

The Company acts as an investment holding company. Its subsidiaries are principally engaged in the processing of raw cowhides, wet blues into finished leather or fully assembled leather products. To accommodate market change, the board of directors of the Company approved and began to develop new business in property and retail industry in late 2007.

2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS

In the current year, the Group has applied, for the first time, a number of new standard, amendment and interpretations issued by the International Accounting Standards Board (the "IASB") and the International Financial Reporting Interpretations Committee (the "IFRIC") of the IASB that are effective for the Group's financial year beginning January 1, 2007.

IFRS 1 (Amendment)	Capital Disclosures
IFRS 7	Financial Instruments: Disclosures
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies
IFRIC 8	Scope of IFRS 2
IFRIC 9	Reassessment of Embedded Derivatives
IFRIC 10	Interim Financial Reporting and Impairment

The adoption of the new standard, amendment and interpretations had no material effect on the results and financial position for the current or prior accounting periods have been prepared. Accordingly, no prior period adjustment has been required.

The Group has applied the disclosure requirements under IAS 1 (Amendment) and IFRS 7 retrospectively. Certain information presented in prior year under the requirements of IAS 32 has been removed and the relevant comparative information based on the requirements of IAS 1 (Amendment) and IFRS 7 has been presented for the first time in the current year.

2. APPLICATION OF NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS *(Continued)*

The Group has not early applied the following new and revised standards or interpretations that have been issued but are not yet effective.

IAS 1 (Revised)	Presentation of Financial Statements[1]
IAS 23 (Revised)	Borrowing Costs[1]
IAS 27 (Revised)	Consolidated and Separate Financial Statements[2]
IAS 32 & 1 (Amendments)	Puttable Financial Instruments and Obligations Arising on Liquidation[1]
IFRS 2 (Amendment)	Vesting Conditions and Cancellations[1]
IFRS 3 (Revised)	Business Combinations[2]
IFRS 8	Operating Segments[1]
IFRIC 11	IFRS 2: Group and Treasury Share Transactions[3]
IFRIC 12	Service Concession Arrangements[4]
IFRIC 13	Customer Loyalty Programmes[5]
IFRIC 14	IFRS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction[4]

1 Effective for annual periods beginning on or after January 1, 2009
2 Effective for annual periods beginning on or after July 1, 2009
3 Effective for annual periods beginning on or after March 1, 2007
4 Effective for annual periods beginning on or after January 1, 2008
5 Effective for annual periods beginning on or after July 1, 2008

The adoption of IFRS 3 (revised) may affect the accounting for business combination for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after July 1, 2009. IAS 27 (revised) will affect the accounting treatment for changes in a parent's ownership interest in a subsidiary that do not result in a loss of control, which will be accounted for as equity transactions.

The directors of the Company anticipate that the application of the other standards or interpretations will have no material impact on the results and the financial position of the Group.

3. PRINCIPAL ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards. In addition, the consolidated financial statements include applicable disclosures required by the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited and by the Hong Kong Companies Ordinance.

The consolidated financial statements have been prepared on the historical cost basis except for certain properties and financial instruments, which are measured at fair values, as explained in the accounting policies set out below.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of the subsidiaries to bring the accounting policies used in line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Minority interests in the net assets of consolidated subsidiaries are presented separately from the Group's equity therein. Minority interests in the net assets consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the consolidation. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations

The acquisition of business is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 Business Combinations are recognised at their fair values at the acquisition date.

Goodwill arising on acquisition is recognised as assets and measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in the profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority's proportion of the net fair values of the assets, liabilities and contingent liabilities recognised.

Acquisition of additional interests in subsidiaries

On acquisition of additional interest in a subsidiary, the difference between the consideration paid and the aggregate of the goodwill (or discount on acquisition) and the carrying values of the underlying assets and liabilities attributable to the additional interests in a subsidiary acquired is debited to reserve on acquisition.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Goodwill

Goodwill arising on acquisition on or after March 31, 2004.

Goodwill arising on the acquisition of a business represents the excess of the cost of acquisition over the Group's interest in the net fair values of the identifiable assets, liabilities and contingent liabilities of the relevant business recognised at the date of acquisition. Goodwill is initially recognised as asset at cost and is subsequently measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. For goodwill arising on an acquisition in a financial year, the cash-generating unit to which goodwill has been allocated is tested for impairment before the end of that financial year. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On subsequent disposal of the relevant cash-generating units, the attributable amount of goodwill capitalised is included in the determination of the amount of profit or loss on disposal.

Investments in associates

An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

The results and assets and liabilities of associates are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in associates are carried in the consolidated balance sheet at cost as adjusted by post-acquisition changes in the Group's share of net assets of the associate, less any identified impairment loss. When the Group's share of losses of an associate equals or exceeds its interest in that associate, the Group discontinues recognizing its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that associate.

Any excess of the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition, after reassessment, is recognised immediately in profit or loss.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interests in the relevant associate.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Jointly controlled entities

Joint venture arrangements that involve the establishment of a separate entity in which venturers have joint control over the economic activity of the entity are referred to as jointly controlled entities.

The results and assets and liabilities of jointly controlled entities are incorporated in the consolidated financial statements using the equity method of accounting. Under the equity method, investments in jointly controlled entities are carried in the consolidated balance sheet at cost as adjusted by post-acquisition changes in the Group's share of net assets of the jointly controlled entities, less any identified impairment loss. When the Group's share of losses of a jointly controlled entity equals or exceeds its interest in that jointly controlled entity, the Group discontinues recognizing its share of further losses. An additional share of losses is provided for and a liability is recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of that jointly controlled entity.

When a group entity transacts with a jointly controlled entity of the Group, unrealized profits or losses are eliminated to the extent of the Group's interest in the jointly controlled entity, except to the extent that unrealized losses provide evidence of an impairment of the assets transferred, in which case, the full amount of losses is recognised.

Revenue recognition

Revenue is measured at the fair values of the consideration received or receivable and represents amounts receivable for goods sold in the normal course of business, net of sales related taxes.

Sales of goods are recognised when goods are delivered and title has been passed.

Interest revenue is accrued on a timely basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Property, plant and equipment

Property, plant and equipment other than construction in progress are stated at cost less subsequent accumulated depreciation and accumulated impairment losses.

Depreciation is charged so as to write off the cost of assets, other than construction in progress, over their estimated useful lives and after taking into account of the estimated residual value, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Construction in progress represents property, plant and equipment in the course of construction for production or for its own use purposes. Construction in progress is carried at cost less any recognised impairment loss. Construction in progress is classified to the appropriate category of property, plant and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the assets (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the consolidated income statement in the year in which the item is derecognised.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Investment property

On initial recognition, investment properties are measured at cost, including any directly attributable expenditure. Subsequent to initial recognition, investment properties are measured using the fair value model. Gains or losses arising from changes in the fair value of investment property are included in profit or loss for the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use or no future economic benefits are expected from its disposals. Any gain or loss arising on derecognition of the assets is included in the consolidated income statement in the year in which the item is derecognised.

Properties for development

Properties for development represent leasehold land located in the PRC for development for future rental or sale in the ordinary course of business. Cost comprises the costs of land use rights and other costs directly attributable to bringing the leasehold land to the condition necessary for it to be ready for development. The costs of land use rights representing leasehold land held for future development are stated at cost less accumulated amortisation and any identified impairment loss. Other costs directly attributable to bringing the leasehold land to the condition necessary for it to be ready for development are stated at cost less any identified impairment loss.

Upon commencement of development, the properties are transferred to properties under development.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term and benefits received and receivable as an incentive to enter into an operating lease are recognised as a reduction of rental expense over the lease term on a straight-line basis.

Rental income from operating leases is recognised in the consolidated income statements on a straight-line basis over the term of the relevant leases.

Foreign currencies

The individual financial statements of each group entity are presented in the currency of the primary economic environment in which the entity operates its functional currency. For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in RMB, which are the functional currency of the Company and the presentation currency for the consolidated financial statements.

In preparing the financial statements of the individual entities, transactions in currencies other than the entities' functional currency ("foreign currencies") are recorded at the rates of exchanges prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the translation of monetary items are recognised in profit or loss in the period which they arise.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Government grants

Government grants are recognised as income over the periods necessary to match them with the related costs. Grants related to expense items are recognised in the same period as those expenses are charged in the consolidated income statement and are reported separately as 'other income'.

Retirement benefits costs

Payments to defined contribution retirement benefits schemes, including mandatory provident fund schemes and state-managed retirement benefit schemes, are charged as expenses when employees have rendered service entitling them to the contributions.

Share-based payments

Equity-settled share-based payments to employees

The fair value of services received is determined by reference to the fair value of the share options at the grant date.

For grants of share options which are conditional upon satisfying specified vesting conditions, the fair value of share options granted at the grant date is expensed on a straight-line basis over the vesting period, with a corresponding increase in equity (share option reserve). The impact of the revision of the estimates during the vesting period, if any, is recognised in profit or loss with a corresponding adjustment to share option reserve.

At the time when the share options are exercised, the amount previously recognised in share option reserve will be transferred to share premium. When the share options are forfeited after the vesting date or are still not exercised at the expiry date, the amount previously recognised in share option reserve will be transferred to retained profits.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized, based on tax rates that have been enacted on substantively enacted by the balance sheet date. Deferred tax is charged or credited to profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Intangible assets

Intangible assets acquired separately

Intangible assets acquired separately and with finite useful lives are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is charged on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Gains or losses arising from derecognizing an intangible asset are measured at the difference between the net disposal proceeds and the carrying amount of the assets and are recognised in the consolidated income statement when the asset is derecognised.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss exists. Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. An impairment is recognised as an expense immediately.

