



annual
report
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The Leather Factory, Inc.



Annual Report 2004

Wray Thompson, CEO
Ron Morgan, President

Shannon Greene, CFO
William Warren, Secretary

Acknowledgements

Our 2004 Annual Report cover carving, by eminent leathercraft artist Al Stohlman, is a tribute to his influence on the art of leathercrafting. Other examples of his mastery can be seen on pages 12 through 16. All were obtained from the collection of his work at the Al Stohlman Leather Museum in Fort Worth, Texas.

Who We Are

We are the world's largest specialty retailer and wholesale distributor of leather and leathercraft related items. We market our products to our growing list of customers through company-owned retail stores and wholesale distribution centers. The key to our success is our ability to grow our base business. We grow our business by opening new locations and by increasing our customer base in our existing locations. We intend to continue to expand both domestically in the short-term, and internationally in the long-term.

Store Count						
YEARS ENDED DECEMBER 31, 1999 through 2003						
Year Ended	LEATHER FACTORY WHOLESALE CNTRS			TANDY LEATHER RETAIL STORES		
	Opened	Conversions(1)	Total	Opened (2)	Closed	Total
Balance Fwd			22			N/A
1999	4	0	26			N/A
2000	2	0	28	1*	0	1
2001	2	0	30	0	0	1
2002	1	(1)	30	14	1*	14
2003	0	0	30	12	0	26
2004	0	0	30	16	0	42

(1) Leather Factory wholesale center converted to a Tandy Leather retail store
 (2) Includes conversions of Leather Factory wholesale centers to Tandy Leather retail stores
 (*) The Tandy Leather operation began as a central mail-order fulfillment center in 2000 that we closed in 2002

LEATHER FACTORY LOCATIONS

Phoenix, AZ
 Tucson, AZ
 Baldwin Park (Los Angeles), CA
 Bay Area (Union City, CA)
 Fresno, CA
 Oakland, CA
 Denver, CO
 Tampa, FL
 Elgin (Chicago), IL
 Des Moines, IA
 Wichita, KS
 Harahan (New Orleans), LA
 Grand Rapids, MI
 Springfield, MO
 Billings, MT
 Albuquerque, NM
 Charlotte, NC
 Columbus, OH
 Portland, OR
 Harrisburg, PA
 Chattanooga, TN
 El Paso, TX
 Mesquite (Dallas), TX
 Missouri City (Houston), TX
 San Antonio, TX
 Salt Lake City, UT
 Spokane, WA

TANDY LEATHER LOCATIONS

Phoenix, AZ
 Tempe, AZ
 Fountain Valley (Orange County), CA
 Sacramento, CA
 Van Nuys, CA
 Colorado Springs, CO
 Westminster (Denver), CO
 East Hartford, CT
 Orlando, FL
 Tucker (Atlanta), GA
 Boise, ID
 Peoria, IL
 Speedway (Indianapolis), IN
 Louisville, KY
 Essex (Baltimore), MD
 Westland (Detroit), MI
 Bloomington (Minneapolis), MN
 Kansas City, MO
 St. Louis, MO
 Omaha, NE
 Las Vegas, NV
 Reno, NV
 Albuquerque, NM
 Santa Fe, NM
 Syracuse, NY
 Cleveland, OH
 Columbus, OH

Oklahoma City, OK
 Tulsa, OK
 Delmont (Pittsburgh), PA
 Memphis, TN
 Nashville, TN
 Austin, TX
 Dallas, TX
 Fort Worth (West), TX
 Houston, TX
 Salt Lake City, UT
 Richmond, VA
 Seattle, WA
 Tacoma, WA
 Milwaukee, WI

COMBINATION LOCATIONS

Edmonton, AB, Canada
 Mississauga (Toronto), Canada
 Winnipeg, MB, Canada
 Columbus, OH
 Fort Worth (East), TX

ROBERTS, CUSHMAN & CO.

Long Island City, NY



Message to Shareholders



2004 was a year in which we started well and finished strong. In the first quarter, we announced record revenues in January and February and recorded the highest quarterly earnings since the company started. The second and third quarters were solid and profitable, but nothing to brag about. We finished the year well, however, setting a new quarterly sales record in the fourth quarter. And while we didn't set any annual earnings records, we made some solid progress in positioning ourselves for the future.

Some of our achievements in 2004 were as follows:

- 2004 was our sixth year of consecutive sales gains and our eighth year of consecutive gross profit margin improvement.
- We opened thirteen Tandy Leather retail stores.
- We acquired our primary competitor in Canada, adding three more retail stores to our growing store chain.
- We repaid 72% of our bank debt.

While the year was a good one overall, there were a few disappointments. The sales decline to our national account group was a consistent problem throughout 2004. While we are working to turn this around, we are fortunate in that our national account group is not pivotal to the long-term growth and success of our company. Our main focus is our wholesale centers and more importantly, our retail stores, and we believe those operations have solid growth potential. We believe there is always room for improvement in our operating margins and would liked to have seen more improvement in this area in 2004.

Looking ahead, we expect to open Tandy Leather retail stores at a pace of an average of twelve stores per year. As we begin our fourth year of expansion, I'm reminded of a comment I made when we announced our expansion plans in 2002: "As we continue the expansion of the Tandy stores, we are committed to two things: (1) we will not sacrifice earnings for the sake of revenue growth, and (2) we don't want to incur additional debt to open stores." Our income from operations has increased every year since 1999 and we paid off our bank debt earlier this year which I think proves that we have remained true to that commitment.

We are excited about our future. We have a solid wholesale leathercraft operation that we are very proud of. Our retail leathercraft operation is strong and growing. We're well positioned financially to support our growth and have a great management team committed to the long-term success of our company. We're proud of our company and hope you as stockholders are too.

Please consider yourselves personally invited to the 2005 Annual Meeting of Stockholders. I would appreciate the opportunity to meet and visit with you in person. Thank you for your continued support and commitment to The Leather Factory, Inc.

Wray Thompson

Chairman and Chief Executive Officer

April 2005

Operations

Wholesale Leathercraft
Operating as



Retail Leathercraft
Operating as



WHOLESALE LEATHERCRAFT

The wholesale leathercraft operation distributes its broad product line of leather and leathercraft related products in the United States and internationally through Leather Factory wholesale distribution centers.

We operate Leather Factory wholesale centers in 20 states and three Canadian provinces. The centers range in size from 2,600 square feet to 19,800 square feet, with the average size of a center being approximately 6,000 square feet. Our business concept centers around the wholesale distribution of leather and related accessories to retailers, manufacturers, and end users. Our strategy is that a customer can purchase the leather, related accessories and supplies necessary to complete his project from one place. The size and layout of the centers are planned to allow large quantities of product to be displayed in an easily accessible and visually appealing manner.

Leather Factory centers serve customers through various means including walk-in traffic, phone and mail order. We also employ a distinctive marketing tactic in that we maintain an internally-developed target customer mailing list for use in our aggressive direct mail advertising campaigns. We staff Leather Factory wholesale centers with experienced managers whose compensation is tied to the operating profit of the center they manage. Sales are generated by the selling efforts of the store personnel, our direct mail advertising, our website (www.leatherfactory.com), and our participation at trade shows.

Our customer base consists of individuals, wholesale distributors, tack and saddle shops, institutions (prisons and prisoners, schools, hospitals), western stores, craft stores and craft store chains, other large volume purchasers, manufacturers, and retailers dispersed geographically throughout the world. Wholesale sales constitute the majority of our Leather Factory business, although retail customers may purchase products from Leather Factory centers. Leather Factory sales generally do not reflect significant seasonal patterns.

