POLA ORBIS HOLDINGS

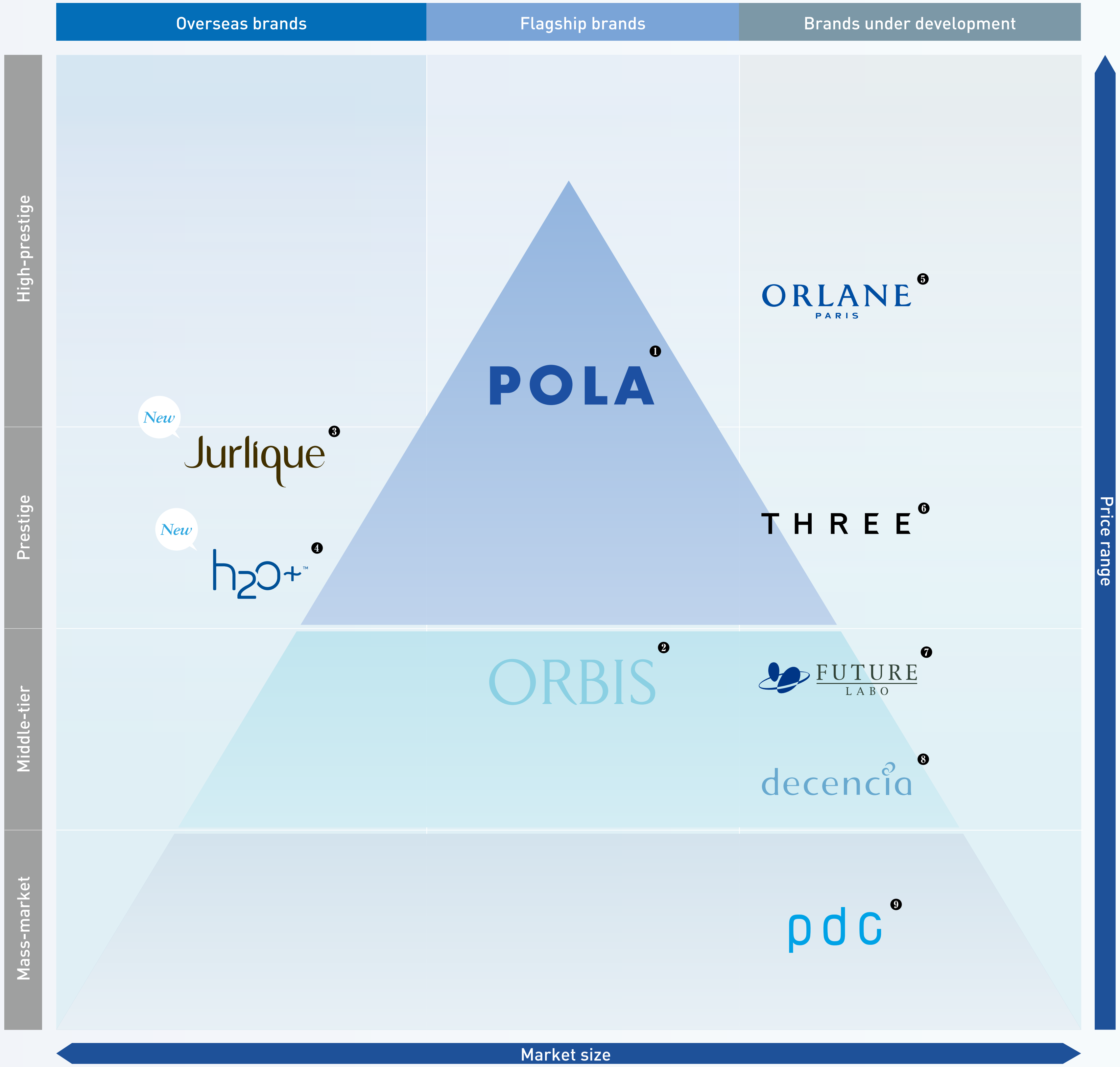
Annual Report 2012 Year ended December 31, 2012

Group Philosophy

Inspire all people and touch their hearts.

Overview of Our Business

The POLA ORBIS Group is engaged in businesses related to beauty and health, centering on cosmetics, a segment that dates back to 1929 and the establishment of POLA INC. The Group subscribes to a multi-brand strategy designed to utilize the unique qualities and well-defined identity of each brand to fuel growth and capture bigger shares in various markets.



❶ ***POLA INC.***
Boasts strengths built on leading-edge technology in the fields of anti-aging and skin-whitening. Promotes consulting-based sales through a domestic network of approximately 4,700 sales offices and more than 145,000 POLA LADIES.

❷ ***ORBIS Inc.***
Provides original-concept 100% OIL-FREE skincare products along with services that have earned a high level of customer satisfaction. Utilizes mail-order channels, such as online sales and catalogs, as well as retail stores, to market products.

❸ ***Jurlique International Pty Ltd***
Operations based on a cosmetics brand with organic benefits, exemplified by ingredients made from the herbs grown on Jurlique's 153-acre farm in South Australia under pesticide-free, biodynamic farming methods.

❹ ***H2O PLUS HOLDINGS INC.***
Markets products made with natural, sea-derived ingredients, such as seaweed.

❺ ***ORLANE JAPON INC.***
Exclusive distributor of ORLANE, a luxury brand of anti-aging skincare cosmetics from France, in Japan.

❻ ***ACRO INC.***
Markets THREE, a prestige brand of natural skincare products and innovative cosmetics, at department stores.

❼ ***FUTURE LABO INC.***
Offers products with unique features through TV shopping channels.

❽ ***decencia INC.***
Markets products for dry, sensitive skin primarily through mail-order sales.

❾ ***pdc INC.***
Sells affordably priced cosmetics through general retail channels, such as drugstores.

Table of Contents

Forward-looking statements
This annual report contains projections of performance and other projections based on information available as of February 14, 2013 and certain assumptions judged to be reasonable. Actual performance may materially differ from these projections resulting from changes in the economic environment and other risks and uncertainties.