When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised immediately in profit or loss.

Inventories

Inventories are stated at the lower of cost and net realizable value. Costs are determined on the weighted average cost method. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Financial assets

The Group's financial assets are classified into loans and receivables, available-for-sale investments and financial assets at fair value through profit or loss ("FVTPL"). All regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame estimated by regulation or convention in the marketplace and is recognised and derecognised on a trade date basis. The accounting policies adopted in respect of each category of financial assets are set out below.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Amounts due from related companies, trade and other receivables, bank balances and cash and pledged bank deposits

These financial assets have fixed or determinable payments that are not quoted in an active market and are classified as loans and receivables.

Loans and receivables are measured at initial recognition at fair value, and are subsequently measured at amortized cost using the effective interest method. Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. At each balance sheet date subsequent to initial recognition, loans and receivables (including trade receivables, loan receivables, other receivables, pledged bank deposits, bank balances and cash) are carried at amortized cost using the effective interest method, less any identified impairment losses (see accounting policy on impairment loss on financial assets below).

Available-for-sale investment

Available-for-sale investments are non-derivatives. The Group classified unlisted equity securities as available-for-sale financial assets.

For available-for-sale equity investment that do not have a quoted market price in an active market and whose fair value cannot be reliably measured, they are measured at cost less any identified impairment losses at each balance sheet date subsequent to initial recognition.

Impairment of financial assets

Financial assets, other than those deemed as held for trading, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the financial assets have been impacted.

Objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organisation.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 30 to 90 days, observable changes in national or local economic conditions that correlate with default on receivables.

For financial assets carried at amortised cost, an impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Impairment of financial assets (Continued)

For financial assets carried at cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment loss will not be reversed in subsequent periods.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables and other receivables, where the carrying amount is reduced through the use of an allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss. When a trade receivable or other receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited to profit or loss.

For financial assets measured at amortised cost, if, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment losses was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Financial liabilities and equity

Financial liabilities and equity instruments issued by a group entity are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument.

The accounting policies adopted for financial liabilities are set out below.

Bank and other borrowings

Borrowings are initially measured at fair value, and are subsequently measured at amortized cost, using the effective interest method. Any difference between the proceeds (net of transaction costs) and the settlement or redemption of borrowings is recognised over the term of the borrowings.

Trade, bills and other payables and amounts due to related companies

The above financial liabilities are initially measured at fair value, and are subsequently measured at amortized cost, using the effective interest method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

3. PRINCIPAL ACCOUNTING POLICIES *(Continued)*

Financial instruments *(Continued)*

Derivative financial instruments

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit and loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in profit and loss depends on the nature of the hedge relationship.

Financial guarantee liabilities

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instruments. Financial liabilities are recognised in respect of the financial guarantee provided by the Group to a third party. Financial guarantee liabilities are recognised initially at fair value plus transaction costs that are directly attributable to the issue of the financial guarantee liabilities. After initial recognition, such contracts are measured at the higher of the present value of the best estimate of the expenditure required to settle the present obligation and the amount initially recognised less cumulative amortization.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the assets expire or, the financial assts are transferred and the Group has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognised directly in equity is recognised in profit or loss.

Financial liabilities are derecognised when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit or loss.

4. KEY SOURCES OF ESTIMATION UNCERTAINTY

The following are the key estimations that the directors have made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in financial statements.

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Group to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate the present value.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

(a) Categories of financial instruments

	2007 RMB'000	2006 RMB'000
Financial assets		
Loans and receivables (Including cash and cash equivalents)	**1,121,145**	1,143,666
Financial assets at fair value through profit or loss (FVTPL)	**16,151**	–
Available-for-sale financial assets	**43,278**	310
Financial liabilities		
Amortised cost	**1,936,088**	1,836,858

(b) Financial risk management objectives and polices

The Group's major financial instruments include trade and other receivables, bank balances and cash, pledged bank deposits, derivative financial instruments, amounts due from/to related companies, trade, bills and other payables and bank and other borrowings. Details of these financial instruments are disclosed in respective notes. The Group's activities expose it to a variety of financial risks: market risk (including foreign currency risk, interest rate risk), credit risk and liquidity risk. The board of directors review and agree policies for managing each of these risks and are summarized below.

There has been no significant change to the Group's exposure to market risks or the manner in which it manages and measures the risk.

Market risk

Interest rate risk

The Group's exposure to fair value interest rate risk relates primarily to bank balances and bank and other borrowings (see notes 29 and 31 for detail). The Group has not entered into any interest rate hedging contracts. The directors monitor the Group's exposure on continuing basis and will consider hedging interest rate risk should the need arise.

Foreign currency risk

The Company and its subsidiaries' functional currency is RMB since majority of the revenue of the companies are derived from operations in the PRC.

The Company's exposure to foreign currency risk related primarily to the sales and purchases that denominated in US dollars and such related bank balances and cash, trade and other receivables and trade and other payables arising from time to time. In addition, the Group has short term bank and other borrowings denominated in US dollars. The derivative financial instrument used has no direct relationship with the transactions denominated in US dollars but also give rise to foreign exchange risk exposure for the Group.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Market risk *(Continued)*

Foreign currency risk (Continued)

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Assets		Liabilities	
	2007	2006	**2007**	2006
	RMB'000	RMB'000	**RMB'000**	RMB'000
USD	**554,143**	539,522	**332,014**	279,116
EUR	**18**	–	**23,469**	–
HKD	**192**	1,463	**1,646**	862
GBP	**12**	–	**–**	–

The notional amount of the Group's outstanding foreign currency derivative contracts are set out in note 28.

Sensitivity analysis

As at December 31, 2007, if RMB had strengthened by 5% against USD, loss for the year would have been decreased by RMB3.5 million (including the effect of foreign currency forward contract) (2006: profit for the year would have been RMB13.0 million lower). If RMB had weakened by 5% against USD, loss for the year would have been increased by RMB3.5 million (2006: profit for the year would have been RMB13.0 million higher), mainly as a result of foreign exchange losses on translation of USD denominated trade and other receivables and bank balances and cash cannot be compensated by foreign exchange gains on translation of USD denominated trade and other payables, foreign currency forward contracts and bank and other borrowings.

Credit risk

The carrying amount of pledged bank deposits, bank balances and cash, amounts due from related companies, trade and other receivables and the financial guarantees provided by the Group as disclosed in note 42, represent the Group's maximum exposure to credit risk in relation to its financial assets.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews regularly the recoverable amount of trade and other receivables to ensure that adequate impairment losses are made for irrecoverable amounts. During the year, the Group maintained export credit insurance of major customers to protect the Group against the risk that the overseas customers may default settlement. The Group has no significant concentration of credit risk by customers, with exposure spread over a number of counterparties and customers, however there is concentration of credit risk by geographical location as 85% of the trade receivables amounting to RMB362 million are concentrated on the United States.

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Liquidity risk

Liquidity risk is the risk that the Group is unable to meet its current obligations when they fall due. The Group measures and monitors its liquidity through the maintenance of adequate level of liquid assets to ensure the availability of sufficient cash flows to finance the Group's operations.

The following tables detail the Group's remaining contractual maturity for its financial liabilities as well as derivative and non-derivative financial assets which are monetary in nature. The table has been drawn up based on the undiscounted cash flows of financial assets and financial liabilities. In the case of financial liabilities, the cash flows are categorised based on the earliest date on which the Group can be required to pay. The table include both interest and principal cash flows.

	Weighted average effective interest rate %	Within 1 year RMB'000	1-5 years RMB'000	Total RMB'000
2007				
Non-derivative financial assets				
Trade and other receivables		**530,853**	**–**	**530,853**
Pledged bank deposits	**0.72**	**86,360**	**–**	**86,360**
Bank balances and cash	**0.72**	**508,182**	**–**	**508,182**
Derivative financial instruments (net settlement)				
Foreign currency forward contracts		**16,151**	**–**	**16,151**
Total		**1,141,546**	**–**	**1,141,546**
Non-derivative financial liabilities				
Trade, bills and other payables		**378,795**	**–**	**378,795**
Amounts due to related companies		**81**	**–**	**81**
Bank and other borrowings	**6.24**	**1,643,333**	**11,049**	**1,654,382**
Total		**2,022,209**	**11,049**	**2,033,258**
2006				
Non-derivative financial assets				
Trade and other receivables		599,472	–	599,472
Pledged bank deposits	0.72	164,396	–	164,396
Bank balances and cash	0.72	383,716	–	383,716
Total		1,147,584	–	1,147,584
Non-derivative financial liabilities				
Trade, bills and other payables		560,302	–	560,302
Amounts due to related companies		19,467	–	19,467
Bank and other borrowings	6.71	1,330,341	11,098	1,341,439
Total		1,910,110	11,098	1,921,208

5. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES *(Continued)*

Liquidity risk *(Continued)*

Fair value

The fair value of financial assets and financial liabilities are determined as follows:

The fair value of financial assets and financial liabilities (including derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices or rates from observable current market transactions as input.

The directors consider that the carrying amounts of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values.

Capital risk management

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern while maximising the return to equity holders through the optimisation of the debt and equity balance. The Group's overall strategy remains unchanged from prior year.

The capital structure of the Group consists of debt, which includes the borrowings disclosed in note 31 and equity attributable to equity holders of the Company, comprising issued share capital, reserves and retained earnings.

The directors of the Company review the capital structure on a regular basis. As part of this review, the directors consider the cost of capital and the risks associated with each class of capital. The Group will balance its overall capital structure through the payment of dividends, new share issues and share buy-backs as well as the issue of new debt or the redemption of existing debt.

