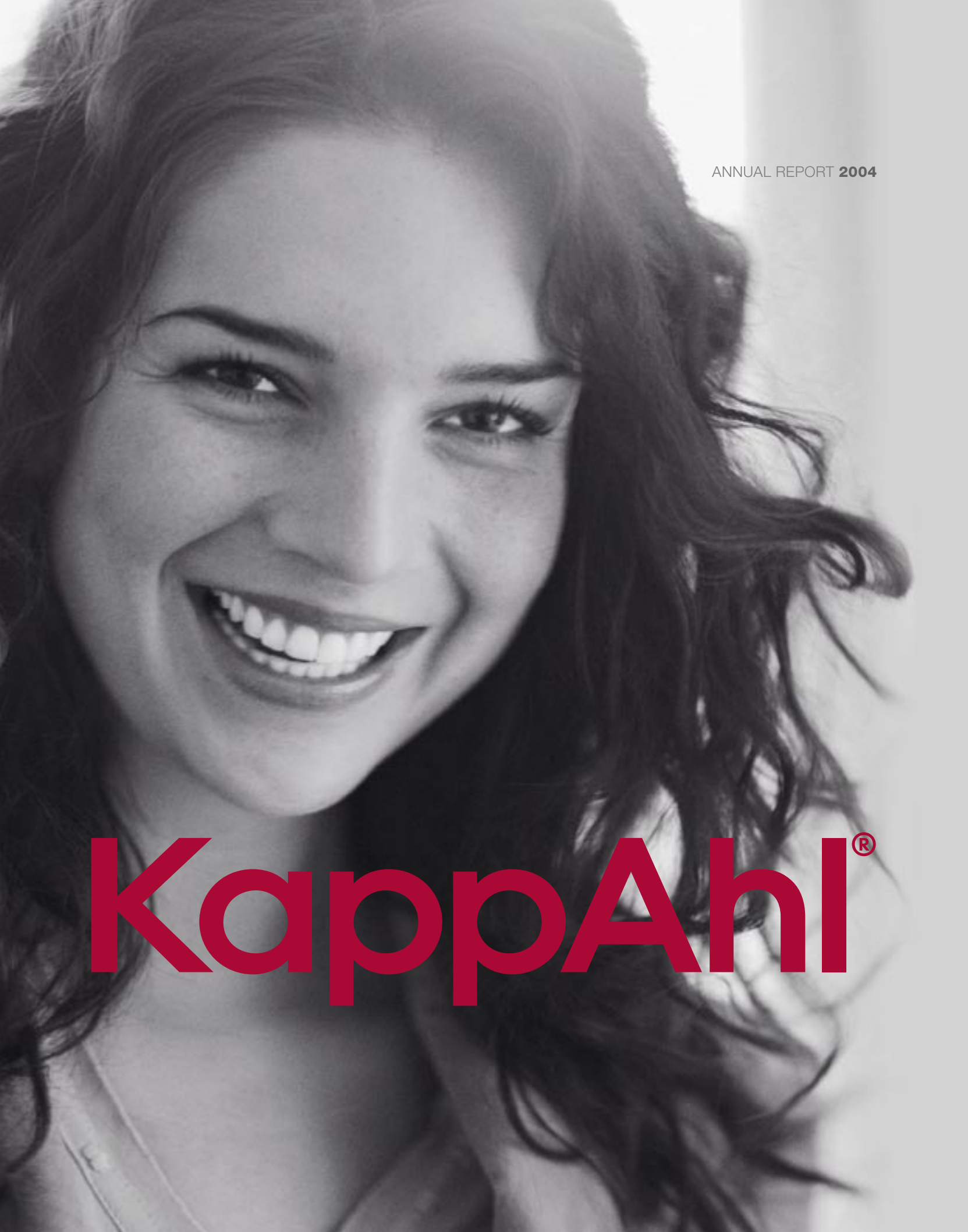
ANNUAL REPORT **2004**



KappAhl®

OUR CUSTOMERS ARE SATISFIED. WE RECEIVE PROOF OF THAT EACH DAY. IN KAPPAHL STORES WOMEN ARE FINDING CLOTHES THEY WANT FOR THEMSELVES AND FOR THE REST OF THE FAMILY. THE FOLLOWING PAGES WILL PROVIDE YOU WITH A GLIMPSE OF THE MERCHANDISE'S LONG PATH FROM IDEA ALL THE WAY INTO THE STORE. WE WILL ALSO INFORM YOU ABOUT THE WORK BEHIND THIS YEAR'S POSITIVE RESULTS.

2004 HAS BEEN A SUPERB YEAR FOR KAPPAHL, STATES CHRISTIAN W. JANSSON, PRESIDENT & CEO, KAPPAHL. PROFITS FINISHED WELL ABOVE SEK 200 MILLION, WE BECAME MARKET LEADERS IN THE SWEDISH RETAIL CLOTHING INDUSTRY AND OPENED LARGE CITY CENTRE STORES IN GOTHENBURG AND STOCKHOLM.

For the third straight year, KappAhl is showing a profit and has broken the barrier of SEK 200 million, with record results of SEK 223 million (120 MSEK). Sales have continued to increase in all business areas and during the autumn KappAhl took over as market leader within the Swedish retail clothing industry. Between December 2003 and December 2004, market share has increased from 7.3 to 7.9 percent in total sales (source: GfK). In women's apparel the increase was close to 21 percent (an increase from 6.7 to 8.1 percent).

"We feel that our customers like us more and more", says Christian W. Jansson. "They appreciate our range of clothing and are returning on a regular basis to shop. I also believe that the clarity of our customer image, women 30-50 years of age with families has contributed to a significantly more secure customer. It is clear what KappAhl stands for and who our targetgroup is.

Paul Frankenius, Executive Vice President & COO, asserts that it has taken a very long time, internally, to reach this point, but it is thanks to perseverance, that the employees throughout the entire company now have a clear image of the KappAhl customer. Our mission is to make sure that the customer is provided with a fashion that suits her.

Something that the entire clothing industry has experienced quite distinctly is the increasingly high demands of customers for a continuous flow of new fashion. A garment's lifecycle is already shortened once it appears in the store, which is why a high rate of turnover is required and KappAhl has managed this task quite well.

"In the past, all we had to do was lower the price and the garment would sell sooner or later, but today we have to lower prices immediately", says Christian W. Jansson. "We cannot afford to have unsold stock in the stores."

As a result of this, KappAhl has spent a lot of time during the past year streamlining purchasing practices; prices, quality and lead times. Head office staff has been relocated to purchasing offices around the world, which has created significant advantages by, for example, increasing understanding between KappAhl and its suppliers.

"We have achieved a higher degree of secure deliveries with respect to orders this year by being more explicit and exact in our requests than previously", says Paul Frankenius.

"Internally our tolerance level with respect to faults has also decreased", says Christian W. Jansson. "Close to 50 million garments per year or 200,000 per day pass through our distribution centre and even if we have a 99 percent accuracy rate, that means that 2000 garments end up at the wrong destination. That is too many, so we shall continue to try and improve in this area even if it will be difficult to achieve 100% accuracy given the volumes we deal with."

During the year, KappAhl has once again conquered central Gothenburg by overtaking the well-known Gillblads premises located on Kungsgatan in the city centre. On the whole, 2004 has been the biggest year for new openings of KappAhl stores with large centrally located stores opening in Stockholm and Helsinki as well. According to Christian W. Jansson, next year KappAhl would like to open a considerable number of new stores.

"We would very much like to provide even more consumers with the opportunity to have access to our offers. Premises in the right location is a necessity. We are extremely particular and will only open stores in locations where we are certain of reaching the right flow of customers."

The acquisition of KappAhl by Nordic Capital and Accent Equity Partner will not bring about any changes with respect to the successful cooperation with the Coop/MedMera card in Sweden, the Norwegian NKL card or the Finnish Ykkösbonus.

During the past year KappAhl's management has formulated a new corporate culture with four value statements: courage, commitment and the will to win, simplicity, clarity and pace. "A corporate culture is not an end in itself, but rather a way to describe what we do," says Christian W. Jansson. "KappAhl has a fundamentally well-functioning business model that we have no intention of fiddling with. On the other hand, we will poke around in the details of it in order to become even better. It is about trying to get everyone to understand that we may never reach the finish line but that through constant hard work we can get a little bit further ahead."

FROM A MARKETING PERSPECTIVE THERE IS ENORMOUS UNTAPPED GROWTH POTENTIAL WITHIN THE 40 PLUS CUSTOMER SEGMENT. WHILE OTHER COMPANIES FOCUS ON YOUNGER CUSTOMERS, THE "OLDER" CUSTOMER IS WILLING TO SHOW LOYALTY TO A SPECIFIC STORE AND THIS MARKET SEGMENT ALSO MAKES UP A LARGER PERCENTAGE OF THE BUYING PUBLIC.

KappAhl's target group is women between the ages of 30-50 with families. The majority of customers are around 40 years old. They make up a large group of fashion interested women who, it would seem, are largely ignored by other clothing companies, but who collectively spend large sums when they buy for themselves and their families. This is why KappAhl has placed even more focus on this customer and now know much more about her. We know, for example, what she buys, when she buys it and how much money she spends. She likes comfortable clothes that are suitable for everyday wear and can be used for more than one season. She also wants to feel modern and well-dressed but has no need to be super trendy or be first with the absolute latest fashion.