Our Authorized Sales Center ("ASC") program was developed to create a presence in geographical areas where we do not have a distribution center. An unrelated person operating an existing business who desires to become an ASC must apply and upon approval, place a minimum initial order.



There are also minimum annual purchase amounts the ASC must adhere to in order to maintain ASC status. In exchange, the benefits to the ASC are free advertising in certain sale flyers, price breaks on many products, advance notice of new products, and priority shipping and handling on all orders. Leather Factory centers service 208 ASC's: 115 located in the U.S., 69 located in Canada, and 24 located outside North America.

We carry a wide assortment of products including leather, lace, hand tools, kits, and craft supplies. We operate a light manufacturing facility in Fort Worth whose processes generally involve cutting leather into various shapes and patterns using metal dies. The factory produces approximately 20% of our products and also assembles and repackages product as needed. Products manufactured in our factory are distributed through our stores under the Tejas™ brand name. We also distribute product under the Tandy Leather™ and Dr. Jackson's™ brands. We develop new products through the ideas and referrals of customers and store personnel as well as the tracking of fads and trends of interest in the market. Our personnel walk trade shows and various specialty stores with the purpose of obtaining product ideas that are then developed in-house.

We offer an unconditional satisfaction guarantee to our customers. Simply stated, we will accept product returns for any reason. We believe this liberal policy promotes customer loyalty. We offer credit terms to our non-retail customers, upon receipt of a credit application and approval by our credit manager. Generally, our open accounts are net 30 days.

We currently purchase merchandise and raw materials from approximately 200 vendors dispersed throughout the United States and in more than 20 foreign countries.

Because leather is sold internationally, market conditions abroad are likely to affect the price of leather in the United States. Outbreaks of mad cow and hoof-and-mouth disease (or foot-and-mouth disease) in certain parts of the world can influence the price of leather we purchase. As such an occurrence is beyond the control of the Company, we cannot predict when and to what extent we could be affected in the future. Aside from increasing purchases when we anticipate price increases (or possibly delaying purchases if we foresee price declines), we do not attempt to hedge our inventory costs.

Hours of operations vary by location, but generally range from 8:00 am to 6:00 pm Monday through Friday, and from 9:00 am to 4:00 pm on Saturdays. The distribution centers maintain uniform prices, except where lower prices are necessary to meet local competition.

Most of our competition comes in the form of small, independently-owned retailers who in most cases are also our customers. We estimate that there are several hundred of these small independent stores in the United States and Canada. We compete on price, availability of merchandise, and delivery time. While there is competition in connection with certain products, to our knowledge there is no direct competition affecting our entire product line. Our size relative to most competitors creates an advantage in our ability to stock a full range of products as well as in volume purchasing.

The Leather Factory distribution centers receive the majority of their inventory from our central warehouse located in Fort Worth, Texas, although occasionally, merchandise is shipped directly from the

vendor. Inventory is shipped to the distribution centers from our central warehouse once a week to meet customer demand without sacrificing inventory turns. Customer orders are filled as received, and we do not have backlogs.

We attempt to maintain the optimum number of items in our product line to minimize out-of-stock situations against carrying costs involved with such an inventory level. We generally maintain higher inventories of certain imported items to ensure a continuous supply. The number of products offered changes every year due to the introduction of new items and the discontinuance of others. We carry approximately 2,750 items in the current lines of leather and leather-related merchandise. All items are offered in both the Leather Factory distribution centers and the Tandy Leather retail stores.

Leather Factory's expansion across the United States has been fairly consistent since we purchased the original six distribution centers in 1985. The newest center opened in August 2002, bringing the number of distribution centers to thirty. While we do not believe there is a significant and immediate opportunity for expansion of the Leather Factory distribution system in terms of opening additional locations, we do believe expansion could be achieved by acquiring companies in related areas/markets which offer synergistic aspects based on the local markets and/or the product lines of the businesses.

The Common Stock of the Company is traded on the American Stock Exchange using the symbol TLF. The high and low prices for each calendar quarter during the last two fiscal years are as follows:





RETAIL LEATHERCRAFT

Our Retail Leathercraft division consists of a growing chain of retail stores operating under the name, Tandy Leather. Tandy Leather Company, established in 1919 as Hinkley-Tandy Leather Company, is the oldest and best-known supplier of leather and related supplies used in the leathercraft industry. We offer a product line of quality tools, leather, accessories, kits and teaching materials.

The Tandy Leather retail chain currently has 42 stores (as of March 1, 2005) located in 27 states and three Canadian provinces with plans to reach 100 stores as opportunities arise over the next several years. The stores range in size from 1,200 square feet to 3,800 square feet, with the average size of a store being approximately 2,000 square feet. The type of premises utilized for a Tandy Leather store is generally an older strip shopping center located at well-known crossroads, making the store easy to find.

Tandy Leather has long been known for its reputation in the leathercraft industry and its commitment to the furthering of the craft through education and customer development. We are committed to this strategy as evidenced by our re-establishment of the retail store chain throughout the United States following our acquisition of the assets of Tandy Leather in 2000. We continue to broaden our customer base by working with various youth organizations and institutions where people are introduced to leathercraft, as well as hosting classes in the stores.

The retail stores serve walk-in, mail and phone order customers as well as orders generated from its website, www.tandyleather.com. Tandy Leather stores are staffed by knowledgeable sales people whose compensation is based, in part, upon the profitability of their store. Sales by Tandy Leather are driven through the efforts of the store staff, trade shows, and our direct mail and e-mail marketing program.

Individual retail customers are our largest customer group, representing more than 70% of Tandy Leather's 2004 sales. Youth groups, summer camps, schools, and a limited number of wholesale customers complete our customer base. Like Leather Factory, Tandy fills orders as they are received, and there is no order backlog. Tandy maintains reasonable amounts of inventory to fill these orders. Tandy Leather's retail store operations historically generate slightly more sales in the 4th quarter of each year (30-35%) while the other three quarters remain fairly even.

We carry a wide assortment of products including leather, hand tools, kits, dyes & finishes, and stamping tools.

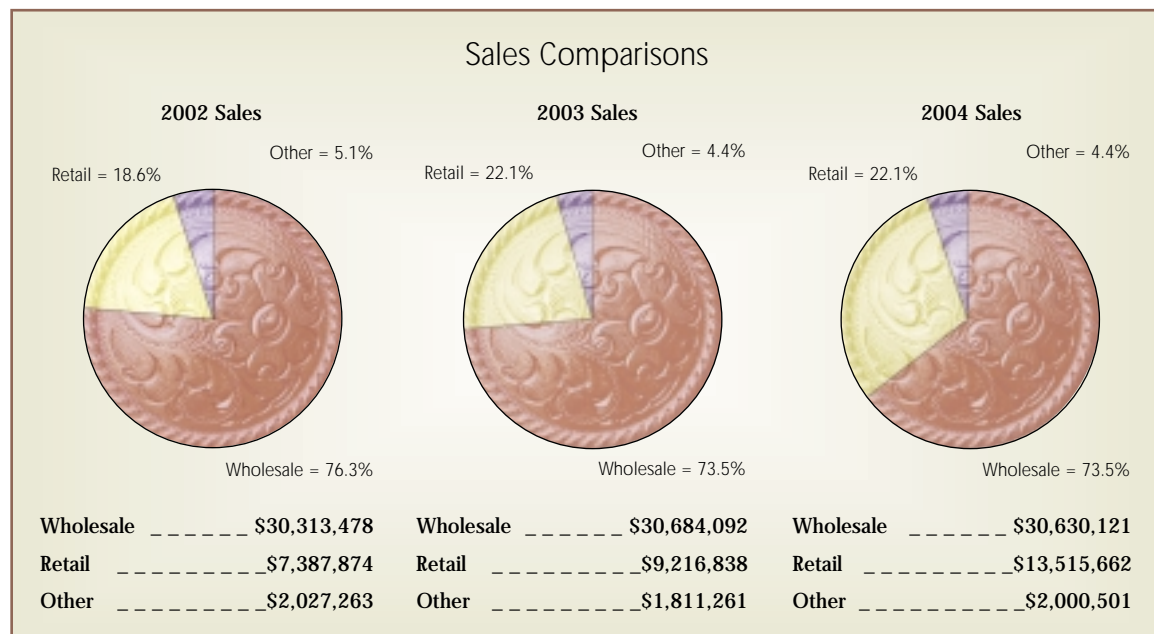
As indicated above, the products sold in our Tandy Leather stores are also sold in our Leather Factory wholesale centers. Therefore, the discussion above regarding products for the Wholesale Leathercraft division also applies to the Retail Leathercraft division. Sales at Tandy Leather stores are generally cash transactions or through national credit cards. We also sell on open account to selected wholesale customers including schools and other institutions and small retailers. Our terms are generally net 30 days. Like Leather Factory, Tandy Leather has an unconditional return policy.

