

UNITED ARROWS LTD.
Fiscal 2015 Earnings Announcement Q&A

UNITED ARROWS LTD. held an earnings announcement presentation attended by the mass media, analysts, and institutional investors on May 8, 2015 and May 11, 2015. Details of principal questions received and answers given by category during each session are presented as follows. Certain details have been expanded or modified to provide readers with a deeper understanding of the UNITED ARROWS Group's performance and activities.

About Business Results in FY15 (April 1, 2014 to March 31, 2015)

Q. Can you provide us with details of business unit gross profit in the 4Q?

A. The gross margin for business units in the 4Q was 50.6%, down 2.7 points compared with the previous year. Looking at this downturn in more detail, markdown losses had a negative impact of around 1.8 points while the higher proportion of procured products in the sales mix had a negative impact of roughly 0.2 of a point. Despite the positive impact on the gross margin of about 0.5 of a point attributable to CHROME HEARTS (CH) sales, an upswing in procurement costs of other products had a negative impact of approximately 1.3 points. Slightly less than half of this 1.3 point decline is due to a decrease in the value of the yen. The remainder, or just over half, reflects growth in sales of procured products with a high cost of sales including sneakers, outerwear, and bags.

Q. Why did UNITED ARROWS (UA), including BEAUTY&YOUTH UNITED ARROWS (BY), and UNITED ARROWS green label relaxing (GLR) sales decline compared with the previous year?

A. Looking at trends in casual wear, the women's category in the BY business found favor among customers thanks to successful efforts aimed at providing a rich lineup of private label brands. In contrast, and reflecting on specific shortcomings, we did not adequately put forward proposals to address the needs of select shop users in the UA men's category. On this point, we will make the necessary adjustments to ensure that we promote products that are a half-step ahead of the times. In the women's category, we placed too much emphasis on trends. As a result, support from customers waned. Our failure to put forward fresh ideas and appealing products was also a factor that contributed to difficult conditions. Looking ahead, we will work diligently to bring a fresh appeal to our stores by finely tuning efforts aimed at launching products. In the GLR business, the men's category was favorably received by customers. This was largely attributable to product enhancements including the levels at which prices were set. In contrast, we are currently taking steps to review women's light apparel and other products in the GLR business due to mistakes made when initially setting prices.

About FY16, the Fiscal Year Ending March 31, 2016

Q. Can you provide us with details of specific measures that each department plans to implement in a bid to bolster the cycle of collaboration between the product, sales, and promotion departments, which have been identified as a priority issue for FY16?

A. Purchasing patterns today are polarized between customers, who are looking to purchase items for the future, and customers, who desire items for immediate use. It is therefore vital that the product department keeps in mind these parallel needs. While promoting product planning that takes into account the need to address this desire for immediate use, equal weight will be placed on providing a lineup of items for the future in line with the attributes of each brand. For its part, the sales department will continue to engage in passionate customer service. A key strength of the Company is its ability to deliver a level of customer service that leaves its customers with a lasting impression. Rather than rest on our laurels, we will continue to hone this facet of our operations. The promotion department will undertake sales and promotional activities while remaining sensitive to the manner in which customers gather information. In today's ubiquitous hi-tech world, the use of such mobile devices such as smartphones to gather information is commonplace. With this in mind, it is therefore important that we disseminate information in a manner that is both appropriate and effective. Accordingly, we will place the utmost emphasis on delivering information in a manner that will not only inspire and excite customers, but that can be easily shared.

Q. From an organizational perspective, can you accommodate visits by the product department to the sales frontline?

A. We have established a supervisory function between the product and sales departments. This function serves to gather, collate, and organize customer feedback, which is then channeled to the Company's head office. We recognize that this function has weakened over time and issued instructions that greater efforts be made to glean feedback from customers.

Q. What steps do you intend to take to address costs and boost profits in line with prolonged weakness in the yen throughout FY16?

A. One step will be to raise the ratio of regular price sales. We will finely tune our efforts to release products, refrain from holding excessive levels of inventory, and control any decrease in the gross margin attributable to markdowns. Another step will be to expand our "China Plus One" strategy. Production mainly in Vietnam and the ASEAN region as a ratio of total production has followed an upward path since last year. By holding down costs compared with China, we will gradually expand operations in the ASEAN region where the potential exists to ensure stable supply.

Q. To what degree do you plan to introduce 8-season merchandising in FY16 and FY17?

A. 8-season merchandising is a concept that equates closely to global branding and includes the fast fashion and other fields. The structure of merchandise is classified into eight seasons over the course of the year in line with consumers' sensory perceptions. Currently, 8-season merchandising is being introduced into the GLR business as well as SBUs with certain exceptions, where the ratio of SPA activities is high. We will reevaluate efforts while taking into consideration future progress. While items for immediate use will account for a large number of proposals in businesses that engage primarily in SPA activities, proposals put forward by UA, which boasts a strong select shop format, and BY will be weighted toward items that are a half-step ahead of the times. For this reason, we will maintain existing season classifications.

