

MANAGEMENT'S DISCUSSION OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Financial information contained in this section is based on the consolidated financial statements included in this annual report, which have been prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP). The Wacoal Group consists of 37 consolidated subsidiaries and 9 affiliates accounted for by the equity method. Wacoal Corp. is engaged in the manufacturing, wholesaling, and—

for certain products—retailing of women's foundation garments and lingerie, nightwear, children's underwear, outerwear and sportswear, hosiery, and other textile products. Other operations include restaurant businesses, cultural and service-related operations, and the construction of interiors for commercial premises. In fiscal 2004, ended March 31, 2004, the following four companies were newly included in the consolidated financial statements.

Subsidiary: Dalian Wacoal Co., Ltd. (China)

Affiliates accounted for by the equity method: Wacoal Malaysia Sdn. Bhd. (Malaysia),

House of Rose Co., Ltd. (Japan) and New Urban Co., Ltd. (Japan)

BUSINESS OVERVIEW

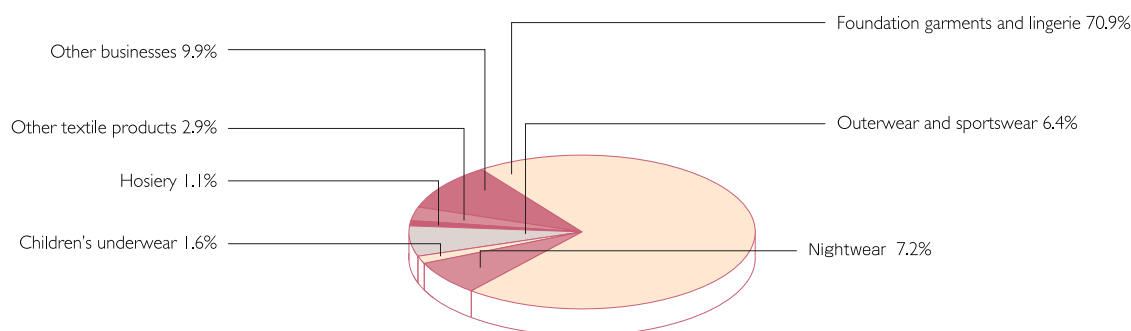
Wacoal is a leading designer, manufacturer, and marketer in Japan of women's intimate apparel, with the largest share of the Japanese market for foundation garments and lingerie. In fiscal 2004, foundation garments—primarily brassieres and girdles—and lingerie—primarily slips, bra-slips, and ladies' briefs—accounted for 70.9% of consolidated net sales. We also design, manufacture, and sell nightwear, children's underwear, outerwear and sportswear, hosiery,

and other textile products and engage in several business lines that are ancillary to our core intimate apparel business.

Revenues

We principally generate revenues from sales of the above-mentioned products. The following table sets forth information with respect to our total sales by product category for the fiscal years ended March 31, 2004, 2003, and 2002.

Share of Net Sales (2004)



Sales by Product Category

	Millions of yen			% Change 2004 vs 2003
	2004	2003	2002	
Foundation garments and lingerie	¥115,674 (70.9)	¥116,741 (71.3)	¥116,096 (71.3)	-0.9
Nightwear	11,823 (7.2)	12,710 (7.8)	12,714 (7.8)	-7.0
Children's underwear	2,583 (1.6)	2,515 (1.5)	2,470 (1.5)	+2.7
Outerwear and sportswear	10,409 (6.4)	9,440 (5.8)	9,588 (5.9)	+10.3
Hosiery	1,798 (1.1)	1,672 (1.0)	1,777 (1.1)	+7.5
Other textile products	4,658 (2.9)	4,299 (2.6)	3,793 (2.3)	+8.4
Other businesses	16,210 (9.9)	16,332 (10.0)	16,391 (10.1)	-0.7
Total	¥163,155 (100.0)	¥163,709 (100.0)	¥162,829 (100.0)	-0.3

Note: Figures in parentheses represent percent of total sales.

In fiscal 2004, approximately 80% of our total sales were apparel sales made on a wholesale basis to department stores, general merchandising stores, and other general retailers, and approximately 10% were apparel sales made through our SPA specialty shop, mail-order catalog, and Internet sales channels. Sales from other businesses, which include the sale of mannequins, store design and construction, housing design, restaurant businesses, cultural projects, and other services, accounted for the remaining 10% of our total sales in fiscal 2004.

Over the past five fiscal years, fluctuations in our sales have typically reflected changes in unit volume, as average unit prices have generally remained stable during this period.

Cost of Sales

Our cost of sales arises principally from material, labor, and other manufacturing costs related to the production of our apparel products.

Selling, General and Administrative Expenses

Our selling, general and administrative expenses principally consist of compensation and benefits for employees in our textile business and promotional expenses, such as advertising costs and expenses associated with remodeling our sales counters at department stores. Other selling, general and administrative expenses include shipment costs, payment fees, including outsourcing payments, and rents for SPA shops.

KEY INDUSTRY TRENDS

We believe that the following have been key trends in our industry during the last three fiscal years:

- Consumer spending in Japan has generally been stagnant, which has negatively impacted performance at general retailers, our key distribution channel.
- The sale of lower-priced garments in Japan—to a large degree manufactured in China and other lower-cost countries—has increased. This has generally resulted in a greater degree of price competition in our industry.
- There has been increased demand for higher-end innerwear products. This phenomenon combined with increased demand for lower-end products has resulted in greater market segmentation.
- Manufacturers have placed growing importance on reducing costs by sourcing fabric and producing garments in China and other lower-cost countries.
- Alternative marketing concepts, such as catalog marketing and e-commerce, are becoming more prevalent as apparel companies seek to diversify their sales channels and reach new customer groups.

During the last three fiscal years, we have taken steps to address these key industry trends, building on the core strengths of our strong market position and brand awareness with Japanese consumers. We believe that our strategic emphasis on higher-end products has helped us to reach consumers seeking high-quality innerwear garments, and to mitigate the adverse impact on sales and margins from lower priced garments. To reduce expenses, we are producing more of our apparel in lower-cost countries, such as China and Vietnam, and we have reduced the number of our product distribution centers and expanded our early retirement program. We are also seeking to expand sales in overseas markets—in particular China, the U.S., and Europe—and enlarge the percentage of our overall sales made through our own SPA specialty retail stores, catalog sales, and the Internet. We plan to continue implementing these steps and others to address challenges and opportunities in the industry going forward.

REVIEW OF OPERATIONS

Consolidated net sales edged down 0.3% in fiscal 2004, to ¥163,155 million.

Sales of products of our mainstay innerwear business, consisting of foundation wear, nightwear, and children's underwear, which comprises 79.7% of total consolidated sales, decreased 1.5% in fiscal 2004, to ¥130,080 million. A principal factor in this decrease was reduced sales of our mid-priced innerwear products. For example, sales of our *Wing* brand products declined 2.9% in fiscal 2004, reflecting lower customer demand for these products. Additionally, we believe that the adverse effect of unseasonable weather in Japan during the summer and fall months hurt our innerwear sales. Unusually cold weather in the summer months negatively impacted our typical slight seasonal increase in innerwear sales in the summer season, as many women tend to purchase new undergarments to accompany their lighter summer wardrobes. Also, the unusually warm fall in Japan hurt sales of our cool weather innerwear products.

Sales of our high-end innerwear garments and campaign products supported our sales performance in fiscal 2004. Several of our high-end innerwear products achieved significant sales growth, including *La Vie Aisée*, a brand for older women (¥4,408 million in sales, representing a 16.4% sales increase from fiscal 2003); *Parfage*, a brand designed specifically for career women (¥5,276 million in sales, representing a 6.0% sales increase from fiscal 2003); and *Salute*, a boutique brand (¥3,354 million in sales, representing a 14.2% sales increase from fiscal 2003). Our leading *Wacoal* brand seasonal campaign products in fiscal 2004 were *T-Shirt bra NAMI-NAMI*, launched in summer 2003 (sales of 850,000 pieces in fiscal 2004), and *Kanjiru Bra*, launched in fall 2003 (sales of 700,000 pieces in fiscal 2004). Product sales at our SPA specialty shops were up ¥1.6 billion in fiscal 2004, reflecting the addition of 17 stores during the year.

Despite our efforts to increase sales in our key markets outside Japan, these sales remained flat in fiscal 2004. Our sales in Asia outside of Japan, including China, Hong Kong, and Singapore, which repre-

sented 3.0% of total consolidated sales in fiscal 2004, were adversely affected by the SARS outbreak and the depreciation of the currencies of these countries against the yen. In the United States, which represented 7.5% of total consolidated sales in fiscal 2004, our sales during the first half of fiscal 2004 decreased 7.7%, due in part to weakened consumer spending stemming from the war in Iraq. Although U.S. sales on a unit basis rebounded during the second half of the fiscal year (13.5% more than fiscal 2003), this improvement was largely offset by the dollar's decline against the yen.