Financial Highlights

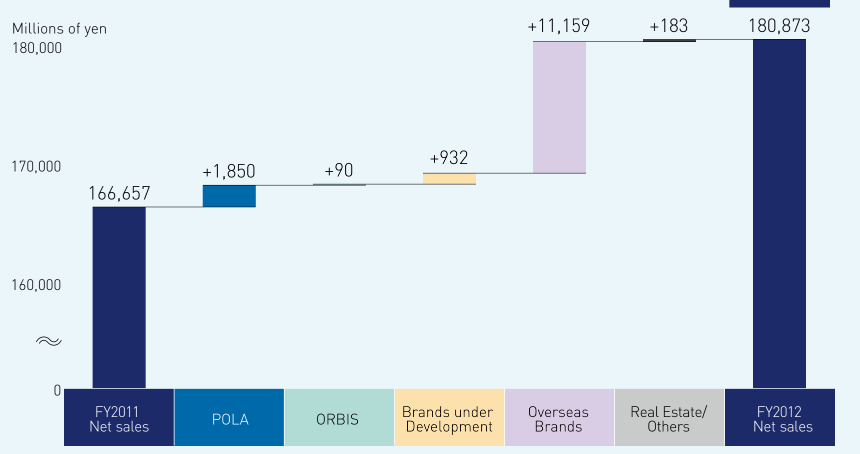
POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

Five-Year Summary of Selected Financial Data

Years ended December 31	2008	2009	2010	2011	2012	2012
	Millions of yen (Except per share data)					Thousands of U.S. dollars*1 (Except per share data)
Operating Results						
Net sales*2	¥170,838	¥162,332	¥165,253	¥166,657	**¥180,873**	**$2,089,094**
Beauty Care		150,330	153,091	154,778	**168,811**	**1,949,780**
POLA		96,363	96,543	97,353	**99,204**	**1,145,810**
ORBIS		47,663	49,356	47,918	**48,009**	**554,506**
Brands under Development		6,304	7,192	7,654	**8,587**	**99,183**
Overseas Brands				1,851	**13,011**	**150,281**
Real Estate		3,216	3,102	3,089	**2,841**	**32,819**
Others		8,787	9,059	8,790	**9,220**	**106,495**
Operating income	10,868	9,706	12,270	12,853	**13,520**	**156,158**
Beauty Care		7,910	10,165	10,787	**11,812**	**136,438**
POLA		4,702	5,592	6,168	**7,031**	**81,218**
ORBIS		5,364	6,169	6,526	**7,881**	**91,033**
Brands under Development		(2,156)	(1,596)	(1,826)	**(1,202)**	**(13,892)**
Overseas Brands				(81)	**(1,897)**	**(21,921)**
Real Estate		1,598	1,304	1,283	**1,139**	**13,159**
Others		(696)	223	501	**335**	**3,872**
Operating margin (%)	6.4	6.0	7.4	7.7	**7.5**	
Net income	6,559	4,059	7,086	8,039	**6,681**	**77,170**
Financial Position						
Net assets	137,564	140,890	153,104	157,057	**164,896**	**1,904,556**
Total assets	180,664	181,909	187,771	193,027	**209,140**	**2,415,577**
Cash Flows						
Cash flows from operating activities	16,419	12,530	17,906	14,401	**17,592**	**203,193**
Cash flows from investing activities	(5,808)	(4,374)	(40,367)	(3,444)	**(39,625)**	**(457,674)**
Cash flows from financing activities	36	(1,125)	(2,789)	(4,093)	**(3,280)**	**(37,886)**
Cash and cash equivalents at end of year	61,803	68,817	43,507	50,246	**25,106**	**289,980**
Depreciation and amortization	4,602	4,973	5,361	5,374	**6,466**	**74,686**
Capital expenditure	5,655	8,639	6,245	5,048	**9,609**	**110,989**
Financial Indicators						
Equity ratio (%)	76.0	77.4	81.5	81.3	**78.8**	
Return on equity (%)	4.9	2.9	4.8	5.2	**4.2**	
Return on assets (%)	5.2	5.7	6.6	7.0	**7.3**	
Price-earnings ratio (times)*3	—	—	12.3	14.3	**20.5**	
Per Share Data						
Net income per share	127.91	79.16	137.36	145.43	**120.86**	**1.40**
Net assets per share	2,677.47	2,743.87	2,767.55	2,839.36	**2,980.48**	**34.42**
Cash dividends per share	20	20	40	45	**50**	**0.58**

*1 Dollar amounts are shown for convenience only and are calculated based on the prevailing exchange rate of U.S.$1=¥86.58 as of December 31, 2012.
*2 Net sales do not include consumption taxes.
*3 The price-earnings ratio is not shown for fiscal 2008 and 2009 as the stock was not listed.

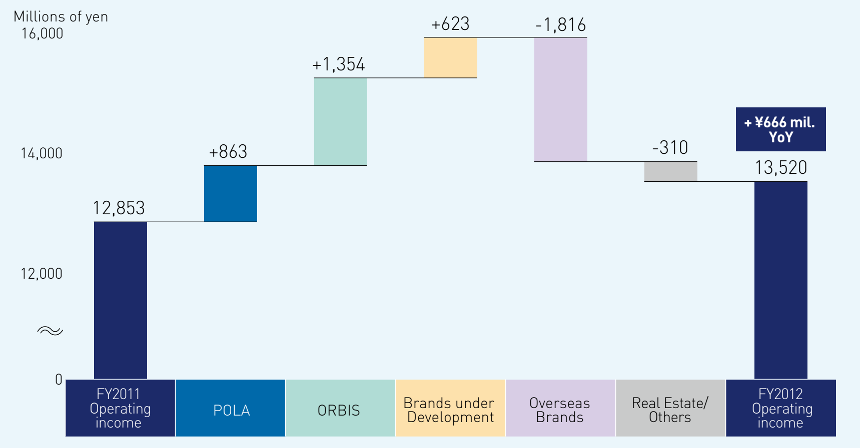
Factors Impacting Net Sales



Key Points: Net Sales

Consolidated net sales was ¥180,873 million, a ¥14,215 million, or 8.5%, increase from the previous fiscal year. In addition to the solid performances of the flagship brands POLA and ORBIS, Jurlique, which was newly consolidated in February 2012, recorded net sales of ¥10,018 million; and the net sales of H2O PLUS, which joined the Group in July 2011, was fully reflected in the consolidated financial results. These factors led to a significant increase in consolidated net sales.

