

TO OUR SHAREHOLDERS

Resolved to Change

THE WACOAL GROUP HAS INITIATED A NEW MEDIUM-TERM MANAGEMENT PLAN THAT POSITIONS THE PERIOD FROM APRIL 2007 AS “THREE YEARS OF SHIFTING TO GROWTH AND HEIGHTENING EARNING POWER.” WE ARE FULLY COMMITTED TO CHANGE THAT WILL ENABLE US TO ACHIEVE OUR BUSINESS PLANS.



Yoshikata Tsukamoto
Representative Director

Evaluation of Fiscal 2007 Business Results and the Previous Medium-Term Management Plan

Fiscal 2007, ended March 31, 2007, was the final year of the medium-term management plan that we launched in April 2004. (see Table 1)

Net sales fell significantly short of our management target. We sincerely regret that, when preparing the medium-term management plan, our projections of market trends were inaccurate and that our response to these disparities was inadequate. Based on the mainstay *Wacoal* and *Wing* brands, domestic wholesaling operations did not maintain stable revenues through the Group's mainstay department stores and general merchandising stores sales channels, as planned, and revenues and sales volumes declined. Further, in domestic direct marketing business operations, which mainly comprise directly managed stores, developing SPA operations and strengthening Internet sales and mail-order catalog sales did not produce the significant increase in sales hoped for.

Meanwhile, despite being slightly below target, operating income was our highest in eight years. We achieved favorable operating income thanks to progress in reforming our profit structure. For example, we have reduced manufacturing costs by transferring production overseas in recent years. Also, we have pursued initiatives under CAP21 (Corporate Activation Project 21) since 2005 that include the integration and elimination of domestic sewing subsidiaries, the liquidation of a poorly performing outerwear subsidiary, and the reduction of personnel costs through the introduction of our first-ever voluntary retirement scheme.

Having learned the lessons of our inaccurate projections of market trends, we are keenly aware of the need to establish product development and sales systems that can steadily grow sales in any business conditions. Further, aiming to increase flexibility and responsiveness of production, we will rigorously eliminate waste to improve operational efficiency and reduce costs, allowing us to add value to products and market new low-cost products.

business plans & growth strategies

Market conditions: Challenging conditions are likely to continue in the Group's mainstay market Japan. Demographically, we expect a steepening decline in the number of women in the Group's primary customer group: women between the ages of 20 and 69. In the domestic retail industry, although markets for Internet sales and specialty store shopping malls are expanding, markets for mainstay department stores and general merchandising stores are contracting. Against that backdrop, Japan's innerwear market has trended toward yearly decreases in revenues, volumes, and prices since peaking in 1998.

Moreover, in sales channels other than department stores, innerwear prices continue to fall. And, increasing numbers of outerwear companies are breaking into the innerwear market. At the same time, new markets are forming centered on products that emphasize fashion, lifestyles, and price rather than function and quality. Amid such market and product diversification, individual customers now choose where to buy which product according to their varying needs and priorities.

New medium-term management plan and CAP21: In light of those market conditions, the Group must develop business close to customers and increase points of contact with more customers to establish a firm footing in markets. In addition, the Group must pursue the following three goals.

- Establish a business model and an earnings platform that adapt to changes in market conditions
- Expand overseas operations and new businesses in response to the shrinking domestic innerwear market
- Seek fast-paced growth by exploiting the capabilities of other companies rather than relying solely on in-house resources

Mindful of those goals, we launched a new medium-term management plan in April 2007 (see Table 2), themed on Getting Closer to Customers and positioning the coming period as Three Years of Shifting to Growth and Heightening Earning Power. The plan sets out net sales of ¥180.0 billion and operating income of ¥15.3 billion as targets for fiscal 2010. Further, since 2005 the Group has pursued the strategies of CAP21 (Medium-to-Long-Term Growth Strategies) (see Table 3) created to enhance enterprise value by enabling the Group to make a fresh start and step up the pace of growth. CAP21 targets net sales of ¥200.0 billion and operating income of ¥18.0 billion for fiscal 2011, the year after the end of the new medium-term management plan. Aiming to reach those targets, we have already begun strategic moves, including the active consideration of mergers and acquisitions.

In measures aimed at shifting to growth, the Group will enlarge the domestic market presence of its mainstay innerwear business through the decisive development of market areas it has yet to fully exploit. In overseas operations, the Group will further strengthen and expand operations in the United States, which have been a major contributor to earnings. Also, we will develop operations in earnest in China's rapidly developing market.