Hours of operations vary by location, but generally range from 9:00 am to 6:00 pm Monday through Friday, and from 9:00 am to 4:00 pm on Saturdays. In addition, most of the stores stay open late one night a week for leathercrafting classes taught in the stores. Selling prices are uniform throughout the Tandy Leather store system.

Our competitors are generally small local craft stores that carry a limited line of leathercraft products. Several national retail chains that are customers of The Leather Factory also carry leathercraft products on a very small scale relative to their overall product line. To our knowledge, our retail store chain is the only one in existence solely specializing in leathercraft.

The Tandy Leather stores receive their inventory from the Leather Factory central warehouse located in Fort Worth, Texas. The stores generally restock their inventory once a week with a shipment from the warehouse.

We intend to expand the Tandy Leather retail store chain to 100 stores throughout the United States at an average rate of approximately twelve stores per year. Fourteen stores were opened in 2002; twelve stores were opened in 2003; sixteen were opened in 2004 (including four in Canada). Seven of the 42 stores opened through 2004 were independent leathercraft stores that we acquired. Separately, these acquisitions are not material. The other thirty-five stores have been de novo stores opened by us. Management's plans for 2005 are to open 6-8 retail stores in the United States to keep us on pace of averaging twelve new stores per year. Two new stores opened in the first three months of 2005.





OTHER

Our wholly-owned subsidiary, Roberts, Cushman & Co., Inc., rounds out our consolidated operations. However, this subsidiary is immaterial to our company as a whole and does not fit our business model for the future. We are assessing our long term strategic options for this segment. Roberts, Cushman, founded in 1856, produces made-to-order trimmings for the headwear industry.

Roberts, Cushman has long been considered one of the leaders in the field of headwear trimmings. It designs and manufactures exclusive trimmings for all types of hats. Trims are sold to hat manufacturers directly. We do not employ an outside sales force. Instead, customers visit our facilities in New York and, with an on-site designer, incorporate their ideas into a customized product. The customer is provided samples or photographs of each design before they leave the premises. These samples can then be used as a sales tool to obtain hat orders from their customers. This “design-on-site” process is unique in the industry.

We design and manufacture trims for over 75 of the headwear manufacturers worldwide, supplying customized trims, ribbons, buckle sets, name pins, feathers, and other items. Our success in developing and maintaining long-standing relationships with our customers is due primarily to our ability to deliver quality products in a timely manner. Roberts, Cushman’s sales generally do not reflect significant seasonal patterns.

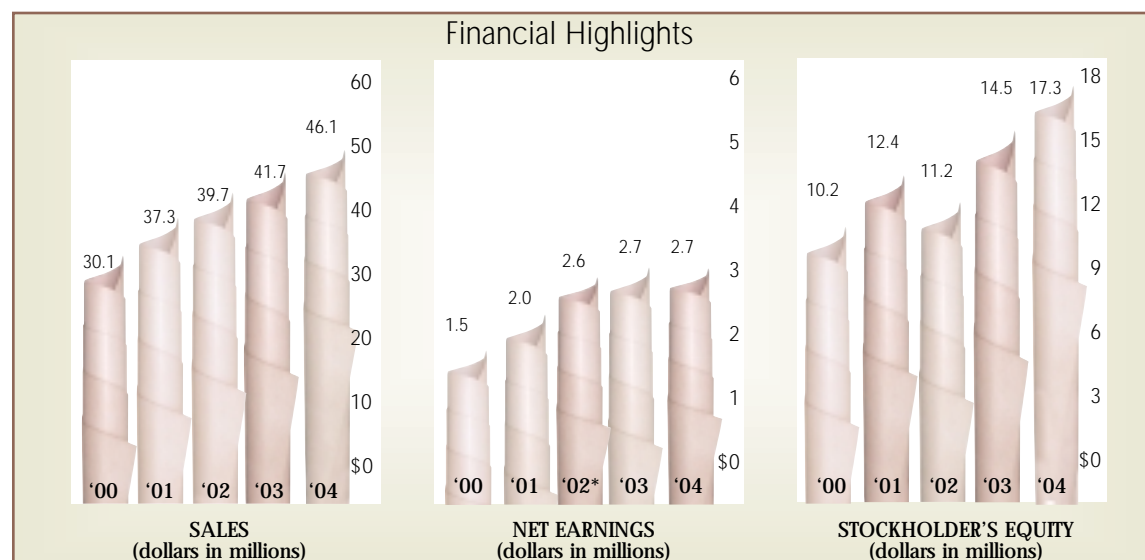
Our hat bands are generally produced from leather, ribbon, or woven fabrics, depending on the style of hat. They are created by cutting leather and/or other materials into strips, and then enhancing the trim by attaching conchos and/or three-piece buckle sets, braiding with other materials, and finishing the end or borders by stitching or by lacing with leather lace. We also supply custom-designed buckles and conchos, feathers for dress hats, and name pins, separate from hat bands. Roberts, Cushman purchases components from over 25 vendors, located predominately in the United States. Products are sold on terms that generally range from net 30 to net 90 days. Because our products are custom-designed, we do not accept product returns, except in the case of defective merchandise.

Cushman has been successful providing a very specific product line directly to headwear manufacturers. Given the current industry conditions, we do not believe there is much potential for expansion, other than to capture additional market share.