In our other apparel businesses, sales of outerwear and sportswear in fiscal 2004 increased 10.3%, or ¥969 million, driven principally by sales growth in our CW-X conditioning wear line. Hosiery sales, which include products sold under our *Carlson* label, increased ¥126 million, or 7.5%, to ¥1,798 million in fiscal 2004. Sales from our other businesses, which include the sale of mannequins, store design and construction, housing design, restaurant businesses, cultural projects, and other services, declined slightly to ¥16,210 million in fiscal 2004, or 0.8%, from ¥16,332 million in the previous year.

Our cost of sales decreased 0.8%. Cost of sales as a percentage of net sales decreased 0.2 percentage points from 52.1% to 51.9% in fiscal 2004, due largely to an increase in the proportion of our products produced in China, Vietnam, and other low-cost overseas manufacturing centers (from 16% in fiscal 2003 to 20% in fiscal 2004 on a unit basis). Reduced material costs, reflecting the effects of deflation in Japan and efforts by our suppliers to reduce their costs, also contributed to the decrease.

Selling, general and administrative (SG&A) expenses increased to ¥75,501 million in fiscal 2004, or 6.1%, from ¥71,139 million in fiscal 2003. Items that drove the increase in SG&A expenses included the following:

- We recognized a one-time impairment loss of ¥2,574 million on properties we own in Japan, which resulted from a change of our business plan in 2004 with respect to the use of certain assets, including buildings and land;
- Promotional activity expenses increased by ¥1,020 million, or 9.0%, in fiscal 2004, reflecting increased costs associated with the refurbishment of our sales counters at department stores and chain stores, increased television advertising, and start-up costs for our new *wannabe* innerwear mail-order catalog sales channel;
- Net amortization of unrecognized net actuarial loss rose ¥1.3 billion, or 72.1%, year on year, due to an increase in unrecognized net actuarial loss on the assets of pension plans in the previous fiscal year; and
- Rent costs increased ¥363 million, or 12.9%, in fiscal 2004, principally due to the opening of 17 new SPA specialty stores during fiscal 2004.

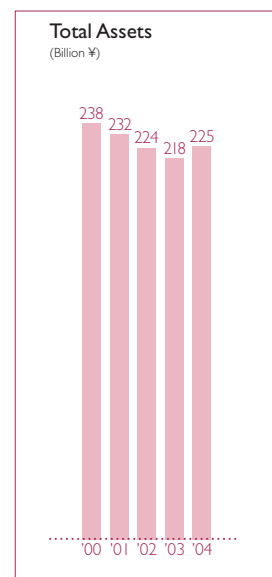
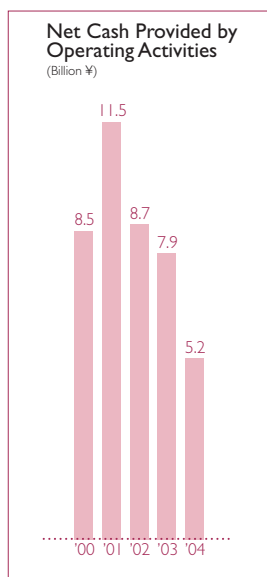
We had net other income of ¥1,516 million in fiscal 2004, compared with net other expenses of ¥2,660 million in fiscal 2003. This result was mainly attributable to a decrease in valuation losses on investment securities from ¥3,566 million in fiscal 2003 to ¥142 million in fiscal 2004, reflecting improvement in the Japanese equity markets in fiscal 2004 as compared with prior years. Also contributing to net other income was a gain of ¥932 million on the sale of equity securities.

Due to the above factors, net income in fiscal 2004 was ¥2,902 million, which was approximately the same amount as in fiscal 2003. Net income per American Depositary Receipt (“ADR,” equivalent to five shares of common stock) increased from ¥97 in fiscal 2003 to ¥99 in fiscal 2004.

LIQUIDITY AND CAPITAL RESOURCES

Our main source of liquidity is cash from operations. Our cash from operations has allowed us to fund our working capital requirements and our capital expenditures, including our SPA specialty shop expansion, without material borrowings or other external financing. We believe that we consistently generate and maintain sufficient cash to cover our needs for working capital for our operations and for our anticipated capital requirements and other expenditures. Some of our overseas subsidiaries also currently maintain credit facilities with bank lenders for working capital purposes.

Capital expenditures in fiscal 2004 and 2003 were ¥2,338 million and ¥2,104 million, respectively. In fiscal 2004, our most significant capital expenditures were incurred in connection with the addition of 17 stores to our SPA specialty shop network and improvement of IT infrastructure in Japan. We made significant capital expenditures in fiscal 2002 and 2003 in connection with the establishment and development of our SPA specialty shop network, to purchase computer equipment for the Wacoal Corp. parent entity, and to construct a new factory for Saradona Mfg. Corp., our



subsidiary operating in the Dominican Republic.

In fiscal 2005, we expect that our principal capital expenditures will be for the expansion of our SPA specialty shop network by approximately 15 stores (approximately ¥0.5 billion) and the construction of our Dalian, China, production facility (approximately ¥1.0 billion).

Cash Flows

Net cash provided by operating activities decreased to ¥5,201 million in fiscal 2004, or a 33.8% decrease from ¥7,858 million in fiscal 2003. The decrease resulted primarily from a significant build-up in product inventory of ¥2,124 million at the end of fiscal 2004, caused principally by overstock of certain fall/winter items and build-up in anticipation of the summer season.

Net cash provided by investing activities was ¥1,328 million in fiscal 2004, compared with ¥9,839 million used in investing activities in fiscal 2003. Net cash provided by investing activities in fiscal 2004 was mainly attributable to an ¥11,594 million, or 17.1%, year-on-year decrease in amounts spent to acquire marketable securities.

This decrease was offset in part by a ¥1,540 million increase in payments to acquire investments, which relates principally to our acquisitions of House of Rose Co., Ltd., and Wacoal Malaysia Sdn. Bhd. in fiscal 2004.

Net cash used in financing activities increased to ¥6,138 million in fiscal 2004 from ¥6,006 million in fiscal 2003. The increase is mainly attributable to the repayment of ¥1,595 million in short-term loans by certain of our subsidiaries; our payment of ¥2,456 million in connection with a share repurchase; and the payment of cash dividends of ¥1,987 million. We expect to pay cash dividends of ¥2,159 million in fiscal 2005, and we will consider additional repurchases of our shares.

MARKET RISKS

Our business, performance, and financial condition are subject to risks and uncertainties, including the following risk factors. These risks and uncertainties could result in a material adverse effect on Wacoal and a material decline in the trading price of our common stock and ADRs.

1. Continued weak consumer spending in Japan would hurt our business.
2. Continued weakness of department stores and other general retailers in Japan would hurt our business.
3. Our success depends on our ability to effectively anticipate and respond to consumer tastes and preferences.
4. We are subject to inventory risks that could negatively impact our operating results.
5. Growth in our profitability will depend in large part on our ability to reduce costs.
6. We may experience difficulties in successfully expanding our SPA specialty shop network.
7. We may experience difficulties in successfully increasing our catalog and Internet sales.
8. Our business is highly competitive.
9. Our business is affected by seasonality.
10. We may face increasing risks relating to conducting business internationally.
11. Our holdings of equity securities expose us to risks.
12. We may be adversely affected by our employee benefit obligations.
13. We may become a passive foreign investment company in the future, which could result in adverse U.S. tax consequences to U.S. holders of our stock or ADRs.
14. Yen-dollar fluctuations could cause the market price of the ADRs to decline and reduce dividend amounts payable to ADR holders as expressed in U.S. dollars.
15. Holders of ADRs, will have fewer rights than a shareholders, and must act through the depositary to exercise those rights.
16. There are restrictions on the withdrawal of shares from our depositary receipt facility.



FORWARD-LOOKING STATEMENTS

Statements contained in this annual report that are not historical facts are forward-looking statements that reflect Wacoal's plans and expectations. These forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause the Company's actual results, performance, or achievements to differ materially from those anticipated in these statements.

CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of the financial statements requires our management to make estimates and assumptions. We believe that the following are some of the more critical judgment areas in applying our accounting policies in the preparation of our consolidated financial statements.

Valuation of Inventories

Inventories are stated at the lower of cost or market, cost being substantially determined on the first-in, first-out method for raw materials and the average cost method for work in process and finished products. We continuously review our inventories for their salability and for indications of obsolescence to determine if a write-down to market value is necessary. The revaluation of inventories is based on the age of inventories, likelihood of obsolescence, actual product movements, changes in market demand, and other factors.

