

Business Results for Fiscal 2020 Third Quarter (September 2019 to May 2020)

Below are some questions from our analysts' meeting concerning Fast Retailing business results for the third quarter of FY2020. The answers have been edited for clarity.

Q: Inventories increased by approximately 20% year on year at the end of May. Can you give a more detailed picture of how you are running down Spring Summer and Fall Winter inventory?

Takeshi Okazaki, Group Senior Executive Officer & CFO – Looking first at end-August expected inventory levels, with many stores temporarily closed for business from March into May, we expect to see a particular excess of Spring inventory. However, many of those Spring items are year-round products that can be sold in certain volumes in midsummer and early fall as well. While we do want to offload some of that inventory by October time, we are not going to rush to heavily discount mainstay products that can command value in coming seasons and will, instead, gradually sell them off through the 2021 Spring Summer season. Naturally, we are preparing to introduce new products as well in the Spring Summer season, so customers feel they are seeing a fresh range. By contrast, in terms of excess Summer inventory, we are discounting trend-driven items to ensure we can run those down, but, given the recovery in sales that we have witnessed in May and June, we do expect to be able to normalize Summer inventory by the end of the season.

In terms of Fall Winter inventory, we have been restricting orders to a certain extent, but I would rather wait and see how the launch of our 2020 Fall Winter range goes before making any further adjustments.

Q: To what extent did you restrict orders of Fall Winter products?

CFO Okazaki – I can't give you a specific figure. Demand in Japan has recovered to previous year levels, so I also have to consider how to ensure we don't restrict orders for Fall Winter ranges too far and find ourselves unable to keep up with demand. In addition to controlling orders, I want to work together with factories to control production and ensure we have measures in place to be able to provide the products if sales recover sharply. Having said that, since it is difficult to predict what will happen with COVID-19, we are managing things very attentively so we can respond equally swiftly to any downturn in demand.

Q: Within UNIQLO International, can you give us a clearer idea of sales trends and the sense of recovery in Southeast Asia and China?

CFO Okazaki – Conditions in Southeast Asia vary markedly for each market, and those conditions are different again now than they were at the end of May. In Singapore for instance, the lockdown continued through late June, during which period we could only offer e-commerce, so the consequent decline in overall sales was extremely severe. However, once stores reopened towards the end of June, business has been gradually getting back to normal, and I think sales will return to pre-COVID-19 levels if we don't experience a second wave of the disease in that market.

In Malaysia and Thailand, we were able to reopen stores comparatively quickly. Sales started to recover in May and have been regaining normal levels from June. In fact, we are sensing that sales are recovering at an even faster pace in these markets than they did in China.

Indonesia and the Philippines suffered a very large blow from COVID-19, so we are seeing delayed recoveries there. A recovery in the Philippines is likely to come later than in Indonesia due to the still strong impact of COVID-19 in the areas of the country in which we operate stores. For Southeast Asia as a whole, while the impact of COVID-19 has been comparatively strong, if it is brought under control, I think we can regain former sales levels. In order to grow our operations further from that point, we will need to think of many new measures and strategies and put them into action, so we are not especially pessimistic on this region.

Moving onto Mainland China, we were very pleased with that market's strong performance in May. In June, sales were not bad compared to our plan, but we did notice a lull compared to May. There are several probable causes for this: 1) We didn't rush in with heavy discounts in order to grab sales around the time of the 618 mid-year shopping festival (an annual bumper online sales campaign in Mainland China centered around June 18 that rivals the Double 11 Singles' Day sales in November), but decided to continue selling items at stable prices: 2) Sales were dampened by the renewed expansion of new COVID-19 infections in Beijing, and: 3) June sales also failed to regain previous year levels due to unseasonal weather in Mainland China's southern and central regions. However, we have not seen any fundamental business concerns emerge, so, as long as we do not witness a second wave of COVID-19 infections, we should be able to get back on an upward growth track.

Q: Southeast Asia typically features high travel-related demand and that portion of the market is likely to take a considerable amount of time to recover. However, in terms of Malaysia and Thailand, are we to understand that the pace of recovery has been fairly fast even without travel-related demand?

CFO Okazaki – We can't make a clear judgement on that until we have run the business for a fairly long period of time. Travel demand is non-existent right now given that, in reality, almost no-one is currently travelling. Thailand is managing to offset that gap with demand from local customers right now. To keep

that up, we must launch new initiatives and devise new ways to encourage local customers to return to our stores more often. We are certainly not taking an optimistic approach here and we know that we have to give much additional thought to how we can change and improve the way we conduct our business.

Q: You said that the pace of recovery has been faster than you expected in Mainland China, but you have disclosed a forecast range of -15% to ±0% for fourth-quarter revenue. What is your view on demand and the competitive environment in Mainland China, and can you also share more details about China's e-commerce sales environment?