Factors Impacting Operating Income

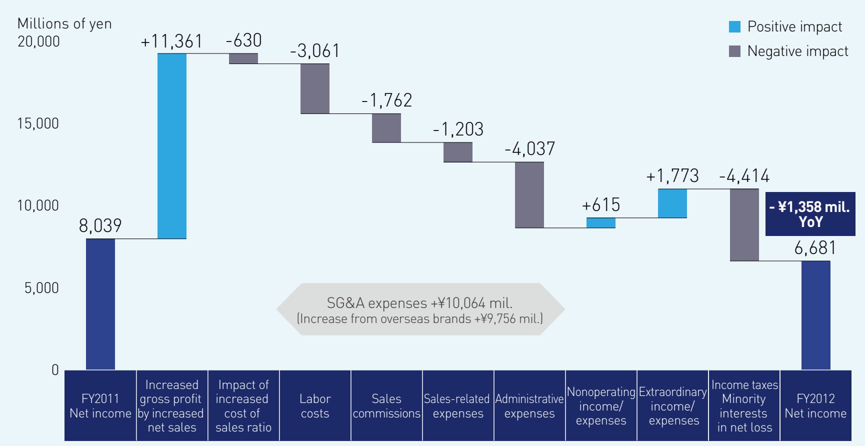


Key Points: Operating Income

Consolidated operating income was ¥13,520 million, a ¥666 million, or 5.2%, increase from the previous fiscal year. POLA generated an increase in net sales and controlled SG&A expenses, while ORBIS actively pursued the rebuilding of its brand. These factors led to significant increases in their operating income. Jurlique recorded an operating loss of ¥1,185 million owing to M&A-related expenses totaling ¥1,886 million, which included a one-time expense of ¥901 million.

Note: The year-on-year change of -¥47 million in reconciliations is not shown.

Factors Impacting Net Income



Key Points: Net Income

Consolidated net income was ¥6,681 million, a ¥1,358 million, or 16.9%, decrease from the previous fiscal year. Gross profit increased ¥11,361 million, accompanying the increase in consolidated net sales. However, amortization expenses from M&A activity, SG&A expenses associated with overseas brands, and a significant hike in the tax rate led to a decrease in consolidated net income.

Note: Jurlique consolidated from February 2012
H2O PLUS consolidated from July 2011

President's Message

We will move steadily forward, maximizing our inherent strengths, to realize our long-term vision of becoming a "highly profitable global company."

The POLA ORBIS Group adheres to each strategy implemented by POLA ORBIS HOLDINGS, starting with a multi-brand strategy, and uses these strategies to overcome various challenges and introduce necessary innovations. In the last few years, this commitment has begun to yield rewards, and in fiscal 2012, ended December 31, 2012, amid persistently difficult market conditions, the Group posted higher sales and higher operating income for the third consecutive year. Net sales rose 8.5% over the previous fiscal year, to ¥180,873 million, and operating income increased 5.2%, to ¥13,520 million. Indeed, fiscal 2012 was a year of definite progress on the road to realizing the Group's long-term vision of becoming a "highly profitable global company."

Going forward, we will not rest on our laurels but rather strive for higher levels of success. With this in mind, we will take our growth strategies to the next stage in fiscal 2013, the last year of the medium-term management plan.

Satoshi Suzuki

鈴木郷史

President

An Interview with the President

Q What trends have characterized the domestic and overseas cosmetics markets in recent years?

A In Japan, amid generally flat demand for cosmetics, interest in skincare products has been relatively favorable. In overseas markets, demand in Asia has sustained growth.

The domestic cosmetics market continued to rally from the impact of the Great East Japan Earthquake in March 2011, but the momentum of economic recovery was rather weak and business conditions remained difficult. A bright point, however, was the skincare field, a key domain for the Group and a business area that enjoyed relatively favorable demand. In the immediate future, demand for cosmetics is likely to remain flat overall, and demand for skincare products will probably hold steady or rise slightly.

Overseas, demand for cosmetics continued to expand, particularly in Asia. Regarding China, there is a sense that the economic powerhouse is slowing, but the prospect of double-digit growth is still a strong possibility. The ASEAN region, the next growth market after China, should maintain a 5%–8% annual growth rate.

Q How were domestic results in fiscal 2012, and how do you plan to proceed with your strategies going forward?

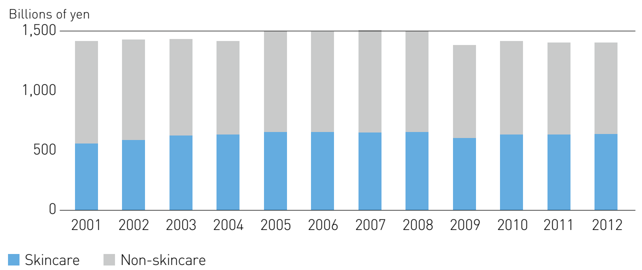
A Flagship brands delivered higher sales and a huge improvement in profits. Existing strategies will be maintained.

The flagship brand POLA achieved solid results through ongoing efforts to enhance the *B.A* series and a favorable market reception to new products. To strengthen its sales channels, POLA pushed measures to invigorate the frontline sales structure. The total number of sales offices continued to grow, increasing by 115 from fiscal 2011, and the opening of new POLA THE BEAUTY stores along with higher sales at existing stores led to a steady improvement in net sales. Operating income climbed more than 10%, primarily through more efficient use of the marketing budget.

In fiscal 2013, POLA will aim for a larger share of the luxury skincare market and boost sales from the POLA THE BEAUTY network.

ORBIS actively pursued the rebuilding of its brand and promoted measures to emphasize structure rather than expansion in sales. Under a new brand statement, "*OIL-FREE STYLE,* WE ARE.," ORBIS attracted more customers who identified with the sense of values that this brand embodies and set the stage for stable growth into

Domestic Cosmetics Shipments



Source: The Office of Current Survey for Mining and Manufacturing, Ministry of Economy, Trade and Industry

Overseas Cosmetics Market Trends

China	Slowing down from CAGR of 12%–15% but likely to sustain double-digit growth
ASEAN	Forecasted growth of CAGR of 5%–8%
Russia	Expected growth of CAGR of 3%–5%

Note: CAGR calculated by POLA ORBIS HOLDINGS INC.

the future. In fiscal 2012, ORBIS posted higher sales per customer, larger contributions from both skincare sales and online sales. This underpinned an operating margin exceeding 16% and a significant increase in profitability.