Allowance for Doubtful Receivables and Returns

We are required to assess the collectibility of notes and accounts receivable. A considerable amount of judgment is required in assessing the ultimate realization of these notes and receivables, including the current creditworthiness of each applicable customer taking into account business conditions, the turnover of receivables, and financial positions for significant customers. In the event that a customer's financial condition worsens, the allowance for doubtful receivables may increase and may adversely affect our financial condition and performance.

We allow our customers to return their unsold products when the customers meet certain criteria established by us, as outlined in our applicable trade terms. We establish the allowance for estimated returns based on historical experience, and we regularly review and revise the allowance if necessary, in consideration of actual returns, planned product discontinuances, and promotional sales. We record the allowance for estimated returns as a reduction to sales.

Deferred Tax Assets

We currently have significant deferred tax assets and liabilities, which are subject to periodic recoverability assessments. The realization of our deferred tax assets is principally dependent upon the achievement of projected future taxable income. Our judgments regarding future profitability may change due to future market conditions and other factors. These changes, if any, may require recognition of a significant valuation allowance for these deferred tax asset balances. In the event we determine that certain deferred tax assets may not be recoverable, such amounts will be reserved for and may adversely affect net income.

Impairment of Investment Securities

An impairment of investment securities is charged to earnings when a decline in fair value below the cost is other than temporary. Management principally considers that an other-than-temporary impairment has occurred when the decline in fair value below the carrying value continues for over nine consecutive months. The Company may also consider other factors, including its ability and intent to hold the applicable investment securities and the severity of the decline in fair value.

Management believes that the criteria for evaluating impairment are

reasonable; however, changes in the market or circumstances of each individual investment due to unforeseen changes in economic and business assumptions could affect the valuations of the investments.

Impairment of Long-Lived Assets

When we determine that long-lived assets and certain intangible assets held have been impaired based on estimated future cash flows, the amount of carrying value in excess of the fair market value of such assets is recognized as impairment loss. We believe that our assessment of estimated future cash flows and the fair values of such assets has been reasonably performed. However, changes in estimated future cash flows and fair values may affect our impairment assessment.

Employee Retirement Plans

We provide a number of retirement benefit plans to a substantial portion of our employees. We have a contributory retirement plan and certain subsidiaries have qualified pension plans. The amount of the projected retirement benefit obligation and pension costs are dependent on management's assumptions used by actuaries in calculating such amount. The key assumptions include discount rates, the expected long-term rate of return on plan assets, retirement rates, mortality expectations, and other factors. Our management believes that these actuarial assumptions and methods are appropriate in light of our circumstances. However, due to a change in an actuarial assumption, the amount of the projected retirement benefit plan liabilities and costs may be adversely affected.

Our approach to establishing the discount rate is based upon the national debt and corporate bond indices. The discount rate assumption is based upon the five-year average of the effective yields on the 20-year national debt, adjusted for an incremental yield of approximately 25 basis points that is achieved by selecting corporate bonds whose credit characteristics satisfy the quality requirements but whose yields are slightly higher than the national debt. At March 31, 2004, the discount rate used for the contributory retirement plan was 2.5%. For other plans, similar indices and methods are used.

We determine the expected long-term rate of return on plan asset assumptions by evaluating both historical returns as well as estimates of future returns. Our expected return on assets was based on expected equity and debt securities returns weighted by the percentage of each of the major asset classes. Our estimates of the long-term rate of return on assets for the contributory retirement plan are 2.5%, and 3.0% for the years ended March 31, 2004 and 2003, respectively. The estimated long-term rate of return is based on an asset allocation of equity securities of 60.0%, debt securities of 22.0%, and other investments of 18.0%.

These assumptions have a significant effect on the amount of the obligation and periodic benefit cost reported. A half-percentage-point change in the discount rate and the expected long-term rate of return on plan assets would have the following effects:

	Millions of Yen		Thousands of U.S. Dollars	
	0.5 Percentage Point Decrease	0.5 Percentage Point Increase	0.5 Percentage Point Decrease	0.5 Percentage Point Increase
Discount rate:				
Effect on periodic benefit costs	¥ (145)	¥ 152	\$ (1,392)	\$ 1,459
Effect on benefit obligation	¥5,117	¥(4,651)	\$49,117	\$ (44,644)
Expected long-term rate of return on plan assets:				
Effect on periodic benefit costs	¥ 123	¥ (123)	\$ 1,181	\$ (1,181)
Effect on benefit obligation	¥ 0	¥ 0	\$ 0	\$ 0



La Vie Aisée

In accordance with the Defined Benefit Pension Plan Law enacted in April 2002, the Company applied for an exemption from the obligation to pay benefits for employee services related to the substitutional portion which would result in the transfer of the pension obligations and related assets to the government upon approval. In January 2003, the Company received approval from the government for an exemption from the obligation to pay benefits for future employee service related to the substitutional portion. In January 2004, the Company received approval for exemption of the benefit obligation for past service related to the substitutional portion. (Note 8 to Consolidated Financial Statements, page 31)



Tréfle



Swimwear



Maternity



Imported products



CW-X

Eleven-Year Financial Summary

WACOAL CORP. AND SUBSIDIARIES
Years ended March 31

	2004	2003	2002
For the year:			
Net sales	¥163,155	¥163,709	¥162,829
Cost of sales	84,638	85,306	86,567
% of net sales	51.9%	52.1%	53.2%
Selling, general and administrative expenses	75,501	71,139	69,076
% of net sales	46.3%	43.5%	42.4%
Operating income	3,016	7,264	7,186
Other income and expenses, net	1,404	(2,800)	310
Net interest income (expense)	112	140	117
Income before income taxes, equity in net income of affiliated companies and minority interests	4,532	4,604	7,613
Income taxes	2,520	2,487	3,785
Net income	2,902	2,898	4,983
Return on assets	1.3%	1.3%	2.2%
Return on equity	1.8%	1.8%	2.9%
Net cash provided by operating activities	5,201	7,858	8,653
Net cash provided by (used in) investing activities	1,328	(9,839)	(9,412)
Net cash used in financing activities	(6,138)	(6,006)	(5,472)
Depreciation and amortization	3,081	2,971	3,533
Capital expenditures	2,338	2,104	2,484
Per 5 shares of common stock (in yen):			
Net income	¥ 99	¥ 97	¥ 166
Cash dividends	75	68	68
Shareholders' equity	5,931	5,487	5,640
At year-end:			
Total current assets	¥123,045	¥124,486	¥127,390
Total current liabilities	33,094	33,576	37,095
Cash and cash equivalents	27,443	27,246	35,381
Net property, plant and equipment	49,932	54,171	57,291
Total assets	224,803	218,105	223,985
Short-term bank loans and long-term debt, including current portion	4,450	6,301	8,079
Total shareholders' equity	170,758	160,839	168,205

Millions of Yen

2001	2000	1999	1998	1997	1996	1995	1994
¥162,023	¥165,937	¥169,996	¥169,967	¥168,330	¥159,162	¥153,170	¥150,830
87,493	89,290	91,951	91,474	90,640	85,470	83,162	83,421
54.0%	53.8%	54.1%	53.8%	53.8%	53.7%	54.3%	55.3%
64,906	65,530	66,613	62,066	65,291	61,942	59,353	57,677
40.1%	39.5%	39.2%	36.5%	38.8%	38.9%	38.7%	38.2%
9,624	11,117	11,432	16,427	12,399	11,750	10,655	9,732
10,443	338	595	(110)	549	937	416	787
62	(54)	195	256	324	619	935	1,138
20,129	11,401	12,222	16,573	13,272	13,306	12,006	11,657
9,058	4,961	4,749	8,170	7,018	7,181	6,119	6,985
10,889	7,254	8,489	8,929	7,336	7,227	6,688	7,229
4.6%	3.1%	3.6%	3.9%	3.2%	3.2%	3.4%	4.0%
6.3%	4.2%	5.0%	5.5%	4.6%	4.6%	4.7%	5.6%
11,480	8,451	8,813	12,971	5,474	11,231	12,015	10,518
(13,686)	(9,624)	(10,624)	2,045	962	(5,044)	(1,203)	(5,656)
(6,478)	(2,611)	(105)	(296)	(7,882)	(3,412)	(2,559)	(2,933)
3,265	3,157	2,447	2,269	2,368	2,404	2,643	2,734
1,182	7,757	8,604	5,941	2,480	1,555	2,958	3,910
¥ 356	¥ 235	¥ 275	¥ 290	¥ 236	¥ 228	¥ 211	¥ 229
83	68	68	68	68	68	68	68
5,709	5,632	5,485	5,314	5,219	4,573	4,398	4,273
¥129,508	¥127,734	¥129,206	¥130,319	¥117,579	¥116,705	¥105,153	¥100,822
41,449	38,490	39,541	42,319	37,884	41,861	35,720	34,993
41,196	49,889	53,933	55,622	40,313	41,350	38,443	30,545
58,644	59,990	56,339	52,878	50,482	50,914	51,698	51,913
232,262	237,721	233,817	231,226	226,103	238,634	214,792	181,554
8,865	9,658	10,649	8,602	6,757	7,025	8,135	4,944
172,558	173,612	169,065	163,800	160,869	160,926	150,390	131,719

