# UNITED ARROWS LTD.
## First Quarter Fiscal 2017 Earnings Announcement Q&A

UNITED ARROWS LTD. held earnings announcement presentations on August 5, 2016 and August 8, 2016, at which the media, analysts, and institutional investors were in attendance. The principal questions received and answers given by category during each session are presented as follows, with certain details expanded or modified in an attempt to provide readers with a deeper understanding of the UNITED ARROWS Group's performance and activities.

### *About Business Results for the First Quarter (April 1, 2016 to June 30, 2016) of Fiscal 2017 (April 1, 2016 to March 31, 2017)*

Q. How did sales, gross profit, and selling, general and administrative (SGA) expenses compare with plans?

**A.** Sales and gross profit in the 1Q of FY17 were slightly below plans. SGA expenses were also lower than the forecast amount. The gross margin is projected to improve 0.9 of a percentage point for the full fiscal year. In the 1Q of the fiscal year under review, the gross margin improved 0.1 of a percentage point. Over the immediate term, the cost of goods purchased ratio is showing signs of steady improvement. That is largely due to the positive flow-on effects of a variety of measures as well as trends in foreign currency exchange rates. The ratio of heavy clothing sales as well as profit levels tend to increase in the 2H. As a result, we expect the gross margin will show a strong improvement in the latter half of the fiscal year under review.

Q. Can you provide us with a breakdown of the gross margin?

**A.** In the 1Q of FY17, the non-consolidated gross margin of total business units decreased 0.4 of a percentage point compared with the 1Q of the previous fiscal year. Markdown losses had a negative impact of approximately 0.2 of a percentage point, which was largely offset by a change in the composition of sales between private label brands and procured products. An increase in procurement costs is estimated to have pushed down the non-consolidated gross margin of total business units by roughly 0.4 of a percentage point. This increase in procurement costs mainly reflects our inability to thoroughly implement control measures. Efforts to adhere strictly to a cost control policy were initiated at the beginning of this year. As such, initiatives aimed at the spring and summer seasons were not undertaken in time. We will strengthen cost control measures targeting the fall and winter seasons. We will also work to boost the gross margin by improving the cost of goods purchased ratio and holding down markdown losses.

Q. Consumers remain acutely sensitive to prices. Do you believe it will become increasingly difficult to set prices? How will UNITED ARROWS LTD. improve the cost of goods sold ratio in the 2H given this difficult environment?

A. Consumers are indeed adopting a harsh approach toward product prices. While we have made minor adjustments to the prices of products after completing a review of specifications, for the most part we have made no major change to our product price ranges. Looking ahead, we have also decided not to lower prices. We will focus our cost control efforts on ensuring an optimal balance between product prices and value.

Q. Why has inventory increased as of the end of the 1Q?

A. Looking at a breakdown of inventory as of the end of the 1Q, the increase is made up of spring and summer items as well as fall and winter items for the current period. Past inventories are around 90% of the previous fiscal year's level. We tended to overcompensate with instructions to reduce inventories in the previous fiscal year, which led to instances of sales opportunity loss. Recognizing that inventories tended to run down toward the final stages of clearance sales conducted in the previous fiscal year, we have to some extent strategically introduced products to boost inventory this fiscal year. A large number of store clearance sales began on July 1, 2016. As a result, we are promoting the sale of spring and summer inventories during July. As far as fall and winter items are concerned, we have beefed up inventories of late summer products in line with policies regarding the classification and segmentation of seasons. Here, our goal is also to reduce inventories over the July and August period. Taking into consideration each of these factors, inventory increased as of the end of the 1Q. Looking at the full fiscal year, trends are essentially in line with plans.

Q. Which specific items within SGA expenses have been reduced?

A. Personnel expenses in the 1Q of FY17 were lower than projected. Other costs, variable and fixed expenses, and such temporary costs as repairs and maintenance were also below their forecast amounts. The downturn in personnel expenses mainly reflects the Company's inability to recruit staff according to plans due to the difficult employment market. Other contributing factors include efforts to control the numbers of employees hired as a result of performance trends in each business.

Q. Please tell us about tax-free sales in the 1Q.

A. Tax-free sales in the 1Q of FY17 came to ¥1.1 billion, up 5% compared with the corresponding period of the previous fiscal year, and accounted for 3.7% of total sales, which was roughly the same as the year before. While the rate of growth has stalled compared with the previous fiscal year, tax-free sales continue to grow.