6. BUSINESS AND GEOGRAPHICAL SEGMENTS

For management purposes, the Group is currently organized into five 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;

– Properties development; and

– Others (including sale of wooden frame, retail and others)

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Segment information about these businesses is presented below:

	Upholstered furniture RMB'000	Furniture leather RMB'000	Automotive leather RMB'000	Others RMB'000	Eliminations RMB'000	Total RMB'000
2007						
Turnover						
External sales	**2,573,856**	**461,269**	**217,980**	**57,622**	**–**	**3,310,727**
Inter – segment sales	**994,756**	**948,459**	**–**	**121,107**	**(2,064,322)**	**–**
2006						
Turnover						
External sales	3,122,953	615,104	150,141	28,315	–	3,916,513
Inter – segment sales	603,005	2,249,976	–	126,818	(2,979,799)	–

Inter – segment sales are charged at prevailing market prices.

	Year ended December 31, 2007 RMB'000	2006 RMB'000
Result		
Segment result		
– Upholstered furniture	**(83,458)**	195,956
– Furniture leather	**(27,631)**	(17,748)
– Automotive leather	**(11,042)**	(9,391)
– Others	**8,214**	(246)
	(113,917)	168,571
Unallocated income	**40,292**	31,361
Unallocated expenses	**(10,339)**	(10,345)
Share of profit of associates	**103**	937
Finance costs	**(91,579)**	(85,390)
(Loss) profit before taxation	**(175,440)**	105,134
Taxation	**(14,584)**	(21,707)
(Loss) profit for the year	**(190,024)**	83,427

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Other Information

	Year ended December 31, 2007 RMB'000	2006 RMB'000
Impairment loss recognised in respect of property, plant and equipment		
– Upholstered furniture	**2,252**	–
– Furniture leather	**2,951**	–
– Automotive leather	**1,801**	–
	7,004	–
Impairment loss recognised (reversed) in respect of trade and other receivables		
– Upholstered furniture	**15,610**	5,747
– Furniture leather	**(6,128)**	10,398
– Automotive leather	**(2,250)**	1,392
– Others	**3,136**	89
	10,368	17,626
Allowances for inventories		
– Upholstered furniture	**14,448**	1,480
– Furniture leather	**69,021**	9,924
– Automotive leather	**15,855**	–
– Others	**315**	–
	99,639	11,404
Capital additions		
– Upholstered furniture	**13,926**	52,518
– Furniture leather	**17,646**	15,102
– Automotive leather	**1,724**	493
– Properties development	**19,260**	–
– Others	**6,742**	5,653
	59,298	73,766
Addition to other non-current assets		
– Properties development	**387,881**	32,901
Depreciation and amortization		
– Upholstered furniture	**43,340**	45,911
– Furniture leather	**40,734**	42,497
– Automotive leather	**5,680**	3,825
– Others	**5,244**	3,975
	94,998	96,208
Goodwill impairment		
– Upholstered furniture	**157,958**	10,138
– Automotive leather	**–**	12,910
	157,958	23,048

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Balance Sheets

	As at December 31,	
	2007	2006
	RMB'000	RMB'000
ASSETS		
Segment assets		
– Upholstered furniture	**1,178,095**	1,656,269
– Furniture leather	**1,402,775**	1,475,264
– Automotive leather	**185,323**	200,962
– Properties development	**471,133**	–
– Others	**105,826**	128,275
Subtotal	**3,343,152**	3,460,770
Investments in associates	**15,833**	26,728
Investment in a jointly controlled entity	**2,614**	2,614
Unallocated corporate assets	**777,851**	584,416
	4,139,450	4,074,528
LIABILITIES		
Segment liabilities		
– Upholstered furniture	**353,699**	437,400
– Furniture leather	**116,240**	119,390
– Automotive leather	**6,844**	7,410
– Others	**45,653**	39,836
Subtotal	**522,436**	604,036
Unallocated corporate liabilities	**1,647,168**	1,287,515
	2,169,604	1,891,551

6. BUSINESS AND GEOGRAPHICAL SEGMENTS *(Continued)*

Geographical segment

Segment assets are substantively located in the People's Republic of China ("PRC").

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

	2007 RMB'000	2006 RMB'000
United States	**2,041,107**	2,825,773
PRC, including Hong Kong	**792,301**	736,138
Europe	**293,506**	160,326
Australia	**100,546**	122,253
Others	**83,267**	72,023
	3,310,727	3,916,513

7. OTHER INCOME

Details of other income are as follows:

	2007 RMB'000	2006 RMB'000
Government grants		
Grants for technology development	**1,480**	2,830
Grants for export sales	**9,676**	18,362
Incentive for business development	**3,691**	4,274
Other grants	**4,177**	3,456
	19,024	28,922
Net gain from sale of raw materials	**3,755**	10,947
Interest income	**6,358**	8,905
Discounts on acquisition of an additional interest in a subsidiary	**–**	10,279
Gain on disposals of subsidiaries (note 36)	**7,720**	8,838
Gain on disposal of an associate	**1,056**	–
Gain on fair value change on foreign currency forward contracts	**16,151**	–
Gain on fair value change on investment property	**5,671**	–
Others	**11,186**	3,339
	70,921	71,230

8. OTHER EXPENSES

	2007 RMB'000	2006 RMB'000
Goodwill impairment (note 16)	**157,958**	23,048
Impairment loss on property, plant and equipment	**7,004**	–
Donation	**1,394**	2,919
Loss on disposal of property, plant and equipment	**–**	2,161
Others	**2,557**	1,869
	168,913	29,997

9. FINANCE COSTS

	2007 RMB'000	2006 RMB'000
Interest on:		
Bank borrowings wholly repayable within five years	**90,797**	84,611
Other borrowings wholly repayable within five years	**272**	269
Other borrowings not wholly repayable within five years	**510**	510
	91,579	85,390

10. (LOSS) PROFIT BEFORE TAXATION

(Loss) profit before taxation has been arrived at after charging:

	2007 RMB'000	2006 RMB'000
Amortization of intangible assets (included in administrative expenses)	**500**	350
Amortization of prepaid lease payments	**2,707**	3,277
Depreciation of property, plant and equipment	**94,498**	95,858
Total depreciation and amortization	**97,705**	99,485
Auditor's remuneration	**5,064**	4,619
Cost of inventories recognised as expense	**3,011,190**	3,489,136
Impairment loss recognised in respect of trade and other receivables	**10,368**	17,626
Operating lease rentals in respect of land and buildings	**10,051**	1,892
Net foreign exchange losses	**26,740**	17,836
Expenses of sampling and products upgrading	**9,453**	8,048
Gain on disposal of listed securities	**(157)**	–
Total employee benefit expenses	**270,209**	286,659

Notes to the Consolidated Financial Statements (cont'd)

For the year ended December 31, 2007

11. DIRECTORS AND EMPLOYEES' EMOLUMENTS

The emoluments paid or payable to the directors were as follows:

2007

	Zhu Zhangjin ("Mr. Zhu") RMB'000	Zhou Xiaosong RMB'000	Zhu Jianqi RMB'000	Li Hui RMB'000	Lu Yungang RMB'000	Chow Joseph RMB'000	Zhang Huaqiao RMB'000	Total RMB'000
Fees	–	–	–	–	–	–	–	–
Other emoluments								
Salaries and other benefits	340	238	238	–	175	175	175	1,341
Contributions to retirement benefits schemes	2	2	2	–	–	–	–	6
Share based payment	378	378	378	–	76	76	–	1,286
Total emoluments	720	618	618	–	251	251	175	2,633

2006

	Mr. Zhu RMB'000	Zhou Xiaosong RMB'000	Zhu Jianqi RMB'000	Li Hui RMB'000	Lu Yungang RMB'000	Chow Joseph RMB'000	Zhang Huaqiao RMB'000	Shi Zhengfu RMB'000	Sun Qiangchang RMB'000	Total RMB'000
Fees	–	–	–	–	–	–	–	–	–	–
Other emoluments										
Salaries and other benefits	340	238	238	–	150	150	75	75	–	1,266
Contributions to retirement benefits schemes	2	2	2	–	–	–	–	–	–	6
Share based payment	1,039	1,039	1,039	–	208	208	–	–	–	3,533
Total emoluments	1,381	1,279	1,279	–	358	358	75	75	–	4,805

11. DIRECTORS AND EMPLOYEES' EMOLUMENTS *(Continued)*

Three (2006: three) of the five individuals with the highest emoluments in the Group were directors of the Company whose emoluments are included in the disclosures as above. The emoluments of the remaining two (2006: two) individuals was as follows:

	2007 RMB'000	2006 RMB'000
Basic salaries and other benefits	**653**	854
Contributions to retirement benefits schemes	**12**	14
Share based payment	**453**	1,247
	1,118	2,115

The emoluments of the two individuals with the highest emoluments are within the following bands:

HK$	**2007 Number of individuals**	2006 Number of individuals
1,000,000 or below	**2**	1
1,000,001-1,500,000	**–**	1

During the year, no emoluments were paid by the Group to the directors and five highest paid individuals as an inducement to join or upon joining the Group or as compensation for loss of office. None of the directors has waived any emoluments during the year.

12. TAXATION

	2007 RMB'000	2006 RMB'000
Hong Kong Profits Tax		
– current year	**19**	1,027
– (over)under provision in previous year	**(42)**	58
PRC enterprise income tax		
– current year	**15,602**	18,717
– (over)under provision of income tax in previous year	**(995)**	1,905
	14,584	21,707

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 years of 2007 and 2006 ("Tax Holidays"). The maximum Tax Holidays period is 5 years from the first taxable profit year.