Consolidated Balance Sheets

WACOAL CORP. AND SUBSIDIARIES
March 31, 2004 and 2003

ASSETS	Millions of yen		Thousands of U.S. Dollars (Note 2)
	2004	2003	2004
Current Assets:			
Cash and cash equivalents:			
Cash	¥ 6,847	¥ 7,084	\$ 65,723
Time deposits and certificates of deposit	20,596	20,162	197,696
Total	27,443	27,246	263,419
Marketable securities (Note 3)	44,316	48,250	425,379
Notes and accounts receivable:			
Trade notes	1,226	1,742	11,768
Trade accounts	19,053	18,688	182,885
Allowance for returns and doubtful receivables (Note 4)	(2,140)	(2,288)	(20,541)
Inventories (Note 5)	26,060	24,346	250,144
Deferred income taxes (Note 11)	5,219	4,653	50,096
Other current assets	1,868	1,849	17,931
Total current assets	123,045	124,486	1,181,081
Property, Plant and Equipment (Note 6):			
Land	19,910	22,924	191,112
Buildings and building improvements	55,879	55,801	536,370
Machinery and equipment	12,413	12,248	119,149
Construction in progress	370	78	3,551
Total	88,572	91,051	850,182
Accumulated depreciation	(38,640)	(36,880)	(370,896)
Net property, plant and equipment	49,932	54,171	479,286
Other Assets:			
Investments in affiliates	12,838	10,840	123,229
Investments (Note 3)	29,872	17,968	286,735
Deferred income taxes (Note 11)	959	3,616	9,205
Lease deposits and other	8,157	7,024	78,297
Total other assets	51,826	39,448	497,466
Total	¥224,803	¥218,105	\$2,157,833

See notes to consolidated financial statements.

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of yen		Thousands of U.S. Dollars (Note 2)
	2004	2003	2004
Current Liabilities:			
Short-term bank loans (Note 6)	¥ 3,954	¥ 5,633	\$ 37,954
Notes and accounts payable:			
Trade notes	2,885	2,499	27,692
Trade accounts	9,343	8,627	89,681
Other payables	5,340	5,437	51,257
Accrued payroll and bonuses	6,895	7,520	66,184
Income taxes payable	2,724	2,796	26,147
Current portion of long-term debt (Notes 6 and 13)	374	213	3,590
Other current liabilities	1,579	851	15,157
Total current liabilities	33,094	33,576	317,662
Long-term Liabilities:			
Long-term debt (Notes 6 and 13)	122	455	1,171
Liability for termination and retirement benefits (Note 8)	14,794	20,650	142,004
Deferred income taxes (Note 11)	3,424	39	32,866
Other long-term liabilities	805	764	7,727
Total long-term liabilities	19,145	21,908	183,768
Minority Interests	1,806	1,782	17,336
Shareholders' Equity (Note 9):			
Common stock, no par value –			
authorized, 229,900,000 and 232,500,000 shares in 2004 and 2003;			
issued 144,016,685 and 146,616,685 shares in 2004 and 2003	13,260	13,260	127,280
Additional paid-in capital	25,242	25,242	242,292
Retained earnings (Note 14)	129,941	131,466	1,247,274
Accumulated other comprehensive income (loss) (Note 10):			
Foreign currency translation adjustments	(3,512)	(1,947)	(33,711)
Unrealized gain (loss) on securities	6,831	(846)	65,569
Minimum pension liability	(954)	(6,293)	(9,157)
Total accumulated other comprehensive income (loss)	2,365	(9,086)	22,701
Less treasury stock at cost – 52,860 and 46,254 shares in 2004 and 2003	(50)	(43)	(480)
Total shareholders' equity	170,758	160,839	1,639,067
Total	¥224,803	¥218,105	\$2,157,833

Consolidated Statements of Shareholders' Equity

WACOAL CORP. AND SUBSIDIARIES
Years Ended March 31, 2004, 2003 and 2002

	Shares of Outstanding Common Stock (Thousands)	Millions of Yen				Treasury Stock
		Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	
Balance, April 1, 2001	151,117	¥13,260	¥25,242	¥132,322	¥ 1,734	
Net income				4,983		
Other comprehensive loss					(4,917)	
Cash dividends paid, ¥68 per 5 shares of common stock				(2,040)		
Repurchase of treasury stock for retirement ...	(2,000)			(2,374)		
Repurchase of treasury stock — other	(5)					¥ (5)
Balance, March 31, 2002	149,112	13,260	25,242	132,891	(3,183)	(5)
Net income				2,898		
Other comprehensive loss					(5,903)	
Cash dividends paid, ¥68 per 5 shares of common stock				(2,013)		
Repurchase of treasury stock for retirement ...	(2,500)			(2,310)		
Repurchase of treasury stock — other	(42)					(38)
Balance, March 31, 2003	146,570	13,260	25,242	131,466	(9,086)	(43)
Net income				2,902		
Other comprehensive income					11,451	
Cash dividends paid, ¥68 per 5 shares of common stock				(1,978)		
Repurchase of treasury stock for retirement ...	(2,600)			(2,449)		
Repurchase of treasury stock — other	(6)					(7)
Balance, March 31, 2004	143,964	¥13,260	¥25,242	¥129,941	¥ 2,365	¥(50)

	Thousands of U.S. Dollars (Note 2)				
	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock
Balance, March 31, 2003	\$127,280	\$242,292	\$1,261,912	\$ (87,215)	\$(413)
Net income			27,856		
Other comprehensive income				109,916	
Cash dividends paid, \$0.65 per 5 shares of common stock			(18,986)		
Repurchase of treasury stock for retirement			(23,508)		
Repurchase of treasury stock — other					(67)
Balance, March 31, 2004	\$127,280	\$242,292	\$1,247,274	\$ 22,701	\$(480)

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

WACOAL CORP. AND SUBSIDIARIES
Years Ended March 31, 2004, 2003 and 2002

	Millions of Yen			Thousands of U.S. Dollars (Note 2)
	2004	2003	2002	2004
Operating Activities:				
Net income	¥ 2,902	¥ 2,898	¥ 4,983	\$ 27,856
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	3,081	2,971	3,533	29,574
Deferred income taxes	(3,254)	(2,756)	(620)	(31,234)
Loss on sale or disposal of property, plant and equipment	455	143	740	4,367
Impairment charges on long-lived assets	2,574	556		24,707
Gain on sale or exchange of investments	(932)	(436)	(502)	(8,946)
Impairment charges on investments	142	3,566	507	1,363
Undistributed earnings of affiliates, less dividends	(726)	(643)	(1,028)	(6,969)
Changes in assets and liabilities:				
(Increase) decrease in notes and accounts receivable	(46)	3,110	1,306	(442)
(Increase) decrease in inventories	(2,124)	154	1,262	(20,388)
(Increase) decrease in other current assets	(346)	(1,365)	395	(3,321)
Increase (decrease) in notes and accounts payable	1,020	(2,236)	(2,049)	9,791
Increase in liability for termination and retirement benefits	3,212	1,672	1,400	30,831
(Decrease) increase in accrued expenses, income taxes and other current liabilities	(657)	771	(1,293)	(6,306)
Other	(100)	(547)	19	(960)
Net cash provided by operating activities	5,201	7,858	8,653	49,923
Investing Activities:				
Proceeds from sales and redemption of marketable securities	59,977	59,681	29,248	575,706
Payments to acquire marketable securities	(56,019)	(67,613)	(35,148)	(537,714)
Proceeds from sales of property, plant and equipment	369	1,416	115	3,542
Proceeds from sales and redemption of investments	2,130	1	65	20,445
Capital expenditures	(2,338)	(2,104)	(2,484)	(22,442)
Payments to acquire investments in affiliated companies	(1,690)	(150)		(16,222)
Payments to acquire investments	(776)	(716)	(895)	(7,449)
Increase in other assets	(325)	(354)	(313)	(3,119)
Net cash provided by (used in) investing activities	1,328	(9,839)	(9,412)	12,747
Financing Activities:				
Decrease in short-term bank loans	(1,595)	(1,647)	(1,018)	(15,310)
Proceeds from issuance of long-term debt	49	183	521	470
Repayments of long-term debt	(158)	(181)	(556)	(1,516)
Repurchase of treasury stock	(2,456)	(2,348)	(2,379)	(23,575)
Dividends paid on common stock	(1,978)	(2,013)	(2,040)	(18,986)
Net cash used in financing activities	(6,138)	(6,006)	(5,472)	(58,917)
Effect of Exchange Rate Changes on Cash and Cash Equivalents	(194)	(148)	416	(1,862)
Net Increase (Decrease) in Cash and Cash Equivalents	197	(8,135)	(5,815)	1,891
Cash and Cash Equivalents, Beginning of Year	27,246	35,381	41,196	261,528
Cash and Cash Equivalents, End of Year	¥ 27,443	¥ 27,246	¥ 35,381	\$ 263,419
Additional Cash Flow Information:				
Cash paid for:				
Interest	¥ 114	¥ 154	¥ 231	\$ 1,094
Income taxes	5,846	4,543	5,402	56,114
Noncash Investing Activities:				
Fair value of marketable securities received in exchange for certain other marketable securities with a recorded amount of ¥60 million and ¥1,069 million in 2003 and 2002, respectively.		496	1,927	