In fiscal 2013, ORBIS will accelerate efforts to rebuild its brand and strive to achieve further improvement in profitability, with an emphasis on greater cost-efficiency in logistics operations.

Q Why has the POLA ORBIS Group been able to realize growth that outpaces that of the market?

A Our success demonstrates excellence through the strengths of our multi-brand strategy, direct selling, and product development.

The favorable progress made by the POLA ORBIS Group reflects steady expansion of market share, driven by ongoing efforts to respond to the diversification of customer needs through our multi-brand strategy as well as brand images made distinctly clear through a structure that assigns one brand to one company under the scope of the Group.

Another major strength is our personal approach to customers through direct selling, a marketing approach that facilitates access to customer information and close follow-up and also supports administrative processes such as inventory control.

In regard to product development, we utilize a database of 13.8 million data sets of Japanese women's skin attributes in the course of business, and we concentrate the investment of resources, such as capital and personnel, into the skincare business. This emphasis underpins the successful development of original ingredients with a high level of excellence from a market perspective for application in equally outstanding products. Our capabilities are top tier, substantiated by such honors as an IFSCC* Poster Award at the IFSCC Congress—the Olympics of the cosmetic science and technologies field—in fiscal 2012.

Our multi-brand strategy, adept use of a direct-selling business model, and strong capabilities in skincare development are the pillars that support the Group's growth. These factors will undoubtedly sustain business results that consistently exceed the industry average.

* International Federation of Societies of Cosmetic Chemists

B.A Summer series

AQUAFORCE EXTRA series

Q What strides did the Group make in overseas operations in fiscal 2012, and what is on the activity agenda going forward?

A1 We brought Jurlique into the Group in February 2012. Overseas sales, as a percentage of total consolidated sales, edged up five percentage points.

Jurlique, which came under the scope of the Group in February, contributed favorably to consolidated performance, most notably with net sales of ¥10.0 billion. Expansion of the brand in China was particularly outstanding, supported by an increase of 29 locations in the store network, to 69.

H2O PLUS, which became a part of the Group in 2011, is working toward medium- to long-term growth of its brand, and in this pursuit engaged a different agent in China. The switch caused some setbacks, including stalled shipments, which prevented H2O PLUS from reaching its initial target for the fiscal year ended December 31, 2012. Nevertheless, the launch of products developed jointly with POLA CHEMICAL INDUSTRIES was a tangible result of synergies fostered by the use of management resources within the Group.

A2 We maximized the resources of the two overseas brands to raise our profile as a global enterprise.

Going forward, we will aggressively promote strategies designed to achieve our long-term vision. (Please refer to page 12.) In January 2013, we set up the Global Business Strategy Division as a base point for the Group's overseas development process. This division will formulate marketing strategies geared to each country and region, in line with the multi-brand strategy which seeks to boost market share through several brands, and accelerate efforts to demonstrate synergies among the brands handled by Group companies. A priority will be placed on China and other key areas in Asia where demand for skincare is particularly high.

Jurlique will continue a program of aggressive investment, emphasizing China, and aims for better than double-digit sales growth. In the medium term, Jurlique is sure to become a brand that contributes significantly to enhanced profitability on a consolidated basis.

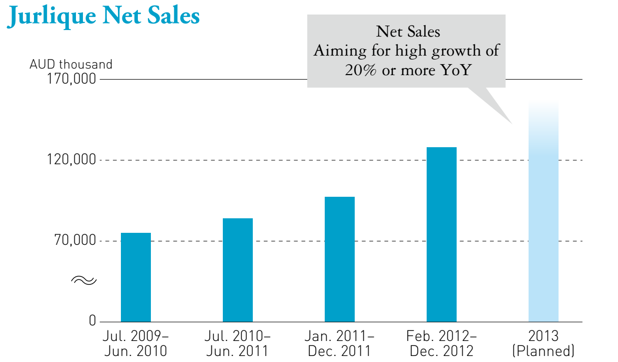
H2O PLUS is also targeting sales growth in the double-digit-plus range, supported by the new agency structure.

THREE will benefit from the distribution know-how acquired from overseas brands and apply this advantage in promoting its products in Thailand.

For our flagship brands, ORBIS will step up efforts to build a stronger presence in the ASEAN region, and POLA will emphasize a higher profile in Thailand and China.

Graceful Beauty series

Jurlique Net Sales



Q What are your thoughts on capital policy?

A We will make investments for future growth as we strengthen profitability, and improve efficiency to enhance our corporate value.

In our long-term vision, we have set performance goals of ¥250 billion for consolidated net sales, a ratio of between 13% and 15% for operating margin, and an overseas sales ratio of 20% to be achieved by 2020. Working toward these targets, the POLA ORBIS Group will prioritize a three-point strategy that balances investments for future growth, profitability, and efficiency, based on a solid financial footing and sufficient cash to finance business expansion.

Investments for Future Growth

The primary application of cash will continue to be for overseas investments, such as M&As. The perspective that guided our acquisition of Jurlique and H2O PLUS will continue to direct us toward carefully selected targets with well-defined brand concepts and the potential to raise profitability to the level we seek to achieve in our long-term vision.

Profitability

While we make investments for future growth, we will also actively pursue investment opportunities overseas while seeking to reinforce the profitability of domestic operations. In fiscal 2012, in our flagship brands we lowered the cost of sales ratio by focusing on skincare products and also effectively distributed marketing expenses. These efforts led to an increase in operating income of over 10%. Going forward, we will strive to enhance the efficiency of the entire supply chain, emphasizing reduced costs and lowering the cost of sales ratio, by optimizing production and our logistics structure.

Efficiency

From a selection-and-concentration perspective, we have withdrawn from several business areas since 2000, selling our food company and bookstore operations, and then in 2011, our commercial printing business and real estate with low profitability. We will continue to concentrate management resources into the cosmetics business, which is expected to generate high returns over the medium to long term and thereby boost asset efficiency.

