

## **UNITED ARROWS LTD. Fiscal 2011 Earnings Announcement Q&A**

UNITED ARROWS LTD. held an earnings announcement presentation and undertook conference calls with the mass media, analysts, and institutional investors on May 11, 2011 (Wednesday) and May 12, 2011 (Thursday). 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.

### ***The UNITED ARROWS Group's financial and operating performance for fiscal 2011, the fiscal year ended March 31, 2011, and its business activities***

**Q.** Please provide us with specific details of campaigns conducted to promote online sales and the level of investment undertaken.

**A.** During the fiscal year ended March 31, 2011, the UNITED ARROWS Group implemented various sales promotion activities utilizing wide-ranging media and initiatives including TV commercials, banner advertising, and free delivery campaigns. Sales promotions were undertaken on a large scale at a total cost of around ¥150 million to ¥160 million. In March 2011, UNITED ARROWS LTD. also launched an online site that allows users to freely coordinate ensembles to their own personal tastes using an innovative "kisekae" simulation tool.

**Q.** What is the ratio of UNITED ARROWS own online store sales and ZOZOTOWN sales to total online sales?

**A.** UNITED ARROWS own online store sales comprise around 15% while ZOZOTOWN sales cover about 75% of total online sales.

### ***The UNITED ARROWS Group's financial and operating performance for fiscal 2012, the fiscal year ending March 31, 2012, and its business activities***

*(Sales forecasts)*

**Q.** What are the underlying assumptions and reasons for providing a forecast range for net sales in fiscal 2012?

**A.** Recognizing that approximately 50% of UNITED ARROWS LTD.'s non-consolidated net sales are derived from the Kanto area, uncertainties surrounding future operating conditions including the impact of measures implemented by commercial facilities to conserve energy due largely to restricted supplies of electric power during the summer across areas serviced by The Tokyo Electric Power Company, Incorporated as well as the affect on consumer sentiment has forced us to provide a forecast range for net

sales. UNITED ARROWS LTD. has factored into the upper forecast limit for net sales in the Kanto area a drop of 2% in net sales for the full fiscal year to set a lower limit. In overall terms, this translates to a 1% difference between the upper and lower forecast limits.

**Q.** Does this lower limit also take into account reduced operating hours as a result of rolling blackouts?

**A.** UNITED ARROWS LTD. is not at this point in a position to determine the extent to which operating hours will be reduced during the summer. It is therefore difficult to gauge and explain the impact on the Group's lower limit forecast. Currently, the lower limit mainly reflects the perceived affect on consumer sentiment.

**Q.** Results during April 2011 were robust. What are your forecasts for summer and autumn? How you think existing stores will perform from May and beyond?

**A.** UNITED ARROWS LTD. has not provided forecasts for the six-month period to September 30, 2011. Projections including existing store performance therefore cover the full fiscal year ending March 31, 2012. In overall terms, we anticipate weak results during the first half and a strong recovery in the second half. This is largely attributable to shortages in the supply of electric power over the summer months. Consumer sentiment was forecast to deteriorate in the aftermath of the Great East Japan Earthquake. However, results in April were robust with the pace of consumption recovery exceeding expectations. Buoyed by the uplifting spirit that fashion provides, purchasing patterns have been firm. Despite favorable results at the start of the fiscal year, UNITED ARROWS LTD. is not in a position to determine for how long this positive trend will continue. The Company is therefore adopting a cautious approach.

**Q.** Forecasts for fiscal 2012 indicate UNITED ARROWS green label relaxing sales will improve. UNITED ARROWS' performance, on the other hand, is projected as weak. What is the rationale behind these estimates?

**A.** The UNITED ARROWS Group plans to implement large-scale promotions to boost sales in its UNITED ARROWS green label relaxing business, which is recognized as a driver of future growth. Through these means, we anticipate raising the level of existing store sales. At this stage, we have no similar intentions for the UNITED ARROWS business category, which is the principal rationale behind the discrepancy.

*(Earnings forecasts)*

**Q.** Gross profit in fiscal 2012 on a non-consolidated basis is forecast to improve. In addition to the rise in raw material costs, gross profit has been negatively affected by withdrawal from the TOKISHIRAZU and SOUNDS GOOD businesses during the previous fiscal year. Taking these factors into consideration, can

you provide us with your thoughts on gross profit trends?