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

WACOAL CORP. AND SUBSIDIARIES

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Financial Statements

Wacoal Corp. (the “Company”) and its subsidiaries are predominantly engaged in one industry, the manufacture and sale of apparel, including foundation garments, lingerie, nightwear and outerwear in Japan, the United States of America, Europe and certain Asian countries.

The accompanying consolidated financial statements, stated in Japanese yen, have been prepared on the basis of accounting principles generally accepted in the United States of America except for the omission of segment information as required by Statement of Financial Accounting Standards (“SFAS”) No. 131, “Disclosures about Segments of an Enterprise and Related Information”.

Consolidation

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries (collectively, the “Companies”). All significant intercompany transactions and balances are eliminated.

Certain foreign subsidiaries of the Company have a fiscal year ending December 31. The accounts of those subsidiaries are included in the Company’s consolidated financial statements based on the subsidiaries’ fiscal year.

Investments in affiliated companies where the Company’s ownership is 20% to 50% are accounted for using the equity method.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include all time deposits and certificates of deposit (all of which are interest-bearing) with original maturities of three months or less, which can be withdrawn at face value at any time without diminution of principal.

Foreign Currency Translation

Assets and liabilities of international subsidiaries have been translated to Japanese yen at period-end exchange rates and income and expenses have been translated using weighted average exchange rates for the period. Translation adjustments are included in other comprehensive income (loss). Exchange gains and losses resulting from foreign currency transactions and the conversion of monetary assets and liabilities denominated in foreign currencies are included in the consolidated statements of income.

Marketable Securities and Investments

The Companies classify their marketable debt and equity securities as available-for-sale and carry them at fair value with a corresponding recognition of unrealized holding gains or losses (net of tax) in other comprehensive income (loss), a separate component of shareholders’ equity, until realized. Equity securities that do not have readily determinable fair values

are recorded at cost. Gains and losses on sales of investments are computed based on cost determined using the average cost method.

If decline in the fair value of marketable securities is determined to be other than temporary, an impairment charge is recorded in the consolidated statements of income.

Inventories

Inventories are stated at the lower of cost or market, cost being substantially determined on the first-in, first-out method for raw materials and the average cost method for work in process and finished products.

Property, Plant and Equipment

Property, plant and equipment is stated at cost less accumulated depreciation. Depreciation of property, plant and equipment is computed by the declining-balance method, except for buildings acquired on or after April 1, 1998, which are depreciated using the straight-line method, based upon the estimated useful lives of the assets. The estimated useful lives are as follows:

Buildings and building improvements:	5 – 50 years (Mainly 38 years)
Machinery and equipment:	5 – 20 years

Impairment of Long-Lived Assets

The carrying values of long-lived assets, held and used by the Companies, are evaluated for impairment whenever there is an event or change in circumstances that indicates that such assets have been impaired or that the carrying amounts of such assets might not be recoverable. The Companies recorded ¥2,574 million (\$24,707 thousand) and ¥556 million in impairment charges on long-lived assets for the years ended March 31, 2004 and 2003, respectively, which resulted from the impairment of primarily land and buildings related to a warehouse facility in 2004, and an apartment complex in 2003 held and operated by the Companies with fair value of ¥1,252 million (\$12,018 thousand) and ¥398 million, respectively.

In 2004, as a result of changes in business plans in which the Companies reconsidered the intended use of the land and warehouse facility, the Companies evaluated the recoverability of the assets and recognized an impairment. The fair values of the land and warehouse facility were determined by an independent appraisal. In 2003, the Companies evaluated the recoverability of the apartment complex and recognized an impairment loss, due to the significant deterioration of real estate value in Japan. The fair value of the apartment complex assets was determined by the discounted cash flow approach.

Derivatives

Derivative instruments, including certain derivative instruments embedded in other contracts, are accounted for in accordance with SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities”, SFAS No. 138, “Accounting for Certain Derivative Instruments and Certain Hedging Activities as Amendment of FASB Statement No. 133” and SFAS No. 149, “Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities”. Changes in the fair value of a derivative are recorded in other comprehensive income (loss) or in earnings, depending on its intended use. The Company had no outstanding derivative contracts as of March 31, 2004.

Termination and Retirement Plans

Termination and retirement benefits are accounted for in accordance with SFAS No. 87, "Employers' Accounting for Pensions". Provisions for termination and retirement benefits include those for directors and corporate auditors of the Companies.

As allowed under SFAS No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits", the Companies do not recognize gain or loss on settlement of the pension obligation when the cost of all settlements in a year is less than or equal to the sum of the service cost and interest cost components of net periodic pension cost for the plan for the year.

Advertising Expenses

Advertising costs are expensed as incurred. Advertising expenses for the years ended March 31, 2004, 2003 and 2002 were ¥12,878 million (\$123,613 thousand), ¥11,850 million and ¥10,855 million, respectively.

Revenue Recognition

The Companies recognize revenue on sales to retailers when (1) persuasive evidence of an arrangement exists, (2) delivery has occurred resulting in transfer of title and risk of loss, (3) the sales price is fixed or determinable and (4) collectibility is reasonably assured. Retail sales are recognized at the point of sale. The Companies establish allowances for estimated returns based on historical experience. As for consignment sales, the Companies recognize revenue when the products are sold to the ultimate customer.

Income Taxes

The provision for income taxes is determined under the liability method pursuant to SFAS No. 109, "Accounting for Income Taxes". Under this method, deferred tax assets and liabilities are determined for temporary differences between the financial statements and tax bases of assets and liabilities at presently enacted tax rates. A valuation allowance is recorded when it is more likely than not that some portion or all of the deferred tax assets will not be realized in the future.

Provisions are made for taxes on undistributed earnings and cumulative translation adjustments of foreign subsidiaries whose earnings are not deemed to be permanently invested.

Reclassifications

Certain reclassifications have been made to the prior years' financial statements to conform with the current year's presentation.

Recent Accounting Pronouncements

(1) *Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities* — In April 2003, the Financial Accounting Standards Board ("FASB") issued SFAS No. 149, "Amendment of Statement No. 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS No. 133. The statement is effective for contracts entered into or modified

and for hedging relationships designated after June 30, 2003. The adoption of SFAS No. 149 had no effect on the Companies' consolidated financial statements.

- (2) *Financial Instruments with Characteristics of both Liabilities and Equity* — In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity". This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003, and for pre-existing instruments is effective in the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 had no effect on the Companies' consolidated financial statements.
- (3) *Employers' Disclosure about Pensions and Other Postretirement Benefits* — In December 2003, the FASB issued SFAS No. 132 (revised 2003), "Employers' Disclosure about Pensions and Other Postretirement Benefits". This statement revises employers' disclosures about pension plans and other postretirement benefit plans and requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans. SFAS No. 132 (revised 2003) is effective for fiscal years ending after December 15, 2003. The Companies adopted the new disclosure requirements under SFAS No. 132 (revised 2003) in the year ended March 31, 2004. (See Note 8)
- (4) *Consolidation of Variable Interest Entities* — In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003) ("FIN 46R"), "Consolidation of Variable Interest Entities", which replaces FASB Interpretation No. 46, "Consolidation of Variable Interest Entities". This interpretation addresses the consolidation of variable interest entities as defined in the interpretation. The Companies adopted the provisions of FIN 46R as of March 31, 2004 and such adoption did not have a material effect on the Companies' consolidated financial statements.
- (5) *Impairment of Securities Investments* — In November 2003, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 03-01, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments". EITF Issue No. 03-01 establishes additional disclosure requirements for each category of FAS No. 115 investments in a loss position. In March 2004, the EITF also reached a consensus on the additional accounting guidance for other-than-temporary impairments and its application to debt and equity investments. In accordance with the new disclosure requirements under EITF Issue No. 03-01, Note 3 has been expanded to include certain additional information regarding the Company's investments in marketable securities.