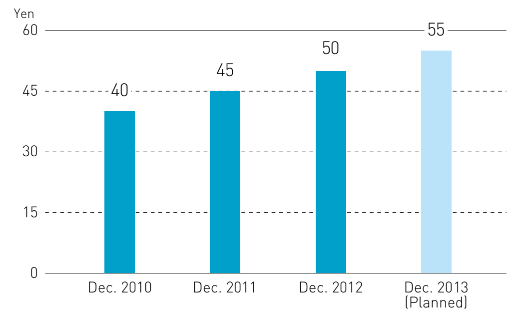
These strategies will guide our efforts to achieve our long-term vision, that is to say enhancing corporate value, and we will push forward on organized and flexible investments for future growth and promote measures to realize higher profitability and efficiency.

Q What are your thoughts on return to shareholders?

A We will strive to realize a higher return to shareholders while working to maintain our investments aimed at future growth.

We consider the return of profits to shareholders to be one of our most important management obligations, and our general policy is based on stable dividends with increases pegged to profit improvement. Since the IPO, we have increased the dividend by ¥5 every year, with accompanying increases in operating income. Thanks to a robust performance in fiscal 2012, the dividend has been set at ¥50 per share, up ¥5 from a year ago. Going forward, we will make every effort to realize a higher return to shareholders while working to maintain our investments aimed at future growth.

Dividends per Share



Q What is the outlook for fiscal 2013, and what can shareholders expect from the POLA ORBIS Group?

A We are united in our quest to achieve one of the industry's highest operating margins.

We anticipate a fourth consecutive year of higher sales and income for fiscal 2013, with net sales of ¥188,500 million, up 4.2% year on year; operating income of ¥16,000 million, up 18.3%; and net income of ¥8,200 million, up 22.7%. These results would warrant a ¥5 increase in the dividend, to ¥55 per share.

The cosmetics market is seeing a steady influx of new participants, which will create a more competitive operating environment. Nevertheless, the POLA ORBIS Group will uphold the multi-brand strategy, and each Group company will steadily build an enhanced profile for its assigned brand and promote complementary strategies that make the most of inherent strengths.

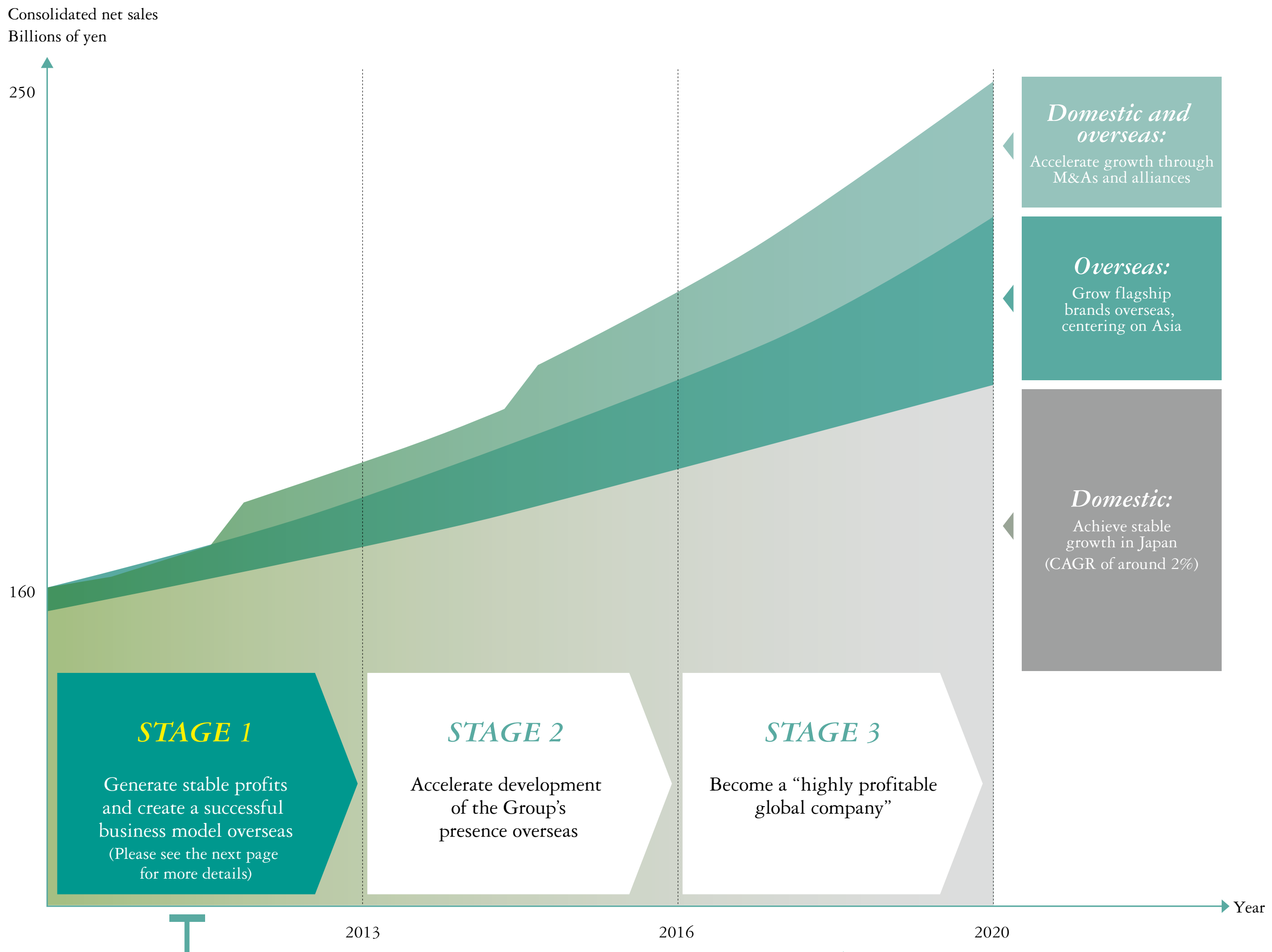
Our goal is to become a "highly profitable global company" in the field of beauty and health, and we will strive, as a group, to reach this goal.

Management Plan

To ensure further growth and create additional corporate value, we formulated a long-term vision for the POLA ORBIS Group that looks ahead to 2020 and embarked on a medium-term management plan that runs from fiscal 2011 through fiscal 2013. We will accelerate development of the Group's presence overseas with the aim of becoming a global company in the field of beauty and health.