**A.** We anticipate raw material and labor costs to increase during the current fiscal year. Our activities accordingly take into account an upswing in procurement costs. Moving forward, UNITED ARROWS LTD. is bolstering collaboration between the product, sales, and promotion divisions, working to increase the rates of inventory reduction and final sales, enhance inventory efficiency, reduce opportunity loss, and improve gross profit.

**Q.** Please provide us with details of gross profit margins on an individual business basis as well as underlying assumptions.

**A.** We do not provide gross profit margin information by business. In overall terms, the gross profit margins for non-consolidated business units and outlet stores are 57.6% and 30.6%, respectively, with other costs estimated at around ¥1.0 billion.

**Q.** UNITED ARROWS LTD. has assumed little or no increase in outlet store profit margins. Why is this?

**A.** During the previous fiscal year, we temporarily raised the proportion of specialty merchandise at outlet stores. We plan to return to historic merchandise mix levels in the current fiscal year with specialty merchandise comprising around 30% of the total. Rather than randomly increasing specialty merchandise offerings, we will focus more on reducing inventories through transfers from regular stores.

*(Plans relating to the opening of new stores)*

**Q.** With respect to the opening of new stores during fiscal 2012, is there room for further future increase?

**A.** At this stage, we are narrowing our activities to focus on stores with a high degree of certainty. In the second half, we anticipate a positive upward trend with respect to the opening of new stores. There is the possibility that the number of new stores to be opened will increase in February and March 2012.

**Q.** For which brands are you fielding the most inquiries regarding the opening of new stores?

**A.** Inquiries regarding the BEAUTY&YOUTH UNITED ARROWS and UNITED ARROWS green label relaxing brands, which are expected to drive future medium-term growth, are strong. There are also promising signs that demand for stores in such new sales channels as railway stations and along expressways will increase.

**Q.** The number of COEN stores, also recognized as fueling medium-term growth, to be opened is low. Is there any possibility that this number will be increased during fiscal 2012?

**A.** Plans are in place for three new COEN stores to be opened during the fiscal 2012. Taking into account

the relocation of an existing store within the same district, there are actually four new stores to be opened, with the potential to increase this number during the period. Our intention is to boost the number of stores in fiscal 2013 and over a three-year span to open between eight and 10 stores annually. The UNITED ARROWS Group has in the past put in place a policy of accelerating the pace of new store openings. Our mission for the current fiscal year is to consolidate our operations and concentrate more on raising profitability.

*(Selling, general and administrative (SG&A) expenses)*

**Q.** What are your thoughts regarding operating overhead budgets?

**A.** We have not disclosed SG&A expense forecasts on an individual line item basis. We will however, carry forward from the previous fiscal year efforts to bolster advertising and promotions. Plans call for large-scale UNITED ARROWS green label relaxing promotions, initiatives to boost sales of our own online store, TV commercials as well as other measures including the upgrade and expansion of catalogues. Moreover, personnel expenses will naturally rise in line with the opening of new stores. On a year-on-year basis, UNITED ARROWS LTD. will cut back on maintenance and repairs, store furniture and fixtures, consumables, and related expenses. Our aim is to implement a diversified cost control policy, investing where necessary and cutting back as required.

**Q.** Please provide us with details if UNITED ARROWS LTD. has decided on a specific advertising strategy utilizing social and mass media.

**A.** In addition to using print media, UNITED ARROWS LTD. has historically relied primarily on SNS and other social media. Coordinating each of the aforementioned, our strategy will revolve around increasing the number of customers on a comprehensive basis encompassing both our brick-and-mortar as well as online stores. Specific details and development are to follow.

**Q.** Personnel expenses remain stagnant during fiscal 2011. Given the Group's plans to open new stores, how do you propose controlling personnel expenses?

**A.** We intend to control personnel expenses at two distinct levels. The first is head office personnel costs. Over the past three years, UNITED ARROWS LTD. has worked diligently to clarify head office personnel requirements and expenses and to streamline its workforce to an optimum minimum level. Our focus has been on eliminating waste between head office and business operations. As a result, the ratio of personnel expenses to total expense will not increase even with an improvement in the Group's revenues and top line. On the front lines, a labor control system was introduced at UNITED ARROWS green label relaxing stores with steps being taken to promote cross-sectional expansion including the UNITED ARROWS and BEAUTY&YOUTH UNITED ARROWS businesses. As this system is increasingly

adopted throughout the Group, we anticipate improved operating efficiencies. Addressing personnel expenses from each of these perspectives, we are confident of our ability to appropriately control personnel expenses over the medium term.