FINANCIAL HIGHLIGHTS

	Years Ended December 31,				
	2004	2003	2002	2001	2000
Net sales	\$46,146,284	\$41,712,191	\$39,728,615	\$37,279,262	\$30,095,264
Cost of sales	20,706,239	19,020,292	18,393,914	17,934,935	15,147,547
Gross profit	25,440,045	22,691,899	21,334,701	19,344,327	14,947,717
Operating expenses	21,181,599	18,594,240	17,202,927	15,442,359	11,702,633
Operating income	4,258,446	4,097,659	4,131,774	3,901,968	3,245,084
Operating income per share - basic	\$0.40	\$0.40	\$0.41	\$0.39	\$0.33
Operating income per shares - diluted	\$0.39	\$0.38	\$0.38	\$0.37	\$0.32
Other expense	44,800	125,169	311,917	533,482	653,779
Income (loss) before income taxes	4,213,646	3,972,490	3,819,857	3,368,486	2,591,305
Income tax provision (benefit)	1,559,605	1,232,116	1,224,868	1,362,053	1,049,985
Income (loss) before cumulative effect of change in accounting principle	2,654,041	2,740,374	2,594,989	2,006,433	1,541,320
Cumulative effect of change in accounting principle	-	-	(4,008,831)	-	-
Net income (loss)	\$2,654,041	\$2,740,374	\$(1,413,842)	\$2,006,433	\$1,541,320
Earnings (loss) per share	\$0.25	\$0.27	\$(0.14)	\$0.20	\$0.16
Earnings (loss) per share-assuming dilution	\$0.24	\$0.25	\$(0.13)	\$0.19	\$0.15
Weighted average common shares outstanding for:					
Basic EPS	10,543,994	10,323,549	10,063,581	9,976,181	9,875,606
Diluted EPS	10,957,518	10,861,305	10,761,670	10,449,306	10,182,803

	As of December 31,				
	2004	2003	2002	2001	2000
Total assets	\$22,167,163	\$19,058,406	\$19,675,602	\$19,548,323	\$19,686,079
Notes payable, capital lease obligations and current maturities of long term debt	134,067	1,134	4,218,968	4,527,904	5,759,626
Notes payable, capital lease obligations and long-term debt, net of current maturities	750,944	1,792,984	2,256	7,691	13,025
Total Stockholders' Equity	\$17,310,233	\$14,509,493	\$11,170,062	\$12,423,671	\$10,295,637



*before cumulative effect of change in accounting principle



G R O W T H



We grow our business by opening new locations and by increasing our customer base in existing locations.

DISTRIBUTION



The wholesale leathercraft operation distributes its broad product line both in the United States and internationally.

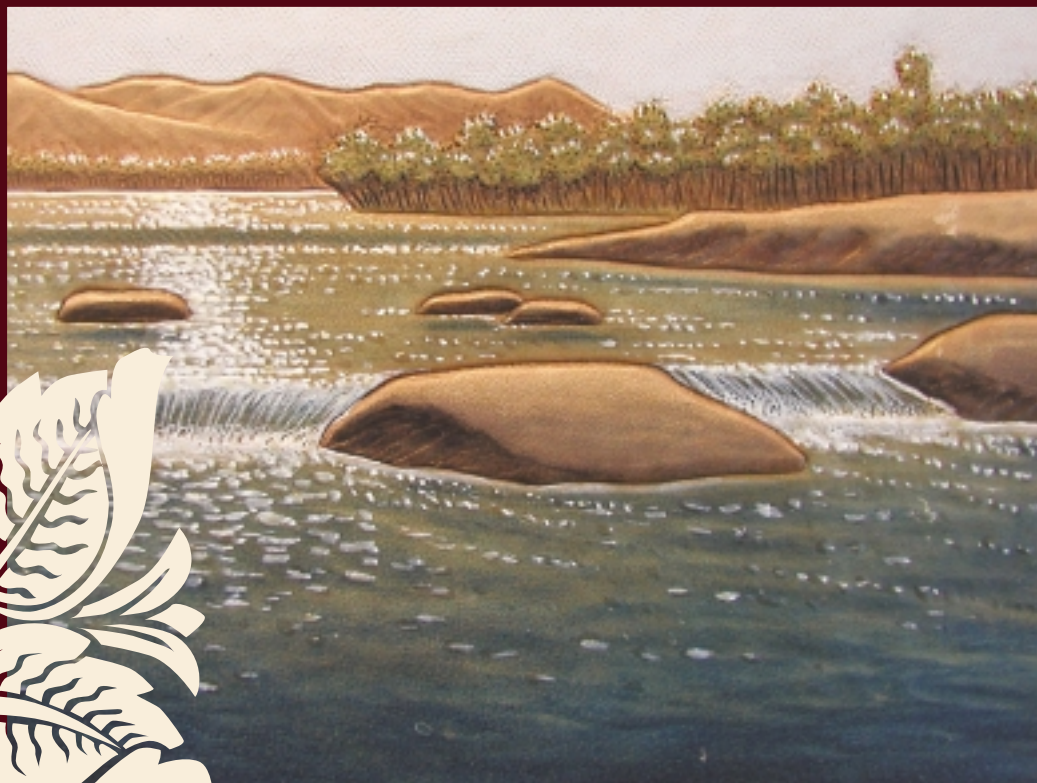


DEVELOPMENT



Our Research and Development division advances new products as well as revives classic, old favorites.

DIVERSITY



By diversifying our company into both retail and wholesale markets, we feel we are positioned well for the future.



ACQUISITION



Following our acquisition of Tandy Leather Company in 2000, we purchased Heritan Ltd., of Canada, in December 2004.

A C C E S S



Our products are easily available, both from brick and mortar locations and over the internet.



MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

We intend for the following discussion to provide you with information that will assist you in understanding our financial statements, the changes in certain key items in those financial statements from year to year, and the primary factors that accounted for those changes, as well as how certain accounting principles affect our financial statements. This discussion also provides information about the financial results of the various segments of our business so you may better understand how those segments and their results affect our financial condition and results of operations as a whole. Finally, we have identified and discussed trends known to management that we believe are likely to have a material effect.

This discussion should be read in conjunction with our financial statements as of December 31, 2004 and 2003 and the two years then ended and the notes accompanying those financial statements. You are also urged to consider the information under the caption "Summary of Critical Accounting Policies."

Summary

We operate in three segments. First, Wholesale Leathercraft, consisting of our Leather Factory warehouse distribution centers and our national account group, is the largest source of revenues (\$30.6 million in 2004). This division has generally offered steady but modest increases in sales. Sales in 2004 were flat compared to sales in 2003, falling short of our target of annual sales growth of 2% to 4%. The decrease in sales to national accounts in 2004 accounted for the shortfall. Excluding national account sales, the distribution centers produced a sales gain of 4.5% for 2004.

Since acquiring its assets in 2000, we have focused on re-establishing Tandy Leather as the operator of retail leathercraft stores. These retail stores comprise our second segment, Retail Leathercraft. Because of growth here, this segment has experienced the greatest increases in sales (\$13.5 million in 2004, up from \$9.2 million in 2003). Our business plan calls for opening an average of 12 stores annually as we work toward a goal of 100 stores from 42 stores at the end of 2004.

Our third segment is Roberts, Cushman, a manufacturer of trimmings for headwear. Its operations are not material to us. In 2002, we wrote off the goodwill related to our investment in Roberts, Cushman in connection with an accounting change.

On a consolidated basis, a key indicator of costs, gross margin as a percent of total net sales, increased in 2003 and again in 2004, reflecting a number of factors including more retail sales with higher profit margins. However, opening additional Tandy Leather stores, more dollars spent on employee benefits, and new costs associated with Sarbanes-Oxley compliance in 2004 resulted in a 1.3% increase in operating expenses as a percent of total net sales in 2004. Operating expenses were also up 1.3% as a percentage of total net sales in 2003 when compared with 2002 as a result of opening additional Tandy Leather stores and more dollars spent on advertising.

We reported consolidated net income for 2004 of \$2.7 million. Consolidated net income for 2003 was also \$2.7 million. In 2002, we reported a consolidated net loss of \$1.4 million due to an accounting change. We have used our cash flow to fund our operations, to fund the opening of new Tandy Leather stores and to reduce our bank debt. In 2004, we reduced our bank debt by \$1.3 million, and, at the end of 2004, our stockholders' equity had increased to \$17.3 million from \$14.5 million the previous year.