CFO Okazaki – First, the fourth-quarter performance in Mainland China is being compared to an extremely strong period in the previous year. In addition, as I explained earlier, June sales declined slightly year on year, and we have made somewhat conservative assumptions for July and August. This does not mean that we are apprehensive about our long-term prospects in Mainland China.

While we do intend to aggressively discount products that we need to sell down quickly, we would prefer to maintain prices and gradually sell off items that have long-term appeal rather than enter a discounting war with our competitors. In other words, our fundamental strategy is not to discount excessively to artificially push sales higher but to operate a commercial business of firm substance. We are not concerned about China's growth potential, but we are making conservative assumptions for the reasons I have mentioned.

The pace of e-commerce sales growth has dulled slightly, but, again, this is due to our decision not to discount products too strongly simply to draw in customers. However, e-commerce is improving as a core business. In addition, online-to-offline (O2O) transactions, where online orders are dispatched from stores using store inventory, are rising very strongly in Mainland China. If we include O2O transactions, overall e-commerce sales are growing strongly.

Q: We are witnessing a much stronger global shift towards online shopping. Are you changing your new store opening strategy as a result?

CFO Okazaki – Our fundamental store-opening strategy has not changed, but we do think O2O will continue to grow further. If we can deliver online orders from our stores, then we can also use e-commerce orders to fill any product shortages in stores. In that sense, we are looking to expand sales by advantageously linking store and e-commerce operations. Based on that premise, we must make sure that our stores are places that are worth visiting. The three strategic stores which we opened this spring, UNIQLO PARK Yokohama Bayside Store, UNIQLO Harajuku Store, and UNIQLO TOKYO, represent one possible future model. We must also open more conveniently located smaller stores in

residential and highly populated areas that enable customers to choose from the full range of UNIQLO clothing, and we will also strengthen and develop click and collect and other O2O models.

Store numbers might decline somewhat in markets with mature stores, but those individual stores are likely to increase in size under our scrap and build policy of replacing smaller, less profitable stores with larger, better located ones. That doesn't mean that we are going to increase the size of all our stores, but rather to adjust store size to fit more appropriate locations. In regions where we still haven't built a sufficient store network, such as Mainland China and Southeast Asia, we must continue to open new stores at a robust pace.

Q: Can you tell us about your store rent negotiations during the temporary store-closure period?

CFO Okazaki – While I can't comment on individual contracts, I can tell you that rent was waived completely for some stores and not for others. Conditions also varied in different markets, but, basically, we negotiated tenaciously in individual markets to try and find a level that both sides could agree on, and I think we were reasonably successful.

Q: UNIQLO Japan same-store sales rose 26.2% in June and GU Japan sales recovered extremely quickly to post a 16.4% year-on-year rise in June. How do you evaluate these latest results at UNIQLO Japan and GU?

CFO Okazaki – June sales were greatly influenced by the fact that we were unable to conduct business properly over the May Golden Week holiday and that our regular May anniversary sale was delayed until June. We usually run a four-day anniversary sale, but this time we extended the sale period to two weeks to avoid crowding. The sale was extremely successful and helped to significantly boost June sales. Another key point, we were able to satisfy regular underlying June demand as well.

Customer demand for casualwear, loungewear, “one-mile wear” for indoors and popping out of the house, and sports utility wear is extremely high right now, and our LifeWear product lineup matches this demand perfectly. We began feeling the benefits of that and enjoying strong customer support for LifeWear from the middle of May onwards, and I want to see us match or exceed previous year sales levels in July and August.

Our product strategy was equally or even more successful at GU. The fashion trend right now is for extremely comfortable clothing and the GU operation was able to compile and sell a strong range of trendy comfortable items such as sheer tops, dresses, and men's chef pants. We realized that, even in these tough circumstances, you can earn customer support if you have a strong grasp of the latest mass fashion trends. GU's strong performance reflects that success.

Q: I get the impression that inventories are increasing at a higher-than-expected rate in Europe. How big an impact is this having on performance given the difficulties with reopening stores in that region?

CFO Okazaki – Nearly all our stores in Europe remained closed in the third quarter, so we are holding excess inventory from that region. Most stores are now reopening for business, so, depending on how much inventory we can run down through the end of FY2020 in August and if we can conduct business over the 2020 Fall Winter season without acquiring further excess inventory, then we should be able to orchestrate a recovery in profits in Europe over the first half of FY2021.

Q: If you can't give specific details, just the essence will do, but what is CEO Tadashi Yanai saying within the company right now?

CFO Okazaki – Mr. Yanai says this is a severe time, and the future is unclear. However, he insists the companies that will survive will be those that can firmly grasp changes occurring worldwide precisely at times like these, question their existing methods, search for new ways of doing things and challenge whatever lies ahead with determination. We can't deny the possibility of a second or third wave of COVID-19 infections and must build up defenses to cope with that possibility, but Mr. Yanai stresses the importance of not focusing entirely on that one endeavor but also on issuing new products and ideas, and attacking problems with a bold offensive approach.