

# EVOLVING ON STRENGTHS

Message from the Management

*“We will regain our ability to respond to changing market conditions and strengthen growing business areas even further.”*



Yoshikata Tsukamoto  
Representative Director

### Report on Business Results for the Fiscal Year

In the fiscal year under review, ended March 31, 2010, the Wacoal Group recorded year-on-year declines of 5.2% in net sales, to ¥163.3 billion; 62.4% in operating income, to ¥3.8 billion; and 51.7% in net income attributable to shareholders of the Company, to ¥2.5 billion.

In the fiscal year, conditions remained tough, despite signs of recovery from the downturn that began with the 2008 worldwide financial crisis. In Japan's retail sector, there was a strengthening of a tendency among consumers to favor lower priced products and spend carefully. As a result, the Wacoal Group's mainstay sales channels—department stores and general merchandising stores—saw very challenging business conditions continue unabated.

Faced with these business conditions, the Wacoal Group's mainstay operating company Wacoal Corp. led initiatives that concentrated on increasing product appeal even further and marketing products to meet consumer needs more accurately. However, due to an overall downturn in sales of women's innerwear, business conditions were severe. On the other hand, although not compensating for slumping sales of women's innerwear, men's innerwear and SPA (specialty store retailer of private label apparel) operations posted sales on the same level as those of the previous fiscal year. Moreover, growing consumer health awareness provided a following wind for the Wellness Business, which achieved a year-on-year increase in sales.

Overseas, operations improved profitability due to cost reductions and the absence of the previous fiscal year's losses related to the DKI and DKNY designer brands. Other positive developments included *b.tempt'd by Wacoal*, which outperformed initial sales targets after marketing at the beginning of 2009. As for China, we steadily grew market share among existing stores, mainly department store channels, by promoting three brands: our mainstay *Wacoal* brand, *amphi* targeting young women, and the high-value-added brand *Salute*.

### Overview of the Previous Medium-Term Management Plan

The fiscal year marked the final year of our previous three-year Medium-Term Management Plan, which set out net sales of ¥180 billion and operating income of ¥15.3 billion as numerical targets for the fiscal year. Unfortunately, however, we fell short of these targets. Similarly, reaching the numerical targets of our CAP21 growth strategy for the current fiscal year is likely to be very challenging. Setting our sights on net sales of ¥200 billion and operating income of ¥18 billion, we began this growth strategy four years ago.

We did not reach our targets for three main reasons. First, the recent volatility of business conditions led to a significant slump in mainstay women's innerwear wholesale operations in Japan. Second, our operational structure was unable to respond fully to such changing business conditions. Third, our overseas operations, which should have driven growth, did not expand quickly enough.

Behind the first reason was the shrinking of the women's innerwear and men's innerwear segments in Japan's innerwear market. While high-end product sales are sluggish, high-volume markets are shifting toward low-priced products. In particular, the women's innerwear market is much smaller than it was a decade ago and is likely to become smaller still. This shrinking of markets was a major factor in the Group's lackluster performance.

The backdrop of the second reason was the diversification of the sales channel used by consumers today in recent years, as well as our existing sales channels undergoing dramatic structural change. The business results of business partners in our main sales channels—department stores, specialty stores, and general merchandising stores—are trending downward, with department stores seeing particularly marked decreases. Because Wacoal Corp. focuses on mid-to-high-end products, the department store channel accounts for a large share of its sales. Consequently, not only the downturn among department stores but also our inability to respond quickly to this change adversely affected business results.