KappAhl's business idea is value-for-money fashion with a wide appeal. Today we are already among the largest with respect to women's apparel in the Nordic region. Our objective is also to be the leading and most profitable fashion chain for our target group. We will succeed by continuing to meet our customers' demands for current and price worthy fashion.

KAPPAHL DOES NOT CREATE FASHION BUT WE CAPTURE WHAT IS OUT THERE AND TURN IT INTO SOMETHING GOOD FOR OUR CUSTOMERS. DESIGNERS, BUYERS AND THE MANAGERS FOR THE VARIOUS BUSINESS AREAS WORK CLOSELY AND INTENSIVELY TOGETHER IN ORDER TO TURN CURRENT TRENDS AND IMPULSES INTO ATTRACTIVE GARMENTS.

The path from idea all the way into the customer's shopping bag is long, but knowledge about the customers makes the work easier for those who decide what items should be made available in the KappAhl stores. Access to information regarding trends and the latest news is the same for all the actors on the markets, so it is very much about using one's intuition to determine when the timing is right for KappAhl's customers. Certain fashion trends can be excluded immediately since they do not correspond with our target group. An example of such a trend is the extremely short and tight tops that show the stomach. It is, on the other hand, extremely important to always include a few cutting edge pieces in the assortment so that the customers feel that KappAhl is up-to-date with respect to current fashion trends. The poncho has been spot on during the autumn of 2004 and has sold just as well with 15 year olds as with their grandmothers.

"The first thing we do prior to each new collection is to gather all the trend information", says Gabrielle Grennard, Carina Ekman and Daniel Landström, designers for KappAhl. Travel is an important factor in the search for trends, and designers and buyers often travel together. At fashion and fabric exhibitions they collect ideas and have the opportunity to grasp quality and materials. London is a favourite destination among the big cities. The pulse of the streets and the vibe in the stores and cafés provide as much inspiration as the trends from the world of film and music. All possible forms of everyday impressions are also stored for future reference. Our designer for childrenswear, Carina Ekman thinks that MTV and Internet are indispensable and she also checks out her target group in the city.

»Designers and buyers who travel together see the same things but through different eyes.«

Daniel Landström was very inspired by a visit to a jeans manufacturer.
"Jeans have been a big seller this year, which is why I travelled to the factory in Turkey with a buyer. We worked there creating samples and doing testing. We learned terms and concepts that are going to make it easier for us to communicate with this supplier in the future. We also got a clearer idea of what is possible to do and what is not. That visit was worth more than all the visits to fancy stores combined."

Designers and buyers who travel together see the same things but through different eyes and are able to compare their impressions immediately, which means that by the time they return home the thought process has already been started. Their impressions and ideas are later presented to the rest of the team on special fashion trend days and then each business area continues their part of the work. The seasons are broken down into shorter periods and one can see, for example, how many garments need to be sold in order to reach budget and incorporate with the planned campaigns. When the theoretical segment of the work is done the creative side starts up again. However, a new collection does not appear out of nowhere. There is a basic collection that is continuously being developed, improved and updated. One always puts customer ahead of product so when the latest fashion trends are added, it is done so cautiously and they are "kappahlised" in order not to appear too teenagey or too boring. The customer's tastes and needs are what guides us and they want modern garments that bring out their best attributes. They also like colour.
"Just finding the right colour means that one has come quite far in the work process", says Gabrielle Grennard.

THERE IS ALWAYS A MARKET, ALBEIT A SMALL ONE, FOR THE VERY LATEST FASHION NEWS, BUT KAPPAHL HAS CHOSEN TO FOCUS ON A TARGET GROUP THAT DOES NOT BUY JUST BECAUSE SOMETHING HAPPENS TO BE "IN".
A CONSCIOUS EFFORT TO CREATE THE RIGHT RANGE AND PROVIDE ATTRACTIVE OFFERS IS THEREFORE NECESSARY.

"We have stood by our target group, which is why this year has been such a success", explains Mari Svensson, Vice President Commercial. Design, product development and sales planning are the hub of the entire purchasing department with everything else having been rationalised.
"Close cooperation between the marketing and sales departments is essential so that everyone is aware of our direction and how to get there. We must live up to our promise that the entire family can buy clothes at KappAhl."
Even at the design stage it is imperative to think coordination and have an image of how the garment can be exposed with as much inspiration as possible in the store. Customers like convenience and they have very little time. They want to enter the store and quickly find combinations that go together irrespective of whether it is women's, men's or children's clothing. An overall view must be available right from the start and that is made simple as KappAhl has all sorts of clothing: work clothes, everyday, festive, outerwear and underwear.

KappAhl engages in intensive campaign work where it is essential to formulate clearly defined offers that customers are easily able to relate to. This is why as part of the product development considerable effort is put into finding the right products for campaigns.

This year's well-dressed fashion has suited KappAhl perfectly. "We have simply been better than our competitors and have dominated the market with the dressy fashion", says Mari Svensson.

CLOTHES ARE PERISHABLE GOODS AND, ON A DAILY BASIS THROUGHOUT THE YEAR, THE LATEST NEWS IN FASHION IS RECEIVED BY KAPPAHL. THIS MEANS THAT THE MAJORITY OF THE ASSORTMENT CONSISTS OF CURRENT FASHION TRENDS. ONLY 15 PERCENT MAKE UP THE BASE COLLECTION, WHICH IS AVAILABLE YEAR ROUND.

When a woman feels the desire to buy something new, her preferred choice is most often a top and preferably in a cheerful colour. It is a simple way to renew oneself without spending a fortune.

"We have approximately one thousand different tops per year in our assortment, so it is always possible to find something new and fun, says Carina Ladow, one of the business area managers with womenswear.

Tops is one of the most profitable product groups and KappAhl is the market leader in this area with up to 15 percent of the Swedish market during certain months (source: GfK).

Accessories are another product group that is doing extremely well. New fashion accessories can update clothes in the closet without breaking the bank.

This year's well-dressed yet comfortable fashion has brought about a giant boost for two other product groups, jackets and jeans. "Jackets have been the year's absolute biggest seller and jeans have done brilliantly across the board for women, men and children and have contributed to other sales such as tops, sweaters, shirts and T-shirts. Trousers have been selling well since the major fitting project was carried out. Customers quickly discovered that KappAhl's trousers fit perfectly and sales are still on the increase."

The same holds true for XLNT, KappAhl's own brand for womenswear with sizes ranging from 42-56.

Another cause for rejoicing is the festive clothing collection, in which KappAhl has been investing considerably and dominates the market in October, November and December. Customers know that they will find their festive top or party dress in a KappAhl store.

The majority of the clothing sold is nonetheless, garments that function well in everyday life; both at work and leisure. "Our customer is interested in fashion but is not at the forefront of the absolute latest fashion trends but, at the same time, she absolutely does not want to dress in boring fashion. She often falls for a new colour and to help her with styling we use both mannequins and certain areas in the store", says Carina Ladow. "We have a lot to offer but there are still women out there who have not discovered us. I think that they will be here next year and then we'll be trampled!"

MENSWEAR HAS FINALLY STARTED TO TAKE OFF. THE PERIOD BETWEEN AUGUST AND OCTOBER DID BETTER THAN EXPECTED, FIRST AND FOREMOST FOR JEANS, SHIRTS AND ACCESSORIES. IN CONTRAST TO THE MARKET IN GENERAL, KAPPAHL HAS INCREASED ITS MARKET SHARE IN JEANS.

"Some fashion trends have sold extremely well", says Thommy Bäcklin, business area manager for menswear. "If this is due to the fact that we have fashion conscious customer or that they are inspired by what they see in the stores, is impossible to say."

The product group, jackets and shirts have increased considerably during the year. The Madison Avenue venture, for the well-dressed man, has turned out very well. This applies specifically to product groups such as trousers, shirts and jackets, clothes that are good-looking and functional in a variety of situations without being too formal.

The success of the U.S. Polo Association has continued and shirt sales, in particular have done extremely well during the autumn. The jeans venture that is a part of the Redwood collection, KappAhl's casual leisure collection has surpassed expectations. Sales of other 5-pocket trousers have also increased.

"The outerwear season has been somewhat incredible with more or less all outerwear selling despite the warm and wet autumn weather. We have a wide assortment of jackets compared to most other clothing stores. It is a product group that is difficult to make profitable but the KappAhl customer will gladly pay for the right jacket.

Festive clothing is a big seller for KappAhl and the menswear section is no exception.

"Our campaigns for festive shirts have been a giant success. When girls buy glitter tops, guys buy a new shirt", says Thommy Bäcklin. "All in all, one can say that the current fashion image suits KappAhl and our customers extremely well. At the moment jeans are popular, which along with more dressy items make for a well-dressed but relaxed look."

IN 2004 EVERY EIGHTH CHILDREN'S GARMENT WAS BOUGHT AT KAPPAHL. GIVEN THE FACT THAT PARENTHOOD IS ARRIVING LATER AND LATER IN LIFE FOR MANY OF US, MOST NEW PARENTS BELONG TO KAPPAHL'S TARGET GROUP. THE FAMILY CONCEPT, FROM BABY TO TEENS, WOMENSWEAR AND MENSWEAR IS SPOT ON.

