

Business Model

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The Retail Apparel Market and the UNITED ARROWS Group

The retail apparel market

The scale of the Japanese retail apparel market is just under ¥10 trillion. Structural issues including Japan's aging demographic profile and low wage growth are leading directly to lower consumer spending on apparel. As a result, the market scale is showing steady signs of contraction.

The economic downturn triggered by the global financial crisis since September 2008 is making consumers more cautious in their spending patterns, more reluctant to purchase clothing, and more inclined to choose lower-priced items. In addition to the drop in customer numbers, the "fast fashion" boom together with the rise in specialty stores that place considerable emphasis on pricing are prompting a decline in average customer spending and by association contraction in the market's overall scale.

Operating within a retail apparel market that continues to confront increasingly harsh business conditions, the UNITED ARROWS Group is working diligently to open new stores while lifting annual sales. Buoyed by a wide variety of initiatives, the Group is endeavoring to generate ongoing and stable sales growth.

Channel diversification

Over the past decade, sales channels have undergone significant change. Department and general merchandise store sales growth has stalled. Specialty store and others channel* sales, on the other hand, have remained firm by comparison.

The mail-order route, included in others channel, and particularly online sales have enjoyed remarkable growth. As the sophistication and scope of infrastructure increases, spurred by developments in broadband environments as well as portable devices such as smart and mobile phones, online retailers have taken significant strides in offering enhanced user-friendliness and functionality. At the same time, sharp expansion in the online sales channel reflects successful efforts by operators to overcome the stigma and need to physically try on garments prior to purchasing.

Despite expectations that the market scale will continue to shrink, the online sales market is projected to experience ongoing growth.

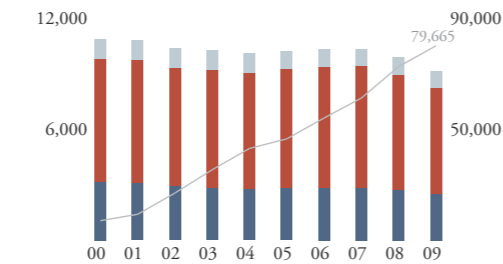
* Includes mail order (Internet, catalogue, television, others) as well as discount stores.

Select shops

Select shops are stores that provide customers with products procured from all over the world, based on unique brand concepts and the discerning judgment of their buyers.

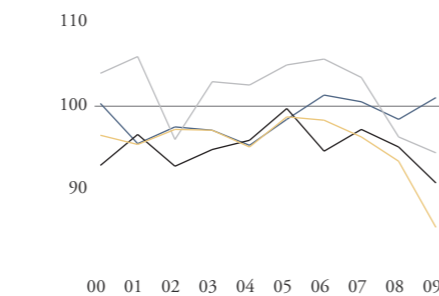
There are also companies that adopt an SPA (specialty store retailer of private label apparel) strategy under which they offer a mix of purchased and private label products. In handling products that offer the appeal of high-value-added

Trends in the scale of Japan's retail apparel market and UNITED ARROWS Group sales
billions of yen/millions of yen



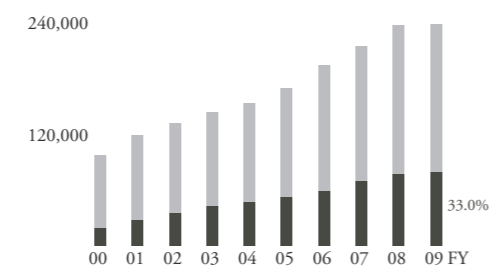
UNITED ARROWS Group sales
Children's apparel Women's apparel Men's apparel
Source: UNITED ARROWS LTD., and Yano Research Institute Ltd. "Apparel Industry," modified by the Company

Trends in rates of sales growth by sales channel
%



Department stores General merchandise stores
Specialty stores Others
Source: Yano Research Institute Ltd. "Apparel Industry," modified by UNITED ARROWS LTD.

Trends in total sales of five major select shop companies and UNITED ARROWS LTD.'s market share
millions of yen



UNITED ARROWS LTD. Total of four other major select shop companies
Source: Yano Research Institute Ltd. "Apparel Industry," modified by UNITED ARROWS LTD.

attributes and a distinctive uniqueness, select shops are positioned between department and specialty stores at the mid- to high-end price range. As such, they are relatively unaffected by trends in economic conditions.

UNITED ARROWS LTD. maintains a balance between attracting customers by carefully handpicking selected designer brands from Japan and overseas and ensuring high profitability by offering private label brands. The Company has the largest sales of any company adopting a select shop business model and is the only such company to have publicly listed its stock.

