

# TO OUR SHAREHOLDERS AND OTHER INVESTORS

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Representative Director Yoshikata Tsukamoto

Fiscal 2008 was the first year of our Medium-Term Management Plan, which calls for *Three Years of Shifting to Growth and Heightening Earning Power*.

Stepping up the pace of corporate management, the Wacoal Group rolled out products reflecting current trends, strengthened its presence in existing markets, and cultivated new markets.



# EMBRACING CHANGE

## EVALUATION OF BUSINESS RESULTS AND INITIATIVES IN THE FISCAL YEAR

In the fiscal year under review, ended March 31, 2008, net sales edged down 0.4% year on year, to ¥165.8 billion; operating income rose 5.0% year on year, to ¥13.5 billion; and net income decreased 45.0%, to ¥5.0 billion. Among the first-year targets set out in the Medium-Term Management Plan, although we did not reach the ¥170 billion target for net sales, we did achieve the target of ¥13.5 billion for operating income. Net income was down significantly from the previous fiscal year. However, that decrease was due to recognition as equity in losses of affiliates of a ¥4.7 billion write-down of our 49% interest in Peach John Co., Ltd., acquired in the previous fiscal year as part of a capital alliance.

Net sales were below target for two main reasons. First, we did not meet sales volume targets for new Style Science functional undergarments, which our domestic subsidiary Wacoal Corp. marketed mainly through autumn and winter sales campaigns. In the third year since *Hip Walker* debuted, we believe sales fell short because store promotional efforts that were smaller than in the first two years did not effectively appeal to new customers or spur replacement demand among existing customers. Second, U.S. operations, which had been growing steadily, entered a temporary correction phase. As part of our efforts to roll out products in a variety of stores, we sought to increase sales at mid- to high-end department stores in the fiscal year. However, while some stores contributed steadily to sales growth, others saw a mismatch between the customer groups of stores and product price ranges. Pulling out products from such stores increased returned products and worsened profitability.

On the other hand, Wacoal's new *LALAN* brassieres, the focus of a marketing campaign from spring 2007, and *Sugoi*, a lineup of new-fabric innerwear marketed in the autumn-winter season, sold briskly. Our *LALAN* brassieres feature unique designs for each cup type and size, thereby accurately catering to a wide variety of bust sizes. Further, *Sugoi* offerings proved popular because they are much thinner, lighter, and warmer than traditional innerwear. In addition, we launched *Cross Walker* as a Style Science innerwear lineup for men in spring 2008. Amid growing consumer interest in such health issues as metabolic

syndrome prevention, the response to those lineups has been enthusiastic, and we are currently increasing production. Although women's lineups missed fiscal-year targets, I am convinced that we can develop Style Science, including products for men, into a major lineup and earnings mainstay.

I think we can take some positives from our business results in the fiscal year. We did not achieve the target for net sales, but reductions in manufacturing costs and SG&A expenses enabled us to reach the operating income target.

## BUSINESS CONDITIONS AND MANAGEMENT ISSUES

In the past several years, Japan's apparel industry has generally faced tough business conditions. And conditions in the innerwear industry do not warrant optimism.

Japan's innerwear market has matured in recent years due in part to the aging of Japanese society. As a result, that market is unlikely to grow significantly. Moreover, amid those conditions, competition is becoming fiercer as more apparel manufacturers, retailers, and other companies enter the innerwear manufacturing industry. Nevertheless, I think we should welcome such competition because it energizes the market, which increases consumer interest in innerwear. The emerging innerwear market is centered on low-price fashionable products and differs from our traditional mainstay market, which focuses on high-value-added products with advanced functionality. In order to establish a presence in that emerging market, we will have to use unprecedented products, sales methods, sales channels, and pricing strategies. In my view, adopting such new approaches to realize further growth is a key corporate management issue. Making Peach John a subsidiary partially addresses that issue by providing Wacoal with a strategic foothold in a new market segment.