2. TRANSLATION INTO U.S. DOLLAR STATEMENTS

The financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for convenience of readers outside of Japan and have been made at the rate

of ¥104.18 to \$1, the buying rate for yen in New York City at March 31, 2004. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at the above or any other rate.

3. MARKETABLE SECURITIES AND INVESTMENTS

The fair value of marketable debt and equity securities is based on quoted market prices at March 31, 2004 and 2003. The fair values of the marketable debt and equity securities were as follows:

2004	Millions of Yen			Fair Value
	Cost	Gross Unrealized Gain	Gross Unrealized Loss	
Current:				
Corporate debt securities	¥22,962	¥ 19	¥ 4	¥22,977
Bank debt securities	12,781	87	5	12,863
Fund trusts	5,722	43	9	5,756
National debt securities	2,722	2	4	2,720
Total	¥44,187	¥ 151	¥22	¥44,316
Noncurrent:				
Equity securities	¥15,457	¥13,805	¥ 6	¥29,256

There are no securities which have been in a continuous unrealized loss position over 12 months at March 31, 2004.

2003	Millions of Yen			Fair Value
	Cost	Gross Unrealized Gain	Gross Unrealized Loss	
Current:				
Corporate debt securities	¥23,944	¥ 30	¥ 16	¥23,958
Bank debt securities	18,696	39	14	18,721
Fund trusts	2,829	17		2,846
National debt securities	2,720	5		2,725
Total	¥48,189	¥ 91	¥ 30	¥48,250
Noncurrent:				
Equity securities	¥16,293	¥2,672	¥1,352	¥17,613

2004	Thousands of U.S. Dollars			Fair Value
	Cost	Gross Unrealized Gain	Gross Unrealized Loss	
Current:				
Corporate debt securities	\$220,407	\$ 182	\$ 38	\$220,551
Bank debt securities	122,682	835	48	123,469
Fund trusts	54,924	413	86	55,251
National debt securities	26,128	19	38	26,109
Total	\$424,141	\$ 1,449	\$210	\$425,379
Noncurrent:				
Equity securities	\$148,368	\$132,511	\$ 58	\$280,822

Future maturities of debt securities (including fund trusts) classified as available-for-sale at March 31, 2004 were as follows:

	Millions of Yen		Thousands of U.S. Dollars	
	Cost	Fair Value	Cost	Fair Value
Due within one year	¥24,825	¥24,850	\$238,289	\$238,529
Due after one year through five years	16,558	16,588	158,936	159,224
Due after five years through ten years	2,804	2,878	26,916	27,626
Total	¥44,187	¥44,316	\$424,141	\$425,379

Proceeds from sales of available-for-sale securities were ¥2,631 million (\$25,254 thousand), ¥1,741 million and ¥12,208 million for the years ended March 31, 2004, 2003 and 2002, respectively. The gross realized gains on the sales of available-for-sale securities for the years ended March 31, 2004, 2003 and 2002 were ¥932 million (\$8,946 thousand), ¥1 million and ¥6 million, respectively. The gross realized losses on the sales of available-for-sale securities for the years ended March 31, 2004, 2003 and 2002 were ¥4 million (\$38 thousand), ¥53 million and ¥333 million, respectively.

The Companies exchanged certain equity securities for other securities. The Companies recorded the newly received securities at fair value and recognized a gain of ¥436 million and ¥858 million in the years ended March 31, 2003 and 2002, respectively. No such exchanges were made in the year ended March 31, 2004.

The Companies recognized impairment charges on investments of ¥142 million (\$1,363 thousand), ¥3,566 million and ¥507 million in the years ended March 31, 2004, 2003 and 2002, respectively.

4. VALUATION AND QUALIFYING ACCOUNTS

Information related to the Companies' allowance for doubtful receivables was as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	2004
Balance at beginning of year	¥222	¥645	¥521	\$2,131
Charged to costs and expenses	13	83	425	124
Balances written-off	(86)	(506)	(301)	(825)
Balance at end of year	¥149	¥222	¥645	\$1,430

Information related to the Companies' allowance for returns was as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	2004
Balance at beginning of year	¥ 2,066	¥ 2,320	¥ 2,348	\$ 19,831
Charged to costs and expenses	1,991	2,066	2,320	19,111
Balances utilized	(2,066)	(2,320)	(2,348)	(19,831)
Balance at end of year	¥ 1,991	¥ 2,066	¥ 2,320	\$ 19,111

5. INVENTORIES

Inventories at March 31, 2004 and 2003 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Finished products	¥21,955	¥19,960	\$210,741
Work in process	2,730	2,920	26,205
Raw materials	1,375	1,466	13,198
Total	¥26,060	¥24,346	\$250,144

6. SHORT-TERM BANK LOANS AND LONG-TERM DEBT

Short-term bank loans at March 31, 2004 and 2003 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Unsecured bank loans	¥1,339	¥1,773	\$12,853
Collateralized bank loans	2,615	3,860	25,101
Total	¥3,954	¥5,633	\$37,954

The weighted average annual interest rates on short-term bank loans as of March 31, 2004 and 2003 were 1.6% and 1.8%, respectively.

Long-term debt at March 31, 2004 and 2003 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Unsecured loans principally from banks and an insurance company, with interest at 0.6% to 2.1% (based on current market rates), maturing through 2008	¥317	¥352	\$3,043
Other	179	316	1,718
Total	496	668	4,761
Less current portion	374	213	3,590
Long-term debt, less current portion	¥122	¥455	\$1,171

The annual maturities of long-term debt at March 31, 2004 were as follows:

	Millions of Yen	Thousands of U.S. Dollars
Year Ending March 31:		
2005	¥374	\$3,590
2006	72	691
2007	25	240
2008	25	240
Total	¥496	\$4,761

At March 31, 2004, assets pledged as collateral for short-term bank loans and long-term debt were property, plant and equipment with a net book value of ¥230 million (\$2,208 thousand).

As is customary in Japan, the Companies maintain deposit balances with banks and certain financial institutions with which they have short- or long-term borrowings. Such deposit balances are not legally or contractually restricted as to withdrawal.

In addition, collateral must be given if requested by a lending bank and such bank has the right to offset cash deposited with it against any long- or short-term debt or obligation that becomes due and, in case of default and certain other specified events, against all other debt payable to the bank. The Companies have never received any such requests.

7. LEASES

The Companies rent certain facilities and equipment under lease arrangements classified as operating leases. Future minimum rental commitments on non-cancelable operating leases are presented below:

	Millions of Yen	Thousands of U.S. Dollars
Year Ending March 31:		
2005	¥ 750	\$ 7,199
2006	686	6,585
2007	557	5,347
2008	293	2,812
2009	6	57
Total	¥2,292	\$22,000

Rental expense was ¥3,174 million (\$30,467 thousand), ¥2,811 million and ¥2,870 million for the years ended March 31, 2004, 2003 and 2002, respectively.

8. TERMINATION AND RETIREMENT PLANS

Employee Retirement Plans

The Companies sponsor termination and retirement benefit plans that cover substantially all employees. Benefits are based on the employee's years of service, position in the Companies and performance. If the termination is involuntary or caused by death, the employee is usually entitled to greater payments than in the case of voluntary termination.

The Companies have a contributory retirement plan, several partially funded plans administered by independent trustees and several unfunded termination plans administered by the Companies. The contributory retirement plan is interrelated with the Japanese government social welfare program which consists of a substitutional portion requiring employee and employer contributions plus a corporate portion established by the

Companies. Periodic pension benefit payments required under the substitutional portion are prescribed by the Japanese Ministry of Health, Labour and Welfare, commence at a certain age and continue until the death of the employee or the surviving spouse. Benefits under the corporate portion are usually paid in a lump sum at the earlier of termination or retirement, although periodic payments are available under certain conditions.

In accordance with the Defined Benefit Pension Plan Law enacted in April 2002, the Company applied for an exemption from the obligation to pay benefits for employee services related to the substitutional portion which would result in the transfer of the pension obligations and related assets to the government upon approval. In January 2003, the Company received approval from the government for an exemption from the obligation to pay benefits for future employee service related to the substitutional portion. In January 2004, the Company received approval for exemption of the benefit obligation for past service related to the substitutional portion.

In January 2003, the Emerging Issue Task Force reached a final consensus on Issue 03-2, "Accounting for the Transfer to the Japanese Government of the Substitutional Portion of Employee Pension Fund Liabilities" ("EITF 03-2"). EITF 03-2 addresses accounting for a transfer to the Japanese government of a substitutional portion of an Employees' Pension Fund plan ("EPF").