Issues confronting Japan's apparel market:

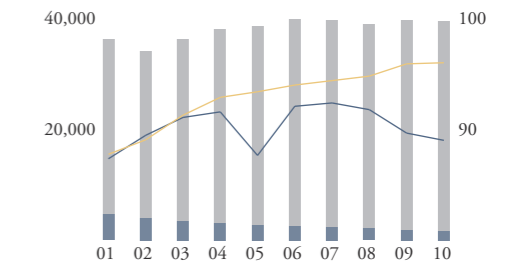
problems with the manufacture of products in China

Since the Plaza Accord in 1985, the manufacture of Japanese apparel has shifted steadily overseas due largely to appreciation in the value of the yen. Given its close geographic proximity and competitive wage structure, China is an attractive base for the relocation of production operations. Over the years, it is purported that this dependence on China by Japan's apparel companies has risen to approximately 90% of total goods produced.

More recently, however, the face of manufacturing in China has exhibited considerable change. This is largely attributable to the sharp growth in domestic consumption in China as well as the preference shown by Chinese factories toward major apparel companies in Europe and the United States as a result of the slump in the Japanese market. At the same time, dramatic increases in the cost of such raw materials as cotton fiber and demands for higher wages, coupled with the drop in quality and delays in delivery as a result of insufficient Chinese factory capacity are imposing considerable burdens on Japan's apparel companies. Taking the aforementioned into consideration, Japanese companies are therefore looking at potential alternatives prompting many to adopt a "China Plus One" strategy that entails cultivating opportunities in the ASEAN region.

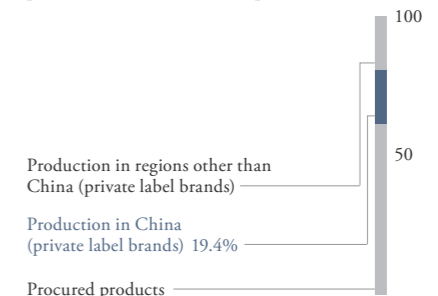
Currently, approximately 20% of the Company's products are manufactured in China (private label brands). On this basis, the risk to UNITED ARROWS LTD. is in relative terms quite low. Moving forward, the Company does not plan to adjust its product prices for the foreseeable future. We will regulate procurement costs in order to maximize gross profit. While implementing appropriate countermeasures to address issues arising out of China, UNITED ARROWS LTD. will increase sales and the number of customers, optimize and reduce inventories, and undertake additional initiatives in order to boost efficiency. In this manner, the Company is confident in its ability to enhance gross profit and to offset increases in procurement costs.

Trends in the domestic manufacturing of apparel in Japan and imports
hundreds of thousands item/%



Domestic production Imports Rate of import penetration*
Ratio of Chinese products to total imports
Source: Senken Shimbun Co., Ltd. "Senken Shimbun" and "2010 Fashion Business Databank," modified by UNITED ARROWS LTD.
*Rate of import penetration: The ratio of imported products to the total volume supplied in Japan

Breakdown of UNITED ARROWS LTD.'s products manufactured in Japan



Data calculated using procurement cost results for the fiscal year ended March 31, 2011

Countermeasures implemented by UNITED ARROWS LTD. to address issues relating to the manufacture of products in China

- Brought forward planning with an eye to future protracted production lead times
- Secured orders and production capacity earlier than usual
- Compiled background information on production across wide-ranging businesses as the basis for negotiations
- Maintained quality through the implementation of third-party inspections
- Further strengthened activities at plants both in China and Japan
- Cultivated production bases other than in China (the ASEAN region) to ensure stability in procurement costs and production capacity

Ramped up efforts to promote the product platform

The markets in which the UNITED ARROWS Group operates
The Japanese retail apparel market can be divided into two categories: the volume market, which mainly consists of relatively low-priced daily clothing, and the trend-conscious market for consumers who are highly sensitive to fashion trends. The UNITED ARROWS Group targets this trend-conscious market.

Our target customers are people who have a strong interest in fashion and want to enrich their lives through it. All our activities, including product development, store exterior and interior design, customer service, and advertising, promotions and other marketing initiatives, are driven by our awareness of them.