Until now, we have developed new pillars of our business, such as the Wellness Business, men's innerwear operations, SPA operations, and Internet sales to counteract the downward trend in the women's innerwear market. However, these new businesses were unable to fully offset

the economic slump. Nonetheless, our new businesses have reached a size where they can steadily contribute to business results. And, the outlook for these businesses is very promising. Looking at the Group as a whole, business development possibilities are multiplying. For example, we are steadily moving forward to increase points of contact with customers through such initiatives as making Peach John Co., Ltd., and Lecien Corporation wholly owned subsidiaries. Over the past three years, our efforts to expand operations in growing business areas have produced solid benefits. Further, we have almost finished building a structure for higher earnings by integrating the manufacturing operations of the *Wacoal* brand and the *Wing* brand. This initiative is enabling us to consolidate varieties and colors for each *Wacoal*-brand product, which lowers inventory loss and thereby reduces the cost of sales as a percentage of net sales. Going forward, however, I think we need to reform the women's innerwear wholesale operations in order to respond to changes in sales channels.

Behind the third reason was the strong growth of markets in emerging countries such as China, Brazil, Russia, and India. These countries have high-market potential. Another factor was the attempts to expand market shares in the U.S. and Europe. In this environment, expanding overseas operations was critical to our growth. The reason we did not meet targets was because we did not develop these operations rapidly enough. However, we did take a range of different measures to develop overseas operations. In mainstay U.S. operations, sales declined due to low consumer spending and the cancellation of a contract for licensed products for DKI and DKNY designer brands. However, we took steps toward building highly profitable operations by changing over to our original brand products, which have higher profit margins. A good example is our *b.tempt'd by Wacoal* brand, which debuted in January 2009 to a favorable reception. Also, in China we continued to grow market share by heightening the name recognition of three key brands through sales initiatives and stepped-up advertising.

Bearing in mind the many tasks and successes that efforts under the previous Medium-Term Management Plan have given us, we will steadily push forward with measures under the new Medium-Term Management Plan, which began from April 2010. Furthermore, in light of the progress of these measures and trends in business conditions, we will continue to seek new growth by pursuing our CAP21 growth strategy.



## CORPORATE ACTIVATION PROJECT 21

### A Summary of CAP21

CAP21 is an abbreviation of Corporate Activation Project 21. Under this growth strategy, we are reorganizing and strengthening existing operations while developing operations in business areas that promise growth. In these development efforts, rather than limiting ourselves to independent efforts, we actively seek M&As as well as capital and operational tie-ups.

## NEW MEDIUM-TERM MANAGEMENT PLAN

### A Summary of the New Medium-Term Management Plan

#### Period

April 2010–March 2013

#### Target corporate profile

Global Wacoal Group

#### Group strategies over three years

- Heighten the overall capabilities of the Wacoal Group through collaboration among Group companies to realize each company's strengths
- Secure and increase earnings
  - Restructure operations focusing on innerwear wholesale operations
  - Accelerate expansion in growing business areas at home and abroad
- Strengthen system for Groupwide management

#### Target corporate profile for 2013

- New revenue and earnings pillars established alongside existing innerwear wholesale operations
- Overseas operations such as those in the U.S. and China support growth
- Restructured innerwear wholesale operations see profitability improve
- System for Groupwide management further developed and strengthened
- Meeting corporate social responsibilities and compliance requirements

#### Numerical targets

For fiscal 2013, net sales of ¥190 billion and operating income of at least ¥8 billion

The main focuses of our new Medium-Term Management Plan, launched from April 2010, are improving our ability to respond to dramatic changes in market conditions while stepping up initiatives in growing business areas. In accordance with the above Group strategies, our efforts to regain responsiveness to market change will mainly involve realizing our overall capabilities as a corporate group and restructuring women's innerwear wholesale operations. During the previous Medium-Term Management Plan, we were unable to completely reflect sudden changes in market conditions due to the structure of our operations. As a result, revenues and earnings continued to decline, causing the Group to lose momentum. Given that the women's innerwear market is unlikely to grow in Japan, we must shift to an operational structure geared toward securing earnings. Vice president Hideo Kawanaka will explain these structural reform efforts in more detail later in this section.

Meanwhile, to add further impetus to efforts in growing business areas, we will accelerate the expansion of a range of initiatives that are already contributing earnings and thereby achieve further growth. Specifically, overseas operations will play a central role in supporting growth. In particular, we will focus on restoring growth in operations in the U.S., which is showing signs of economic recovery, and claiming a larger market share through our fast-growing operations in China. Our director responsible for international operations, Tadashi Yamamoto, will cover these initiatives in more detail later in this section.