Comparing the December 31, 2004 balance sheet with the prior year's, we increased our investments in inventory (\$12.7 million from \$11.1 million) and accounts receivable (\$2.0 million from \$1.8 million), while total cash increased to \$2.6 million from \$1.7 million. In addition to cash on hand, we have a \$3 million bank line of credit, of which \$505,000 was drawn on December 31, 2004.

Net Sales

Net sales for the three years ended December 31, 2004 were as follows:

Year	Wholesale Leathercraft	Retail Leathercraft	Other	Total Company	Total Company Increase from Prior Year
2004	\$30,630,121	\$13,515,662	\$2,000,501	\$46,146,284	10.6%
2003	30,684,092	9,216,838	1,811,261	41,712,191	5.0%
2002	30,313,478	7,387,874	2,027,263	39,728,615	6.6%

Our net sales grew by 10.6% in 2004 when compared with 2003 and 5.0% in 2003 when compared with 2002. These annual increases resulted primarily from our retail leathercraft expansion program.

Costs and Expenses

In general, our gross profit as a percentage of sales (our gross margin) fluctuates based on the mix of customers we serve, the mix of product we sell, and our ability to source product globally. Our negotiations with suppliers for lower pricing is an on-going process and we have varying degrees of success in those endeavors. Sales to retail customers tend to produce higher gross margins than sales to wholesale customers due to the difference in pricing levels. Therefore, as retail sales increase in the overall sales mix, higher gross margins tend to follow. Finally, there is significant fluctuation in gross margins between the various merchandise categories we offer. As a result, our gross margins can vary depending on the mix of products sold during any given time period.

For 2004, our cost of sales decreased as a percentage of total net sales when compared to 2003, resulting in an overall increase of 0.7% in the Company's gross margin from 54.4% in 2003 to 55.1% in 2004.

Similarly, our total cost of sales as a percentage of our total net sales had decreased for 2003 when compared to 2002 resulting in an overall increase in gross margin of 0.7% from 53.7% for 2002 to 54.4% in 2003. These increases in gross margin were primarily due to increased retail sales over the three years.

Our gross margins for the three years ended December 31, 2004 were as follows:

Year	Wholesale Leathercraft	Retail Leathercraft	Cushman	Total Company
2004	54.10%	61.98%	30.31%	55.13%
2003	53.23%	62.98%	30.62%	54.40%
2002	53.56%	59.49%	34.64%	53.70%

Our operating expenses increased 1.3% as a percentage of total net sales to 45.9% in 2004 when compared with 44.6% in 2003. This increase was primarily due to operating costs associated with the twelve Tandy stores opened in 2004 (an increase of \$650,000), bonuses awarded to corporate and operational management (\$400,000) the cost of employee health care (an increase of \$500,000), an increase in advertising expenses (\$200,000), and expenses associated with compliance with Section 404 of the Sarbanes-Oxley Act (\$200,000). We believe that our advertising efforts - particularly our direct mail campaigns - generate sales. As we expand into new markets, the number of customers and potential customers increases resulting in an increase in the number of direct mail pieces produced and distributed. While we monitor our advertising costs with great scrutiny, management believes that the trend of increased advertising and marketing costs could continue for at least the near future.



We have completed the initial phase of design and documentation in our efforts to comply with Section 404 of the Sarbanes-Oxley Act with the assistance of outside consultants. While additional and on-going testing of our control processes is necessary, we hope to complete the majority of that work without the need for significant outside assistance. Management is analyzing the status of this project to determine if we will be able to accomplish this work satisfactorily with internal staff. If not, we will incur additional costs in 2005.

For 2003, operating expenses increased 1.3% as a percentage of total net sales to 44.6% in 2003 when compared with 2002. This increase was primarily due to operating costs (rents, utilities, telephones, etc.) associated with the twelve Tandy stores opened in 2003 (an increase of \$700,000) as well as an increase in advertising expenses (an increase of \$500,000) and investor relation expenses (an increase of \$200,000).

Other Expenses (net)

Other expenses (net), which consists primarily of interest expense and currency exchange gain and loss, was \$45,000 in 2004 compared to \$125,000 in 2003, a decrease of approximately 64%. This decrease is attributable to the interest paid on our outstanding debt.

In 2003, other expenses (net) were \$125,000 in 2003 compared to \$312,000 in 2002, a decrease of approximately 60%. Our interest expense continues to decrease due to the reduction in our outstanding bank debt. The currency exchange gain and loss, resulting from our Canadian operation, was a gain of \$102,000 in 2003 compared to a gain of \$10,000 in 2002.

Net Income

During 2004, we earned net income of \$2.65 million, a slight decrease from our net income of \$2.74 million for 2003. The overall improvement in gross margin and a reduction in interest and other expenses contributed positively to our net income while increased operating expenses and income tax expense in 2004 offset that improvement.

During 2003, we earned net income of \$2.74 million, a substantial increase over our net loss of \$1.4 million for 2002. (As discussed in previous filings, a new accounting pronouncement required us to record a \$4.0 million charge against earnings as a result of the write-off of the goodwill of Roberts, Cushman in 2002, resulting in a net loss. This charge was reported as a cumulative effect of a change in accounting principle. Net income before the change was \$2.6 million.) As a result of the increase in our overall gross margin and a reduction in interest and other expenses, our profits in 2003 grew at a rate faster than sales. Partially offsetting gross margin and other expense improvements were increased operating expenses in 2003 as discussed above.

Re-categorization of operating divisions

Until the fourth quarter of 2004, we provided division or segment information on a legal entity basis. More specifically, the Leather Factory segment consisted of 27 U.S.-based warehouse distribution centers and 3 Canadian-based warehouse distribution centers which were owned and operated by the legal entity of the same name. The Tandy Leather segment consisted of the expanding U.S.-based retail store chain which was owned and operated by Tandy Leather Company. With the opening of our Calgary store in October 2004, which is owned by The Leather Factory but operated as a Tandy Leather retail store, management has determined that it is more useful to provide segment financial information based upon wholesale and retail operating divisions rather than on a legal entity basis. The acquisition of the three Canadian retail stores of Heritan Ltd. in December 2004, which are owned by the Leather Factory but operated as Tandy Leather stores, further strengthened our decision to make a change in the way we report divisional, or segment, information.

If we continued entity reporting, the segments would be as follows:

<u>As of 9/30/04:</u>	<u>As of 12/31/04:</u>
Leather Factory: 27 locations in U.S. 3 locations in Canada	Leather Factory: 27 locations in U.S. 7 locations in Canada**
Tandy Leather: 36 retail stores in U.S.	Tandy Leather: 38 retail stores in U.S.

**3 warehouse distribution centers and 4 retail stores

Changing reporting to a wholesale and retail division reporting, the segments are as follows:

<u>As of 9/30/04:</u>	<u>As of 12/31/04:</u>
Wholesale: 27 locations in U.S. 3 locations in Canada	Wholesale: 27 locations in U.S. 3 locations in Canada
Retail: 36 retail stores in U.S. 4 retail stores in Canada	Retail: 38 retail stores in U.S.

As indicated in the tables above, this change in divisional reporting does not affect prior periods for comparison purposes as there were no retail stores in the Leather Factory legal entity until October 2004.