Please refer to the FY15 3Q Earnings Announcement for details regarding 8-season merchandising.

http://www.united-arrows.co.jp/en/ir/lib/data/p/presentation_e_2703_3q.pdf

Q. Are there any cost-related problems associated with increasing quick response (QR) activities?

A. With an emphasis on costs throughout FY15, a certain portion of products for sale were manufactured a half-year in advance. This in turn delayed our response to shifts in trends. As a result, products were sold on the basis of an increase in clearance sale discount rates, which placed considerable downward pressure on gross profit. In making sure that we learn from the mistakes of this recent past, we are limiting the procurement of spring items in FY16 to around 90% of the previous year. We have also allocated a supplementary budget to facilitate a quick response once the season is in full swing. While QR activities will lift costs, we anticipate in the final analysis to secure sound gross profit by increasing the ratio of regular price sales.

Q. Is it correct to assume that the year-on-year downturn in the gross margin in FY16 is mainly attributable to the impact of reducing past inventories?

A. The gross margin in FY16 is projected to decline 0.2 of a point year on year to 51.1% on a non-consolidated basis. The gross margin for business units is expected to remain essentially unchanged compared with the margin reported in FY15. The forecast downturn in the non-consolidated gross margin is for the most part attributable to deterioration in the gross margin of the outlet store category on the back of efforts to reduce past inventory levels and an increase in the ratio of outlet store sales reflecting the opening of new outlet stores. While we are unable to provide a clear-cut answer for March 2017, we are looking at eliminating the negative impact of efforts aimed at reducing past inventory levels in FY16.

Q. When you say that the gross margin for business units is expected to remain essentially unchanged compared with the margin reported in FY15, does this mean that the gross margin will be down for the 1H and up for the 2H on a year-on-year basis?

A. The gross margin for the 1H is forecast to come in at 55.6%, down 0.7 of a point compared with the corresponding period of FY15. The gross margin for the 2H is projected to reach 55.3%, up 0.7 of a point year on year. The principal factor that is expected to contribute most to this improvement in the 2H is the successful effort to control markdown losses. To date, we have controlled costs by manufacturing products on an aggregated basis. Unfortunately, this meant that we were unable to respond quickly to changes in trends, which ultimately forced us to increase the sale of markdown items. In the future, we will shorten the lead times of items that are marketed in response to each trend. Even if there is a slight increase in costs, we will move to offset by lifting the ratio of regular price sales.

Q. What will happen to overall prices following a review of your pricing strategies?

A. We regret having raised the prices of certain products last year that did not require or warrant a price increase. We plan to restore the prices of products that are purchased to supplement consumers' wardrobes including shirts and cut & sewn items to levels that meet the expectations of customers. For those products that we intend to market at higher revised prices, we will carefully craft each item using our atelier and ensure that we secure a balance between price and value. As a result, we are projecting a slight increase in prices in relative terms.

Q. Can you elaborate on your forecasts for existing store sales in FY16 by business?

A. We are looking at year-on-year increases in the UA, GLR, and CH businesses of over 3%, over 2.5%, and over 1%, respectively. Existing store sales for SBUs are projected to climb above 6.5%. We are also anticipating an overall improvement across each SBU business.

Q. What are your thoughts on the number of existing store customers in FY16? Can you provide details of any specific measures aimed at increasing the number of customers?

A. We have not identified a forecast for the number of existing store customers in FY16. In addition to strengthening customer service and our sales capabilities, we will make every effort to deliver attractive and appealing stores while pursuing Omni Channel Retailing initiatives in a bid to increase the number of customers at actual stores. Recently, we are also seeing an upswing in the number of customers that use both actual and online stores. After showcasing the appeal of products using online store sites, systems are now in place to have items delivered to actual stores where customers can view and feel actual merchandise. Through a combination of total actual and online store initiatives, we will employ a host of measure aimed at meeting the needs of customers going forward. This in turn is expected to increase the number of customers.

Q. Total sales floor space for the Group as a whole is forecast to climb 9% in FY16. Is this an accelerated figure compared with total sales floor space for FY15?

A. Growth in sales floor space in FY15 was more than 5.5% compared with the previous fiscal year. The increase in FY16 of 9% is comparatively high. In FY15, there were a lot of stores opened as a part of our new business activities. As a result, the growth in floor space was small compared with the number of stores opened. In FY16, particular emphasis will be place on opening relatively large-scale stores in various existing businesses including BY, GLR, and COEN. At the same time, plans include an increase in the sales areas of stores by a significant margin. Accounting for each of these factors, growth in floor space will be substantial in proportion to the number of stores opened.

* FY15: Number of stores opened: 29; Closed: 9; FY16 (forecast): Number of stores opened: 32; Closed: 6

About the Reduction in Inventory

Q. Will the reduction in inventory attributable to online store sales be posted as online sales? How will sales attributable to events conducted outside stores be classified?