The childrenswear department at KappAhl is larger than ever with a market share in Sweden of just above 12 percent (source: GfK). Anna Bredberg is business area manager and has three comprehensive explanations for the good results:
"We have found the right assortment, we focus on our customer and we are very good at operating in season.

By being present in the stores, analysing and keeping track of sales, one can quickly determine the level of activity required i.e. if something needs to be replenished or put on sale. It is a matter of starting and stopping simultaneously and it has worked. We have also been accurate in our assessment of when to introduce the newest items."

Thanks to a wide and fashionable assortment of outerwear, KappAhl's results are better than in 2003 for that particular product group despite the warm autumn. Mini Girl, the collection for small girls has grown considerably during the year and also the baby collection has increased in sales. The basic collection Kaxs has continued to sell extremely well.
"It is the adults and in most cases, moms who buy children's clothing" says Anna Bredberg. As children get a little older, however, they want to have more influence over clothing purchases, which is why it is very important that they like the clothes. We must be on the right track as children between the ages of 10-12 spontaneously choose KappAhl.

KappAhl is already among the leaders in clothing for older children and in the future we plan to expand the assortment further in order to attract even more new customers.

A GARMENT WILL BE HEAVILY SCRUTINISED ALONG ITS ROUTE FROM SKETCH TO NEWLY DRESSED AND SATISFIED CUSTOMER. KAPPAHL CONDUCTS TESTING SEVERAL TIMES DURING THE PRODUCTION PROCESS IN ORDER TO ENSURE THAT GARMENTS MEET THE QUALITY REQUIREMENTS.

KappAhls clothes shall be free from harmful substances and chemicals. They shall retain colour and form and continue to look good even after many washes. Children's clothing shall be safe. In order to live up to such demands, KappAhl has an extensive testing and inspection regime. It is ultimately about the environment and the health of the customers and those working with the manufacturing.

KappAhl's quality control department decides what requirements shall apply for the various product categories and materials. Textile engineers, Ann Lind and Pernilla Ho give some examples of what one looks for.

"It is a matter of the chemicals and colour substances that are permitted, how much colour a garment is allowed to lose and how much pilling is acceptable. Shrinking should remain within certain limitations and a zipper that bubbles and interlining that creases are not acceptable."

Inspections are carried out throughout the entire production process and when the goods arrive at KappAhl's distribution centre. The laboratories that conduct the testing, receive specific instructions as to how they should be performed, the standards to be followed and KappAhl's requirements for these. The system is set up so that both the correct method and correct amount of tests are carried out.

At the head office the quality department has its own lab where they can examine things that fall outside of the scope of the external laboratories' testing, such as assessments that are difficult to measure objectively. Certain types of reclamations are also handled here.

"We take the returned garment, analyse it and investigate the cause," says Ann Lind. "In certain cases we contact the customer personally, explain what happened and then compensate them. We also inform our purchasing offices abroad, suppliers and buyers so that the fault will not be repeated."

"It is impossible to safeguard oneself against everything" says Pernilla Ho, "but our work is first and foremost about anticipating and preventing problems, so that our customers are not affected."

THE STORE IS THE CENTRAL CHANNEL OF COMMUNICATION IN THE MEDIA MIX. THE USE OF VERY ENTICING OFFERS DURING CAMPAIGNS AND ATTRACTIVE PRICES HAVE CAUSED CUSTOMERS TO FLOCK TO KAPPAHL STORES. FIRST AND FOREMOST, MARKETING ACTIVITIES SHALL LEAD TO SALES OF EVEN LARGER VOLUMES.

For the past two years, KappAhl has defined the store as the most important form of media and during 2003 and 2004, major investments have been made to increase standards and overall impression.

"The exterior should be so attractive that the customer is drawn in. Once inside she should experience the store as being fresh-looking, pleasant and so well-arranged that she can quickly orient herself and make her choices," says Cathrine Simonsson, marketing manager.

Clearly displayed goods simplifies the shopping process for the customer which is why so much effort has been put into matching and coordination of the garments. More mannequins provide better possibilities to show entire silhouettes, which provide inspiration and assistance. Various activities overlap one another in order to maintain a high pace and make the store feel lively and up-to-date.

"We work according to sales plans that specify what goods are included in various activities and campaigns, the business areas that are affected and the volumes.

The sales plan is one of KappAhl's most important instruments of communication and is produced jointly by the purchasing and marketing departments. The sales plan is subsequently applied to all the markets."

In addition to the store, the customer card is an important link to the customer, especially on the Swedish market where the MedMera card is widely used.

"The MedMera card is a fantastic media channel which enables us to provide various customer groups with enticing offers at the right time", says Cathrine Simonsson.

In addition to store and card activities KappAhl has also invested in outdoor advertisement during the year.

"We wanted to combine the offer itself with promotion of the KappAhl trademark. Surveys show that we received a good level of attention."

Another way to reach the market is via our website, which has been improved and now has a modern and inspiring look.

During 2004 it was decided that, for the first time, KappAhl would take part in the sponsorship of an entertainment event. The event is the musical, Mamma Mia, which represents much of what KappAhl stands for: warmth, popularity and generations that come together.

"It is fun and exciting and provides us with many possibilities for a variety of activities", concludes Cathrine Simonsson.

A STORE FILLED WITH ATTRACTIVE GOODS IS NOT ENOUGH. IT IS THE BUYING SITUATION ON THE WHOLE THAT DETERMINES IF THE CUSTOMER CHOOSES KAPPAHL OR THE COMPETITOR NEXT DOOR. THIS IS WHY KAPPAHL STORES ARE BOTH INSPIRING AND EFFECTIVE.

It is important that the actual meeting with the customer goes as well as possible; that she feels welcome and easily finds what she is looking for and also, that the process of trying on clothes is fast and that it is easy to pay.
"We are very focused on creating a good shopping environment for the customer and invest a great deal of resources into customer contact", says Linda Hamberg, Vice President, Retail.

For the customer accompanied by children, a fun children's corner can provide her with a little extra time alone and, for that matter, even be the deciding factor in choosing KappAhl instead of the store next door.

With 235 stores in Sweden, Norway, Finland and Poland, it is unavoidable that some stores perform better than others, but during the year the differences have evened out and the low performers have shown improvement. There are several explanations: stores have moved to better locations and have come closer to the flow of customers. The major project of freshening up and refurbishing current stores has picked up speed and a number of new stores have opened.

According to Linda Hamberg the year's newly opened stores are just the beginning of the company's expansion. The potential exists to increase the number of stores in all the markets. "New establishments are an offensive way to increase our turnover. All four markets are profitable, now we just have to sell more garments."

There is money to be made by getting the right goods to the right stores at the right time. Goods allocation is highly prioritised and the evaluation of a possible new system is ongoing. A lot of work has been put into improving logistics within the store. The store should be thought of as a distribution centre where the goods should flow through the system as quickly and smoothly as possible; from arrival to the store until the customer leaves the store with her bag.

The customers feel the atmosphere in the store at once, which is why an obvious factor for success is positive and enthusiastic personnel who enjoy their jobs. Attitude also plays a significant role; for example, when a great deal of stock arrives at once, one can either think of it as a hard work or view it as an opportunity to sell and satisfy even more customers.

Linda Hamberg believes that one of KappAhl's strengths is the many motivated employees in the store.
"They love their jobs and their customers and it is thanks to them that we have attained this level of success!"

COOPERATION PROVIDES STRENGTH AND MORE OPPORTUNITIES TO INFLUENCE WORKING CONDITIONS AND ENVIRONMENT IN THE MANUFACTURING COUNTRIES. LEADING EUROPEAN RETAIL BUSINESSES, INCLUDING KAPPAHL, HAVE JOINTLY FOUNDED BSCI (BUSINESS SOCIAL COMPLIANCE INITIATIVE), WHICH HAS DEVELOPED A COMMON CODE OF CONDUCT AND SYSTEM FOR IMPLEMENTATION AND INSPECTION. KAPPAHL IS ALSO A MEMBER OF AMNESTY BUSINESS GROUP AS WELL AS THE NORWEGIAN ORGANISATION, INITIATIVE FOR ETHICAL TRADE.

For many years, KappAhl has taken its social responsibility and worked for improved conditions in manufacturing by implementing a code of conduct with strict demands placed on suppliers. The thought behind the joint code of conduct for BSCI members is that it should gradually replace the companies' own codes. Exactly like these, the BSCI is founded upon the ILO's (International Labour Organization) conventions, which champions causes such as banning child and forced labour, discrimination, working conditions, security, right to regulated working hours and wages and right to collective bargaining. The BSCI stipulates how audits shall be performed and how the process of improvement shall be carried out. Audits are performed by approved auditing companies that have been educated within the BSCI system.

The results of the audits are stored in a database that all the participating companies have access to. Coordination saves time and money and means that KappAhl can put more resources into helping the manufacturers in their efforts to improve.

BSCI approval is a strong sales argument for manufactures. To date, there are approximately a little over 30 European retailers that are members of BSCI.

"BSCI is unique. I do not know of any other operations where competitors cooperate so openly. I think that all of us realise that with the improvement of the working environment we all reap the benefits", says Lena Bergendahl, coordinator for the Code of Conduct for KappAhl.