Wholesale Leathercraft (formerly referred to as "Leather Factory Segment")

Year	Net Sales Incr (Decr) from Prior Yr	Operating Income	Oper Inc Incr (Decr) from Prior Yr	Oper Inc as a % of Sales
2004	(0.2)%	\$3,031,316	(13.0)%	9.5%
2003	1.2%	\$3,462,457	(7.5)%	11.3%
2002	5.6%	\$3,742,844	0.6%	12.3%

Wholesale Leathercraft, consisting of 30 warehouse distribution centers, accounted for 66.4% of total Company net sales in 2004, which compares to 73.5% in 2003 and 76.3% in 2002. The decrease in this division's contribution to our total net sales is the result of the growth in Retail Leathercraft and we expect this trend to continue.

The net sales decrease in 2004 resulted from a decrease in national account sales offset by gains to our wholesale and small manufacturing customer groups. Our sales mix by customer group was as follows:

Customer Group	2004	2003	2002
Retail	23%	23%	20%
Institution	7%	8%	8%
Wholesale	47%	42%	44%
National Accounts	16%	20%	21%
Manufacturers	7%	7%	7%
	<u>100%</u>	<u>100%</u>	<u>100%</u>



The 2004 decrease in operating income as a percentage of divisional sales resulted from an increase of 2.04% in operating expenses (as a percentage of sales) compared with 2003, partially offset by an increase in gross margin (as a percentage of sales) of 0.59%. The operating expense increase as a percent of sales in 2004 was higher than 2003 due to bonuses awarded to corporate and operational management (\$300,000) for 2004 and the cost of our employee health benefits (an increase of \$300,000). In addition, we spent \$170,000 with outside consultants on our Sarbanes-Oxley 404 project. Being the largest division, Wholesale Leathercraft bears the majority of the pro rata allocation of corporate expenses.

The 2003 decrease in operating income as a percentage of sales resulted from a 0.33% decrease in gross margin (as a percentage of sales) and an increase of 0.72% in operating expenses (as a percentage of sales) compared with 2002. The gross margin decline was driven primarily by an increase in the quantities of leather sold during the year. Given that leather is our lowest gross margin item, an increase in leather sales, all other factors being equal, will result in a lower overall gross margin. Our freight costs (shipping merchandise from vendors to us) were up in 2003 as well due an increase in the number of air shipments versus ocean shipments. The operating expense increase as a percent of sales in 2003 was higher than 2002. Advertising and marketing costs are a significant expense in our operation as we believe there is a direct correlation between how much we advertise and how much product we sell. Our increase in investor outreach programs in 2003 also contributed to the decline in operating income this year.

Retail Leathercraft (formerly referred to as "Tandy Leather Segment")

Year	Net Sales Incr (Decr) from Prior Yr	Operating Income	Oper Inc Incr (Decr) from Prior Yr	Oper Inc as a % of Sales
2004	46.6%	\$1,210,566	37.3%	8.9%
2003	24.7%	\$604,291	62.7%	6.6%
2002	11.8%	\$371,372	31.7%	5.0%

Reflecting the growth previously discussed, Retail Leathercraft accounted for 29.3% of our total net sales in 2004, up from 22.1% in 2003 and 18.6% in 2002.

Growth in net sales for Retail Leathercraft division in 2004 and 2003 resulted primarily from our expansion program. Expansion during 2004 and 2003 consisted of the opening of 16 and 12 new stores, respectively.

Our sales mix by customer group was as follows:

Customer Group	2004	2003	2002
Retail	72%	72%	65%
Institution	6%	6%	12%
Wholesale	21%	21%	23%
National Accounts	0%	0%	0%
Manufacturers	1%	1%	0%
	<u>100%</u>	<u>100%</u>	<u>100%</u>

Operating income as a percentage of sales increased to 8.9% for 2004 compared to 6.6% for 2003. Gross margin decreased from 63.0% in 2003 to 61.8% in 2004 due primarily to limitations in increasing selling prices to match cost increases. Selling prices are set at the time the product catalog is produced. As a result, it is difficult to implement price increases to customers until we distribute a new catalog. Historically, we distribute our new catalog at the beginning of each calendar year and did so in January 2004. However, due to the cost increases in metals, fuel, and other items this year and the need to pass on these increases to customers, we accelerated that schedule and distributed our 2005 catalog on November 1, 2004. Operating expenses as a percent of sales in 2004 decreased by 3.61%, from 56.4% for 2003 to 52.8% for 2004 as sales and gross margin grew at a faster pace than that of operating expenses.

Operating income as a percentage of sales increased in 2003 when compared to 2002. Segment gross margin increased from 59.5% in 2002 to 63.0% in 2003 due to increased retail sales and more efficient purchasing of product from vendors. Segment operating expenses as a percent of sales increased by 1.95% in 2003. Expanded advertising initiatives and rent for store space accounted for the operating expense increase, offset partially by a decrease in costs to ship merchandise to customers. The decrease in shipping is a result of the store expansion as more sales occur in the stores as compared to ordering via mail, phone or the Internet.

We intend to continue the expansion of Tandy Leather's retail store chain in 2005 by opening a total of 6-8 new stores throughout the year. As of March 15, 2005, we have opened two new stores this year: Van Nuys, CA and Phoenix, AZ. We remain committed to a conservative expansion plan for this division that minimizes risks to our profits and maintains financial stability.

Others (Roberts, Cushman)

Year	Net Sales Incr (Decr) from Prior Yr	Operating Income	Oper Inc Incr (Decr) from Prior Yr	Oper Inc as a % of Sales
2004	10.4%	\$34,565	11.8%	1.7%
2003	(10.6)%	\$30,911	76.1%	1.7%
2002	3.3%	\$17,558	117.6%	0.9%

The Roberts, Cushman operation accounted for 4.3% of our total sales in 2004 compared with 4.4% and 5.1% in 2003 and 2002, respectively.

For 2004, sales were up 10.4% while gross profit margins decreased slightly from 30.6% to 30.3%. Operating income increased from \$31,000 in 2003 to \$35,000 for 2004. Sales grew faster than operating expenses which accounted for the improvement in operating income.

The 2003 decrease in Roberts, Cushman's net sales resulted from the continued slowdown in the headwear industry overall. Several of our customers (hat manufacturers) are on shortened work weeks due to the decline in orders. Segment gross margin as a percentage of sales decreased 4.0% from 2002. However, operating income improved modestly.

Roberts, Cushman's sales and profits are immaterial to our company as a whole.

Financial Condition

At December 31, 2003, our net total assets were \$19.1 million. We held \$11.1 million of inventory and \$1.9 million of property and equipment. Our cash totaled \$1.7 million and our receivables were \$1.8 million. Current liabilities were \$2.5 million, while our long-term debt was \$1.8 million. Total stockholders' equity at the end of 2003 had increased to \$14.5 million, primarily as a result of the \$2.7 million net income recorded in 2003. The increase in cash from 2002 to 2003 was due primarily to the increase in cash sales at Tandy Leather (as opposed to sales on open account), as well as the decrease in cash tied up in inventory owned at the end of 2003 compared to 2002. While we have no required payment schedule prior to maturity on our revolving line of credit, management strives to apply as much available cash as possible to our outstanding debt balance. Generally speaking, the majority of cash on our balance sheet is funds held in depository accounts with various banks awaiting collectibility for transfer either to our operating account or to the line of credit.

At December 31, 2004, we held \$2.6 million of cash, \$12.7 million of inventory, accounts receivable of \$2.0 million, and \$1.9 million of property and equipment. Goodwill and other intangibles (net of amortization and depreciation) were \$743,000 and \$438,000, respectively. We also own a leather artwork



collection, most of which was created by Al Stohlman, a legendary leathercrafter, valued on our balance sheet at \$250,000. Net total assets were \$22.2 million. Current liabilities were \$3.8 million (including \$134,000 of current maturities of long-term debt), while long-term debt was \$751,000. Total stockholders' equity at the end of 2004 was \$17.3 million.