The process of separating the substitutional portion from the corporate portion occurs in four phases. The four phases are as follows: (I) the EPF submits an application to the Japanese government for an exemption from the obligation to pay benefits for future employee service related to the substitutional portion; (II) upon approval, the EPF is exempted from the obligation for benefits related to future employee service under the

substitutional portion; (III) the EPF submits an application to the Japanese government for separation of the benefit obligation related to past services; and (IV) final approval of separation is granted. EITF 03-2 requires that the entire separation process should be accounted for upon completion of the transfer to the government of the substitutional portion of the benefit obligation and related plan assets as the culmination of a series of steps in a single settlement transaction. Under the consensus reached, at the time the assets are transferred to the government in an amount sufficient to complete the separation process, the transaction is considered to be complete and the elimination of the entire substitutional portion of the benefit obligation would be accounted for as a settlement at that time. The difference between the obligation settled and the assets transferred to the government should be accounted for as a subsidy from the government.

The Company plans to transfer the remaining benefit obligation of the substitutional portion as well as the related government-specified portion of the plan assets of the EPF to the government in the year ending March 31, 2005. Accordingly, there has been no effect on the Companies' consolidated financial statements for the year ended March 31, 2004. The Company is unable to determine the impact on the consolidated financial statements until the completion of the transfer.

The other retirement plans provide either lump-sum termination benefits or periodic payments under certain conditions. Benefits are usually paid as a lump sum at the earlier of the employee's termination or the mandatory retirement age.

The general funding policy of the funded plans is to contribute amounts computed in accordance with actuarial methods accepted by Japanese tax law. The Companies expect to contribute ¥2,619 million (\$27,990 thousand) to its plans in the year ending March 31, 2005.

The following provides a reconciliation of benefit obligations, plan assets and funded status of the plans:

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Change in Benefit Obligation:			
Benefit obligation at beginning of year	¥55,115	¥ 48,431	\$529,036
Service cost	1,589	2,146	15,252
Interest cost	1,302	1,355	12,498
Participants' contributions	131	420	1,257
Actuarial (gain) loss	(1,964)	4,733	(18,852)
Plan amendments	(68)	(244)	(653)
Benefits paid from plan assets	(1,018)	(316)	(9,772)
Benefits paid by the Companies	(169)	(672)	(1,621)
Settlement paid	(300)	(738)	(2,879)
Benefit obligation at end of year	54,618	55,115	524,266
Change in Plan Assets:			
Fair value of plan assets at beginning of year	29,191	31,962	280,198
Actual return (loss) on plan assets	5,466	(3,928)	52,467
Employer contributions	1,912	1,848	18,353
Participants' contributions	131	420	1,257
Benefit payments	(1,018)	(988)	(9,772)
Settlement payments	(169)	(123)	(1,622)
Fair value of plan assets at end of year	35,513	29,191	340,881
Funded Status:			
Funded status at end of year	19,105	25,924	183,385
Unrecognized net actuarial loss	(8,616)	(18,894)	(82,703)
Unrecognized prior service benefit	1,896	2,029	18,199
Unrecognized transition amount		118	
Net amount recognized	¥12,385	¥ 9,177	\$118,881

The accumulated benefit obligation for all domestic defined benefit plans was ¥49,646 million (\$476,541 thousand) and ¥49,225 million at March 31, 2004 and 2003, respectively.

	Millions of Yen		Thousands of U.S. Dollars
	2004	2003	2004
Amounts recognized in the consolidated balance sheets consist of:			
Accrued benefit cost	¥14,188	¥ 20,046	\$136,187
Accumulated other comprehensive loss	(1,803)	(10,869)	(17,306)
Net amount recognized	¥12,385	¥ 9,177	\$118,881
Retirement and pension plans with accumulated benefit obligations in excess of plan assets:			
Projected benefit obligations	¥50,974	¥ 51,400	\$489,288
Accumulated benefit obligations	46,003	45,510	441,572
Fair value of plan assets	34,032	27,669	326,665

The minimum pension liability adjustment included in accumulated other comprehensive income (loss) is recorded on the consolidated balance sheet net of a deferred income tax asset of ¥741 million (\$7,112 thousand) and ¥4,467 million at March 31, 2004 and 2003, respectively.

Net periodic benefit costs for the Companies' plans consist of the following for the years ended March 31 2004, 2003 and 2002:

	Millions of Yen			Thousands of U.S. Dollars
	2004	2003	2002	2004
Service cost, less participants' contributions	¥1,589	¥2,146	¥2,368	\$15,252
Interest cost on projected benefit obligation	1,302	1,355	1,490	12,498
Expected return on plan assets	(642)	(808)	(939)	(6,162)
Net amortization	3,153	1,832	1,105	30,265
	¥5,402	¥4,525	¥4,024	\$51,853

The Companies use a March 31 measurement date for the majority of their plans. The weighted average assumptions used as of March 31, 2004 and 2003 in computing the benefit obligation liabilities shown above were as follows:

	2004	2003
Discount rate	2.5%	2.5%
Rate of increase in future compensation	0.4%	0.4%

The weighted average assumptions used as of March 31, 2004, 2003 and 2002 in computing the net periodic benefit cost shown above were as follows:

	2004	2003	2002
Discount rate	2.5%	3.0%	3.5%
Expected long-term rate of return on plan assets	2.5%	3.0%	3.5%
Rate of increase in future compensation	0.4%	0.4%	1.0%

The unrecognized net actuarial loss and prior service benefit are being amortized over 12 years (the average remaining service life of active participants).

The expected long-term rate of return on plan assets is derived proportionally from return assumptions determined for each of the major asset classes. The return expectations for each of the asset classes are based largely on assumptions about economic growth and inflation, which are supported by long-term historical data.

The asset allocation at March 31, 2004 and 2003 is as follows:

	2004	2003
Equity securities	45.3%	42.7%
Debt securities	16.4%	27.4%
Life insurance company general accounts	10.5%	15.8%
Cash and cash equivalents	27.8%	11.6%
Other		2.5%

In accordance with EITF 88-1, the Companies' investment strategy is to maintain actual asset weightings within a preset range of target allocations. The Companies' investments are broadly diversified, typically consisting primarily of equity and debt securities. The Companies believe these ranges represent an appropriate risk profile for the planned benefit payments of the plans based on the timing of the estimated benefit payment.

The Companies also provide employees with an early retirement program. A retirement benefit of ¥167 million (\$1,603 thousand), ¥1,246 million and ¥110 million was paid in addition to normal benefits and charged to selling, general and administrative expenses for the years ended March 31, 2004, 2003 and 2002, respectively.

Termination Plan for Directors and Corporate Auditors

The Companies have termination plans for directors and corporate auditors. Payment of termination benefits to directors and corporate auditors is made in lump sum upon termination and requires the approval of the shareholders before payment.

In accordance with EITF 88-1, the Companies record a liability for termination benefits for directors and corporate auditors at the amount that would be needed if all directors and corporate auditors resign at each balance sheet date. The liability for termination benefits for directors and corporate auditors at March 31, 2004 and 2003 was ¥606 million (\$5,817 thousand) and ¥604 million, respectively.

9. SHAREHOLDERS' EQUITY

Japanese companies are subject to the Japanese Commercial Code (the "Code").

The Code requires that at least 50% of the issue price of new shares is recorded as common stock and the remaining net proceeds as additional paid-in capital, which is included in capital surplus. The Code permits Japanese companies, upon approval of the Board of Directors, to issue shares to existing shareholders without consideration as a stock split. Such issuance of shares generally does not give rise to changes within the shareholders' accounts.

The Code also provides that an amount at least equal to 10% of the aggregate amount of cash dividends and certain other appropriations of retained earnings associated with cash outlays applicable to each period shall be appropriated as a legal reserve (a component of retained earnings) until such reserve and additional paid-in capital equals 25% of common stock. The amount of total additional paid-in capital and legal reserve that exceeds 25% of the common stock may be available for dividends by resolution of the shareholders. In addition, the Code permits the transfer of a portion of additional paid-in capital and legal reserve to common stock by resolution of the Board of Directors. The Company's legal reserve amount, which is included in retained earnings, totaled ¥4,162

million (\$39,950 thousand) and ¥4,132 million as of March 31, 2004 and 2003, respectively.

The Code allows Japanese companies to repurchase treasury stock by a resolution of the shareholders at the general shareholders' meeting and dispose of such treasury stock by resolution of the Board of Directors. The repurchased amount of treasury stock cannot exceed the amount available for future dividends plus the amount of common stock, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general shareholders' meeting.