***Impact of the earthquake disaster and issues relating to electric power supplies during summer***

**Q.** There are concerns that supplies of electric power will be cut back during summer. What operating measures do you plan to take over this period?

**A.** We are in discussions with individual commercial facilities. Policies and strategies differ with each outlet. Government directives are to be implemented shortly. Thoughts are being given to formulating a policy while probing for future trends. Scenarios that include the closing of businesses on certain days and the shortening of operating hours are not of any benefit to customers. We hope to continue business as usual while doing our utmost to conserve energy.

**Q.** How do you view changes in purchasing trends since the earthquake and what are your thoughts and concerns regarding demand for electric power over the summer?

**A.** In all honesty, we are very much in the dark with respect to the future. Three weeks after the earthquake disaster, our business across affected areas has fully recovered. Results in the Sendai area are robust with existing store growth rates in eastern Japan higher than those in the west. Leading up to the earthquake, sales entered a recovery trajectory as consumers looked to enjoy life's immediate pleasures after a prolonged period of penny-pinching. This trend appears to be gathering momentum. Under these circumstances, consumers, who are seeking enjoyment through the purchase of clothing, are helping to drive up sales. Turning to the impact of measures implemented to conserve electric power over the summer, we are at a loss to gain a clear picture of the future.

***Overseas manufacturing and the sharp rise in costs***

**Q.** The cost of cotton fiber is rising sharply. What are your thoughts on costs?

**A.** The cost of cotton fiber has doubled over the past year. Private label product procurement costs related to manufacturing in China, including fabrics, accessories, and labor charges, have risen 10%. As a countermeasure, we are taking steps to secure factory capacity as quickly as possible, accelerating planning and increasing efficiency. Through these initiatives, which account for approximately 20% of the Group's total, we plan to hold the aggregate increase in procurement costs to between 2.0% and 2.5%, including purchased merchandise as well as private label products manufactured in areas other than China. By lifting the precision of our planning activities and increasing the inventory reduction rate, we will achieve our established gross profit target.

**Q.** What are your thoughts about overseas manufacturing?

**A.** Private label products manufactured in China make up around 20% of all products. While giving careful thought to expanding our share in the ASEAN market through a “China Plus One” strategy, we recognize the critical need to clarify the status of operations at the approximately 50 factories in the Tohoku area of Japan.

**Q.** What impact will the sharp rise in costs have on the Group’s operations and what countermeasures are planned for the future?

**A.** Turning first to manufacturing activities in China, raw material and labor costs have risen sharply over the past several years. Up to the autumn and winter seasons of 2010, procurement costs were reduced thanks largely to the strong yen. Looking at the period up to the spring and summer seasons of 2011, we anticipate little or no affect from increases in costs and other factors. Depending of course on future fluctuations in exchange rates, we expect continued upward pressure with respect to costs and labor charges. In addition to measures implemented through ongoing operations, we will also consider a shift in production to alternative locations. Procurement costs are estimated to have a slight impact from the autumn and winter seasons of 2011. UNITED ARROWS LTD. is accordingly working to secure capacity at factories, to consolidate orders across the Company as a whole, and to increase efficiency by quickly determining plans. From the spring and summer seasons of 2012 and beyond, there are no factors that suggest costs will fall. On this basis, UNITED ARROWS LTD. will pursue increased efficiencies and consider the shift of production against the backdrop of domestic manufacturing. We intend to overcome any difficulties imposed by the sharp hike in procurement costs through product pricing policies, efforts to minimize opportunity loss, and other sales operating initiatives.

***The status and direction of medium-term business strategies***

*(New sales channels)*

**Q.** Will new brands comprise the bulk of new store openings using traffic channels, or will traffic channels revolve around existing brands?

**A.** UNITED ARROWS LTD. intends to pursue traffic channels based on a cross-selling model that involves a mix of multiple businesses. We will make a decision regarding specific brands and then employ a mix.

*(Overseas strategy)*

**Q.** What regions is UNITED ARROWS LTD. looking at with respect to its overseas business

development?