At the same time, to grow dramatically Wacoal must expand its growth driver – overseas operations. Wacoal began developing overseas operations from the 1970s, mainly in Asia. Today, we have built a worldwide operating system with production and marketing bases in the United States, China, and other countries. Going forward, we will expand operations in regions where we have a presence while rolling out *Wacoal*-brand lineups in new countries and regions.

## GROWTH STRATEGIES

In light of the abovementioned business conditions and management issues, Wacoal is simultaneously advancing initiatives under its Medium-Term Management Plan and the CAP21 (Corporate Activation Project 21). With the fiscal year as its first year, the Plan sets out operational strategies over three years under the slogan *Three Years of Shifting to Growth and Heightening Earning Power*. Meanwhile, the CAP21 seeks higher enterprise value by making a fresh start and accelerating growth through initiatives that include mergers and acquisitions. Based on the benefits resulting from the implementation of the Plan and the CAP21, I would like to discuss the Wacoal Group's growth strategies more specifically from two standpoints.

First, I would like to look at our mergers and acquisitions strategy. Following on from a capital tie-up in June 2006, we made Peach John a wholly owned subsidiary in January 2008. Peach John's features and strengths differ from those of Wacoal. Our new subsidiary has grown rapidly by targeting customers in their teens and twenties through mail-order catalog sales and a chain of directly managed stores. Including Peach John in the Wacoal Group not only increases Wacoal's enterprise value and market presence but enables Wacoal to invest management resources in Peach John to accelerate the subsidiary's growth and strengthen its earnings platform. Already, we have prepared plans that capitalize on each company's expertise and customer base, which we will steadily carry out. Making Peach John a wholly owned subsidiary is one of the major successes under the CAP21. Accordingly, we will continue to actively consider mergers and acquisitions. Thus far, we have selected mergers and acquisitions in business areas where we can bring to bear our technology and expertise. However, we will consider expanding our operations beyond such business areas by also looking at areas where we can effectively leverage our financial strength and brand power.

Next, I would like to turn to overseas strategy\*. In mainstay operations in the United States, we will increase sales channels by adding marketing through specialty stores to sales at department stores, which are centered on the *Wacoal* brand. Further, at the end of 2008 we will end our manufacturing and sales contract for DKI and DKNY, designer brands that we manufacture and sell in the United States. To replace them, we will launch new brands. As a result of the contract cancellation, net sales in the current fiscal year will decrease. However, we expect that the roll-out of new brands will bring net sales back to their current level in the following fiscal year, improve the profitability of U.S. operations, and put them on a steady growth track.

Meanwhile, China continues to be the most promising market. China's high-end innerwear market is beginning to become less homogeneous as it segments to reflect the characteristics of a variety of consumer groups. Responding to that market trend, we will roll out a high-value-added brand and a brand that targets younger customers. Also, we will give priority to strengthening our brand image by implementing advertising campaigns and increasing the number of stores carrying our lineups.

In other Asian regions, we will begin sales in Vietnam in January 2009, ten years after establishing our first production base in the country. Vietnam has the potential to contribute to the Group's sales because it will remove regulatory restrictions in the retail industry on foreign capital from 2009, which is likely to rapidly invigorate the country's distribution market and expand the country's innerwear market. Keeping that in mind, we will start sales operations at five department stores and a directly managed store in Hanoi. We will then develop operations in Hanoi and other major cities.

\* For further details, please see pages 11 and 12.

## MEDIUM-TERM MANAGEMENT PLAN OVERVIEW

Period	April 2007 – March 2010	
Theme	<i>Getting Closer to Customers, Three Years of Shifting to Growth and Heightening Earning Power</i>	
Priority measures	1. Reform and strengthen existing businesses to reflect changing markets 2. Increase points of contact with customers for new growth 3. Enforce rigorous quality control that justifies customers' trust	
Numerical targets*	Net sales	194,000
for FY 2010 (¥ million)	Operating income	16,400

\* The Company revised numerical targets upon making Peach John Co., Ltd., a wholly owned subsidiary in January 2008.