Table 1 PREVIOUS THREE-YEAR MEDIUM-TERM MANAGEMENT PLAN – TARGETS AND RESULTS

Millions of Yen	TARGET	RESULT	ACHIEVEMENT RATE
Net sales	¥190,000	¥166,410	87.6%
Operating income	13,500	12,896	95.5%

Table 2 NEW THREE-YEAR MEDIUM-TERM MANAGEMENT PLAN

Period	April 2007–March 2010		
Themes	Getting Closer to Customers Three Years of Shifting to Growth and Heightening Earning Power		
Priority measures	Reform and strengthen existing businesses to reflect changing markets Increase points of contact with customers for new growth Enforce rigorous quality control that justifies customers' trust		
Numerical targets for FY 2010			
Millions of Yen	FY 2010	INCREASE COMPARED WITH FY 2007	
Net sales	¥180,000	+8.2%	
Operating income	15,300	+18.6%	

Table 3 OVERVIEW OF CAP21

Launch	April 2005		
Aims	Reorganize and strengthen existing businesses and develop business in areas that promise growth through mergers and acquisitions, operational tie-ups, capital tie-ups, and independent initiatives		
Numerical targets for FY 2011			
Millions of Yen	FY 2011	INCREASE COMPARED WITH FY 2007	
Net sales	¥200,000	+20.2%	
Operating income	18,000	+39.6%	
Operating income margin	9.0%	+1.3 percentage points	

In new businesses, we will venture into areas peripheral to the innerwear business. Our Wellness Business has been the focus of such efforts so far. But, we will also concentrate on realizing our Body Designing Business* strategy. In addition, we will actively consider mergers and acquisitions, operational tie-ups, and capital tie-ups to draw on the capabilities of other companies and achieve faster growth. In June 2006, we entered into a capital and operational tie-up with Peach John Co., Ltd., a major mail-order retailer of innerwear that is highly popular among women in their teens and 20s. We will develop joint ventures with Peach John that enable us to leverage our respective strengths.

In measures for heightening our earning power, we will seek higher levels of operational efficiency throughout our mainstay innerwear business. We have benefited from reducing personnel costs and manufacturing costs. However, we have lagged in the kind of internal cost efficiency improvements that are achievable by seeking productivity commensurate with cost and rethinking inefficient operational management. Mindful of that, we aim to improve inventory turnover rates by consolidating varieties and colors for each product and optimizing overall production volumes. In addition, we will achieve profitability in SPA operations and other direct marketing business operations. And, we will completely integrate the manufacture of *Wacoal*- and *Wing*-brand products – separate for many years – while stepping up the pace at which we are moving production overseas.

The Group will steadily implement those measures to ensure growth for the future and higher earnings. We are unwaveringly committed to carrying out multifaceted reforms that will transform our management team's and employees' mind-sets, organizational systems, manufacturing procedures, and business strategies.

* Body Designing Business: This is a key business strategy of using core competence in innerwear to expand peripheral businesses and provide value in three areas: beauty, comfort, and health. "Body" refers to the body's physical and emotional attributes.

enterprise value enhancement

The Group will continue doing its utmost to increase earnings steadily and raise enterprise value by implementing its new medium-term management plan and CAP21. Our basic policy is to pay shareholders stable cash dividends that reflect business results. However, we plan to increase returns to shareholders by growing earnings. Also, we are improving capital efficiency. For example, over the six-year period since 2001, we purchased 13.4 million shares of treasury stock, equivalent to approximately 9% of issued shares. We will continue purchases of treasury stock, which we view as a part of overall returns to shareholders comparable with cash dividends. Reflecting that philosophy, we paid cash dividends per ADR of ¥110 for fiscal 2007, compared with ¥100 for fiscal 2006. Moreover, given projected improvements in business results and as part of our efforts to heighten returns to shareholders, for fiscal 2008 we expect to pay cash dividends per ADR of ¥125, up ¥15 from the fiscal year under review.

Meanwhile, we will continue investing retained earnings to enhance earning power and enterprise value. Specifically, we will invest to expand SPA operations; develop points of contact with customers; strengthen overseas business; start new businesses; and enter into mergers and acquisitions, operational tie-ups, and capital tie-ups. Further, the Group has a strong financial base with respect to liquidity and shareholders' equity, which heightens management stability and flexibility, provides strategic options in business development, and enhances enterprise value.

In addition, we need to ensure adequate cash to maintain and strengthen competitiveness that is built on research and development; develop sales channels, including SPA shops, Internet sales, and mail-order catalog sales; and advance growth strategies, including further expansion of overseas business.

outlook

As the innerwear market continues to shrink, the women's innerwear industry in Japan will likely see intensifying competition. In response, the Wacoal Group will focus efforts on developing products that earn the endorsement of customers of all ages, from the young through to senior citizens. At the same time, we will continue developing new points of contact with customers.

In businesses catering to department stores and general merchandising stores, we aim to increase earnings by stepping up the marketing of Style Science lineups, which offer revolutionary functionality. These lineups include *Hip Walker*, which has sold briskly since its launch, and *Onaka Walker*. In domestic direct marketing business operations, plans call for achieving profitability in SPA operations and developing joint operations with Peach John. Overseas, we will step up operational development in the United States and China. Meanwhile, in Southeast Asia we will cultivate a new customer group by marketing a brand that targets young career women.

For the fiscal year ending March 2008, we project increases of 2.2% in net sales, to ¥170.0 billion; 4.7% in operating income, to ¥13.5 billion; and 8.5% in net income, to ¥9.8 billion. Working in concert, our management team and employees will continue unstinting efforts to enhance corporate value and reach management targets. As we take on those challenges, I would like to ask our shareholders and other investors for their continued understanding and support.

August 2007



Yoshikata Tsukamoto
Representative Director