Toward Long-Term Vision 2020

Management Indicators	Net Sales	Operating Margin	Overseas Sales Ratio
	¥250 billion or more	13%–15% (Top tier in the industry)	20% or higher



MANAGEMENT PLAN

2011–2013 Medium-Term Management Plan

STAGE 1 Generate stable profits with flagship brands and invest funds to implement growth strategy

Management Indicators	Net Sales	Operating Income	Operating Margin
	CAGR of 2%–3%	CAGR of 10% or higher	9% (10% in Japan) in 2013

Strategy 1 Generate stable profits with flagship brands

POLA
- Increase profits from POLA THE BEAUTY
- Increase market share in luxury skincare cosmetics
- Accelerate creation of new sales office

P30 Review of Operations

ORBIS
- Implement measures to rebuild the ORBIS brand
- Reinforce earnings structure

P32 Review of Operations

Invest profits

Strategy 2 Accelerate growth of the portfolio of brands under development

pdc
FUTURE LABO
ORLANE PARIS
decencia
THREE

- Establish brand identity and raise respective market shares

P34 Review of Operations

Strategy 3 Develop the Group's presence overseas by capitalizing on the Group's strengths

POLA
- Develop door-to-door sales channels in China

ORBIS
- Expand mail-order sales business in China

Jurlique
- Accelerate growth and improve profitability in Asia

H2O+
- Achieve synergistic effects

P24 Special Feature 2

Strategy 4 Reinforce R&D capabilities

- Reinforce skincare ingredient development capabilities
- Especially in the fields of anti-aging and skin-whitening

P35 Topics

Strategy 5 Reinforce the operating base

- Enhance brand recognition (unaided recall)
- Business process management
- Concentration on core competence
- Step up personnel training

P38 Corporate Governance

Management Insights

In the President's Words: POLA's Recovery, Return to Growth Track

POLA maintains stable growth as a flagship brand of the POLA ORBIS Group, representing 60% of net sales. The brand is back on track after a slump that dates back to the 1980s, paralleling serious challenges to the success of POLA's door-to-door sales channel. Satoshi Suzuki, president of POLA ORBIS HOLDINGS INC., speaks about returning to the desired trajectory.

We applied a foundation of unique components—the DNA of door-to-door sales—to successfully establish a new business model

Today, when shareholders and investors ask "What are POLA's strengths?" everyone at POLA probably rattles off three in quick succession—direct selling, the customer management system, and skincare products.

POLA THE BEAUTY, which debuted in 2005, has been embraced by customers as if the format had existed for ages, and stores have been opened far and wide, all over the country. The customer management system, coordinated by the head office, came on line in 2008 and has become a standardized, indispensable marketing tool. Also, *B.A*, the anti-aging series so readily associated with the POLA name, has permeated market consciousness.

These strengths—a novel sales strategy, a pivotal marketing tool, and an innovative product line—are seamlessly integrated into POLA today, but the road to this destination was a rather long and winding one. The conditions that prevailed and the reasons behind each development were varied. Nevertheless, I was determined to make such important innovations.

Over the next few pages, we offer shareholders and investors some background into the three measures that currently support the growth of the POLA brand, along with comments from staff who were responsible for each of these areas that underpinned a revitalized POLA.

Steps in the Revitalization of the POLA Brand

2000	New president assumes duties. Delivers "Consulting First" corporate message.
2002	New Business Declaration: Establishes system to promote esthetic treatments and provides the necessary training (full-scale start of esthetic business).
2003	Launches REFRESIA business, the precursor to POLA THE BEAUTY. Sells Pola Foods Co., Ltd., a noncore business, and concentrates resources into the cosmetics business.
2005	Opens first POLA THE BEAUTY store. ▶Page 15
2006	POLA ORBIS HOLDINGS INC. is established and the Group transitions to a pure holding company system.
2007	POLA Sales Inc. is integrated into POLA INC., to realize a flat organization.
2008	Platform system "Slim" goes on line. ▶Page 16
2010	Launches *B.A* series with four products at once. ▶Page 17

POLA THE BEAUTY Expansion

The original business model derived through repeated trial and error rejuvenated the frontline sales network as well as the customer base

Realizing the Potential of a Business Model Using Esthetic Treatments to Attract Customers

In 2000, immediately upon assuming the position of president, I traveled around the country for meeting after meeting with sales office managers and frontline POLA LADIES. What came out of these meetings was the idea that a business model incorporating esthetic treatments in the service structure had a chance of success.

There were about 5,000 sales offices at the time, and when I broke them down by business model according to the level of esthetic treatments provided, a gap of close to 10% appeared in the year-on-year results of sales offices that offered such services and those that stayed with traditional door-to-door operations. In addition, in comparing other factors, such as the average age of POLA LADIES and the sales ratios of new POLA LADIES to total sales, the locations that were able to attract customers with the availability of esthetic treatments fared better. Up until then, sales offices had been broken down only by a simple performance ranking, so the content-based classification process was a daunting task. But the effort proved worthwhile, because the analysis of results clearly indicated that a business model using esthetic treatments to attract customers had potential, and in 2002, I decided that we should execute a definitive change in business format.

Successful New Business Model Established Through Trial and Error

In 2003, POLA launched REFRESIA, the precursor to POLA THE BEAUTY, under a business model using esthetic treatments to attract customers, but the REFRESIA strategy was a huge failure. Without sufficient investment from the head office, sales office managers on the frontline could only convert sales offices into visually consistent stores with the facilities to provide esthetic treatments. The cost of opening a store in a high-traffic area was too much of a financial burden, and the subsequent lack of stores in good locations prevented the anticipated increase in customers from materializing.

In light of this history, the head office decided to cover a substantial portion of POLA THE BEAUTY's initial investment, which made it possible to open stores in good locations in the heart of commercial districts. In the past, store expenses were covered by sales commissions, so a change from the accepted practice required a management decision bigger than any I had made before.

Now, seven years after the opening of the first POLA THE BEAUTY store, sales are brisk and contributions to POLA profits are on the rise at stores that have fully written off depreciation. Seeing this progress, I know that my decision back then was the right one.