Market positioning map



* GMS: General merchandise store

The UNITED ARROWS Group's business structure
UNITED ARROWS LTD. started out as a select shop handling men's business attire, focusing mainly on purchased brands. It has since evolved and adopted an SPA strategy that offers a mix of purchased products and private label products, offering men's and women's dressy and casual clothing and miscellaneous lifestyle goods.

key offerings, we now have numerous other businesses with different characteristics, including our brand business, CHROME HEARTS, and our quick response (QR) / SPA business, COEN.

With UNITED ARROWS and UNITED ARROWS green label relaxing, our other full-line store that offers an SPA-type mix of both purchased and private label products, serving as our

By handling a broad range of products for various tastes, we are aiming to expand our customer base and meet diversifying customer needs. In addition, we are also leveraging synergies between our various businesses and transforming into a sustainable group that achieves solid profits and is resilient to changes in the external environment.

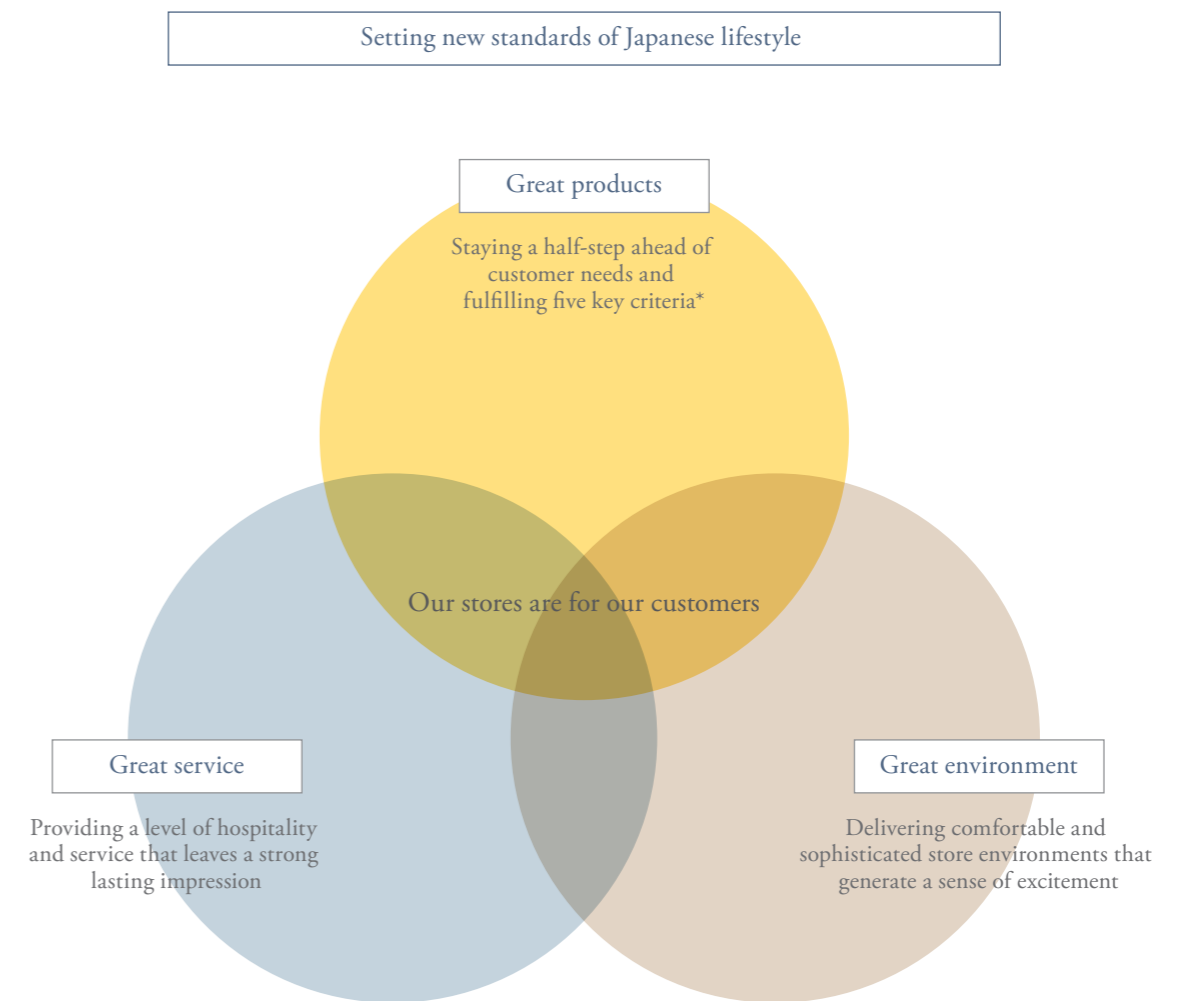


Operating companies: □ UNITED ARROWS LTD. □ FIGO CO., LTD. □ COEN CO., LTD.