During 2004, KappAhl has sponsored BRIS (Childrens Right in Society). During the autumn, a successful campaign was carried out where BRIS recieved SEK 3 for each Kaxs garment sold. In Norway and Finland similar activities were carried out in cooperation with Save the Children. KappAhl started a collaboration with The Hunger Project. The aim of the Hunger Project is to reduce hunger in the world by helping vulnerable people to help themselves. Charity organisations in various countries receive support in the form of clothing or money. In Sweden we cooperate mainly with Erikshjälpen. Our offices abroad contribute to local projects such as orphanages and street children. KappAhl has also contributed monetarily to the nonprofit organisation Mentor.

In the wake of the Tsunami catastrophe in Asia, KappAhl provided homebound tourists with clothing and BRIS recieved an additional contribution.

ENORMOUS AMOUNT OF CARBON DIOXIDE EMISSIONS HAVE BEEN AVOIDED SINCE KAPPAHL STARTED TO COMBINE THE USE OF RAIL AND TRUCK FOR ITS TRANSPORTS WITHIN SWEDEN 15 YEARS AGO. THE GARMENTS ARE TRANSPORTED BY TRAIN FOR THE LONGER DISTANCES AND VIA ROAD THE FINAL ROUTE TO THE STORE. COMMENCING IN 2005 GARMENTS WILL BE TRANSPORTED VIA RAIL TO NORWAY ALSO.

The issue of climate has taken centre stage for the work with the environment at KappAhl. The most important measure is to minimise the environmental impact of the transports. Ann-Marie Heinonen, environment and Corporate Social Responsibility manager:

"Transports within the region of Gothenburg have decreased thanks to the fact that our distribution centre is currently able to handle the pressing and hanging of garments. We had a great deal of transports previously to external contractors, which is no longer the case. Furthermore, as of 2005 all distribution of goods to the stores within the surrounding area will take place via gas driven lorry.

Cost effective logistics with a high degree of delivery precision is not sufficient for KappAhl. The logistics must also be environmentally effective. KappAhl therefore collaborates with Green Cargo. They handle the transports to the stores within Sweden and Norway. In one year the transports correspond to 50 fully loaded 600 meter long freight trains, which mean drastically reduced carbon dioxide emissions compared with road traffic.

Öko-Tex and the EU flower symbolise healthy respectively environmentally labelled clothing. During the year, the number of labelled garments increased further and made up 14 percent of the total number of garments in 2004 (9 percent in 2003). KappAhl's environment management system is updated and approved by SP, Swedish Testing and Research Institute. SP has also carried out the customary audits during the year at the head office, distribution centre and in a selection of Swedish and Finnish stores. KappAhl has been ISO 14001-certified since 1999.

"The Environment Hunt" is the name of KappAhl's interactive education programme, which all employees must take part of. "It will also be used as training for our suppliers", says Ann-Marie Heinonen.

KappAhl continuously does what it can to reduce energy usage and during the year we have carried out a successful internal campaign. Like the head office and distribution centre, all KappAhl stores with its own electricity meter use green marked electricity.

COURAGE, COMMITMENT AND THE WILL TO WIN, SIMPLICITY, CLARITY AND PACE. THESE ARE THE VALUE STATEMENTS IN THE CORPORATE CULTURE THAT HAVE DEVELOPED WITHIN KAPPAHL DURING THE PAST YEAR.

The corporate culture shows the way to KappAhl's vision of becoming the leading and most profitable retail clothing chain for the target group 30-50 year olds within the Nordic region.
"To become more profitable is an important part of the vision. The new motto will provide the support we need in our daily work", says Kajsa Räftegård, Vice President, Human Resources. In the autumn all the managers were involved in the process with the new corporate culture. During 2005 training of all the employees shall take place.

KappAhl is working long-term and strategically with competence development of managers and key personnel on various levels. One of the programmes started during the year is the internal leadership programme for head office managers and KappAhl's abroad offices. Another major venture has also been launched, whereby all KappAhl store managers shall take part in an extensive leadership programme. In order to ensure a continuous supply of store managers, the chosen candidates take part in a one year trainee programme. The position of assistant store manager/sales coach has been implemented. The organisation and candidates are prepared for their new positions by taking part in a two day training course. In connection with new openings, theme days are carried out for the store personnel.

Since 2003 an internal store display course has been available for sales personnel who are interested in changing professional direction.

During the year, all of KappAhl's buyers have taken part in a course in negotiation technique.

Parallel with personnel development, the work with sick absenteeism and working environment has been prioritised. KappAhl has, exactly like the entire industry, a relatively high level of sick absenteeism but according to Kajsa Räftegård it has begun to decrease.
"Along with occupational health services we are working to get employees back to work faster. We are also working preventively by using health profiles, seminars and providing staff with fitness activities."

During the year, KappAhl appointed a "safety coach" who visits the stores and provides information and education in safety issues.

Internal surveys confirm that KappAhl is a good place to work where leadership, working methods and well-being regularly receive high points.

It is noticeable also by the thousands of spontaneous job applications that we receive each year and the hundreds of responses received as a result of advertised positions. KappAhl does not have any problems finding new and competent employees.

FINANCIAL OVERVIEW

KEY FIGURES	2004	2003	2002	2001	2000
Net sales excl. VAT (SEK million)	3,860	3,810	3,869	4,195	3,917
Investments (SEK million)	203	103	149	265	132
Gross margin (%)	5.8	3.2	1.8	–4.7	4.1
Net margin (%)	5.3	2.7	1	–6.3	3.7
Profit/Loss after financial items (SEK million)	204	102	18	–265	144
Sales area (thousands of square metres)	200	199	209	221	213
Return on capital employed (%)	21	13	6	–14	19
EBITA (SEK million)	261	160	112	–145	171
EBITA (%)	6.8	4.2	2.9	–3.5	4.4

DEFINITIONS

Gross margin – Profit/loss before financial items as a percentage of the period's net sales. **Net margin** – Profit/loss after financial items as a percentage of the period's net sales. **Return on capital employed** – Profit/loss after financial items including financial costs as a percentage of the average capital employed. **Capital employed** – Balance sheet total less non-interest-bearing liabilities. **EBITA** – Operating earnings before goodwill amortisation in SEK m and as a percentage of the period's net sales.

DIRECTORS' REPORT

The Board of Directors and the CEO of KappAhl AB, corporate ID number 556060-4158 and registered in Mölndal, hereby present the consolidated financial statements for the financial year, 1 January–31 December 2004.

GENERAL INFORMATION ON OPERATIONS

The Group carries out operations in retail sales of ladieswear, menswear, childrenswear and cosmetics. In addition to the parent company, KappAhl AB, the Group comprises wholly-owned sales companies in Norway, Finland and Poland, and a purchasing company in China. There is also a subsidiary in Norway, Logistikksenter AS, which rents out a distribution centre. In addition, the Group has branches in Turkey, Lithuania, Bangladesh and India, as well as a dormant Swedish subsidiary. In 2004 a store location was acquired through two Swedish companies.

The company in China is responsible for making contact with new suppliers and overseeing production and delivery in the Far East. The sales companies are responsible for retail sales in their respective countries. Branch offices provide support for purchasing operations and conduct quality control in their respective markets.

At the beginning of the financial year, the Group had 237 stores and at the end of the year, 235 stores. During the year, four new stores were opened and six were closed.

Up until 21 December 2004, KappAhl AB was a wholly-owned subsidiary within the Swedish Cooperative Union (KF). On this date KappAhl Holding AB took over 100% of the shares.

Through a financial leasing agreement, the Group rents the distribution centre where all of the Group's clothing is prepared for delivery to the various stores.

IMPORTANT EVENTS IN 2004

Efforts to increase profits continued and were successful during the year. The main focus was on improving the gross margin. Several steps have been taken to achieve this objective. The most important measure has been ensuring that the range of products is better suited to our target customer groups. We have also tackled specific components of merchandise costs to further improve the margins. Since a large portion of our purchases are made in US and Hong Kong dollars, foreign exchange trends had a positive impact on our margins. All in all, this improved margins for all of our business areas in all markets. In 2004 we continued to see the results of the extensive improvement programme that was launched in spring 2002. We have increased our operating margin from –6.3% in 2001 to +5.3% in 2004. Measures that have already been implemented are expected to have further positive effects in 2005.

During the year, investments were concentrated on maintaining the existing stores. Apart from our range of products, the stores' design and atmosphere are the most important factors in creating a pleasant experience, which brings the customer back. The investment in store maintenance is an important factor in ensuring the Group's long-term earning capacity.

A write-down of the value of fixed assets in unprofitable stores was made in the amount of SEK 19 million (0). In connection with the company's change of ownership, the seller received payment for a number of foreign currency contracts and this lowered the earnings by SEK 34 million.

SALES

The KappAhl Group's total sales amounted to SEK 3,860 million excluding VAT (3,810). Measured in local currencies, the sales increased by 3%. The gross margin was 54% (52). The portion of Group sales attributable to operations in other countries decreased to 42% (44).

PROFITS

The Group's profits before financial items amounted to SEK 222.6 million (120.3), which is the highest in KappAhl's history. The net margin for the Group amounted to 5.3% (2.7). The return on total equity amounted to 14% (8) and the return on capital employed was 21% (13). The equity/assets ratio, which is calculated as equity in relation to the balance sheet total, was 44% (45).