However, I would like to first explain our strategies for growing business areas in Japan beyond our existing innerwear wholesale operations. In SPA operations, which are tasked with building new sales channels by developing directly managed stores, we intend to increase store openings while maintaining profitability. Over three years, we aim to increase total sales from direct retail operations 33%, from ¥150 billion for the fiscal year to ¥20 billion.

In the Wellness Business, which is developing the sports conditioning wear product *CW-X* and seeing sales grow favorably as a result, we will redouble business development efforts. Aiming to boost sales by one-third in three years, from ¥9 billion for the fiscal year to ¥12 billion, we will bring new products to market, enrich our existing product lineups, diversify sales channels through new store openings, raise name recognition through advertising, and increase overseas sales.

Another growing business area is men's innerwear. Since making a full-fledged entry into this market by introducing *Cross Walker*, our operations have been performing well. We intend to develop these operations vigorously in order to establish an unshakable position in the men's innerwear market. Plans call for a 25% rise in sales, from ¥4 billion for the fiscal year to ¥5 billion, by increasing the number of stores carrying our products, taking advantage of Internet sales, and launching new brands targeting senior customers.

At the same time, in existing women's innerwear wholesale operations we aim to secure our solid position as the company with the largest share of the market. To that end, based on its unique R&D, the Wacoal Group will develop high-quality products with advanced functionality so that it can offer products that truly have value for customers. Moreover, we will extend our market share by introducing products to low-price high-volume markets, a large area that we have not yet actively exploited. These efforts to win further market share will draw on the combined expertise of Peach John, which sells low-priced products for young women, and Lecien, which specializes in low-cost production for high-volume markets.

As we take these steps to increase profitability and strengthen our growth potential, I think we need to make sure of reaching the numerical targets we have set out for the three-year period. I hope that we can meet our new targets ahead of schedule and get back on a growth track.

### Capital Measures and Returns to Shareholders

The Wacoal Group's basic financial policy is to pursue flexible capital measures based on a strong financial foundation and on ample cash flows. Accordingly, as part of efforts to strengthen profitability in growing business areas, we will actively invest in overseas operations. This investment will target returning U.S. operations to growth and raising brand name recognition through advertising and sales campaigns in China. In Japan, we will continue to invest in operations for which name recognition remains low, such as men's innerwear operations and the Wellness Business. Meanwhile, we must improve operations and reduce costs and expenses in order to increase efficiency and restore the wholesale channel's ability to respond to business condition changes.

Regarding M&As, so far we have implemented major mergers with Peach John and Lecien. Going forward, however, I want to include companies with which we can realize manufacturing synergies as a manufacturer in the innerwear industry in the scope of our M&A activities. Overseas, rather than developing operations independently, we intend to scrutinize potential local partners to find companies that are certain to facilitate operational expansion. Looking forward, based on a stable financial foundation, the Wacoal Group will make the investments needed to increase earnings.

In relation to returns to shareholders, we view meeting the expectations of our shareholders by steadily increasing earnings to heighten enterprise value as an important management task, in accordance with our basic policy of paying stable dividends in light of consolidated business results. Regrettably, we had to reflect less favorable business results by lowering cash dividends to ¥20 per share for the fiscal year, a reduction of ¥5 from the previous fiscal year. Further, since 2001 we have purchased treasury stock as part of increasing returns to shareholders. In the fiscal year, we improved capital efficiency by purchasing 1,130,000 shares of treasury stock, bringing treasury stock purchased to a total of 21.3 million shares. As for retained earnings, while considering investment in new businesses and M&As, we will purchase treasury stock flexibly to improve capital efficiency and realize returns to our shareholders.