A. At this stage, Asia is our highest priority when it comes to the opening of new stores. This includes such countries as China, Hong Kong, Taiwan, and Singapore. We also see promise for development of our online sales business. In this context, we will identify our overall options and put in place a fixed policy some time during the current fiscal year. Taking into consideration the select shop business model adopted by the Company, cost ratios are higher compared with other types of businesses. To succeed in overseas markets, there are accordingly significant hurdles to overcome. For this reason, venturing overseas is not a simple task. Having said this, UNITED ARROWS LTD. is genuinely considering the Chinese market, which is projected to enjoy notable growth in the future.

Q. What role will overseas business expansion play in increasing earnings over the medium to long term?

A. We are confident that from a long-term perspective, operations in Asia will contribute to the Group's overall earnings. Realistically speaking, however, any new business will encounter pitfalls and difficulties. Compared with other specialty store retailer of private label apparel (SPA) business models, the select shop model in particular poses significant obstacles. Once these difficulties have been overcome, and the business has reached a certain size and scale—for example ¥5.0 billion or more—substantial synergies with domestic operations are sure to emerge, which in turn help hold down costs. Taking the aforementioned into account, UNITED ARROWS LTD. is therefore channeling its energies toward wide-ranging methods aimed at overcoming any impediment to earnings while at the same time working to minimize the impact of difficulties encountered.

*(The licensing business and alliances)*

Q. What prospects are there for the licensing business and forming future alliances?

A. Our licensing activities currently cover between 50 and 100 items. This is an underdeveloped area and we are examining opportunities. Fiscal 2012 will most likely be used to solidify a direction and policy. Concrete action will be undertaken at a later date.

***Other***

Q. After putting in place a new management structure, what changes will be made in how top executives (Osamu Shigematsu, Tetsuya Iwaki, Mitsuhiro Takeda, and Mitsunori Fujisawa) use their time?

A. We will continue the structure of the past two years under which the Company's two representative directors will serve concurrently as executive officers directly overseeing frontline operations. Day-to-day operations will fall under the purview of Messrs. Takeda and Fujisawa. Mr. Iwaki will assume responsibility for strengthening the operations of affiliated companies. Mr. Shigematsu will provide

advice as he has in the past.

**Q.** What is the potential for opening BEAUTY&YOUTH UNITED ARROWS and UNITED ARROWS green label relaxing stores? What is the maximum number of store opening being contemplated?

**A.** We estimate there is potential to open around 100 stores in Japan under the UNITED ARROWS green label relaxing and COEN formats. While looking closely at further enhancing the quality of BEAUTY&YOUTH UNITED ARROWS stores, we are contemplating opening up 70 to 80 stores.

**Q.** Forecast profit margins for fiscal 2012 were essentially unchanged. Is it correct to assume that the Group is basically targeting double digits?

**A.** There is no change to the Group's principle target of a 10% ordinary income margin. While the Group recognizes that those regions in which stores are scheduled to be opened offer reduced profitability, the Group's future growth driver BEAUTY&YOUTH UNITED ARROWS, UNITED ARROWS green label relaxing, and COEN businesses boast high profit margins based on their higher proportion of SPA activities. Looking at the Group's portfolio as a whole, the share of these businesses is also projected to rise. In addition, the UNITED ARROWS Group plans to lift its brand value by adopting a brand equity growth strategy. Through these means we intend to boost earnings capacity. Moreover, when considering business infrastructure personnel expense control, the UNITED ARROWS Group has set a target of 10% over the medium to long term. Potential also exists to achieve management targets in excess of this figure. UNITED ARROWS LTD. will disclose quantitative targets in November 2011.

**Q.** How many stores have introduced LED lighting?

**A.** Effectively all stores have now introduced LED lighting. Each store, however, has areas where LED lighting cannot be installed. As a result, the conversion to LED lighting stands at around 60%.

**Q.** What is the mix between private label products and purchased products?

**A.** The mix is essentially unchanged. Private label products account for approximately 40% of the total.

**Q.** What has been the reaction of customers to the order to take action imposed on the Company regarding errors in the display of the country of origin of certain merchandise?

**A.** UNITED ARROWS LTD. set up a dedicated line to field customer inquiries regarding the Company's erroneous display of the country of origin of certain merchandise. There has been little or no reaction by customers either through this dedicated line or at stores.