Three Key Sources of Satisfaction for Customers

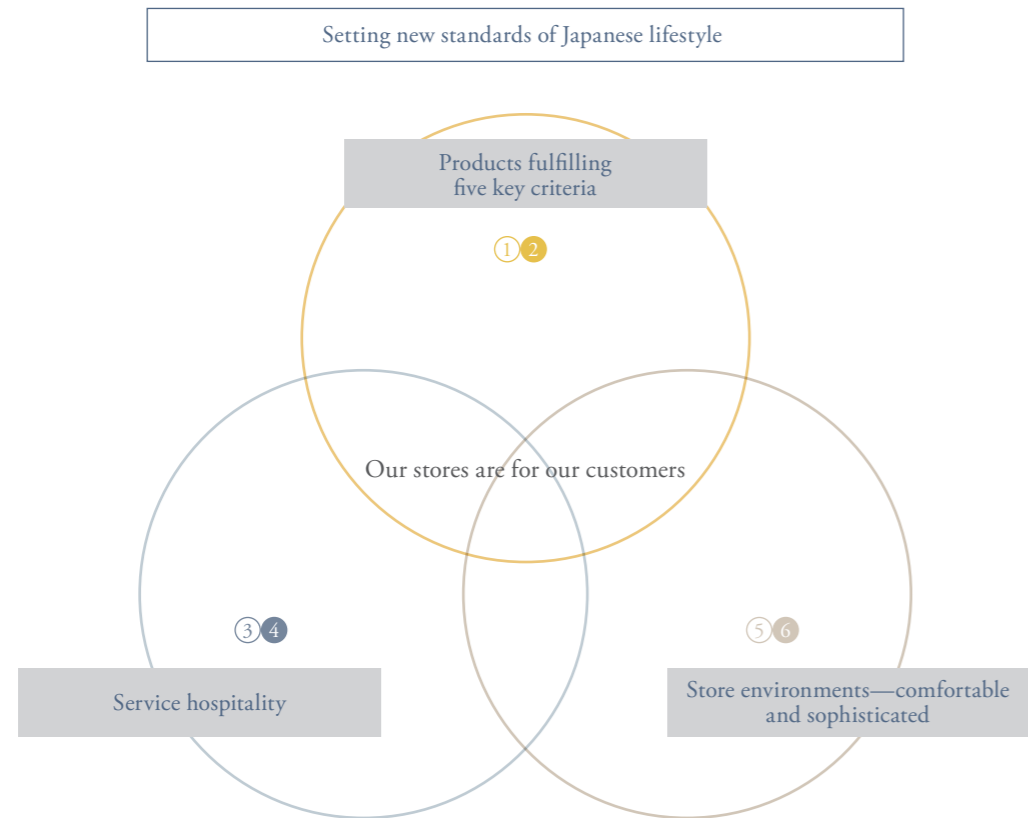
UNITED ARROWS LTD. is guided by the overarching rule that "our stores are for our customers." With this in mind, we strive consistently to hone our service, products, and store environment, which we recognize as the three sources of satisfaction for customers as well as the cornerstone of our competitive strength.

We work to create an atmosphere that allows our service, products, and store environment to naturally evolve. As these three sources of satisfaction continue to flourish and grow, we move closer to realizing our corporate philosophy of setting new standards of Japanese lifestyle.



* Five key criteria: Customers can purchase (1) the products they want, (2) when they want, (3) where they want, (4) in the quantities they want, and (5) at the prices they want.

UNITED ARROWS LTD. engages in a variety of activities in its efforts to strengthen its service, products, and store environment. These activities reflect our goal of simultaneously attaining a high sense of fashion, efficiency, and profitability. In addition to forming an organic bond that generates mutual synergy benefits, these activities also serve as the cornerstones for our unwavering competitive advantage.