EXPECTATIONS FOR FUTURE DEVELOPMENT

With the programme that is in place to improve profits and a continued favourable foreign exchange trend, the profits for 2005 are expected to be better than in 2004.

The termination of a quota system for textile imports to the EU in the beginning of 2005 will facilitate the import of textiles. This should also have a positive impact on KappAhl's profits. However, there is still a significant risk that new import restrictions will be introduced, which could interfere with the flow of merchandise.

FOREIGN CURRENCY EXPOSURE AND POLICY

The purpose of the foreign currency policy is to minimise the risk of negative effects on profits and to increase the predictability of future profits. This is achieved by hedging assets (mainly of subsidiaries) and liabilities. Future goods flows are also hedged 3 – 9 months forward. Hedging is carried out using a combination of forward contracts and currency options. A substantial portion of the Group's goods are purchased in US dollars, which makes the business sensitive to changes in the dollar exchange rate.

FINANCING

All financing and investment of funds is done through KappAhl Holding AB. The cash and bank balances of KappAhl AB and its subsidiaries totalled SEK 274 million.

STORES

	Number of stores at start of year	Stores opened	Store closures	Number of stores at year-end
KappAhl				
Sweden	124	3	3	124
Finland	31	–	1	30
Norway	73	1	2	72
Poland	9	–	–	9
Total	**237**	**4**	**6**	**235**

The investment focus over the past year has been on upgrading the existing stores. This has limited the establishment of new stores.

INVESTMENTS

Overall the Group invested SEK 203 million (103) in tangible and intangible fixed assets during the course of the business year. The invested funds were used essentially to develop and improve the store network.

For information about the company's profits and financial position, please refer to the income statement, balance sheet and notes that follow.

INCOME STATEMENT - GROUP

AMOUNTS IN SEK MILLION	NOTE	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Net sales	1	3,860.3	3,810.4
Cost of goods sold		–1,792.0	–1,815.1
Gross profit		**2,068.3**	**1,995.3**
Selling expenses		–1,714.6	–1,754.4
Administrative expenses		–135.2	–122.2
Other operating income	3	4.1	1,6
Other operating expenses		–	–
Operating profit	**2,4,5,6,17**	**222.6**	**120.3**
Result from financial items			
Interest income	7	1.6	1.7
Interest expense	8	–19.9	–20.0
Profit after financial items		**204.3**	**102.0**
Profit before tax		**204.3**	**102.0**
Tax expense for the year	9	2.2	–5.0
PROFIT/LOSS FOR THE YEAR		**206.5**	**97.0**

BALANCE SHEET - GROUP

AMOUNT IN SEK MILLION	NOTE	2004-12-31	2003-12-31
ASSETS			
Fixed assets			
Intangible fixed assets			
Software, brands	10	11.0	9.6
Tenancy rights	10	13.8	1.1
Goodwill	10	225.2	262.3
		250.0	**273.0**
Tangible fixed assets			
Buildings and land	11	192.8	–
Equipment	11	369.3	314.5
		562.1	**314.5**
Financial fixed assets			
Other investments held as fixed assets		0.0	0.2
Deferred tax assets	12	64.8	19.1
		64.8	**19.3**
Total Fixed Assets		**876.9**	**606.8**
Current assets			
Inventory etc.			
Finished goods and merchandise		476.3	423.6
		476.3	**423.6**
Current receivables			
Accounts receivable		7.2	9.1
Other receivables		18.3	9.6
Prepaid expenses and accrued income	13	81.8	120.6
		107.3	**139.3**
Cash and cash equivalents		**274.3**	**53.9**
Total current assets		**857.9**	**616.8**
TOTAL ASSETS		**1,734.8**	**1,223.6**

AMOUNT IN SEK MILLION	NOTE	2004-12-31	2003-12-31
EQUITY AND LIABILITIES			
Equity	**14**		
Restricted equity			
Share capital		6.0	6.0
Restricted reserves		97,9	107.1
		103,9	**113.1**
Non-restricted equity			
Distributable reserves		443.9	338.5
Profit for the year		206.5	97.0
		650.4	**435.6**
Total equity		**754.3**	**548.6**
Provisions			
Provisions for pensions and similar obligations	15	65.5	52.1
Provisions for deferred tax	12	50.9	24.0
Other provisions	16	50.1	31.8
Total provisions		**166.5**	**107.9**
Long-term liabilities			
Financial leasing loans	11	182.3	–
Other long-term liabilities		49.5	–
Total long-term liabilities		**231.8**	**–**
Current liabilities			
Liabilities to credit institutions	11	25.5	9.4
Accounts payable – trade		163.1	165.5
Liabilities to Group companies		1.2	55.9
Tax liability		29.2	–
Other liabilities		87.8	106.2
Accrued expenses and deferred income	18	275.4	230.1
Total current liabilities		**582.2**	**567.1**
TOTAL EQUITY AND LIABILITIES		**1,734.8**	**1,223.6**

PLEDGED ASSETS AND CONTINGENT LIABILITIES

AMOUNTS IN SEK MILLION	2004-12-31	2003-12-31
Pledged assets		
For own liabilities and provisions		
Floating charge	33.0	33.0
Total pledged assets	**33.0**	**33.0**
Contingent liabilities		
Guarantee undertakings, FPG/PRI	0.4	0.4
Total contingent liabilities	**0.4**	**0.4**

CASH FLOW STATEMENT - GROUP

AMOUNTS IN SEK MILLION	2004-01-01 –2004-12-13	2003-01-01 –2003-12-31
Operating activities		
Profit after financial items	204.3	102.0
Adjustments for non-cash items, etc.	215.1	171.7
	419.4	**273.7**
Current tax	–17.8	–
Cash flow from operating activities before changes in working capital	**401.6**	**273.7**
Cash flow from changes in working capital		
Increase(-)/Decrease(+) in inventories	47.1	143.2
Increase(-)/Decrease(+) in operating receivables	32.0	249.0
Increase(-)/Decrease(+) in operating liabilities	16.0	–41.2
Cash flow from operating activities	**496.7**	**624.7**
Investment activities		
Acquisition of subsidiaries	–12.5	–
Acquisition of intangible fixed assets	–23.0	–3.0
Acquisition of tangible fixed assets	–167.5	–100.0
Cash flow from investment activities	**–203.0**	**–103.0**
Financing activities		
Loan repayment, net	–72.0	–530.0
Cash flow from financing activities	**–72.0**	**–530.0**
Cash flow for the year	**221.7**	**–8.3**
Cash and cash equivalents at beginning of year	**53.9**	**62.6**
Exchange rate differences in cash and cash equivalents	**–1.3**	**–0.4**
Cash and cash equivalents at end of year	**274.3**	**53.9**

ADDITIONAL CASH-FLOW STATEMENT INFORMATION – GROUP

AMOUNTS IN SEK MILLION	2004-01-01 –2004-12-13	2003-01-01 –2003-12-31
Interest paid and dividends received		
Interest received	1.6	1.7
Interest paid	–19.9	–20.0
Adjustments for non-cash items		
Depreciation and impairment of assets	189.1	154.7
Provisions for pensions	8,0	2.0
Other provisions	18.0	15.0
	215.1	**171.7**
Acquisition of subsidiaries and other business units		
Acquired assets and liabilities:		
Intangible fixed assets	10.0	–
Operating receivables	2.5	–
Total assets	**12.5**	**–**
Purchase price	12.5	–
Amount paid for purchase	12.5	–
Effect on cash and cash equivalents (minus = increase)	12.5	–
Cash and cash equivalents		
The following components are included in cash and cash equivalents:		
Cash and cash equivalents	274.3	53.9
	274.3	**53.9**
Inventory		
Inventory at the beginning of year	423.6	
Change in accounting principle not affecting cash	99.8	
Decrease of inventory	–47.1	
Inventory at the end of year	**476.3**	
Operational cash flow		
Operating profit	222.6	120.3
Adjustments for non-cash items	215.1	171.7
Change in working capital	95.0	351.0
Investments	–203.0	–103.0
Operational cash flow	**329.7**	**540.0**
Change in net debt		
Net debt at beginning of year	11.4	586.0
Repayment of interest-bearing liabilities	–72.0	–530.0
Other changes in interest-bearing liabilities	214.5	3.1
Changes in provisions for pensions	–	–56.4
Change in cash and cash equivalents	–220.4	8.7
Net dept at end of year	**–66.5**	**11.4**

Amounts in SEK million

GENERAL ACCOUNTING PRINCIPLES

The annual accounts have been prepared in accordance with the Annual Accounts Act and the recommendations and general guidelines issued by regulatory bodies. Under each heading we have stated which recommendations and general guidelines have been applied. Unless otherwise indicated below, the accounting principles are the same as those used in the 2003 financial year.

VALUATION PRINCIPLES ETC.

Assets, provisions and liabilities have been valued at their acquisition value, unless otherwise indicated below.

INTANGIBLE ASSETS

The Group applies the Swedish Financial Accounting Standards Council's recommendation (hereafter abbreviated to RR) 15 Intangible assets.

Software

Computer software acquired by the company is recognised at acquisition value minus accumulated amortization and impairment.

Goodwill relating to the store network

Goodwill investments relate to a long-term focus on increasing the store network. Acquisitions lead to increased volume and significant synergy benefits in both purchasing and distribution. The amortization period has been set at 10 years.