Specific ratios on a consolidated basis at the end of each year ended December 31 were as follows:

		<u>2004</u>	<u>2003</u>	<u>2002</u>
Solvency Ratios:				
Quick Ratio	Cash+Accts Rec/Total Current Liabilities	1.21	1.40	0.31
Current Ratio	Total Current Assets/Total Current Liabilities	4.79	6.16	1.94
Current Liabilities to Net Worth	Total Current Liabilities/Net Worth	0.22	0.17	0.74
Current Liabilities to Inventory	Total Current Liabilities/Inventory	0.30	0.23	0.66
Total Liabilities to Net Worth	Total Liabilities/Net Worth	0.28	0.31	0.76
Fixed Assets to Net Worth	Fixed Assets/Net Worth	0.11	0.13	0.18
Efficiency Ratios:				
Collection Period (Days Outstanding)	Accounts Receivable/Credit Sales x 365	43.57	41.45	43.54
Inventory Turnover	Sales/Average Inventory	3.87	3.51	3.65
Assets to Sales	Total Assets/Sales	0.48	0.46	0.49
Sales to Net Working Capital	Sales/Current Assets - Current Liabilities	3.21	3.18	5.06
Accounts Payable to Sales	Accounts Payable/Sales	0.04	0.04	0.04
Profitability Ratios:				
Return on Sales (Profit Margin)	Net Profit After Taxes/Sales	0.06	0.07	0.07
Return on Assets	Net Profit After Taxes/Total Assets	0.12	0.14	0.13
Return on Net Worth (Return on Equity)	Net Profit After Taxes/Net Worth	0.15	0.19	0.23

Capital Resources and Liquidity

On November 1, 2004, we entered into a Credit Agreement with Bank One, N.A., which replaced our line of credit with Wells Fargo Bank. The current facility matures in October 2007 and is secured by our accounts receivable and inventory. We opted to reduce the maximum amount that may be borrowed under this line of credit to \$3.0 million in order to reduce the fees required on the un-borrowed portion of the line.

On November 3, 2003, we entered into a Credit and Security Agreement with Wells Fargo Bank, N.A., which replaced a line of credit with another bank affiliated with Wells Fargo. The Wells Fargo current facility would have matured in November 2005 and was secured by all assets of the Company.

We are currently in compliance with all covenants and conditions contained in the Bank One Credit Agreement and have no reason to believe that we will not continue to operate in compliance with the provisions of these financing arrangements. The principal terms and conditions of the Credit Agreement are described in further detail in Note 4 to the Consolidated Financial Statements, Notes Payable and Long-Term Debt.

We borrow and repay funds under revolving credit terms as needed. Principal balances at the end of each quarter are shown below:

<u>4th Qtr. '03</u>	<u>1st Qtr. '04</u>	<u>2nd Qtr. '04</u>	<u>3rd Qtr. '04</u>	<u>4th Qtr. '04</u>
(Wells Fargo)	(Wells Fargo)	(Wells Fargo)	(Wells Fargo)	(Bank One)
\$1,792,984	\$1,267,984	\$1,100,000	\$1,013,565	\$505,154

Total bank indebtedness at the end of 2003 and 2004 are shown below:

	<u>December 31, 2003</u>		<u>December 31, 2004</u>	
	<u>Principal</u>	<u>Accrued Interest</u>	<u>Principal</u>	<u>Accrued Interest</u>
Revolving Line	\$1,792,984	\$6,374	\$505,154	\$6,219

Reflecting the reduction of bank indebtedness during the period, our financing activities for 2004, 2003 and 2002 had net cash requirements (deficits) of \$1.2 million, \$1.3 million and \$214,000, respectively.

The primary source of liquidity and capital resources during 2004 was cash flow provided by operating activities. Cash flow from operations for 2004 was \$2.9 million, the largest portion generated from net income. Cash flow from operations in 2003 was \$3.3 million, generated from net income and the reduction of inventory. Cash flow from operations in 2002 was \$1.4 million.

Consolidated accounts receivable increased to \$2.0 million at December 31, 2004 compared to \$1.8 million at December 31, 2003. Average days to collect accounts slowed slightly from 41.46 days in 2003 to 43.57 days in 2004 on a consolidated basis.

Inventory increased from \$11.1 million at the end of 2003 to \$12.7 million at December 31, 2004. We expect our inventory to slowly trend upward as we continue our expansion of the Tandy Leather store chain. However, we are pleased with our investment in inventory at the end of 2004 as it was within 3% of our internal targets of optimum inventory levels. We attempt to manage our inventory levels to avoid tying up excessive capital.

Consolidated inventory turned 3.87 times during 2004, a slight improvement from the 3.51 times turned in 2003. We compute our inventory turnover rates as sales divided by average inventory.

By operating division, inventory turns are as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Wholesale Leathercraft	3.11	2.97	3.20
Retail Leathercraft	8.88	8.69	8.10
Wholesale Leathercraft distribution centers only	8.69	8.26	7.96

Retail Leathercraft inventory turns are significantly higher than that of the Wholesale Leathercraft because its inventory consists only of the inventory at the stores. The Tandy Leather stores have no warehouse (backstock) inventory to include in the turnover computation as the stores get their product from the Leather Factory central warehouse. Leather Factory's turns are expected to be slower because the central warehouse inventory supports the stores and distribution centers.

Accounts payable increased to \$1.9 million at the end of 2004 compared to \$1.6 million at the end of 2003 due primarily to the increase in inventory purchases.

As discussed above, the largest use of operating cash in 2004 was for debt reduction and inventory purchases. Capital expenditures totaled \$370,000 and \$360,000 for the years ended December 31, 2004 and 2003, respectively. The 2004 capital expenditures consisted of fixtures and equipment for the new Tandy Leather retail stores (\$155,000), the remodel of the accounting offices located at our corporate complex (\$77,000), and miscellaneous computer and other equipment (\$124,000). Capital expenditures in 2003 occurred primarily due to the expansion of the Tandy Leather store chain and the construction of the Stohman Leather Museum and Gallery located at our Fort Worth corporate complex. Also in 2004, we made expenditures of \$557,000 to purchase our primary Canadian competitor as well as three U.S.-based independent leathercraft stores for conversion to Tandy Leather stores. Since we intend to continue opening or acquiring new Tandy Leather stores, expenditures related to this expansion should continue



into 2005.

We believe that cash flow from operations will be adequate to fund our operations in 2005, while also funding expansion and debt reduction. At this time, management knows of no trends or demands, commitments events or uncertainties that will or are likely to materially affect our liquidity, capital resources or results of operations. In addition, we anticipate that this cash flow will enable us to meet the contractual obligations and commercial commitments. However, if cash flows should decrease or uses of cash increase, we may defer debt reduction or increase our borrowings on our line of credit as needed. We believe that, if desired, our present financial condition would permit us to increase the maximum amount that could be borrowed from lenders. Further, we could defer expansion plans if required by unanticipated drops in cash flow. In particular, because of the relatively small investment required by each new Tandy Leather store, we have flexibility in when we make most expansion expenditures.

Off-Balance Sheet Arrangements

We have not had any off-balance sheet arrangements during 2004, 2003 and 2002, and we do not currently have any such arrangements.