12. TAXATION *(Continued)*

The taxation for the year can be reconciled to the (loss) profit before taxation per the consolidated income statement as follows:

	2007 **RMB'000**	2006 RMB'000
(Loss) profit before taxation	**(175,440)**	105,134
Tax rate applicable to the major operation of the Group	**26.4%**	26.4%
Tax at the applicable rate	**(46,316)**	27,755
Tax effect of income not taxable for tax purpose	**(2,796)**	(1,210)
Tax effect of expenses/losses not deductible for tax purpose	**42,717**	6,052
Tax effect of temporary differences not recognised as deferred tax assets	**19,652**	1,693
Tax effect of tax losses not recognised as deferred tax assets	**13,747**	9,519
Tax effect of tax profits not recognised as deferred tax liabilities	**(1,497)**	–
Tax effect of Tax Holidays and concessions	**(13,511)**	(27,988)
Tax effect of different tax rates of subsidiaries operating with different tax regulations in the PRC and in Hong Kong	**3,652**	4,170
(Over) under provision in previous years	**(1,037)**	1,963
Tax effect of share of result of associates	**(27)**	(247)
Taxation for the year	**14,584**	21,707

As at December 31, 2007, the Group has unused tax losses of approximately RMB61,121,000 (2006: RMB43,761,000) available to offset against future profits, of which losses of RMB28,374,000 (2006: RMB5,527,000) will expire in year 2011, losses of RMB32,747,000 (2006: RMB38,234,000) will expire in year 2012. No deferred tax asset has been recognised in respect of unused tax losses due to the unpredictability of future profit streams.

On March 16, 2007, the PRC promulgated Law of the People's Republic of China on Enterprise Income Tax (the "New Law") by Order No.63 of the president of the PRC. On December 6, 2007, the State Council of the PRC issued Implementation Regulations of the New Law. The New Law and Implementation Regulation will change the tax rate from 26.4% to 25% for subsidiaries located in PRC of the Group from January 1, 2008.

Under the New Tax Law and Implementation Regulations issued by the State Council, PRC income tax at the rate of 10% is applicable to interest and dividends payable to investors that are "non-resident enterprises", which do not have an establishment or place of business in the PRC, or which have such establishment or place of business but the relevant income is not effectively connected with the establishment or place of business, to the extent such interest or dividends have their sources within the PRC. If the Company is deemed to be a PRC "resident enterprise", dividends distributed from the Company's PRC subsidiaries to the Company's Hong Kong subsidiaries and ultimately to the Company's Cayman Islands subsidiaries, could be exempted from Chinese dividend withholding tax, and dividends from Cayman Islands subsidiaries to ultimate shareholders would be subject to PRC withholding tax at 10% or a lower treaty rate. There is no such tax implication in 2007.

13. ASSETS/LIABILITIES HELD FOR SALE

Pursuant to a Board resolution dated October 8, 2007 and the shareholders' approval on November 23, 2007, the Company entered into a binding agreement with two independent third parties to dispose a 50.5% held subsidiary, Haining Oyi May Sofa Co., Ltd. ("Oyi May") (海寧歐意美沙發有限公司), for a consideration of RMB24.5 million. As at December 31, 2007, this disposal has not been completed due to delay of local government approval. The assets and liabilities attributable to Oyi May have been classified as a disposal group held for sale and are presented separately in the consolidated balance sheet (see below).

The subsidiary is included in the Group's upholstered furniture production activities for segment reporting purposes (see note 6). The net proceeds of the disposal exceeds the Group's attributable portion of net carrying amount of the relevant assets and liabilities as at December 31, 2007, accordingly, no impairment loss has been recognised.

The major classes of assets and liabilities of Oyi May classified as held for sale are as follows:

	2007 **RMB'000**
Property, plant and equipment	**74,377**
Inventories	**63,064**
Trade and other receivables	**47,772**
Pledged bank deposits	**27,946**
Bank balances and cash	**4,301**
Prepaid lease payment	**9,083**
Intangible assets	**54**
Amount due from related companies	**4,793**
Assets classified as held for sale	**231,390**
Trade, bills and other payables	**148,388**
Amount due to related companies	**2,973**
Bank and other borrowings	**23,652**
Liabilities classified as held for sale	**175,013**
Net assets classified as held for sale	**56,377**
Less: minority interest	**(27,907)**
Net assets classified as held for sale attributable to the Group	**28,470**

The net assets set out above do not include intercompany balances owed to other Group's entities amounting to RMB15.8 million.

14. DIVIDEND

Dividends recognised as distributions during the year:

	2007 RMB'000	2006 RMB'000
Final 2005 – HK7.59 cents per share	–	79,575
Interim 2006 – HK3.45 cents per share	–	34,683
	–	114,258

15. (LOSS) EARNING PER SHARE

The calculation of the basic and diluted (loss) earning per share attributable to the equity holders of the Company are based on the following data:

(Loss) earning

	2007 RMB'000	2006 RMB'000
(Loss) earning for the purposes of basic and diluted (loss) earning per share, being (loss) profit attributable to equity holders of the Company	(194,149)	64,143

Number of shares

	2007	2006
Weighted average number of ordinary shares for the purposes of basic and diluted (loss) earning per share	990,048,369	1,004,410,969

The share options granted to the employees of the Group has no effect to the diluted (loss) earning per share because the exercise price of the Company's share options was higher than average market price for shares during the share option outstanding period.

16. GOODWILL

	2007 **RMB'000**	2006 RMB'000
COST		
At January 1 and December 31	**181,006**	181,006
ACCUMULATED IMPAIRMENT LOSS		
At January 1	**23,048**	–
Impairment loss recognised in the year	**157,958**	23,048
At December 31	**181,006**	23,048
CARRYING AMOUNTS		
At December 31	**–**	157,958

Goodwill arose from the Group's acquisition of the subsidiaries from SFT International Pty. Ltd. ("SFT") in September 2004. Goodwill acquired in a business combination is allocated, at acquisition, to the cash generating units (CGUs) that are expected to benefit from that business combination.

During the financial year of 2007, the Group assessed the recoverable amount of the goodwill, and determined that goodwill associated with the Group's upholstered furniture operation was impaired by approximately RMB158 million (2006: automotive leather impairment RMB13 million; upholstered furniture impairment RMB10 million). The recoverable amount of the upholstered furniture operation was assessed by reference to the estimated value in use of the CGUs.

The main factor contributing to the impairment of the cash-generating units were deteriorating demand from customers as a result of the downturn in the U.S. housing market, the appreciation of the RMB against the U.S. dollars, increase in the costs of chemicals, foam, timber and labor, and the reduction of export tax rebates.

Allocation of goodwill to CGUs

Before recognition of impairment losses, the carrying amount of goodwill allocated to the following CGUs:

	2007 **RMB'000**	2006 RMB'000
Haining Kareno Furniture Co., Ltd. ("Kareno")	**60,287**	60,287
Haining Kasen Leather Co., Ltd. ("Haining Kasen")	**97,671**	97,671
Haining Schinder Tanning Co., Ltd.	**12,910**	12,910
Haining Home Direct Furniture Co., Ltd. ("Home Direct")	**10,138**	10,138
	181,006	181,006

16. GOODWILL *(Continued)*

IMPAIRMENT TESTING ON GOODWILL

The carrying amount of goodwill (net of accumulated impairment loss) as at December 31, 2007 is allocated as follows:

	2007 RMB'000	2006 RMB'000
Upholstered furniture operation		
– Kareno	–	60,287
– Haining Kasen	–	97,671
	–	157,958

The recoverable amount of the CGUs is determined based on a value in use calculation which uses cash flow projections based on financial budgets approved by management covering a five-year period, and a discount rate of 10.85% per annum (2006: 11.78% per annum). The cash flows beyond that five year period have been extrapolated using a steady 2% per annum growth rate.

The key assumptions used in the value in use calculations for the above operations are as follows:

Budgeted sales growth rate	The values assigned to the assumptions reflect the past experiences, overall industry situation in PRC, as well as the marketing staff's best estimate for the sales in the next five years. The growth factor is consistent with management development strategies. Management believes that the planned sales decrease and growth per year for the next five years is acceptable.
Budgeted gross margin	The average gross margins achieved in the three years immediately before the budget period, normalized with the effect of increased raw material prices and currency appreciation. This reflects past experience, with management expects that the Group will absorb the adverse effects of increased raw material prices and the appreciation of RMB against US dollars at a reasonable extent.
Raw materials price inflation	The forecast takes into account of major raw materials' price adjustments (included the exchange rate implication) during the budget period for the countries from which raw materials are purchased. The values assigned to the key assumption are consistent with external sources of information.