Brands

Brands acquired by the company are recognised at their acquisition value minus accumulated amortization and impairment.

Tenancy rights

Tenancy rights for the stores are recognised at their acquisition value with an estimated period of use of five to ten years.

DEPRECIATION

The Group applies RR 12 Tangible Fixed Assets.

Depreciation according to plan is based on the original acquisition value of the asset minus the residual value. Depreciation is done on a straight-line basis over the useful life of the asset and is recognised as a cost in the income statement.

Schedule for depreciation/amortization:

Acquired intangible assets	Useful life period 2004	Useful life period 2003
Software	3 years	3 years
Brands	3 years	3 years
Goodwill	10 years	10 years
Tenancy rights	5 years	5 years

Acquired tangible assets	Useful life period
Equipment	3–10 years

The buildings in Mölndal, Sweden, that house the head office and distribution center are rented under a financial leasing agreement and are therefore entered from 2004 as tangible assets in the accounts. The value is depreciated over the duration of the contract, which is fifteen years.

LOAN EXPENSES

The Group applies RR 21 Loan Expenses. Loan expenses are charged to earnings in the period in which they arise, regardless of how the borrowed funds have been used.

IMPAIRMENT

The Group applies RR 17 Impairment of Assets.

The reported values of the Group's assets are reviewed on each reporting date to assess if there is an indication of impairment. If such an indication exists, the asset's recoverable value is assessed as the higher of the asset's value in use and its net realisable value. Impairment write-down is indicated if the recoverable amount is less than the reported value. When calculating the value in use of an asset, future cash flows are discounted at an interest rate before tax that is intended to take into account the market assessment of risk-free interest and risk associated with the specific asset. In the case of an asset that does not generate any cash inflows that are independent from those of other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

RECEIVABLES

Following individual evaluation, receivables are recorded at the amounts that are expected to be paid in.

RECEIVABLES AND LIABILITIES IN FOREIGN CURRENCIES

Receivables and liabilities in foreign currencies have been translated at the exchange rate on the balance sheet date in accordance with RR 8, with the exception of long-term monetary commitments with foreign operations for which the historical rate of exchange is used. Exchange rate differences relating to operating receivables and operating liabilities are included in operating profit, while differences in financial receivables and liabilities are entered under financial items. Where receivables and liabilities in foreign currencies have been hedged through forward contracts, they are translated at the forward rate irrespective of the duration of the forward contract.

INVENTORY

Inventory, valued according to RR 2:02, is entered at the lower of the acquisition value and the net realisable value. The obsolescence risk is thus taken into account. The acquisition value is calculated using the first-in, first-out principle or according to weighted average prices.

REMUNERATION OF EMPLOYEES

The Group

The Group has been applying RR 29 Remuneration of Employees since the beginning of the 2004 financial year. According to this principle, defined benefit pension plans are recorded in the consolidated accounts according to general principles and calculation methods.

The Group offers both defined contribution and defined benefit pension plans. In the case of defined contribution plans, the Group's obligation is limited to fixed contributions that are paid by the respective legal entities. The Group's profits are charged as the benefits are earned. In the defined benefit plans, the Group's obligation is based on the employee's salary at the time of retirement and the number of years served. The Group carries the risk associated with payment of the pledged benefits. In the balance sheet the difference between the present value of the obligations and the actual value of managed assets is recognised as a provision. Defined benefit plans are calculated according to the so-called projected unit credit method. This calculation is done annually by independent actuaries. The company's obligations are assessed at the present value of the expected future payments. Actuarial gains and losses may occur if the actual outcome deviates from previous assumptions or if the assumptions are changed. The portion of the accumulated actuarial gains and losses at the end of the previous year that exceeds 10% of the greater of the present value of the obligations and the managed assets' actual value is recognised as profit over the employees' remaining period of service. See also Note 15.

TAX

The company and the Group apply RR 9 Income Tax. Total tax consists of current tax and deferred tax. Taxes are recorded in the income statement except when the underlying transaction is recognised directly in equity, in which case the associated tax effect is recognised in equity. Current tax is tax that is payable or recoverable for the current year. This also includes adjustments to the current tax of earlier periods. Deferred tax is calculated using the balance sheet method based on temporary differences between the book value of assets and liabilities and their value as assessed for tax purposes. The amounts are calculated based on how the temporary differences are expected to be balanced out and using the tax rates and tax rules that are in effect or announced as of the balance sheet date.

Temporary differences are neither recognised in goodwill on consolidation nor in differences relating to participations in subsidiaries or associated companies that are not expected to be taxed in the foreseeable future. For legal entities, the untaxed reserves are recorded including deferred tax liabilities. In the consolidated accounts, however, untaxed reserves are divided up into deferred tax liability and equity. Deferred tax assets relating to deductible temporary differences and loss carryforward are only recorded to the extent it is likely that these will lead to lower tax payments in the future. The assessment is based on a maximum of five years of forecasted tax payments.

PROVISIONS

A provision is recognised in accordance with RR 16 Provisions, Contingent Liabilities and Contingent Assets in the balance sheet when the company has a formal or informal obligation as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

REVENUE

Revenue is recognised in accordance with RR 11 Revenues. Revenue is recognised at the actual value of the consideration received or receivable, less any discounts provided. All sales are made on a 30-day sale-or-return basis. Revenue is recognised on the date of the sale subject to sale-or-return.

LEASING – LESSEES

RR 6:99 is applied. Leasing is classified in the consolidated accounts either as financial or operational leasing. In the case of operational leasing, the leasing fees are expensed over the lease term on the basis of use, which may differ from the de facto amount of leasing fees paid during the year.

Assets that are leased under financial leasing agreements are recognised as assets in the consolidated balance sheet. Future leasing fee obligations are recorded as long-term and current liabilities. The leased assets are depreciated according to plan, while leasing fees are recorded as interest and repayment of debt.

ITEMS AFFECTING COMPARABILITY

RR 4 is applied, according to which the effects on profits of particular events and transactions of significant importance are specified within the relevant profit/ loss item.

HEDGING COMMERCIAL FLOWS

Where contracted future currency flows are hedged, the exchange rate differences of the forward transaction are entered in the income statement in the same period as the underlying flow. Calculated future net foreign currency flows hedged through forward contracts as of December 31, 2004, amount to SEK 193 million (SEK 279 million in 2003).

CONSOLIDATED ACCOUNTS

The consolidated accounts are prepared in accordance with RR 1:00.

SUBSIDIARIES

Subsidiaries are companies in which the parent company directly or indirectly holds more than 50% of the votes or in another way has a controlling influence over the operations and financial control. Acquisition accounting is normally used for subsidiary reporting. Acquisition accounting means that the acquisition of a subsidiary is regarded as a transaction by which the parent company indirectly acquires the assets of the subsidiary and assumes its liabilities. The acquired company's revenue and costs, identifiable assets and liabilities and any goodwill or negative goodwill that arise are included in the consolidated accounts from the date of the acquisition.

TRANSLATION OF FOREIGN SUBSIDIARIES OR OTHER FOREIGN OPERATIONS

Foreign currency translation is done according to RR 8. The current rate method is used for translation of income statements and balance sheets of independent foreign operations. According to the current rate method, all assets, provisions and liabilities are translated at the exchange rate on the balance sheet date and all items in the income statement are translated at an average rate of exchange. Exchange rate differences that arise are applied directly to equity. In connection with the disposal of independently-run foreign operations, the accumulated translation differences relating to the entity's operations are realised in the consolidated income statement after deduction for any hedging.

GROUP CONTRIBUTIONS AND SHAREHOLDERS' CONTRIBUTIONS

The company accounts for Group and shareholders' contributions in accordance with the statement issued by the Swedish Financial Accounting Standards Council's Emerging Issues Group. Shareholders' contributions are applied directly to the equity of the recipient and are capitalized as shares and participations for the contributor, to the extent that write-down is not required.

Group contributions are entered in the accounts according to their financial significance. This means that Group contributions that have been made in order to minimise the Group's overall tax burden are entered directly against retained earnings after deduction for the current tax effect.

CASH FLOW

The company applies RR 7, the indirect method.

CHANGES IN ACCOUNTING PRINCIPLES

Application of the Swedish Financial Accounting Standards Council's recommendations

The Group applies RR 2:02 Inventory, according to which a re-evaluation has been made of the beginning and ending inventory for the financial year. The effect of the change has been entered directly against equity, in accordance with RR 5 Change in Accounting Principles.

The Group also started to apply RR 29 at the beginning of 2004.

GROUP INFORMATION

In December 21, 2004, the company became a wholly-owned subsidiary of KappAhl Holding AB, with corporate ID number 556661-2312.

RELATED PARTIES

Related party relationships that involve a controlling influence

The company applies RR 23 Information on Related Parties.

The Group is under the controlling influence of KappAhl Holding AB.

TRANSACTIONS WITH RELATED PARTIES

The Executive Vice President of KappAhl, Paul Frankenius, is a shareholder in and Director of Total Logistik Sweden AB, the Norwegian subsidiary of which supplies logistics services for cosmetics for KappAhl's Norwegian stores. For more information on salaries and other remuneration, costs and obligations relating to pensions and similar benefits, and agreements regarding severance pay to the Board of Directors and CEO, please see note 2.