### Outlook for the Current Fiscal Year

Emerging nations are driving recovery in economies worldwide. In Japan, however, the business climate remains harsh, and consumer spending will likely need more time to recover. Mindful of these trends and in accordance with its new Medium-Term Management Plan, the Wacoal Group will regain its ability to respond to changing conditions, restructure operations to ensure earnings, and strengthen measures in growing business areas. As a result, for the current fiscal year we expect to post increases of 5.3% in net sales, to ¥172.0 billion; 31.2% in operating income, to ¥5.0 billion, and 26.8% in net income attributable to shareholders of the Company, to ¥3.2 billion. This forecast assumes a foreign exchange rate of US\$1=¥92, but foreign exchange rate fluctuations could significantly affect consolidated business results because U.S. operations account for a large share of Wacoal's consolidated revenues and earnings.

Our newly launched Medium-Term Management Plan sets out a Global Wacoal Group as a target corporate profile. However, this does not mean that our sole focus will be on building the presence of our overseas operations. We also intend to retain our leading position in Japan, our home market, by continuing to manufacture unique high-quality products with advanced functionality. Establishing an even more dominant position in Japan will heighten our brand equity and product recognition worldwide. This is the type of Global Wacoal Group we should seek. Also, the Wacoal Group's Human Science Research Center, which has conducted basic research on women's physiques for more than 40 years, is unique. None of our competitors have such an organization, which enables us to discover what customers see as offering real value and develop appealing products suited to the times. In accordance with our basic approach to manufacturing, which is also our basic management strategy, we will continue creating products loved by customers and developing products that meet the needs of the times in order to raise enterprise value. In closing, I would like to ask our shareholders and other investors for their continued understanding and support.

August 2010



Yoshikata Tsukamoto  
Representative Director

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*“The Wacoal Group will raise the productivity of each employee and ensure stable profitability.”*

Hideo Kawanaka  
Director and Vice President  
(Business Restructuring and Peach John)



### Restructuring Innerwear Wholesale Operations

I am very much aware that our core operations, women's innerwear wholesale operations in Japan, are facing extremely challenging conditions. As our president Yoshikata Tsukamoto explained, restructuring these core operations is a priority task that we have to tackle quickly. My mission is to accelerate the business restructuring that we have carried out so far while implementing further restructuring decisively in order to improve our ability to respond to dramatic changes in market conditions as set out in our new Medium-Term Management Plan.

Initially, we will concentrate on putting a brake on a rapid decrease in profitability. Because the market is shrinking, women's innerwear wholesale operations in Japan have little prospect of growing. Therefore, we have to change the structure of operations and earnings to suit the size of revenues. We need to realize a leaner structure that secures earnings even in the midst of a sales downturn. While continuing with existing initiatives to revise fixed costs and reduce expenses, we intend to move forward with such new reforms as increasing the productivity of each employee, reforming the profit structure in the department store channel, and deploying personnel with a view to improving productivity. Among these initiatives, I think that increasing the productivity of individual employees is a key strategy. If employees have the motivation to handle multiple roles, it will not only reduce costs but also give rise to synergies that will encourage new ideas.

In order to lead these efforts, we established a restructuring advancement project in April 2010. In its first three months, this project identified tasks, established strategies, and set out improvement targets, which we are trying to reach in one year. This is the first time we have set a time limit on such a project, but we are absolutely determined to meet these targets so that we can respond to volatile times and survive as a company.

### Peach John's Current Standing and Business Strategies

Popular among young women and young career women, Peach John recorded a 12% year-on-year decline in net sales, to ¥13.2 billion, for the fiscal year. In Japan, Peach John has its own sales channels centered on mail-order catalog sales and store sales. Recently, the methods customers use to order have rapidly shifted from telephone and fax to the Internet. Although we developed an IT infrastructure to increase customer convenience, Internet orders were lackluster, and consequently net sales decreased. I believe the main reason for this was a decline in product planning capabilities. With this in mind, we intend to reinforce product planning capabilities and take full advantage of our new IT infrastructure to provide young women and young career women with the very latest product information.