17. PROPERTY, PLANT AND EQUIPMENT

	Buildings RMB'000	Plant and equipment RMB'000	Motor vehicles RMB'000	Furniture, fixtures and equipment RMB'000	Construction in progress RMB'000	Total RMB'000
COST						
At January 1, 2006	883,689	475,158	26,828	47,765	72,636	1,506,076
Additions	5,224	28,941	5,808	5,168	27,734	72,875
Disposals of subsidiaries	(72,242)	(8,839)	(1,672)	(2,568)	(4,029)	(89,350)
Disposals	–	(545)	(133)	(501)	(1,617)	(2,796)
Reclassification	74,970	1,439	1,006	329	(77,744)	–
At December 31, 2006	891,641	496,154	31,837	50,193	16,980	1,486,805
Additions	4,177	18,727	8,580	3,397	4,763	39,644
Disposals	(239)	(17,684)	(150)	(101)	(4,680)	(22,854)
Disposals of subsidiaries	(73,763)	(10,974)	(791)	(2,303)	(496)	(88,327)
Reclassification	(295)	–	–	295	–	–
Transfers	13,117	584	–	–	(13,701)	–
Reclassified as held for sale	(63,312)	(23,137)	(3,809)	(2,386)	–	(92,644)
At December 31, 2007	**771,326**	**463,670**	**35,667**	**49,095**	**2,866**	**1,322,624**
DEPRECIATION AND IMPAIRMENT						
At January 1, 2006	78,244	115,917	13,327	17,358	–	224,846
Provided for the year	42,085	41,773	3,990	8,010	–	95,858
Elimination on disposals of subsidiaries	(4,937)	(1,241)	(406)	(529)	–	(7,113)
Elimination on disposals	–	(149)	(44)	(192)	–	(385)
At December 31, 2006	115,392	156,300	16,867	24,647	–	313,206
Provided for the year	40,449	41,635	4,773	7,641	–	94,498
Eliminated on disposals	–	(15,708)	(135)	(40)	–	(15,883)
Eliminated on disposal of subsidiaries	(7,532)	(1,727)	(346)	(821)	–	(10,426)
Impairment loss recognised	502	6,502	–	–	–	7,004
Reclassified as held for sale	(9,078)	(6,745)	(1,365)	(1,079)	–	(18,267)
At December 31, 2007	**139,733**	**180,257**	**19,794**	**30,348**	**–**	**370,132**
CARRYING AMOUNTS						
At December 31, 2007	**631,593**	**283,413**	**15,873**	**18,747**	**2,866**	**952,492**
At December 31, 2006	776,249	339,854	14,970	25,546	16,980	1,173,599

The buildings are located on the land leased under medium-term land use rights in the PRC.

17. PROPERTY, PLANT AND EQUIPMENT *(Continued)*

The above items other than construction in progress are depreciated on a straight line basis after consideration of residual value at the following rates per annum:

Buildings	20 years or lease term, if shorter
Plant and equipment	10-15 years
Motor vehicles	5 years
Furniture, fixtures and equipment	5-10 years

The Group has pledged its buildings with a carrying amount of approximately RMB482 million (2006: RMB469 million) to secure general banking facilities granted to the Group.

As at December 31, 2007, the title deeds of buildings with net carrying amount of RMB42 million (2006: RMB45 million) has not been obtained. The directors believe that the relevant title deeds will be granted in the due course and the absence of official certificate does not impair the value of the relevant properties of the Group.

Additional impairment losses recognised in respect of plant and equipment in the year amounted to RMB7.0 million (note 8). These losses are attributable to technological obsolescence in the case of certain plant and equipment and the result of the impairment assessment of the relevant CGUs mentioned in note 16.

18. PREPAID LEASE PAYMENTS

The prepaid lease payments made by the Group are payment for land use rights under medium-term lease in the PRC. An amount of approximately RMB72,325,000 (2006: RMB82,125,000) had been pledged to banks to secure the borrowings of the Group granted by the banks.

	2007 **RMB'000**	2006 RMB'000
Analyzed for reporting purposes as:		
Non-current asset	**102,265**	131,860
Current asset	**2,311**	2,904
	104,576	134,764

	2007 **RMB'000**	2006 RMB'000
Without title deeds	**13,668**	23,189
With title deeds	**90,908**	111,575
	104,576	134,764

The directors believe that the relevant title deeds will be granted to the Group in due course.

19. PROPERTIES FOR DEVELOPMENT

	2007 RMB'000	2006 RMB'000
At January 1, 2007	–	–
Transfer from investment property	51,000	–
Additions	263,781	–
At December 31, 2007	314,781	–

In 2006, the Group acquired a parcel of land in Boao, Hainan Province with acquisition cost of RMB32,901,000 for capital appreciation purpose under medium-term lease in the PRC and it was recorded as an investment property. Further cost of RMB12.4 million was incurred by the Group in relation to the land. Pursuant to a board resolution dated October 8, 2007, the Group decided that the land will be used for properties development purpose. The preliminary design for the development has commenced and the land was, as a result, reclassified to properties for development at its fair value as at October 8, 2007.

The fair value of the land as at October 8, 2007 was RMB51,000,000 and it was arrived at by reference to a valuation carried out by Jones Lang LaSalle Sallmanns Limited, an independent qualified professional valuer. The fair value change on investment property up to October 8, 2007 of approximately RMB5,671,000 was recorded as other income for the year ended December 31, 2007 (2006: Nil).

In 2007, the Group acquired another parcel of land in Changsha, Hunan Province with acquisition cost of RMB263,781,000 for properties development purpose.

20. INTANGIBLE ASSETS

	RMB'000
COST	
At January 1, 2006	1,474
Additions	891
Elimination on disposals of subsidiaries	(147)
At December 31, 2006	2,218
Additions	394
Elimination on disposals of subsidiaries	(5)
Classified as held for sale	(177)
At December 31, 2007	**2,430**
ACCUMULATED AMORTIZATION	
At January 1, 2006	397
Provided for the year	350
Elimination on disposals of subsidiaries	(14)
At December 31, 2006	733
Provided for the year	500
Elimination on disposals of subsidiaries	(1)
Classified as held for sale	(123)
At December 31, 2007	**1,109**
CARRYING AMOUNT	
At December 31, 2007	**1,321**
At December 31, 2006	1,485

Notes to the Consolidated Financial Statements (cont'd)

For the year ended December 31, 2007

20. INTANGIBLE ASSETS *(Continued)*

Intangible assets represent expenditure incurred for upgrade of computer software and are amortized over five years.

21. INVESTMENTS IN ASSOCIATES

At December 2006, the interests in associates represents a 25% interest in 海寧美景海綿有限公司(Future Foam Asia, Inc.) ("Future Foam"), an equity joint venture established in the PRC in 2004, and a 30% interest in 海寧市斜橋森博水務有限公司 (Haining Xieqiao Senbo Water Co., Ltd.) ("Senbo Water"), an associate changed from a subsidiary through additional capital injection by minority shareholders, and a 35% interest in Sichuan Longteng Leather Co., Ltd. ("Longteng"), an equity joint venture established in the PRC in 2006.

At December 31, 2007, the interests in associates represents a 30% interest in 海寧市斜橋森博水務有限公司 (Haining Xieqiao Senbo Water Co., Ltd.) ("Senbo Water"), an equity joint venture established in PRC in 2003; and a 35% interest in Sichuan Longteng Leather Co., Ltd. ("Longteng"), an equity joint venture established in the PRC in 2006.

During the year, the Group has disposed of its 25% interest in Future Foam to an independent third party. The consideration of the disposal was RMB12,054,000 and the Group recorded a disposal gain of RMB1,056,000.

	2007 RMB'000	2006 RMB'000
Cost of unlisted investment in associates	**16,667**	26,905
Share of post-acquisition losses	**(834)**	(177)
	15,833	26,728

	2007 RMB'000	2006 RMB'000
Summarized financial information relating to the associates		
Total assets	**50,609**	130,734
Total liabilities	**(5,276)**	(52,275)
Net assets	**45,333**	78,459
Group's share of net assets of associates	**15,833**	26,728
Revenue	**73,284**	96,309
Profit for the year	**891**	4,048
Group's share of associates' profit for the year	**103**	937

22. INVESTMENT IN A JOINTLY CONTROLLED ENTITY

The interest in a jointly controlled entity represents a 50% interest in 海寧市卡森－美如可思皮革有限公司 (Haining Kasen-Melx Leather Co., Ltd.) ("Kasen-Melx"), an equity joint venture established in the PRC in August 2005. The jointly controlled entity was established for the principal purpose of trading in leather and other furniture products.

Jointly controlled entity is accounted for using the equity method of accounting:

	2007 **RMB'000**	2006 RMB'000
Cost of unlisted investment in jointly controlled entity	**2,614**	2,614

The summarized financial information in respect of the Group's jointly controlled entities which are accounted for using the equity method is set out below:

	2007 **RMB'000**	2006 RMB'000
Current assets	**5,469**	7,891
Non current assets	**190**	240
	5,659	8,131
Current liabilities	**(226)**	(2,778)
Net assets	**5,433**	5,353
Group's share of net assets of jointly controlled entity	**2,614**	2,614
Revenue	**3,062**	2,103
Profit for the year	**80**	164
Group's share of jointly controlled entity's profit for the year	**–**	–

23. AVAILABLE-FOR-SALE INVESTMENTS

	2007 **RMB'000**	2006 RMB'000
Unlisted equity securities		
– Haining China Leather Market Co. Ltd. ("HCLM")	**42,968**	–
– Other	**310**	310
	43,278	310

The Group made a strategic investment of RMB42,968,000 in HCLM in September 2007 which represents 4.92% equity interest in the HCLM.

The equity securities represents investments in unlisted equity securities issued by state owned entities incorporated in the PRC. They are measured at cost less impairment at each balance sheet date because the range of reasonable fair value estimates is so significant that the directors of the Group are of the opinion that their fair values cannot be measured reliably.

Notes to the Consolidated Financial Statements (cont'd)

For the year ended December 31, 2007

24. OTHER LONG TERM ASSETS

Other long term assets represent the deposits and initial payments for acquisition of:

	2007 RMB'000	2006 RMB'000
A subsidiary primarily holding a property (note)	**79,200**	–
An office	**19,260**	–
Land use rights in the PRC under medium-term lease from the Government	**44,900**	–
	143,360	–

note: Pursuant to an equity transfer agreement dated December 20, 2007, the Company agreed to purchase 99% equity interest in Qionghai Bodi Real Estate Co., Ltd. (琼海博地置業有限公司) from an independent third party for a consideration of approximately RMB100 million. As at December 31, 2007, RMB79.2 million have been paid to the vendor and are recorded as an other long term asset at December 31, 2007.