NOTE 1 NET SALES BY GEOGRAPHIC MARKET

	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Net sales by geographic market		
Sweden	2,246.6	2,157.0
Finland	410.7	396.1
Norway	1,093.1	1,142.4
Poland	109.9	114.3
Czech Republic	—	0.6
	3,860.3	**3,810.4**

NOTE 2 EMPLOYEES, PERSONNEL EXPENSES AND FEES FOR THE BOARD OF DIRECTORS AND AUDITORS

Average no. of employees	2004-01-01 –2004-12-31	Of which men	2003-01-01 –2003-12-31	Of which men
Parent Company				
Sweden	1,295	12%	1,269	14%
Total for Parent Company	**1,295**	**12%**	**1,269**	**14%**
Subsidiaries				
Asia	87	44%	105	49%
Finland	259	3%	260	3%
Norway	578	5%	611	10%
Poland	121	14%	149	14%
Total for subsidiaries	**1,045**	**9%**	**1,125**	**9%**
Group total	**2,340**	**11%**	**2,394**	**11%**

Information on distribution according to gender in corporate management

Distribution according to gender in corporate management	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Group total	Percentage of women	Percentage of women
The Board of Directors	50%	38%
Other senior executives	65%	63%

Salaries, other remuneration and social security costs

	2004-01-01–2004-12-31		2003-01-01–2003-12-31	
	Salaries and remuneration	Social security costs	Salaries and remuneration	Social security costs
Parent Company	394.3	180.4	386.7	168.2
(of which pension costs) 1)		*32.6*		*32.6*
Subsidiaries	280.1	64.8	288.4	72.1
(of which pension costs)		*18.2*		*21.7*
Group Total	**674.3**	**245.2**	**675.1**	**240.3**
(of which pension costs) 1)		*50.8*		*54.3*

1) The parent company's pension costs include SEK 0.9 million (SEK 1.7 million in 2003) for the Board of Directors and CEO.

Salaries and other remuneration by country and between board members etc. and other employees

	2004-01-01–2004-12-31		2003-01-01–2003-12-31	
	Board and CEO	Other employees	Board and CEO	Other employees
Parent Company				
Sweden	5.5	388.7	4.9	381.7
(of which bonus etc.)	*0.9*	*4.6*	*1.2*	*20.5*
Parent Company total	**5.5**	**388.7**	**4.9**	**381.7**
(of which bonus etc.)	*0.9*	*4.6*	*1.2*	*20.5*
Foreign subsidiaries				
Asia	1.8	8.6	1.1	8.1
Finland	1.3	61.7	1.3	61.6
Norway	1.9	197.0	1.7	204.9
Poland	0.6	7.3	0.9	8.2
Czech Republic	—	—	—	0.5
Subsidiaries total	**5.6**	**274.6**	**5.0**	**283.3**
Group Total	**11.1**	**663.3**	**9.9**	**665.0**
(of which bonus etc.)	*0.9*	*4.6*	*1.2*	*20.5*

The CEO's salary is SEK 3.4 million (SEK 3.8 million in 2003), SEK 0.8 million (SEK 0.8 million in 2003) of which is bonus. Pension is based on the ITP plan. Of the salaries and remuneration paid to other employees in the Group, the amount of SEK 5.5 million (SEK 7.7 million in 2003) is for senior executives other than the Board and CEO.

Severance pay

If requested by the employer to resign their positions, some senior executives have contracts that guarantee them the right to retain their salaries in full for a period of 6 months. Retirement benefits are based on national pension plans from 65 years of age.

Fees and expenses paid to auditors

KPMG	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Audit assignments	1.1	1.4
Other assignments	0.5	0.7

NOTE 3 OTHER OPERATING INCOME

Group	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Disposal of property	4.1	—
Disposal of Mac Coy A/S (final settlement)	—	1.6
	4.1	**1.6**

NOTE 4 DEPRECIATION/AMORTIZATION OF TANGIBLE/INTANGIBLE FIXED ASSETS

Group	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Depreciation/amortization according to plan by asset		
Software, brands	–7.3	–12.2
Tenancy rights	–1.3	–0.6
Goodwill	–38.3	–39.8
Buildings and land	–28.2	—
Equipment, tools and installations	–108.4	–99.8
	–183.5	**–152.4**
Amortisation according to plan by function		
Cost of goods sold	–19.3	–21.3
Selling expenses	–155.5	–118.6
Administrative expenses	–8.7	–12.5
	–183.5	**–152.4**
Write-down by function		
Selling expenses	–19.1	–2.3
	–19.1	**–2.3**

NOTE 5 LEASING FEES FOR OPERATIONAL LEASES

	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Assets held through operational leasing agreements		
Minimum leasing fees	2.0	2.0
Total leasing expenses	**2.0**	**2.0**
Agreed future minimum leasing fees for non-cancellable agreements due for payment:		
Within one year	1.4	2.0
Between one and five years	1.7	2.7
	3.1	**4.7**

NOTE 6 COSTS FOR PREMISES

The operating profit has been charged with SEK 467 million (SEK 486 million in 2003) for the Group's costs for rented premises. The rents paid by the company are to a large extent turnover-based. The rental agreements have varying durations and periods of notice. For this reason it is difficult to provide an accurate prediction of future rental costs.

NOTE 7 INTEREST INCOME

	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Interest income, other	1.6	1.7
	1.6	**1.7**

NOTE 8 INTEREST EXPENSE

	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Interest expense, other	–4.9	–20.0
Interest expense, financial leases	–13.3	—
Interest expense, pensions	–1.7	—
	–19.9	**–20.0**

NOTE 9 TAXES

	2004-01-01 –2004-12-31	2003-01-01 –2003-12-31
Current tax expense		
Tax expense for the period	–46.8	–1.8
	–46.8	**–1.8**
Deferred tax expense		
Deferred tax relating to temporary differences	8.1	12.3
Deferred tax credit, capitalized tax value in losses carried forward for the year	43.0	–21.1
Deferred tax expense resulting from utilisation of previously capitalized tax value in losses carried forward	–2.1	5.6
Deferred tax pertaining to reappraisal of reported tax assets	—	—
	49.0	**–3.2**
Total reported tax expense for the Group	**2.2**	**–5.0**

Reconciliation of effective tax	2004-01-01–2004-12-31 Percent	Amount	2003-01-01–2003-12-31 Percent	Amount
Profit before tax		204.3		102.0
Tax at effective tax rate for parent company	28.0%	–57.2	28.0%	–28.6
Effect of other tax rates for foreign subsidiaries	1.0%	–2.1	0.4%	–0.4
Other non-deductible expenses	–1.0%	2.1	5.1%	–5.2
Utilisation of previously non-capitalized losses carried-forward	0.0%	—	–29.7%	30.3
Utilisation of previously capitalized losses carried-forward	1.4%	–2.8	0.0%	—
Adjustment of current tax for previous periods	2.0%	–4.1	0.0%	—
Reappraisal of deferred tax asset	–27.3%	55.8	5.6%	–5.7
Other	–5.1%	10.5	–4.5%	4.6
Booked effective tax	**–1.1%**	**2.2**	**4.9%**	**–5.0**

NOTE 10 INTANGIBLE ASSETS

Software

Acquired	
Accumulated acquisition values	
At beginning of year	57.1
Acquisitions	8.7
Exchange rate differences for the year	0.0
At end of year	**65.8**
Accumulated amortization according to plan	
At beginning of year	–47.7
Amortization for the year according to plan	–7.3
Exchange rate differences for the year	0.0
At end of year	**–55.0**
Recorded value at beginning of period	**9.4**
Recorded value at end of period	**10.8**

Tenancy rights

Acquired	
Accumulated acquisition values	
At beginning of year	17.1
Acquisitions	24.2
Disposals and retirement	–0.5
At end of year	**40.8**
Accumulated amortization according to plan	
At beginning of year	–16.0
Disposals and retirement	0.4
Amortization for the year according to plan	–1.3
At end of year	**–16.9**
Accumulated impairment	
At beginning of year	—
Impairment for the year	–10.1
At end of year	**–10.1**
Recorded value at beginning of period	**1.1**
Recorded value at end of period	**13.8**

Goodwill

Acquired	
Accumulated acquisition value	
At beginning of year	429.3
Exchange rate differences for the year	3.3
At end of year	**432.6**
Accumulated amortization according to plan	
At beginning of year	–121.8
Amortization for the year according to plan	–38.3
Exchange rate differences for the year	–1.7
At end of year	**–161.8**
Accumulated impairment	
At beginning of year	–45.2
Exchange rate differences for the year	–0.4
At end of year	**–45.6**
Recorded value at beginning of period	**262.3**
Recorded value at end of period	**225.2**

Brands

Acquired	
Accumulated acquisition values	
At beginning of year	0.2
At end of year	**0.2**
Accumulated amortization according to plan	
At beginning of year	0.0
Amortization for the year according to plan	0.0
At end of year	**0.0**
Accumulated impairment	
At beginning of year	—
At end of year	**—**
Recorded value at beginning of period	**0.2**
Recorded value at end of period	**0.2**