A. Bargain sales items for the year under review conducted through such channels as ZOZOTOWN and UNITED ARROWS LTD. ONLINE STORE will be posted as online sales. Sales conducted through limited period outlet store online sites as well as sales attributable to events conducted outside stores will be posted to the outlet store category.

Q. What is the status of inventory as of the end of March 2015?

A. On a non-consolidated basis, roughly 45%, 36%, and 18% of inventory as of the end of March 2014 was made up of items for sale during spring and summer, past inventories, and products that were not linked to any particular season, respectively. As of the end of March 2015, this breakdown had shifted to approximately 40%, 40%, and 20%, respectively. The most prominent shift was the higher balance of past inventories. In terms of the amount of inventory, the balance had risen about ¥1.7 billion compared with the end of the previous fiscal year. By reducing inventory by approximately ¥2.0 billion, including the aforementioned, during FY16, we will improve the status of inventory from FY17 and beyond.

Q. How often will you hold events during FY16?

A. Six events have been set for the 1H. There is a chance that this number will increase in the future. We will work to reduce inventories through a variety of measures including the use of outlet store online sites also with respect to online stores.

Q. With the major portion of inventory reduction undertaken through sales at outlet stores, can we assume that the impact on business units will be limited?

A. The impact on business unit gross profits will be minimal. This indeed reflects efforts to reduce inventories through the outlet store category.

Q. What targets have you set for inventory turnover for FY16?

A. Inventory turnover came in at roughly six times in FY15 on a non-consolidated basis. We are again looking at inventory turning over around six times in FY16 as a result of reductions in inventory and the launch of new products.

About Online Store Sales

Q. Will you change your approach toward online store sales in the future after taking into consideration current robust conditions and results?

A. This far, we have not adopted a policy of expanding sales by focusing on online stores. Looking ahead, we intend to continue our emphasis on enhancing the convenience of customers through the combined and complementary use of actual and online stores. Based on recent trends, however, online stores have forged an indispensable presence from the point of view of customers. With this in mind, we will consider initiatives aimed at expanding online sales over the medium to long term.

Q. Do you have a target for online sales?

A. At this stage, we have not identified a specific target. Our energies at the moment are being channeled toward the review of various initiatives.

Q. Actual stores are struggling while the performance of online stores is robust. Does this reflect trends across the market as a whole? Or is this the results of initiatives undertaken by the Company? What issues do you envisage will arise in the future?

A. The sharing of stock information is a major factor that has fueled robust online store results. A system is now in place at a number of sites where products that are available at the Company's distribution centers are automatically delivered even when out of stock at online stores. This has led to a reduction in sales opportunity loss. Topical products as well as such items as sneakers that are exclusively developed for the Company have also contributed to online store sales growth. Due to the reluctance by customers to queue up before a store opens and the frustrations associated with not being able to purchase a product in the right size or color because it is out of stock, we are seeing a growing trend toward the ordering of products online in order to secure the desired product. Clearance sales are also helping to boost online sales. As customers seek to avoid the crowds that are part and parcel of most clearance sales,

the number of customers using online sites is increasing. The consolidation of clearance sales products at online stores toward the end of each clearance sales period has provided an underlying strength to online sales. Looking ahead, we will look to lift our capabilities to ensure that the level of service is identical at both actual and online stores. By offering order-made services and other benefits including clothing repair and size adjustments while launching services that are not currently provided online, we will enhance the convenience of online stores thereby boosting sales.

About the Medium-Term Business Plan

Q. When did you decide to withdraw your sales and profit targets under the Company's medium-term business plan, which concludes in FY17? You have not withdrawn your long-term targets for FY22. When do you expect sales will recover?

A. Taking into consideration FY15 results and our original forecasts for FY16, the Company was faced with a substantial high hurdle in achieving its medium-term business plan. The operating environment of the market in general has changed significantly in the wake of the consumption tax rate hike in April last year. While certain pundits are claiming that economic conditions are improving, trends with respect to fashion spending remain shrouded in a cloud of uncertainty. With the aforementioned high hurdle of our medium-term business plan under the existing environment, there is every possibility that we will fall short of our established targets. As a result, we decided to withdraw our forecasts. Looking at the long term, we are currently at a point where we are assessing our options and reevaluating various measures. As a result, we are not in a position to revise targets at this stage.

Q. Despite having withdrawn your quantitative targets under the medium-term business plan, where do you anticipate gross margins will be in FY17?

A. We are not able to determine the level of gross profit in FY17 at this time. However, we believe that the gross margin will improve in FY17 due mainly to efforts aimed at reducing inventory.

Other

Q. What has led you to maintaining dividends in line with forecasts set at the beginning of the period?

A. Management's resolve is to ensure the payment of stable dividends taking into consideration its emphasis on promoting shareholder value.

Q. What is your policy toward the use of treasury stock?

A. In instances where we believe benefits will accrue to stakeholders through an alliance or an M&A transaction, we will consider applying treasury stock. Otherwise, we will contemplate the retirement of treasury stock as appropriate.