25. INVENTORIES

	2007 RMB'000	2006 RMB'000
Raw materials	**258,303**	348,878
Work in progress	**771,779**	806,913
Finished goods	**112,638**	170,425
	1,142,720	1,326,216

26. TRADE AND OTHER RECEIVABLES

	2007 RMB'000	2006 RMB'000
Trade receivables	**400,469**	535,961
Less: allowance for doubtful debts	**(34,153)**	(45,494)
	366,316	490,467
Prepayments	**83,102**	64,917
Other receivables	**129,503**	92,890
Less: allowance for doubtful debts	**(29,333)**	(14,426)
	549,588	633,848

26. TRADE AND OTHER RECEIVABLES *(Continued)*

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

	2007 **RMB'000**	2006 RMB'000
Aged:		
Within 60 days	**256,714**	345,725
61-90 days	**37,943**	53,892
91-180 days	**49,144**	47,468
181-365 days	**19,691**	35,546
1-2 years	**2,824**	7,836
	366,316	490,467

Before accepting any new customers, the Group reviews the credit quality and defines credit limits by customer. Limits attributed to customers are reviewed once a year. The Group believes that 19.56% of the trade receivables that are neither pass due nor impaired have the best credit rating.

Included in the Group's trade receivable balance are debtors with aggregate carrying amount of RMB71,659,000 (2006: RMB90,850,000) which are past due at the reporting date. However, the directors have considered these amounts in the context of the credit quality of the relevant customers and concluded that those balances are not impaired.

Aging of trade receivables which are past due but not impaired:

	2007 **RMB'000**	2006 RMB'000
Aged:		
91-180 days	**49,144**	47,468
181-365 days	**19,691**	35,546
1-2 years	**2,824**	7,836
	71,659	90,850

The Group has provided fully for all receivables over 2 years because historical experience is such that receivables that are past due beyond 2 years are generally not recoverable.

Movement in the allowance for doubtful debts

	2007 **RMB'000**	2006 RMB'000
Balance at beginning of the year	**59,920**	44,413
Amounts written off during the year	**(770)**	(496)
Amount relating to disposal of subsidiaries	**(1,107)**	(1,623)
Increase in allowance recognised in profit or loss	**10,368**	17,626
Classified as held for sale	**(3,218)**	–
Balance at end of the year	**65,193**	59,920

The impairment recognised represented the long-aged overdue debts with uncertain collection.

27. AMOUNTS DUE FROM (TO) RELATED COMPANIES

Details of the amounts due from (to) related companies are as follows:

Name of related companies	Notes	2007 RMB'000	2006 RMB'000
(a) Operating in nature			
海寧宇潔物資回收有限公司 Haining Yujie Material Recycling Co., Ltd. ("Yujie")	(i), (v)	**3,250**	3,783
伊犁霍爾果斯皮革有限公司 Yili Horgos Leather Co., Ltd. ("Yili Horgos")	(i), (v)	**922**	(29)
Starcorp Corporation Pty. Ltd. ("Starcorp")	(i), (v)	**19,861**	28,496
Haining Kasen-Melx Leather Co., Ltd. ("Kasen-Melx")	(v), (viii)	**196**	3,080
澳林家具(上海)有限公司 AoLin Furniture (Shanghai) Co., Ltd.	(i), (v)	**5**	196
海寧長虹進出口有限公司 Haining Changhong Import and Export Co., Ltd. ("Changhong I&E")	(iv), (v)	**–**	193
海派皮業有限公司 Haining Haipai Leather Industry Co., Ltd.	(iv), (v)	**39**	29
(b) Non-operating in nature			
海寧美景海綿有限公司 Future Foam	(ii), (vii)	**–**	(13,438)
North Pole Ltd.	(v), (vi)	**–**	313
海寧市斜橋森博水務有限公司 Haining Xieqiao Senbo Water Co., Ltd. ("Senbo Water")	(iii), (v)	**99**	506
海寧獵馬皮革服裝有限公司 Haining Liema Leather Garments Co., Ltd.	(iv), (ix)	**(81)**	(6,000)
		24,291	17,129
Represented by:			
Amounts due from related companies, included in current assets		**24,372**	36,596
Amounts due to related companies, included in current liabilities		**(81)**	(19,467)
		24,291	17,129

27. AMOUNTS DUE FROM (TO) RELATED COMPANIES *(Continued)*

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

	2007		2006	
	Amounts due from related companies RMB'000	**Amounts due to related companies RMB'000**	Amounts due from related companies RMB'000	Amounts due to related companies RMB'000
Aging:				
Within 60 days	**17,787**	**–**	10,421	(12,621)
61-90 days	**795**	**(81)**	5,619	(6,105)
91-180 days	**5,532**	**–**	12,067	(706)
181-365 days	**245**	**–**	6,303	(35)
1-2 years	**13**	**–**	2,186	–
2-3 years	**–**	**–**	–	–
	24,372	**(81)**	36,596	(19,467)

Aging of trade receivables which are past due but not impaired:

	2007 RMB'000	2006 RMB'000
Aging		
91-180 days	**5,532**	12,067
181-365 days	**245**	6,303
1-2 years	**13**	2,186
	5,790	20,556

The Group has provided fully for all receivables over 2 years because historical experience is such that receivables that are past due beyond 2 years are generally not recoverable.

Details of the operating transactions with the related parties are set out in note 40.

notes:

(i) Mr. Zhu has influence and beneficial interests in these companies through Sunbridge Industrial Group Co., Ltd.

(ii) The amounts are unsecured, interest-free and repayable according to the credit terms.

(iii) Senbo Water ceased to be a subsidiary and became an associate of the Group since May 2006.

(iv) A director of a non-wholly owned subsidiary has influence and beneficial interests in the company.

(v) The amounts are unsecured, interest-free and expected to be settled within one year.

(vi) The company is the subsidiary of one major shareholder of the Company.

(vii) Future Foam ceased to be an associate of the Group in August 2007.

(viii) Jointly controlled entity of the Group.

(ix) The amounts are unsecured, carried annual interest rate of 6.696% and repayable on demand.

28. DERIVATIVE FINANCIAL INSTRUMENTS

	Year ended December 31, Current	
	2007	2006
	RMB'000	RMB'000
Foreign currency forward contracts	**16,151**	–

At balance sheet date, the Company had the following foreign currency forward contracts in order to manage the Company's foreign currency exposure in relation to its foreign currency monetary assets. Major terms of these contracts are as follows:

Notional amount	Maturity	Exchange rates
Sell USD1,000,000	2008/01/04	US$1: RMB7.5707
Sell USD1,000,000	2008/01/05	US$1: RMB7.5800
Sell USD1,000,000	2008/01/15	US$1: RMB7.5645
Sell USD2,500,000	2008/01/15	US$1: RMB7.5619
Sell USD2,000,000	2008/01/22	US$1: RMB7.4600
Sell USD1,000,000	2008/01/25	US$1: RMB7.5610
Sell USD1,000,000	2008/02/05	US$1: RMB7.5568
Sell USD1,000,000	2008/02/05	US$1: RMB7.5690
Sell USD2,500,000	2008/02/15	US$1: RMB7.5499
Sell USD1,000,000	2008/02/15	US$1: RMB7.5530
Sell USD2,000,000	2008/02/20	US$1: RMB7.4600
Sell USD1,000,000	2008/02/25	US$1: RMB7.5490
Sell USD1,000,000	2008/03/05	US$1: RMB7.5580
Sell USD1,000,000	2008/03/05	US$1: RMB7.5452
Sell USD1,000,000	2008/03/14	US$1: RMB7.5413
Sell USD2,500,000	2008/03/17	US$1: RMB7.5394
Sell USD2,000,000	2008/03/20	US$1: RMB7.4600
Sell USD1,000,000	2008/04/05	US$1: RMB7.5470
Sell USD2,500,000	2008/04/15	US$1: RMB7.5205
Sell USD2,000,000	2008/04/21	US$1: RMB7.4600
Sell USD2,500,000	2008/05/15	US$1: RMB7.5071
Sell USD2,000,000	2008/05/20	US$1: RMB7.4600
Sell USD2,500,000	2008/06/16	US$1: RMB7.4933
Sell USD2,000,000	2008/06/20	US$1: RMB7.4600
Sell USD2,500,000	2008/07/15	US$1: RMB7.4804
Sell USD2,500,000	2008/08/15	US$1: RMB7.4682
Sell USD2,500,000	2008/09/15	US$1: RMB7.4565
Sell USD2,500,000	2008/10/17	US$1: RMB7.4448
Buy USD2,000,000	2008/01/24	US$1: RMB7.3860
Buy USD2,000,000	2008/02/22	US$1: RMB7.3565
Buy USD2,000,000	2008/03/24	US$1: RMB7.3285
Buy USD2,000,000	2008/04/23	US$1: RMB7.2980
Buy USD2,000,000	2008/05/22	US$1: RMB7.2735
Buy USD2,000,000	2008/06/24	US$1: RMB7.2420

The foreign currency forward contracts have been classified as financial instruments held for trading. Fair value of these foreign currency forward contracts are determined by using a forward contract pricing model, which discounts the profit/loss of each contract determined based on the movement in market forward rates to the Valuation Date using risk free rate of RMB.

During the year, the Group recorded a gain on fair value changes on foreign currency forward contracts of approximately RMB16,151,000 (2006: Nil) as other income.

29. BANK BALANCES AND CASH

(a) Pledged bank deposits

The amount mainly represents deposits pledged to banks to secure the bills payable issued by the Group and the bank facilities granted to the Group.

The deposits carry an average fixed interest rate of 0.72% (2006: 0.72%). The pledged bank deposits will be released upon the settlement of relevant bill payables and bank borrowings.

(b) Bank balances and cash

Bank balances and cash comprised of bank deposits with short maturity at market interest rate of 0.72% (2006: 0.72%) and cash on hand.

