

[Reference]

Current Status and Outlook for Shiseido's China Business

Shiseido has steadily expanded the foundation of its China business, which began in 1981 with imports and sales through state-owned department stores and other channels. Subsequently, Shiseido established Shiseido Liyuan Cosmetics Co., Ltd. (SLC) as a joint venture in 1991, Shanghai Zotos Citic Cosmetics Co., Ltd. (SZC) as a manufacturing joint venture in 1998, and Shiseido China Co., Ltd. (SCH) as a wholly owned holding company in 2003. Moreover, during the four-year period up to fiscal 2007, Shiseido's China business sustained rapid year-on-year growth in sales that surpassed 30%, and this business has served as an engine of growth for the entire Shiseido Group. Under the next Three-Year Management Plan, which will commence in 2008, Shiseido aims to achieve average annual sales growth of 20% via a highly focused marketing strategy for each sales channel as well as through further efforts to establish a business foundation that will support this sharp growth in sales.

Current Status of China Business

The department store business, centered on the *AUPRES* brand launched exclusively for the China market in 1994, has been handled by Beijing-based SLC. In addition to the locally produced *AUPRES* brand, the department store business sells imported *SHISEIDO* global brand products as well as products from Japan, such as *IPSA*, exclusively within the department store channel, Shiseido prestige brand *Clé de Peau BEAUTÉ* and designer fragrance brands Jean-Paul Gaultier and Issey Miyake. These products are now sold at approximately 700 stores.

Meanwhile, the Cosmetics Specialty Store business, initiated in 2004 and handled by Shanghai-based SCH, has steadily expanded its sales network centered on its mainstay *URARA* brand for Chinese cosmetics specialty stores. As of the end of 2007, the Shiseido Cosmetics Specialty Store business covered 28 administrative regions in China, excluding Beijing, Shanghai, and Chongqing, and has increased the number of its contracted stores to 2,500.

In addition to the department store channel and cosmetics specialty (CS) stores, for other cosmetics sales channels, which have begun to diversify in recent years, Shiseido's *AQUA LABEL* skincare brand is sold at Watsons chain drug stores, along with its *Za* skincare and makeup brand for young consumers and *UNO* men's products, as a means of responding to a wide range of channels and in aiming to meet a broader range of customer needs.

Growth Strategy for the Department Store Channel in China

AUPRES, a core brand at department stores, will undergo a total renewal in April 2008. In the two brands of anti-aging and whitening products, 22 types of products in 10 categories are now sold, and

makeup and other brands will be successively renewed as well. On this occasion, Shiseido will revamp its sales counters, customer response methods and brand communications, and in the future will maintain or raise the positioning of *AUPRES* as a Chinese national brand. Shiseido will strive to achieve a 70% increase in the number of loyal users after three years, from the current 1.2 million to 2.10 million. (Refer to the reference materials.)

Nonetheless, with imported *SHISEIDO* brand products facing increasingly fierce competition from European and U.S. brands, Shiseido will introduce newly designed counters and launch products that are highly popular in Japan as a “regional lines originating from Tokyo.” This approach is in brand with initiatives to strengthen overall marketing, with plans calling for increasing the number of loyal users from the current 200,000 to 350,000 after three years.

Moreover, to establish a structure for cultivating each of these brands, in January 2008 SLC, which oversees all brands handled through the department store channel, will focus exclusively on the *AUPRES* business, while the handling of business for *SHISEIDO* and other imported product business has been transferred to SCH. The Prestige Cosmetics Business Division has been newly established within SCH to handle these imported products. At the same time, the Prestige Business Department (SCH) will handle negotiations with department stores as the representative for all brands within the Group sold at department stores in China, a move aimed at strengthening Shiseido’s negotiating power as a group.

Additionally, to expand the number of prime customers and raise repeat visit rates for stores, Shiseido will renew training for store beauty consultants (BC) while also reflecting the repeat visit rate at stores in BC personnel evaluations.

Shiseido is aiming to secure stable growth in the department store channel via the above strategies, targeting average annual sales growth in the 10% range for the Shiseido Group.

Growth Strategy for Cosmetics Specialty Store Channel

In the cosmetics specialty (CS) store channel, Shiseido will shift product selection and contract conditions, which had been uniform at all stores up to the present, toward a stratification strategy to provide an enhanced range of products according to the store. In addition to the CS store format that until now has handled multiple brands centering on *URARA*, Shiseido will establish new “*PURE&MILD* Excellent Stores,” a format that will be limited to handling mid- and low-price range skincare products, such as *PURE&MILD*, while leaving intact such basic business conditions as full-time sales staff as well as the installation of POS systems and specialized equipment. Unlike CS stores, “*PURE&MILD* Excellent Stores” cannot be designated as “stores handling Shiseido products.” However, limiting the products handled by these stores in this manner will permit a reduction in stores’ initial investments and their inventory burdens. Effectively, by expanding the number of these “*PURE&MILD* Excellent Stores” along with CS stores, Shiseido will broaden its

base of customer segments both in terms of price range as well regions in which stores are opened.

Regarding products, Shiseido will expand and upgrade items for increasing loyal customers of the mainstay *URARA* brand. During 2008, Shiseido will launch sales of *Elixir Superieur*, which is already being sold in Japan, as it strengthens its response to affluent customers in China.

Turning to sales staff training, Shiseido will expand its training curriculum for customer response methods. At the same time, during fiscal 2008, Shiseido will dispatch a total of 45 BCs for a period cumulatively exceeding 2,000 days as we promote the spread of Shiseido-style counseling through on the job training at stores.

By implementing these strengthening measures, Shiseido aims for a more than 2.5-fold expansion in the current number of loyal customers at present, to 1.8 million, and to achieve average annual sales growth of around 20% - 30% in the CS store channel in three years.

Cross-Channel Brand Growth Strategy

Besides brands limited to department stores and CS stores, Shiseido will also strengthen the cultivation of brands sold across multiple channels. Shiseido will strive to raise in-store shares and cultivate established *Za* and *UNO* brand as well as *TSUBAKI* and *Aquair* hair care products, mainly at key customer stores, including department stores, general merchandizing stores, drug stores, and CS stores. At the same time, from March 2008, Shiseido will introduce appealing select *be* brand functional products exclusively for the China market in working to further expand points of contact with customers.

Creating a Foundation for Sustainable Growth

By strengthening marketing within the aforementioned channels, during the next three-year period, Shiseido plans to secure average annual sales increases of 20% for its entire China business. To support this rapid increase in business scale, Shiseido will also continue strengthening various business infrastructures. At the same time, Shiseido will secure and cultivate excellent human resources indispensable for strengthening business competitiveness while bolstering the business infrastructure, in such areas as supply chain management and information systems.

To fulfill its corporate responsibilities as a member of Chinese society, Shiseido will actively undertake social contribution activities more than ever before and raise not only its corporate economic value but also enhance its *raison d'être* in Chinese society in aiming to become a company that is truly trusted by people in China.