The amount of retained earnings available for dividends under the Code was ¥109,209 million (\$1,048,272 thousand) as of March 31, 2004, based on the amount recorded in the parent company's general books of account. In addition to the provision that requires an appropriation for a legal reserve in connection with the cash payment, the Code imposes certain limitations on the amount of retained earnings available for dividends.

Dividends are approved by the shareholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. Semiannual interim dividends may also be paid upon resolution of the Board of Directors, subject to certain limitations imposed by the Code.

10. OTHER COMPREHENSIVE INCOME (LOSS)

The changes in the components of accumulated other comprehensive income (loss) are reported net of income taxes as follows:

	Millions of Yen								
	2004			2003			2002		
	Pre-Tax Amount	Tax (Expense) Credit	Net Amount	Pre-Tax Amount	Tax (Expense) Credit	Net Amount	Pre-Tax Amount	Tax (Expense) Credit	Net Amount
Foreign currency translation adjustments	¥ (1,686)	¥ 121	¥ (1,565)	¥ (1,374)	¥ 364	¥ (1,010)	¥ 1,627	¥ (146)	¥ 1,481
Unrealized gain (loss) on securities:									
Unrealized holding gain (loss)	12,369	(4,781)	7,588	(3,527)	1,534	(1,993)	(7,430)	3,431	(3,999)
Reclassification adjustments	152	(63)	89	1,610	(662)	948	79	(33)	46
Net unrealized gain (loss)	12,521	(4,844)	7,677	(1,917)	872	(1,045)	(7,351)	3,398	(3,953)
Minimum pension liability	9,249	(3,910)	5,339	(6,461)	2,613	(3,848)	(4,224)	1,779	(2,445)
Other comprehensive income (loss)	¥20,084	¥(8,633)	¥11,451	¥(9,752)	¥3,849	¥(5,903)	¥(9,948)	¥5,031	¥(4,917)

	Thousands of U.S. Dollars		
	2004		
	Pre-Tax Amount	Tax (Expense) Credit	Net Amount
Foreign currency translation adjustments	\$ (16,184)	\$ 1,161	\$ (15,023)
Unrealized gain (loss) on securities:			
Unrealized holding gain (loss)	118,727	(45,892)	72,835
Reclassification adjustments	1,459	(604)	855
Net unrealized gain (loss)	120,186	(46,496)	73,690
Minimum pension liability	88,780	(37,531)	51,249
Other comprehensive income (loss)	\$192,782	\$(82,866)	\$109,916

II. INCOME TAXES

The Companies are subject to a number of different taxes based on income. The effective income tax rates differed from the normal statutory rates for the following reasons for the years ended March 31, 2004, 2003 and 2002:

	2004	2003	2002
Normal Japanese statutory rates	42.1%	42.1%	42.1%
Increase in taxes resulting from:			
Permanently non-deductible expenses	9.8	5.8	3.8
Change in valuation allowance	7.6	11.7	6.0
Utilization of loss carryforwards	(8.4)	(0.1)	(3.7)
Undistributed earnings of foreign subsidiaries	(2.7)	4.1	1.1
Additional tax charges	16.8		
Differences in subsidiaries' tax rate	(3.1)	(9.4)	(2.4)
Tax exemption	(5.1)	(1.4)	(0.9)
Other — net	(1.4)	1.2	3.7
Effective tax rates	55.6%	54.0%	49.7%

Under the provisions of SFAS No. 109, the effect of a change in tax laws or rates is included in income in the period the change is enacted and includes a cumulative recalculation of deferred tax balances based on the new tax laws or rates in effect. During the year ended March 31, 2003, the normal statutory tax rate was decreased from 42.1% to 41.1% effective April 1, 2004. The provision for income taxes for the year ended March 31, 2003

includes a ¥61 million charge to record the impact on deferred tax assets and liabilities for the change in the enacted tax rate.

In the year ended March 31, 2004, the Companies were assessed with additional income taxes plus interest of ¥760 million (\$7,295 thousand) as a result of an income tax audit for the fiscal years ended March 31, 1998 through 2003 conducted by the Japanese tax authorities.

The approximate effect of temporary differences and tax loss carryforwards that gave rise to deferred tax balances at March 31, 2004 and 2003 were as follows:

	Millions of Yen				Thousands of U.S. Dollars	
	2004		2003		2004	
	Deferred Tax Assets	Deferred Tax Liabilities	Deferred Tax Assets	Deferred Tax Liabilities	Deferred Tax Assets	Deferred Tax Liabilities
Sales returns	¥ 754		¥ 798		\$ 7,237	
Inventory valuation	1,244		751		11,941	
Accrued bonuses	1,499		1,413		14,389	
Intercompany profits	191		133		1,833	
Valuation loss on investments	794		1,407		7,621	
Gain on sales of property, plant and equipment		¥ 1,631		¥1,711		\$ 15,656
Undistributed earnings of foreign subsidiaries		1,890		2,015		18,142
Net unrealized gain on securities		5,670		579		54,425
Net realized gain on exchange of equity securities		2,015		2,126		19,342
Capitalized supplies	390		388		3,744	
Enterprise taxes	225		250		2,160	
Accrued vacation	922		1,005		8,850	
Pension expense	5,170		7,355		49,626	
Tax loss carryforwards	1,486		1,317		14,264	
Fixed assets	1,642		288		15,761	
Other temporary differences	1,342	514	799	44	12,881	4,933
Total	15,659	11,720	15,904	6,475	150,307	112,498
Valuation allowance	(1,185)		(1,199)		(11,374)	
Total	¥14,474	¥11,720	¥14,705	¥6,475	\$138,933	\$112,498

The valuation allowance decreased by ¥14 million (\$134 thousand) and ¥324 million for the years ended March 31, 2004 and 2002, respectively, and increased by ¥592 million for the year ended March 31, 2003.

At March 31, 2004, certain subsidiaries had loss carryforwards amounting to ¥3,068 million (\$29,449 thousand) for tax reporting purposes, which

are available to offset future taxable income of such subsidiaries. The available loss carryforwards expire in various amounts through 2008. In addition, the Company's subsidiary in France had loss carryforwards of ¥678 million (\$6,508 thousand) which are available indefinitely until utilized.

12. EARNINGS PER SHARE AND AMERICAN DEPOSITARY RECEIPT

The Company accounts for its earnings per share in accordance with SFAS No. 128, "Earnings per Share." Basic net income per share has been computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding during each year. Fully diluted income per share is not computed as there are no common stock equivalents.

The computation of earnings per American Depositary Receipt ("ADR"), each ADR representing 5 shares of common stock, is based on the weighted average number of common shares outstanding. The average number of common shares outstanding used in the computations was 146,226,674 shares for 2004, 148,772,325 shares for 2003 and 149,985,724 shares for 2002.

13. FINANCIAL INSTRUMENTS AND CONCENTRATION OF CREDIT RISK

Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents and short-term bank loans approximates fair value because of the short maturities of these instruments. The fair values of current and noncurrent marketable securities, as presented in Note 3, are primarily estimated based on quoted market prices for these securities. The difference between the fair value of marketable securities in Note 3 and the corresponding amount for noncurrent investments in the consolidated balance sheets represents investments in certain non-publicly traded securities for which fair values are not reasonably determinable.

The fair value of long-term debt at March 31, 2004 and 2003 is ¥498 million (\$4,780 thousand) and ¥674 million, respectively. These fair values are based on comparisons of instruments with similar terms and maturities.

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision.

Concentration of Credit Risk

The Companies' business consists primarily of sales of women's intimate apparel to a large number of diverse customers in the Japanese retail industry, which include well established department stores. The Company's management believes that no concentration of credit risk existed at March 31, 2004.

14. SUBSEQUENT EVENT

The Board of Directors of the Company intends to propose for approval at the shareholders' meeting to be held on June 29, 2004, payment of a cash dividend of ¥75 (\$0.72) per 5 shares of common stock to holders of record as of March 31, 2004 for the year then ended (aggregate amount of ¥2,159 million (\$20,724 thousand)).

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Wacoal Corp.
Kyoto, Japan:

We have audited the accompanying consolidated balance sheets of Wacoal Corp. and Subsidiaries (the "Companies") as of March 31, 2004 and 2003, and the related consolidated statements of income, comprehensive income (loss), shareholders' equity and cash flows for each of the three years in the period ended March 31, 2004, all expressed in Japanese yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Certain information required by Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" has not been presented in the accompanying financial statements. In our opinion, presentation of segment information concerning the Company's operations is required for a complete presentation of the Company's consolidated financial statements.

In our opinion, except for the omission of segment information, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Wacoal Corp. and Subsidiaries as of March 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

Our audits also comprehended the translation of the Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 2. The translation of the financial statement amounts into U.S. dollars has been made solely for convenience of readers outside of Japan.



June 4, 2004