Further, we intend to increase the profitability of each store in order to secure earnings. Based on exacting assessments of the profitability of the 27 stores that Peach John operates primarily in the Tokyo metropolitan area as of August 31, 2010, we will implement a scrap-and-build program in order to create a network of stores that attracts even more customers. Overseas, plans call for establishing an operational platform in China and rapidly expanding operations. We have begun to actively develop a store network while managing operations efficiently through collaboration with the operations of Wacoal Corp. in China. Our two stores in Hong Kong are seeing brisk sales, and store openings are slated for China in August 2010. By advancing these strategies, we aim to achieve net sales of ¥15.6 billion and operating income of ¥0.8 billion in three years time.

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*“We will accelerate the development of overseas operations to make them a growth driver.”*

Tadashi Yamamoto  
Director and Senior Corporate Officer  
(General Manager of International Operations)

### Aiming to Expand Overseas Operations Rapidly

Strengthening and expanding overseas operations has been an important facet of our growth strategy since the previous Medium-Term Management Plan. Because Japan's market is shrinking, overseas operations are key to growth. However, under the previous Medium-Term Management Plan, efforts to strengthen and expand overseas operations lacked speed. While the worldwide recession affected us, I think we did not progress sufficiently in brand loyalty penetration and other efforts to build a foundation from which to accelerate growth. Although the Wacoal Group markets products in 39 countries, market share worldwide remains low because often the Group sells products on a small scale through sales agencies. In response, we will expand overseas operations at a greater pace by strengthening operational platforms in the U.S. and China while laying foundations in new markets with considerable potential such as Germany, Brazil, and Russia through further brand loyalty penetration. As a result, we aim to increase overseas sales, including those of affiliates, ¥17.0 billion, to ¥69.0 billion, by fiscal 2013.

### Operations in China and the U.S. Crucial to Growth

For the immediate future, China and the U.S. will be our priorities overseas. The rapid turnaround of the Chinese market after the business climate worsened testifies to its burgeoning potential. Furthermore, because the Wacoal Group's competence lies in high-quality products with advanced functionality, the growing affluence of the population along China's coastal areas is a major opportunity.

In China, initiatives focus on three brands with a view to catering to a broad range of customers. As well as the mainstay *Wacoal* brand, we are developing *amphi*, for young women, and the high-value-added brand *Salute*. During the fiscal year, we increased their name recognition in China by mounting advertising campaigns on a larger scale. Consequently, our share of sales increased steadily at existing stores centered on the department store channel, comprising 333 stores at the end of the fiscal year. We will continue raising name recognition while increasing the number of stores carrying our products, in coastal areas and inland areas of northeastern China. Also, over three years we plan to open 23 directly managed stores, including factory outlets, giving us 25 stores. Further, to increase points of contact with customers, we began sales through a major Internet shopping site, Taobao, from February 2010. Through such efforts, we aim to realize growth in step with the expansion of China's market and, in three years, grow sales 150%, to ¥10.0 billion.

In the U.S., accounting for the largest portion of overseas earnings, our priority is to raise growth and earnings. During the fiscal year, we raised the name recognition of a new original brand introduced in response to the cancellation of the contract for licensed products for DKI and DKNY designer brands. As a sexy and fashionable brand, *b.tempr'd by Wacoal* has earned strong endorsement from business partners and consumers. In the fiscal year, about half the number of stores carried this new brand compared with the number that carried DKI and DKNY designer brands. However, by raising this number close to the level achieved for DKI and DKNY, we plan to increase sales and brand loyalty in the current fiscal year. Further, we will use U.S. operations to launch the new brand in Canada, Mexico, and Brazil. Although still far from the sales levels of DKI and DKNY products, we look forward to improved profitability because *b.tempr'd by Wacoal* is an in-house brand. Also, we plan to market Shapewear, a women's undergarment with corrective functionality—an area in which we have long-standing expertise. Further, U.S. operations will increase points of contact with customers by launching an Internet sales web site in August 2010. Our goals are to return U.S. operations to growth and increase sales 25%, to ¥13.0 billion, by fiscal 2013.