30. TRADE, BILLS AND OTHER PAYABLES

	2007 RMB'000	2006 RMB'000
Trade payables	**247,576**	346,908
Bills payables (note)	**36,836**	142,479
Other payables and accrued liabilities	**145,164**	114,649
	429,576	604,036

The aging analysis of trade payables is as follows:

	2007 RMB'000	2006 RMB'000
Aging:		
Within 60 days	**186,645**	286,950
61-90 days	**19,851**	20,807
91-180 days	**13,454**	13,080
181-365 days	**17,500**	10,907
1-2 years	**3,169**	8,719
Over 2 years	**6,957**	6,445
	247,576	346,908

note:

The aging analysis of bills payable is as follows:

	2007 RMB'000	2006 RMB'000
Aging:		
Within 60 days	**–**	61,156
61-90 days	**32,022**	26,937
91-180 days	**4,814**	54,386
	36,836	142,479

During the year of 2003, the local government paid approximately RMB53 million to the Group for the construction of certain infrastructure and public facilities on local government's behalf in a location which is under-developed. The Group applied the amount received from the government to the construction of such facilities and entered into various construction contracts. Up to December 31, 2007, the Group recorded a balance of approximately RMB13 million (2006: RMB14 million) which had not been utilized in the constructions and was included in other payables and accrued liabilities. Details of the capital commitments of the Group relating to the construction contracts at the balance sheet dates are set out in note 40.

Notes to the Consolidated Financial Statements (cont'd)

For the year ended December 31, 2007

31. BANK AND OTHER BORROWINGS

	2007 RMB'000	2006 RMB'000
Bank borrowings	**1,546,812**	1,246,689
Other borrowings	**10,400**	10,400
Total	**1,557,212**	1,257,089
Analyzed as:		
Secured	**958,483**	475,936
Unsecured	**598,729**	781,153
	1,557,212	1,257,089
Denominated in Eur Dollars (foreign currency)	**23,469**	–
Denominated in United States Dollars (foreign currency)	**145,143**	124,998
Denominated in Renminbi	**1,388,600**	1,132,091
	1,557,212	1,257,089

The bank and other borrowings are repayable as follows:

	2007 RMB'000	2006 RMB'000
Within one year or on demand	**1,546,812**	1,246,689
After five years	**10,400**	10,400
	1,557,212	1,257,089
Less: Amount due within one year shown under current liabilities	**(1,546,812)**	(1,246,689)
Amount due after one year	**10,400**	10,400

Bank borrowings are substantively fixed-rate borrowings and carry interests ranging from 4.86% to 7.62% (2006: from 4.65% to 8.78%) per annum.

Other borrowings represent loans advanced by independent third parties and carry fixed interest rate of 2.55% (2006: 2.55%) per annum.

RMB100,592,000 borrowings were guaranteed by independent third parties and were also secured by the assets owned by the Group. Details of the assets pledged by the Group in favor of the Group's borrowings are set in note 38.

The directors consider that the carrying amount of bank and other borrowings at December 31, 2007 approximates their fair value.

32. SHARE CAPITAL

	Number of ordinary shares	
		US$'000
Authorized share capital of the Company		
At December 31, 2006 and at December 31, 2007	266,666,666,666	40,000

	Number of ordinary shares		Equivalent to
		US$	RMB'000
Issued and fully paid ordinary shares of the Company			
At January 1, 2006	1,014,045,369	148,511	1,256
Share repurchase	(23,997,000)	(4)	(29)
At December 31, 2006 and at December 31, 2007	990,048,369	148,507	1,227

Pursuant to the general mandate granted by the shareholders of the Company, the board of directors resolved on July 31, 2006 to repurchase the Company's shares of up to 10% of the issued shares of the Company as at the date of May 30, 2006. The repurchase was made at the discretion of the Board. 23,997,000 shares were repurchased during 2006 and the shares were cancelled upon repurchase. None of the Company and its subsidiaries repurchased, sold or redeemed any of the Company's listed shares during the year of 2007.

33. SHARE OPTION

A share option scheme was adopted by the Company pursuant to a resolution passed on September 26, 2005 (the "Scheme") for the primary purpose of providing incentives to directors and eligible employees. The Scheme became effective on October 20, 2005 and the option issued pursuant to the Scheme will expire with no later than 10 years from the date of grant of the option. Under the Scheme, the board of directors of the Company may grant options to any employees of the Company or any of its subsidiaries to subscribe shares of the Company.

The Company granted a total of 29,800,000 share options to the directors and other eligible employees on March 9, 2006. The exercise price of the options is fixed at HK$2.38 (the share price immediately before grant date was HK$2.24). The fair value of the options determined at the date of grant using the Binomial Model was approximately RMB21 million and the Company recorded a share based payment expense of RMB2,438,000 in the year ended December 31, 2007 (2006: RMB15,486,000).

33. SHARE OPTION *(Continued)*

The following assumptions were used in the Binomial model:

	2006 Options to Employees
Average risk-free rate of return	4.44%
Weighted average expected option life	7.58 years
Volatility rate	49%
Dividend yield	5.95%
Average share price at the grant date	HK$2.35

Expected volatility was determined by using the historical volatility of the price return of the ordinary shares of the Company over the period starting from its listing date on October 20, 2005 to March 9, 2006.

The Binomial Model has been used to estimate the fair value of the options. The variables and assumptions used in computing the fair value of the share options are based on the director's best estimate. The value of an option varies with different variables of certain subjective assumptions.

The share options could be exercised during the following periods:

Date	**Percentage of share options**
From January 1, 2007 to March 8, 2016	50%
From January 1, 2008 to March 8, 2016	50%

Details of the share options outstanding during the current year are as follows:

	Number of share options
Granted on March 9, 2006 and outstanding as at December 31, 2006	29,800,000
Forfeited during the year due to resignation of employees	(4,500,000)
Outstanding as at December 31, 2007	25,300,000

No share option has been exercised during the year.

34. RESERVES

(a) The statutory reserve represents amounts appropriated from the profits after tax of certain subsidiaries of the Company established in the PRC to comply with the PRC laws and regulations.

(b) The special reserve arose from the reorganization completed in 2004.

(c) The Company suffered loss of RMB39,574,000 for the year ended December 31, 2007 (2006: loss of RMB53,104,000).

35. ACQUISITION OF ADDITIONAL INTERESTS IN SUBSIDIARIES

In November 2007, the Group acquired 6% additional interest in its subsidiary, Haining Gaosheng Industrial Co., Ltd. ("Gaosheng") from its minority shareholders. The acquisition prices were agreed through negotiation between the Group and the minority shareholders.

In June 2006, the Group acquired 44.55% and 49.5% additional interests in its subsidiaries, Haining Hainix Sofa Co., Ltd. ("Hainix Sofa") and Haining Hidea Furniture Co., Ltd. ("Hidea Furniture"), respectively, from their minority shareholders.

	2007 **RMB'000**	2006 RMB'000
Net assets acquired	**3,600**	29,188
Reserve on acquisition (note)	**–**	30,968
Discounts on acquisition of an additional interest in a subsidiary	**–**	(10,279)
	3,600	49,877
Satisfied by:		
Cash consideration	**3,600**	49,877

note: This represents the portion of the revaluation difference that arose since the original acquisition date that is attributable to the increase of the Group's interests.

36. DISPOSAL OF SUBSIDIARIES

During the year, the Group entered into agreements to dispose of two wholly owned subsidiaries, 海寧家藝傢俱有限公司("Haining Home Craft Furniture Co., Ltd.") ("Home Craft") and 海寧家典傢俱有限公司("Haining Home Point Furniture Co., Ltd.") ("Home Point"), both carried out upholstered furniture manufacturing operations. The disposal was completed on January 29, 2007 and August 31, 2007, respectively, on which date the control of Home Craft and Home Point passed to the acquirers.

In 2006, the Group entered into an agreement to dispose of a non-wholly owned subsidiary, 海寧萬盛沙發有限公司("Haining Wansheng Furniture Co., Ltd.") ("Wansheng Furniture"), which carried out upholstered furniture manufacturing operations. The disposal was completed on June 29, 2006, on which date the control of Wansheng Furniture passed to the acquirer.

Senbo Water ceased to be a subsidiary of the Group from May 2006 due to additional capital injected by its minority shareholder.

The net assets of the disposed subsidiaries at the date of disposal were as follows:

	2007			2006
	Home Point RMB'000	**Home Craft RMB'000**	**Total RMB'000**	RMB'000
Property, plant and equipment	**77,405**	**496**	**77,901**	82,237
Prepaid lease payment	**9,174**	**9,306**	**18,480**	8,928
Amounts due from related companies	**452**	**26,916**	**27,368**	650
Inventories	**18,573**	**–**	**18,573**	50,319
Trade and other receivables	**48,340**	**1**	**48,341**	75,587
Intangible assets	**4**	**–**	**4**	133
Bank balances and cash	**49,656**	**4,593**	**54,249**	26,983
Trade and other payables	**(45,902)**	**–**	**(45,902)**	(112,739)
Tax payable	**(534)**	**–**	**(534)**	–
Bank borrowings	**(120,000)**	**–**	**(120,000)**	(85,800)
Amount due to related companies	**–**	**–**	**–**	(11,595)
	37,168	**41,312**	**78,480**	34,703
Minority interests	**–**	**–**	**–**	(19,230)
Gain on disposal	**4,332**	**3,388**	**7,720**	8,838
	41,500	**44,700**	**86,200**	24,311
Satisfied by:				
Cash consideration received	**34,372**	**44,700**	**79,072**	21,311
Transferred to trade and other receivables	**7,128**	**–**	**7,128**	–
Transferred to interests in associates	**–**	**–**	**–**	3,000
	41,500	**44,700**	**86,200**	24,311
Net cash inflow (outflow) arising on disposal of subsidiaries:				
Cash consideration	**34,372**	**44,700**	**79,072**	21,311
Cash and cash equivalents disposed of	**(49,656)**	**(4,593)**	**(54,249)**	(26,983)
	(15,284)	**40,107**	**24,823**	(5,672)

Home Point and Home Craft did not make any significant contributions to the results and cash flows of the Group during the current year.