### *Progress on Addressing Priority Issues*

Q. What steps are you taking to review the Company's basic product policy?

A. Recognizing the difficulties in fully interpreting the Company's basic product policy and the relative low level of in-house understanding, we took steps to put in place a policy that was easier to grasp by all employees, including personnel hired mid-career and staff who had transferred from stores to the product department. Having witnessed instances where products that were in high demand went out of stock and the buildup of excess inventories of test marketing items, we also took steps to update procedures and focus on the strict adherence to rules.

Q. What changes have been made with respect to product development amid the review of the brand portfolio?

A. In the absence of recent major changes in trends, we are seeing more and more similarities between products, including those of competitor companies. With products being compared on the basis of price, the incidence of markdowns is steadily growing. By reviewing our brand portfolio, we are endeavoring to clarify the unique attributes of each brand as well as customer needs. In this context, we are promoting product development that highlights the individual characteristics of each brand.

Q. To what degree has the Company strengthened the allocation of inventory to online stores?

A. We have increased the allocation of inventory to online stores by between 20% and 30% compared with the previous fiscal year. We have bolstered the depth of mainly strategic products that target high sales, and we are linking this effort with steps to ensure that items are not out of stock. Thanks to this initiative, we have held the number of requests to replenish stock at UNITED ARROWS LTD. ONLINE STORE to around 80% of the level recorded in the previous fiscal year. Despite these efforts, we are still seeing the incidence of sales opportunity loss. We intend to further strengthen the allocation of inventory in the 2H.

Q. Please tell us about results by e-commerce site.

A. By e-commerce site, sales through UNITED ARROWS LTD. ONLINE STORE have increased about 10% and account for roughly 21% of total e-commerce site sales. ZOZOTOWN sales have climbed approximately 31% and make up roughly 57% of total online sales. Among other e-commerce sites, Stylife sales have tripled, growing to about

5%. For such sites as MAGASEEK and i LUMINE, sales have expanded between 20% and 30%. This bump in sales through Stylife and MAGASEEK reflect such factors as the positive flow-on effects of alliances with Rakuten and Docomo d fashion, respectively. Moreover, proactive steps are being taken to hold events and campaigns at each site. These efforts in turn are also contributing to the increase in sales.

Q. Measures to promote discount sales through such initiatives as time sales at online stores are becoming increasingly prominent. Do you have any concerns regarding profitability?

A. The Company determines whether or not it will participate in discount coupon schemes or time sales. It cannot be said, therefore, that we are an aggressive participant Companywide. As far as we are concerned, online stores are a forum for products to be sold at regular prices.

Q. What changes will we see following this month's integration of the Company's House Card with UNITED ARROWS LTD. ONLINE STORE members?

A. In addition to integration, we will consolidate our point system. Up to now, customers who had purchased items with a total value exceeding ¥50,000 over a six-month period would receive points at the rate of 2%. For businesses that exhibited low average spending per customer, the number of customers receiving reward points was quite small. Despite the lower points rate of 1%, the new service system will not attract a minimum purchase amount. Customers can apply their reward points to the value of ¥1 per one point from the very next purchase. All customers can now receive benefits under the revised scheme. We have also put in place a menu of services that are linked to the amount of each purchase on an individual business basis. Our aim is to provide convenient services to as many purchasing customers as possible. Complementing these endeavors, House Card customers can now use their IDs for purchases at UNITED ARROWS LTD. ONLINE STORE and enjoy the freedom to switch smoothly from offline to online stores.

***Other***

Q. Why is COEN CO., LTD. struggling?

A. Customers are continuing to adopt an austere approach toward fashion spending against the backdrop of prolonged deflation. Despite this austere approach, we are seeing certain competitor companies secure robust results through the sale of items at affordable prices in the new trend-conscious market in which COEN operates. Amid diverse customer needs and strong demand for such trend-conscious products as feminine and mode items, COEN, which focuses mainly on American casual wear, has fallen short in its efforts to fully address customer needs. Consequently, results have been weak. Looking ahead, the company will incorporate products that better capture prevailing trends. In this manner, COEN will work toward securing an improvement in its performance.

Q. The Company will announce details of its new Long-Term Vision next year. At this stage, do you anticipate any change in the balance between and priority placed on existing businesses, new businesses, and overseas expansion?

A. We do not see any major change in the direction of our Long-Term Vision. Our new businesses are yet to generate concrete results. At this stage, we are looking at reorganization with other businesses while reviewing the content of each business. We will continue to promote the development of new businesses; we will not only launch activities from a zero base, but we will also consider opportunities that entail tie-ups with other companies as well as foster synergies with other businesses. As far as our overseas business development plans are concerned, we will build a successful model in Taiwan within the period of the new Long-Term Vision and put in place a blueprint for future rollout and expansion. Our efforts are currently progressing in line with plans. While our overseas network is limited to three stores, we are steadily building a strong reputation among customers.