Through POLA THE BEAUTY, we successfully established a new business model that evolved from traditional door-to-door sales corporate DNA. The sales frontline, rejuvenated by an increase in younger customers and younger POLA LADIES, is bursting with energy. Indeed, the whole company has been invigorated by enhanced brand exposure, and the store network is contributing substantially to a recovery in business results.

A Manager's Reflections on Past Achievements

"When we were opening the POLA THE BEAUTY stores, I was determined to support the young managers and POLA LADIES who had this great potential so that they could grow even further. I believed that there would be no future for POLA if they were not given the chance to grow. I spoke with every one of the manager candidates to be sure that they had the right determination and drive to become a manager for POLA THE BEAUTY.

The hardest part was to not only improve the quality of customer service but also to standardize the level of quality at our stores. We devoted ourselves to opening premium POLA stores—stores that offer a high level of customer service that meets customers' expectations. Up until the time we opened our 200th store, I personally visited each and every store to check the quality of service offered. I am very pleased to say that many of these stores became quite successful."

Kyoko Koizumi
Corporate Officer of POLA INC.

Introduction of Platform System "Slim"

"Slim" could be a huge advantage for POLA in an era of one-to-one marketing

PC Installation at Sales Offices Welcomed by POLA LADIES

Back in 2000, it was common for POLA LADIES to keep a notebook of customer profiles and purchase history, so the head office had little way of knowing exactly who bought what and when.

So when I became president, I saw a real need to install personal computers at sales offices throughout Japan and I proposed the idea. This met with some opposition, with comments like "The frontline is getting old and you'll only cause confusion if you try to push computers at seniors." But when I went around to all the sales offices and carefully explained the need for computers and the merits to be gained by using computers, the frontline POLA LADIES were far more receptive than expected and the establishment of a PC environment was quickly completed. As this example aptly demonstrates, the accommodating nature of POLA LADIES and their proactive stance to make the most of an opportunity show that POLA LADIES themselves are a major strength of the POLA brand.

"Slim" Contributes to Higher Sales per Customer and Improved Repeat Ratio

The installation of computers was followed by the introduction of a series of systems, including an order management system and a customer management system. In 2008, the current platform system "Slim" (Sales for Lucid IT Management) was completed, effectively networking sales office computers with the head office. With Slim in place, the head office is able to analyze customer information, which can be used to provide frontline sales offices with fine-tuned support, such as marketing tools for grouping customers and creating lists. The use of Slim also ties into higher sales per customer and an improved repeat ratio, through the use of data to pinpoint customers most likely to purchase debut products and to develop effective and efficient advertising campaigns targeting such customers. I believe the business of skincare centers on the repetition of a simple cycle. That is, the business perpetuates itself if the customers who purchased products three months ago replace those products now. POLA is a company that can make this cycle work.

A Manager's Reflections on Past Achievements

"Before implementing "Slim," customer purchase histories were managed by each sales manager and POLA LADY, so it was difficult to approach or follow up on customers effectively based on their purchase histories. After implementing Slim, a standardized system for managing customer information, the head office could analyze the sales data on Slim and use that analysis to support sales offices.

We set goals and plans for sales managers and POLA LADIES and made sure that these goals and plans were achieved for each customer, by constantly monitoring their progress and proposing recovery plans if and when necessary. As a result, we were able to minimize the number of customers leaving our brand and increase the number of loyal customers. These activities significantly contributed to improving POLA's overall performance.

I truly believe that it is my great responsibility to make as many customers as possible smile and contribute to stably enhancing POLA's performance through utilizing tools like Slim."

Masayuki Sasaki
Niigata Area Manager, POLA INC.

B.A Series Launches Four Products at Once

Created from a customer perspective, the B.A series has become the face of the POLA brand

B.A Series Captures 67 Best Cosmetics Awards

Initially, POLA did not recognize the need to create a brand image through an entire collection of products. Back in 2000 the *B.A* series was adding one new product each year, but the objective was not so much to give customers another choice but rather to spark motivation among POLA LADIES. Essentially, the convenience of the seller was given priority. As I am fond of saying, a cosmetics company must always put the customer first, so I was on the lookout for an opportunity to redirect the perspective that guided corporate activities, away from "product-out" and toward "market-in."

Around the time that expansion of the POLA THE BEAUTY network accelerated and sales really got on track, I looked at the effect that the Lehman Shock had had on business results and realized we needed to focus more on skincare to secure profitability. I knew a product series that would define the brand was essential, and so I decided that four new products in the *B.A* series would debut simultaneously in autumn 2010. Development activities had been moving along under the assumption that just one item—*B.A The Cream*—would be launched, so the announcement must have put the team responsible for *B.A* into quite a panic. Nevertheless, a project was initiated at once to revamp the whole line.

The comprehensive renewal of a pinnacle series, however, is no easy task. Each item in the *B.A* series reflects the successful pursuit of top-quality ingredients and leading-edge technologies, so research and product development must go through an enormous number of stages. The development team carried an extremely large burden. All involved, however, saw their efforts rewarded, as the revitalized *B.A* series was a huge hit.

During the design of the containers for these four products, I indicated that the color would change from *B.A*'s characteristic gold scheme to black. Containers for entry-level *B.A RED*, which was a follow-up line, would be *red* and those for the subsequent *B.A* skin-whitening series would be *white*, arranging *B.A* into a three-color collection. This successfully defined the growing realm of *B.A* products.

Thus far, in the two years since its debut, *B.A* has achieved splendid success, substantiated by a total of 67 Best Cosmetics Awards, mainly from beauty magazines. Many customers now acknowledge POLA as a prestigious cosmetics brand—recognition that bodes well for the future.

A Manager's Reflections on Past Achievements

"Launching the entire product line of *B.A* at once—it took us a while to come to make this decision. Will development be ready in time? Will our sales personnel be able to learn the products and establish the necessary sales operations? But after much consideration, we were determined that this was the right time to launch the *B.A* brand in the best way possible, and this was a great opportunity for us to work on problems we had not yet been able to solve. We truly wanted to strengthen POLA by having absolute presence at cosmetic counters and stores. Also, since we designed these products to have perfect synergies, we thoroughly trained POLA LADIES so that they could present the value of these products to the customers with confidence."

Taeko Nishibara
Corporate Officer of POLA INC.