37. RETIREMENT BENEFITS PLAN

The Group contributes to a local municipal government retirement scheme for all qualifying employees in the PRC. The employer and its employees are each required to make contributions to the scheme at the rates specified in the scheme's rules. The only obligation of the Group with respect to the retirement scheme is to make the required contributions under the scheme.

In addition, the Group operates a Mandatory Provident Fund ("MPF") Scheme for its qualifying employees in Hong Kong. The assets of the MPF Scheme are held separately from those of the Group, in funds under the control of trustees. The Group contributes at the lower of HK$1,000 or 5% of relevant payroll costs monthly to the MPF Scheme, which contribution is matched by employees.

The total cost charged to the consolidated income statement of approximately RMB13,936,000 (2006: RMB8,844,000) represents contributions paid and payable to the above schemes by the Group in respect of the current accounting period. As at December 31, 2007, contributions of approximately RMB2,367,000 (2006: RMB2,589,000) in respect of the reporting period had not been paid to the above schemes.

38. PLEDGE OF ASSETS

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

	2007	2006
	RMB'000	RMB'000
Buildings (note 17)	**481,671**	468,517
Prepaid lease payments (note 18)	**72,325**	82,125
Pledged bank deposits (note 29)	**113,689**	163,221
	667,685	713,863

39. LEASE ARRANGEMENTS

As lessee

At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancelable operating leases, which fall due as follows:

	2007 **RMB'000**	2006 RMB'000
Within one year	**16,253**	1,502
In the second to fourth year inclusive	**89,991**	3,169
	106,244	4,671

The lease payments represent rentals payable by the Group for its retail store and certain of its office properties. The lease terms are various from one year to nine years.

40. CAPITAL COMMITMENTS

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

	2007 **RMB'000**	2006 RMB'000
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of acquisition of property, plant and equipment	**19,260**	1,464
Capital expenditure contracted for but not provided in the consolidated financial statements in respect of construction of certain infrastructure and public facilities in the PRC on behalf of the government (note 30)	**13,202**	14,135
Commitment for acquisition of a subsidiary (note 24)	**20,862**	–
	53,324	15,599

41. CONNECTED AND RELATED PARTY DISCLOSURES

Transactions between group companies have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Group and other related parties are disclosed below.

(a) The Group had the following significant transactions with the connected and related parties during the year:

	Nature of transactions	Notes	2007 RMB'000	2006 RMB'000
Connected and related parties				
Yili Horgos	Purchase by the Group		**34,873**	34,242
Yujie	Sales of production wastes by the Group		**11,040**	8,975
白銀卡森皮革有限公司 Baiyin Kasen Leather Co., Ltd.	Purchase by the Group	(i)	**68,992**	68,854
	Sales by the Group	(i)	**7**	–
克孜勒蘇新蓉皮革有限公司 Kezilesu Xinrong Leather Co., Ltd.	Purchase by the Group	(i)	**15,713**	60,220
Starcorp	Sales by the Group		**53,065**	49,209
Haining Haipai Leather Industry Co., Ltd.	Sales by the Group		**7,608**	74
	Subcontracted manufacturing of leather sofa cover provided by the Group		**1,956**	–
Related parties				
Changhong I&E	Sales by the Group		**414**	259
浙江森橋實業(集團)有限公司 Zhejiang Sunbridge Industrial (Group) Co., Ltd. ("Sunbridge")	Sales by the Group	(ii)	**23**	–
Future Foam	Purchase by the Group		**–**	81,374
Kasen-Melx	Sales by the Group		**764**	3,759
	Purchase by the Group		**2,141**	–
Shanghai Star Furniture Co., Ltd.	Sales by the Group	(ii)	**328**	–
Haining Liema Leather Garments Co., Ltd.	Interest expense charged to the Group		**16**	115
Senbo Water	Provision of sewage treatment service to the Group		**91**	22
AoLin Furniture (Shanghai) Co., Ltd.	Sales by the Group		**238**	196
海寧萬盛絲綢噴織有限公司 Haining Wansheng Silk Weaving Co., Ltd.	Purchase by the Group	(iii)	**–**	9,541
North Pole Ltd.	Sales by the Group		**–**	10,830

41. CONNECTED AND RELATED PARTY DISCLOSURES *(Continued)*

(a) The Group had the following significant transactions with the connected and related parties during the year: *(Continued)*

notes:

(i) Mr. Zhu has influence and beneficial interests in the company through Sunbridge.

(ii) Mr. Zhu has influence and beneficial interests in the company.

(iii) A director of a non-wholly owned subsidiary has influence and beneficial interests in the company.

(b) Share options granted to the directors

	As at December 31,	
	2007	2006
Number of share options granted to the directors	**6,800,000**	6,800,000

(c) Details of the balances with the related companies are set out in note 27.

(d) Key management of the Group is all directors whose remunerations were disclosed in note 11.

42. CONTINGENT LIABILITIES

As at December 31, 2007, the Group provided guarantee to the banks in connection with short-term bank loans of RMB120 million extended to a former subsidiary, Haining Home Point Furniture Co., Ltd ("HHPF"), see note 36. HHPF has also pledged its properties to secure bank loans of approximately RMB90 million for the Group as at December 31, 2007.

In the opinion of the directors of the Company, no relevant financial liabilities have been recognised in the consolidated financial statements as the effect of such financial liabilities to the Group's financial statement was immaterial and the possibility that the third party defaults the bank loan repayment is remote.

43. PRINCIPAL SUBSIDIARIES

The following table lists major subsidiaries of the Company as at December 31, 2007 and 2006 which, in the opinion of the directors, principally affected the results or net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

Name of the company	Country of incorporation/ establishment and operations	Issued and fully paid share capital/ registered capital	Attributable equity interest of the Company		Principal activities
			Direct %	Indirect %	
Haining Gaosheng Industrial Co., Ltd. (Formerly known as: Haining Gaosheng Leather Co., Ltd.) 海寧高盛實業有限公司 (原名：海寧高盛皮革有限公司) (note a)	PRC	RMB60,000,000	–	95	Production and processing of leather and tailored products
Haining Hainix Sofa Co., Ltd. 海寧漢林沙發有限公司 (note b)	PRC	US$6,000,000	–	95.05	Production and sale of sofas, dining chairs and other furniture products
Haining Hengsen Furniture Co., Ltd. 海寧恒森傢俱有限公司 (note a)	PRC	RMB30,000,000	–	100	Production of furniture and glass fiber reinforced plastic products; wood processing
Haining Hidea Furniture Co., Ltd. 海寧慧達傢俱有限公司 (note b)	PRC	US$7,800,000	–	100	Production and sale of sofas, dining chairs and other furniture products
Zhejiang Kasen Property Development Co., Ltd. (Formerly known as: Haining Higher Points Investment Development Co., Ltd.) 浙江卡森置業有限公司 (原名：海寧高點投資有限公司) (note a)	PRC	RMB400,000,000	–	100	Investment holding
Haining Home Impression Furniture Co., Ltd. 海寧家美傢俱有限公司 (note b)	PRC	US$2,000,000	–	100	Production and sale of upholstered furniture
Haining Kareno Furniture Co., Ltd. 海寧卡雷諾傢俬有限公司 (note b)	PRC	US$3,600,000	–	100	Production and sale of upholstered furniture
Haining Kasen Leather Co., Ltd. 海寧卡森皮革有限公司 (note b)	PRC	US$3,000,000	–	100	Production and sale of upholstered furniture
Haining Oyi May Sofa Co., Ltd. 海寧歐意美沙發有限公司 (note b)	PRC	US$5,000,000	–	50.5	Production and sale of upholstered furniture

43. PRINCIPAL SUBSIDIARIES *(Continued)*

Name of the company	Country of incorporation/ establishment and operations	Issued and fully paid share capital/ registered capital	Attributable equity interest of the Company Direct %	Indirect %	Principal activities
Haining Schinder Tanning Co., Ltd. 海寧森德皮革有限公司 (note b)	PRC	US$1,000,000	–	100	Production and sale of automotive leather
Richmond International Trading Limited 富華國際貿易有限公司 (note a)	Hong Kong	HK$100	–	100	Trading of leather and other furniture products
Shanghai La Kassa Furniture Co., Ltd. 上海禾美傢俱有限公司 (note b)	PRC	US$4,000,000	–	100	Production and sale of upholstered furniture
Zhejiang Kasen Industrial Co., Limited 浙江卡森實業有限公司 (note b)	PRC	RMB896,240,000	–	100	Research, development, production and sales of furniture leather
Zhejiang Liema Furniture Co., Ltd. 浙江獵馬傢俬有限公司 (note b)	PRC	US$7,000,000	–	50.5	Production and sale of upholstered furniture

notes:

(a) The companies are limited liability companies.

(b) The companies are Sino-foreign owned enterprises.

None of the subsidiaries had issued any debt securities at the end of the year.

44. POST BALANCE SHEET EVENTS

Pursuant to an equity transfer agreement dated February 19, 2008, a wholly owned subsidiary of the Company has agreed to purchase from an independent third party 49.5% equity interest in Chengdu Longteng Shoes Market Investment and Development Co., Ltd. (成都隆騰鞋城投資開發有限公司) for a consideration of RMB29.7 million. This transaction has been approved by local authority on March 7, 2008. Chengdu Longteng Shoes Market Investment and Development Co., Ltd. becomes the associate of the Group since then.