Total intangible assets

Acquired	
Accumulated acquisition values	
At beginning of year	543.2
Acquisitions	32.9
Disposals and retirement	–0.5
Exchange rate differences for the year	3.4
At end of year	**579.0**
Accumulated amortization according to plan	
At beginning of year	–189.4
Disposals and retirement	0.4
Amortization for the year according to plan	–46.9
Exchange rate differences for the year	–1.8
At end of year	**–237.7**
Accumulated impairment	
At beginning of year	–80.8
Impairment for the year	–10.1
Exchange rate differences for the year	–0.4
At end of year	**–91.3**
Recorded value at beginning of period	**273.0**
Recorded value at end of period	**250.0**

NOTE 11 TANGIBLE ASSETS

Equipment

Accumulated acquisition value	
At beginning of year	918.5
Acquisitions	167.5
Disposals and retirement	–8.0
Exchange rate differences for the year	9.5
	1,087.5
Accumulated depreciation according to plan	
At beginning of year	–601.7
Disposals and retirement	7.2
Reclassification	–1.6
Depreciation of acquisition value for the year according to plan	–108.4
Exchange rate differences for the year	–2.8
	–707.3
Accumulated impairment	
At beginning of year	–2.3
Impairment reversal during the year	0.3
Impairment for the year	–9.0
Exchange rate differences for the year	0.1
	–10.9
Recorded value at end of period	**369.3**

Buildings

Accumulated acquisition value	
At beginning of year	—
Change in accounting principle for financial leasing	221.0
Accumulated depreciation according to plan	**221.0**
At beginning of year	—
Change in accounting principle	–13.5
Depreciation of acquisition value for the year according to plan	–14.7
	–28.2
Recorded value at end of period	**192.8**

The buildings that house KappAhl's head office and distribution centre are rented under a financial leasing agreement and have therefore been entered in the accounts as tangible assets from the beginning of the 2004 financial year.

The present value of future minimum leasing fees are entered in the accounts partly as a current liability, SEK 22.3 million, which falls due within one year, and partly as a long-term liability, SEK 182.3 million.

NOTE 12 DEFFERED TAX ASSET

Group 2004-12-31	Deferred taxes recoverable	Deferred tax liability	Net
Untaxed reserves	—	38.7	–38.7
Inventory	—	8.0	–8.0
Other	4.7	4.2	0.5
Losses carried-forward	60.1	—	60.1
	64.8	**50.9**	**13.9**
Set off	—	—	—
Net deferred tax asset	**64.8**	**50.9**	**13.9**

Group 2003-12-31	Deferred taxes recoverable	Deferred tax liability	Net
Untaxed reserves	—	24.0	–24.0
Losses carried-forward	19.1	—	19.1
	19.1	**24.0**	**–4.9**
Set off	—	—	—
Net deferred tax liability	**19.1**	**24.0**	**–4.9**

Unrecognized deferred tax amounts to SEK 78 million and pertains to losses carried forward. SEK 48 million of the unrecognised deferred tax asset pertains to KappAhl AS in Norway, where the period in which it can be utilized is limited to ten years from each year of assessment when losses arise (here 2005). The remaining amount of the unrecognised deferred tax relates to the other subsidiary in Norway, Vestfold Logistikksenter AS.

NOTE 13 PREPAID EXPENSES AND ACCRUED INCOME

	2004-12-31	2003-12-31
Prepaid rentals	67.3	59.3
Other	14.5	61.3
	81.8	**120.6**

NOTE 14 EQUITY

	Equity	Restricted reserves	Non-restricted equity
At beginning of year	6.0	107.1	435.6
Opening balance impact of change of accounting principles			
- for inventory valuation according to RR 2:02			71.9
- financial leasing			–66.6
- pensions			–4.4
Transfer between non-restricted and restricted equity		–9.1	9.1
Profit for the year			206.5
Exchange rate difference for the year		–0.1	–1.7
At year-end	**6.0**	**97.9**	**650.4**

Change of accounting principles concerning inventory refers to the revised calculation methods concerning cost and net realisable value. Financial leasing refers to the adoption of the new shareholders application of RR6 for the leasing contracts related to the previous years sold and subsequently lease-back of the headquarters and the distribution center.

NOTE 15 PROVISIONS FOR PENSIONS AND SIMILAR OBLIGATIONS

PRI/FPG	21.0
Other pension provisions	44.5
	65.5
Amount of this covered by credit insurance through FPG/PRI	21.7
Defined-benefit obligations and value of the managed assets	
Present value of unfunded defined benefit obligations	67.4
Net obligation before adjustment	67.4
Adjustments:	
Accumulated unrecognised actuarial gains (+) and losses (-)	–1.9
Net amount in balance sheet (obligation)	**65.5**
Net amount is recognised in the the following items in the balance sheet:	
Provisions for pensions and similar obligations	65.5
Net amount is divided between plans in the following countries:	
Sweden	35.2
Norway	30.3
Net amount in the balance sheet (obligation)	**65.5**
Pension costs	
Defined-benefit plans	
Cost of pensions earned during the year	–17.0
Interest expense	–6.2
Anticipated return on managed assets	3.4
Actuarial gains (-) and losses (+) recognised during the year	—
Cost of defined benefit plans	**–19.8**

The following table explains the changes in the net amount in the balance sheet over the period:

Net amount in the balance sheet, 31 Dec 2003	–47.1
Effect of change in accounting princible to RR 29, 1 Jan 2004	–5.0
Net amount, 1 Jan 2004	**–52.1**
Cost of defined-benefit plans	–19.8
Disbursment of benefits	0.3
Payment of fees by the company	6.1
Net amount in the balance sheet, 31 Dec 2004	**–65.5**

Actuarial assumptions
The following actuarial assumptions have been applied in calculating the obligations (weighted average amounts):

Discount rate	4.3%
Future salary increases	3.0%
Future increases in pensions	2.0%
Employee turnover	5.0%
Inflation	2.0%
Anticipated returns	4.3%

Pledged assets for pension obligations

Guarantee undertakings to FPG/PRI	0.4

NOTE 16 OTHER PROVISIONS

Reported value at beginning of period	31.8
Liabilities to customers with Medmera customer loyalty cards	0.6
Stores closures [1)]	17.7
Reported value at end of period	**50.1**

[1)] Includes increases in existing provisions.

Specification of closing balance

Liabilities to customers with Medmera customer loyalty cards	7.4
Stores closures	42.7
	50.1

NOTE 17 ITEMS OF ONE TIME CHARACTER

Cost of goods sold includes the cost of releases under currency contracts of SEK 34 million. Selling expenses includes a write-down of an investment in a store of SEK 19 million.

NOTE 18 ACCRUED EXPENSES AND DEFERRED INCOME

	2004-12-31	2003-12-31
Accrued salaries and holiday pay	104.2	108.6
Accrued social security expenses	54.7	44.5
Other	116.5	77.0
	275.4	**230.1**

MÖLNDAL, 16 DECEMBER 2005

Finn Johnsson
Chairman of the board

Amelia Adamo

Kristoffer Melinder

Bodil Nilsson
Staff representative

Jan Samuelson

Pernilla Ström

Bo Söderberg

Rose-Marie Zell-Lindström
Staff representative

Christian W. Jansson
CEO

Vår revisionsberättelse har avgivits 2005-12-16
PricewaterhouseCoopers AB

Bror Frid
Authorized Public Accountant

AUDIT REPORT

To the board of KappAhl AB

Corporate Identity Number 556060-4158

We have audited the consolidated accounts of KappAhl AB for the year 2004. These accounts and the application of the Annual Accounts Act when preparing the consolidated accounts are the responsibility of the board of directors and the managing director. Our responsibility is to express an opinion on the consolidated accounts based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Sweden. Those standards require that we plan and perform the audit to obtain reasonable assurance that the consolidated accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the accounts. An audit also includes assessing the accounting principles used and their application by the board of directors and the managing director and significant estimates made by the board of directors and the managing director when preparing the consolidated accounts as well as evaluating the overall presentation of information in the consolidated accounts.

We believe that our audit provides a reasonable basis for our opinion set out below.

The consolidated accounts have been prepared in accordance with the Annual Accounts Act and, thereby, give a true and fair view of the group's financial position and results of operations in accordance with generally accepted accounting principles in Sweden.

Gothenburg 16 December 2005

Bror Frid
Authorized Public Accountant

THE BOARD OF DIRECTORS from left to right: Melinda Hedström employee representative/deputy, **Kristoffer Melinder** board member, **Pernilla Ström** board member, **Finn Johnsson** chairman of the board, **Jan Samuelson** board member, **Amelia Adamo** board member, **Eva Larsson** employee representative/deputy. **ABSENT FROM PICTURE: Henrik Lif** deputy, **Jan Ohlsson** deputy, **Bo Söderberg** board member, **Bodil Nilsson** employee representative, **Rose-Marie Zell-Lindström** employee representative.

»There are still areas where we have
considerable potential to be even better.
It stimulates and compels us.«

THE EXECUTIVE MANAGEMENT TEAM from left to right: Mari Svensson Purchasing & Marketing, **Christian W. Jansson** President & CEO, **Gudrun Fahlback** Business development, **Kajsa Räftegård** Human Resources, **Håkan Westin** Finance, **Linda Hamberg** Sales, **Paul Frankenius** Excutive Vice President

d.t.r.t. reklambyrå and Tools. Photos (except p.1, 18, 19, 52): David Eskils Tryckeri Borås. 2005.

www.kappahl.com

KappAhl AB, Idrottsvägen 14, Box 303, SE-431 24 Mölndal, Sweden. Tel. +46 31-771 55 00