①②③ Activities aimed at maintaining a high sense of fashion
 ④⑤⑥ Activities aimed at maintaining high levels of efficiency and profitability

- ① – Product development based on direction and marketing
 - Product differentiation through the presence of buyers and designers
 - Product planning based on collaboration between product and sales divisions
- ② – Product planning and procurement as well as production and inventory reduction based on 52-week merchandising and the Group’s product platform
 - An outstanding distribution and inventory management system
 - Appropriate timing and volumes of store inventory
 - Clarifying the role and position of brands through statement management
- ③ – Nurturing a customer service mindset based on a corporate philosophy curriculum
 - Enhancing sales knowledge and expertise at the UNITED ARROWS University
- ④ – Smooth customer service based on customer management and analysis systems
 - Maximizing customer contact through labor management
- ⑤ – A brand that expresses a world view built on high exterior and interior design standards
- ⑥ – Purchasing functionality based on high exterior and interior design standards
- ③ – Improving practical customer service skills through on-the-job store training
 - Implementing an awards program for talented sales personnel
 - Putting in place a workplace environment conducive to the long-term retention of employees

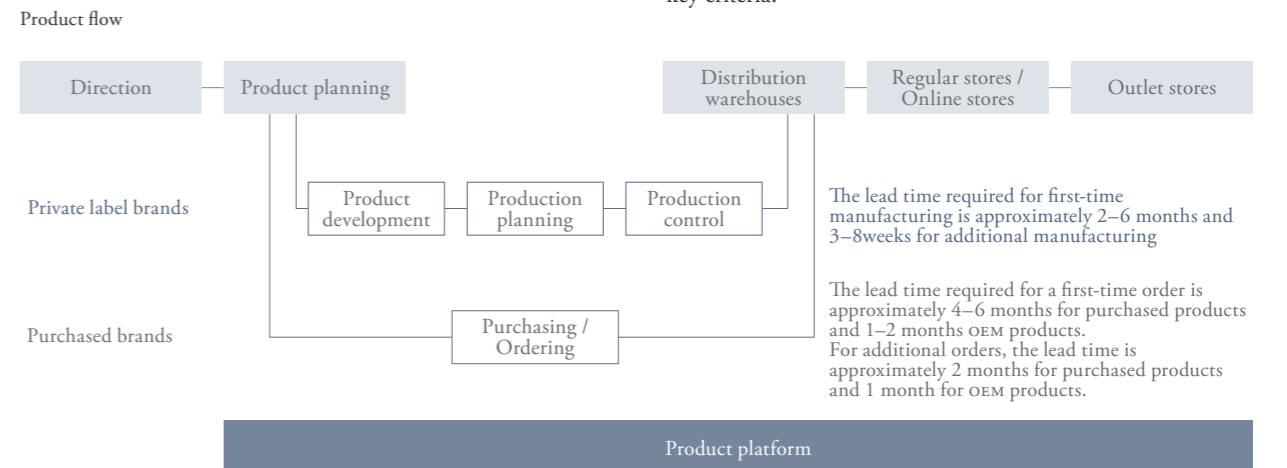
Product development based on direction and marketing / Product differentiation through the presence of buyers and designers
 A feature that defines UNITED ARROWS LTD. is the direction that initiates all activities related to product development. Direction, which is based on a detailed analysis of trends in fashion colors and materials, overseas collection information, and shifts in social tastes, allows us to put in place a common theme across all businesses on a seasonal basis. In addition, marketing divisions consistently undertake research into the latest fashion trends providing this information across the Group. Each business then draws on this information to establish specific themes that incorporate particular attributes. Buyers, who travel all over the world, and designers responsible for private label brands regularly exchange information. This serves as the wellspring for differentiating our products and consistently delivering a fresh and unique appeal.

Product planning based on collaboration between product and sales divisions
 Collaboration between product and sales division is the driving force behind product planning that accurately captures customer needs. Sales divisions meet regularly with head office personnel to report on the comments received from customers at stores. At the same time, sales divisions participate in every stage of the product planning process from design through sample manufacture to finished product. In the fiscal year ending March 2012, we will take steps to further enhance collaboration between product and sales divisions. In an effort to address priority issues, we will incorporate the promotion function within product and sales division collaboration with the aim of placing increased emphasis on increasing the number of store customers.

Product planning and procurement as well as production and inventory reduction based on 52-week merchandising and the Group’s product platform
 The Company’s sales activities are the culmination of a comprehensive product planning, procurement, production, and inventory reduction process that involves the ongoing validation and modification of plans on a trial and error basis. Tentative plans for the sale of products at stores are put in place after dividing the year into 52 weeks and undertaking a detailed analysis of past sales performance as well as market needs and trends.