Contractual Obligations

The following table summarizes by years our contractual obligations and commercial commitments as of December 31, 2004 (not including related interest expense):

	Payments Due by Periods				
Long-Term Debt (1)	\$ 505,154	-	\$ 505,154	-	-
Capital Lease Obligations	379,857	\$ 134,067	134,067	\$ 11,723	-
Operating Leases (2)	6,237,775	2,107,214	3,933,668	196,893	-
Total Contractual Obligations	<u>\$ 7,122,786</u>	<u>\$ 2,241,281</u>	<u>\$ 4,572,889</u>	<u>\$ 308,616</u>	<u>-</u>


(1) Our loan from Bank One matures in October 2007. The loan's maturity can be accelerated in the event of a material adverse change or upon other occurrences described in the related credit agreement.

(2) These are our leased facilities.

In addition to the information shown in the table above, estimated annual interest to be paid on our line of credit with Bank One would be approximately \$30,000 per year, assuming an average interest rate of 5.00% and there was no repayment of principal until maturity. Management expects to continue repaying principal as our cash flow allows and as a result, would expect the interest to be paid to be lower than the \$30,000 estimate. The interest rate on the capital lease is 0%. Any imputed interest over the term of the lease would be insignificant.

Summary of Critical Accounting Policies

Management strives to report the financial results of the Company in a clear and understandable manner, although in some cases accounting and disclosure rules are complex and require us to use technical terminology. We follow generally accepted accounting principles in the U.S. in preparing our consolidated financial statements. These principles require us to make certain estimates and apply judgments that affect our financial position and results of operations. Management continually reviews its accounting policies, how they are applied and how they are reported and disclosed in our financial statements. Following is a summary of our more significant accounting policies and how they are applied in preparation of the financial statements.



Basis of Consolidation. We report our financial information on a consolidated basis. Therefore, unless there is an indication to the contrary, financial information is provided for the parent company, The Leather Factory, Inc., and its subsidiaries as a whole. Transactions between the parent company and any subsidiaries are eliminated for this purpose. We own all of the capital stock of our subsidiaries, and we do not have any subsidiaries that are not consolidated. None of our subsidiaries are “off balance sheet.”

Revenue Recognition. We recognize revenue for retail (over the counter) sales as transactions occur and other sales upon shipment of our products provided that there are no significant post-delivery obligations to the customer and collection is reasonably assured, which generally occurs upon shipment. Net sales represent gross sales less negotiated price allowances, product returns, and allowances for defective merchandise.

Allowance for Accounts Receivable. We reduce accounts receivable by an allowance for amounts that may become uncollectible in the future. This allowance is an estimate based primarily on our evaluation of the customer’s financial condition, past collection history, and the aging of the account. If the financial condition of any of our customers deteriorates, resulting in an impairment or inability to make payments, additional allowances may be required.

Inventory. Inventory is stated at the lower of cost or market and is accounted for on the “first in, first out” method. This means that sales of inventory treat the oldest item of identical inventory as being the first sold. In addition, we periodically reduce the value of our inventory for slow-moving or obsolete inventory. This reduction is based on management’s review of items on hand compared to their estimated future demand. If actual future demand is less favorable than those projected by management, additional write-downs may be necessary. Goods shipped to us are recorded as inventory owned by us when the risk of loss shifts to us from the supplier.

Goodwill. We have indicated previously that a change in the accounting rules necessitated a change in 2002 in how we report goodwill on our balance sheet. As a result, we incurred an impairment write-down in 2002 of our investment in Roberts, Cushman in the amount of \$4.0 million. The remaining goodwill on our balance sheet is analyzed by management periodically to determine the appropriateness of its carry value. As of December 31, 2004, management determined that the present value of the discounted estimated future cash flows of the stores associated with the goodwill is sufficient to support their respective goodwill balances. If actual results of these stores differ significantly from management’s projections, such difference could affect the present value calculation in the future resulting in an impairment of all or part of the goodwill currently carried on our balance sheet.



Forward-Looking Statements

“Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this report contain forward-looking statements of management. In general, these are predictions or suggestions of future events and statements or expectations of future occurrences. There are certain important risks that could cause results to differ materially from those anticipated by some of the forward-looking statements. Some, but not all, of the important risks which could cause actual results to differ materially from those suggested by the forward-looking statements include, among other things:

- We might fail to realize the anticipated benefits of the opening of Tandy Leather retail stores or we might be unable to obtain sufficient new locations on acceptable terms to meet our growth plans. Also, other retail initiatives might not be successful.
- Political considerations here and abroad could disrupt our sources of supplies from abroad or affect the prices we pay for goods.
- Continued involvement by the United States in war and other military operations in the Middle East and other areas abroad could disrupt international trade and affect the Company’s inventory sources.
- The recent slump in the economy in the United States, as well as abroad, may cause our sales to decrease or not to increase or adversely affect the prices charged for our products. Also, hostilities, terrorism or other events could worsen this condition.
- As a result of the on-going threat of terrorist attacks on the United States, consumer buying habits could change and decrease our sales.
- Livestock diseases such as mad cow could reduce the availability of hides and leathers or increase their cost. Also, the prices of hides and leathers fluctuate in normal times, and these fluctuations can affect the Company.
- If, for whatever reason, the costs of our raw materials and inventory increase, we may not be able to pass those costs on to our customers, particularly if the economy has not recovered from its downturn.
- Other factors could cause either fluctuations in buying patterns or possible negative trends in the craft and western retail markets. In addition, our customers may change their preferences to products other than ours, or they may not accept new products as we introduce them.
- Tax or interest rates might increase. In particular, interest rates are likely to increase at some point from their present low levels. These increases will increase our costs of borrowing funds as needed in our business.
- Any change in the commercial banking environment may affect us and our ability to borrow capital as needed.
- Other uncertainties, which are difficult to predict and many of which are beyond the control of the Company, may occur as well.

The Company does not intend to update forward-looking statements

Board of Directors and Executive Officers

INDEPENDENT DIRECTORS

T. Field Lange
President
Lange & Associates, PC
Fort Worth, Texas

Joseph R. Mannes
Managing Director
SAMCO Capital Markets
Dallas, Texas

H.W. Markwardt
Retired
Fort Worth, Texas

Michael A. Markwardt
Managing Partner
Legare, LP
Fort Worth, Texas

Michael A. Nery
Manager
Nery Capital Partners
Asheville, North Carolina

EXECUTIVE OFFICERS AND DIRECTORS

Wray Thompson
Chairman of the Board and Chief Executive Officer

Shannon L. Greene
Chief Financial Officer and Treasurer

Ronald C. Morgan
President and Chief Operating Officer

EXECUTIVE OFFICERS (NON DIRECTORS)

Robin Morgan
Vice President – Administration

William M. Warren
Secretary & General Counsel

Stockholder and Other Information

SEC FORM 10-K

STOCKHOLDERS MAY OBTAIN A COPY OF THE COMPANY'S ANNUAL REPORT TO THE SECURITIES AND EXCHANGE COMMISSION ON FORM 10-K WITHOUT CHARGE (EXCEPT FOR EXHIBITS) BY WRITING TO:
INVESTOR RELATIONS
THE LEATHER FACTORY, INC.
PO BOX 50429
FORT WORTH, TEXAS 76105-0429

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TRANSFER AGENT

Securities Transfer Corporation
2591 Dallas Parkway, Suite 102
Frisco, Texas 75034
Phone: 469/633-0101
Facsimile: 469/633-0088

STOCK EXCHANGE LISTING

The common stock is listed on the American Stock Exchange (trading symbol: TLF).

ANNUAL MEETING

The annual meeting of stockholders will be held at 10:00 a.m. on Monday, May 23, 2005 Hall of Fame Room at the Wyndham Hotel 1500 Convention Center Drive Arlington, Texas 76011.





The Leather Factory, Inc.