## CAP21\* OVERVIEW

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	Net sales	200,000
for FY 2011 (¥ million)	Operating income	18,000
	Operating income margin	9%

\* Corporate Activation Project 21

## BASIC POLICY FOR RETURNS TO SHAREHOLDERS

Guided by the Medium-Term Management Plan and CAP21, corporate management concentrates on strengthening our earnings platform and continuously heightening enterprise value. Our basic earnings appropriation policy is to pay stable dividends in light of consolidated business results. In addition, since 2001 we have continuously purchased treasury stock as part of returns to shareholders. Over the past seven fiscal years, we have improved capital efficiency by purchasing 17.4 million shares of treasury stock, equivalent to approximately 12% of issued shares.

Increasing dividends for the third consecutive year, we paid cash dividends per ADR of ¥125, compared with ¥110 in the previous fiscal year. For the current fiscal year, ending March 2009, we plan to maintain dividends at the same level as in the fiscal year and pay cash dividends per ADR of ¥125.

Meanwhile, we will continue investing retained earnings to increase earning power and enterprise value. Specific investments will include developing new markets through SPA operations; cultivating points of contact with new customers; strengthening overseas businesses; and starting new businesses. Further, we will consider capital and operational alliances or mergers and acquisitions that accelerate growth.

## OUTLOOK AND FISCAL 2009 BUSINESS RESULTS PROJECTIONS

Challenging market trends and fierce competition are likely to continue characterizing business conditions. Faced with those conditions, I feel strongly that we must be alert to market changes and steadily revolutionize our mind-set and corporate structures so that we can respond promptly to such changes. Happily, signs of such reform are emerging. Last year, Hideo Kawanaka (please see page 6 for details) joined our corporate management team. Drawing on extensive experience and a long track record in the retail industry, he is spearheading reform initiatives. In the past year, we have begun revising all operational processes from development and manufacturing through to sales to reflect the priorities of customers rather than those of manufacturers. And, our management team and other employees continue to unite and advance reforms whenever and wherever needed.

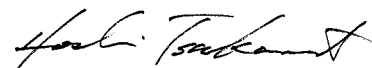
Regarding SPA operations, an area on which we have been focusing efforts in recent years, the existing shops and new shops of independently operated subsidiary Une nana cool Corp. are performing well. Also, we are improving the profitability of *amphi*, *Subito*, and *Sur la plage* – brands which the directly managed store operations of Wacoal Corp. develop – by closing unprofitable shops, creating shared lineups from approximately half of the lineups previously planned and manufactured separately under each brand, and reducing production costs and inventory loss.

In efforts to roll out new products, men's innerwear operations are approaching a period of full-fledged growth. With the introduction of health checkups and consultations for metabolic syndrome, such Style Science offerings as the men's innerwear *Cross Walker*, which can help reduce body fat, are rapidly attracting attention. By building on the success of *Cross Walker*, we can transform the image of men's innerwear to significantly grow the market for these products, thereby creating a major business chance. Mindful of such potential as well as of issues, we will continue to develop new businesses and reform corporate management.

In the current fiscal year, ending March 31, 2009, year on year we expect a 10.4% increase in net sales, to ¥183.0 billion, a 7.7% decrease in operating income, to ¥12.5 billion, and a 41.0% rise in net income, to ¥7.0 billion. The decrease in operating income is principally attributable to an anticipated loss of ¥0.7 billion accompanying the liquidation of a sewing subsidiary; a ¥0.9 billion increase in retirement benefit payments – associated with an increase in recognition of actuarial loss in the current fiscal year likely to arise from deterioration in management of the Company's pension assets due to such external factors as falling share prices – and a ¥0.3 billion loss due to currency volatility, counteracting an expected ¥0.9 billion contribution to earnings from Peach John, which became a subsidiary in January 2008. At the present juncture, we are assuming a foreign currency exchange rate of US\$1 = ¥102. Because U.S. operations represent a considerable portion of the Company's consolidated financial statements, foreign currency fluctuation could significantly affect consolidated business results.

In closing, I ask our shareholders and other investors for their continued understanding and support.

August 2008



Yoshikata Tsukamoto  
Representative Director