Product procurement, production, product launch, and inventory reduction activities are conducted in accordance with the Group’s product platform, which is in turn composed of its merchandising and production platforms.
 The merchandising platform provides the mechanism for determining the current status of merchandise flows and the basis for making decisions. Utilizing the progress management tables and indices consistent across all businesses, UNITED ARROWS LTD. has established a swift and easy-to-implement decision-making process that allows the Group to promote the additional production of top-selling items while reducing production and inventories of slow-selling items. As a result, UNITED ARROWS LTD. has witnessed increases in the rates of inventory reduction as well as final sales. This is in turn leading to improvements in gross profit, inventories, and cash flows.

The production platform works to formulate the product procurement and production strategies that take us from merchandising planning through to realization. While manufacturing is outsourced, the choice of external plant or factory for each item is based on a Group-wide consolidation of the raw materials procured by each business as well as manufacturing plant information. Accordingly, this has led to positive adjustments in procurement costs relating to purchases and production as well as lead times in a way that satisfies the five key criteria.



An outstanding distribution and inventory management system / Appropriate timing and volumes of store inventory Product management including price tagging conducted at warehouses and concentrated inventory control at the direction of the Company's head office are consistent throughout each of the Group's four nationwide distribution centers. Every effort is made to ensure that the right products are stored in the right quantities at the right time. This not only leads to optimal product quality control, but also significantly alleviates the operating and administrative burden. More importantly, this allows us to maximize the time spent in direct contact with and service to customers.

UNITED ARROWS LTD. has installed a point of sale (POS) system to facilitate coordination between nationwide stores and distribution centers. Products sold are promptly replenished in a prearranged period according to each region. This process is designed to ensure that top-selling products remain available at all times minimizing sales opportunity loss.

Clarifying the role and position of brands through statement management

UNITED ARROWS LTD. recognizes the importance of clarifying to whom its products are directed, with whom, and what it is competing, and what unique benefits it seeks to provide when promoting a consistent brand image. These considerations form a major component of efforts to put in place a statement for each brand. Moreover, to avoid duplication and any potential for direct internal competition, the Company takes stock of its Company-wide brand portfolio and engages in sales activities after clarifying the role and position of each brand.

Smooth customer service based on customer management and analysis systems

UNITED ARROWS LTD. has introduced a House Card initiative for use by customers at all business stores. This initiative allows the Company to maintain a record of each customer's purchases, which is shared Group-wide, and to maintain and analyze an invaluable pool of customer information. Rather than manage and handle this data at a head office level, individual stores keep track of each individual's information to ensure an appropriate and flexible response. Data encompassing purchasing frequency, type, and amount provide the basis for decisions made by each store. Drawing on this information, stores can then select the most appropriate medium to promote products, such as via telephone, direct mail, or e-mail magazines.

Nurturing a customer service mindset based on a corporate philosophy curriculum / Enhancing sales knowledge and expertise at the UNITED ARROWS University
The UNITED ARROWS rule that "our stores are for our

customers" provides the platform for its sales activities. The UNITED ARROWS University, which is an internal training program, has put in place a corporate philosophy curriculum aimed at fostering a deeper understanding and awareness of this rule and the customer service mindset.

In addition, the University provides the opportunity for employees to learn UNITED ARROWS LTD.'s basic sales and product policies and customer service techniques such as measuring, interpretation of quality labeling, and consumer motivation. Combining practical on-the-job training with opportunities to gain theoretical and systematic sales knowledge helps sales personnel enhance their customer service skills.

Implementing an awards program for talented sales personnel
In order to maintain and increase the knowledge and motivation of sales personnel, UNITED ARROWS LTD. recognizes the need for a human resource rating system that evaluates the level of achievement against established quantitative goals that focus not only on sales performance but the initiative and actions of each employee. In this context, and among a host of initiatives, a representative selected from each Group brand participates in the UNITED ARROWS Grand Prix, a role-playing sales contest. The Sales Master system is also an initiative created to reward sales personnel who specialize and excel at their work. Furthermore, the Sales Master system provides a goal to which all sales personnel can aspire, thereby bringing a greater sense of Group-wide unity.



Role playing as a part of the UNITED ARROWS Grand Prix

Putting in place a workplace environment conducive to the long-term retention of employees

Store operations in the retail apparel industry are characterized by the substantial use of part-time employees. Against this backdrop, UNITED ARROWS LTD. maintains an employment policy of, in principle, recruiting only full-time, permanent employees. In this context, the Company maintains a robust employee support and backup system that allows each employee to pursue an optimal balance between work and home life. In addition to support programs that assist employees in gaining qualifications, UNITED ARROWS LTD. makes it a point to nurture a workplace environment that is conducive to lifelong employment.