Business Results Represent a Mountain of Management Decisions over the Past 10 Years

POLA THE BEAUTY sales grew 9% over the previous year, and sales of the *B.A* series were also up 9% in fiscal 2012. As a welcome complement, the door-to-door cosmetics business has charted a steady increase in sales and profits over the past few years. These results are a reflection of POLA's business performance and represent the eventual effect from a mountain of reforms implemented over the past decade—the steps described above.

Reviving sluggish door-to-door sales was the biggest issue I inherited from my predecessor, and we are starting to see real progress in the rebuilding of this business. I am especially pleased to see the cheerful, happy faces of everyone in the sales organization and at the head office. Just by looking at the enthusiasm of the people who work at this invigorated POLA, I can say with confidence that we have set the stage for steady growth over the next five years.

However, changes in society and the market do not permit us to be complacent. I am sure that POLA can achieve long-lasting growth as long as it maintains an organizational culture that inspires people to go to the next level, to strive to achieve something more than that which exists now. POLA is built upon a foundation of unique components—door-to-door sales DNA, a customer-first/market-in perspective and associated practices, and the world's best skincare technologies—and I hope this foundation will be utilized as a platform to promote growth strategies that consistently distinguish POLA from the competition.

Satoshi Suzuki, President

Special Feature

SPECIAL FEATURE 1

Why is POLA THE BEAUTY able to keep growing?

We often receive questions from our shareholders and investors on the reason why POLA THE BEAUTY is able to keep growing in such harsh conditions in the domestic market. Here, we will explain why POLA THE BEAUTY has done so well by introducing three key features and the competitive nature of POLA THE BEAUTY.

What is POLA THE BEAUTY?

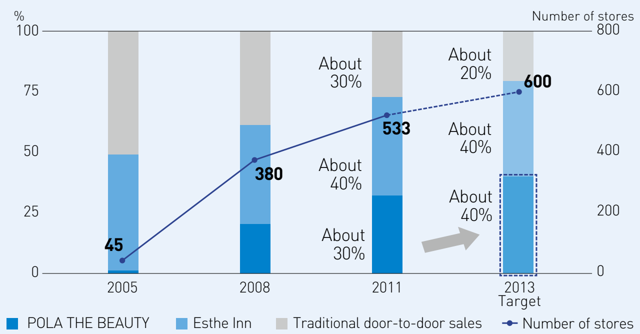
POLA THE BEAUTY commenced operations in 2005 and is a network of retail stores that integrate sales, consulting, and esthetic treatments. These unique specialty stores created by POLA are a fusion of traditional door-to-door sales and retail sales, providing the full value and services of the POLA brand. The total number of POLA THE BEAUTY stores is 572*, and thanks to their tremendous appeal, they are showing steady growth, with a year-on-year increase of 9.1%.

* As of December 2012

POLA THE BEAUTY net sales growth as of December 2012

Total including new stores	Existing stores
Up 9.1%	Up 8.4%

Ratio of Sales by Business Format/ Number of POLA THE BEAUTY Stores



How POLA THE BEAUTY Works

1
POLA's Competitiveness

POLA LADIES and Their DNA of Success—Door-to-Door Sales

POLA's DNA is rooted in door-to-door sales. POLA LADIES engage their customers by visiting their homes to offer POLA's products and services. This culture of door-to-door sales has been inherited by POLA THE BEAUTY and the next generation of POLA LADIES who comprise this new sales channel, who are actively seeking new opportunities and undertaking innovative activities to connect with new customers and establish strong relationships.

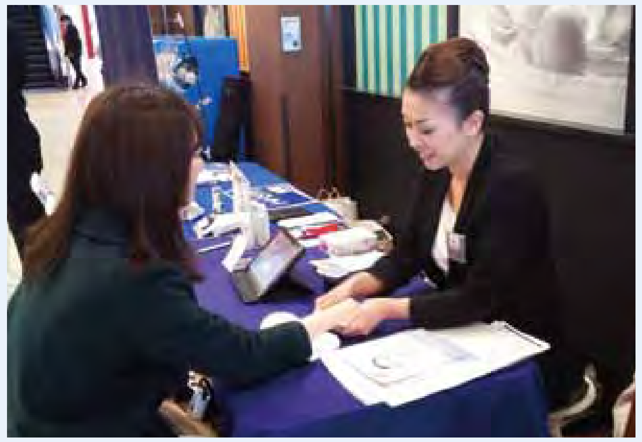
The activities at POLA THE BEAUTY, as described below, allow POLA LADIES to contact potential customers directly and attract new customers to their stores without spending much money on TV commercials and newspaper advertisements. In fact, the POLA brand spends only 2.5% of sales on advertisements while its three major domestic competitors spend 6.5% on average.

❶ Activities: Attracting Customers with Trial Esthetic Treatments

To secure new customers, it is important to invite them into the store so that they can experience the services and high added value offered by POLA THE BEAUTY. With this in mind, POLA LADIES actively communicate with potential customers by hand-delivering flyers in residential areas and in front of train stations, inviting them to trial esthetic treatments which are priced comparatively less than those of competitors. These esthetic treatments include POLA's unique scientific skin analysis and original style of consulting, which provide strong motivation for potential customers to visit the store.
(Please refer to the Price Comparison of Esthetic Treatments table below.)

❷ Activities: Holding Collaborative Events with Other Industries to Seek Out Potential Customers

Recently, POLA LADIES have planned promotion events with companies in other industries such as car dealers to seek out potential customers. POLA LADIES offer hand treatments as well as the opportunity to try out a variety of cosmetic products as incentives to attract potential customers to their stores.



Price Comparison of Esthetic Treatments

	POLA THE BEAUTY	Esthetic salon A	Esthetic salon B	Esthetic salon C
Number of stores	572	124	54	33
First time trial	¥3,150/¥5,250	¥3,980	¥5,250	¥1,050
Regular	¥6,825/¥8,925	¥24,150	¥17,850	¥18,900
Duration	55 min/60 min	60 min	75 min	75 min

2
POLA's Competitiveness

Consulting Skills That Support Sales of High-Value-Added Products

POLA LADIES use consulting and esthetic treatments to sell high-value-added skincare products to their customers, which is the major source of income for POLA THE BEAUTY. In addition to these luxury skincare products that meet the highest level of customer satisfaction, consulting and esthetic treatments provided by POLA LADIES lead to a high percentage of repeat customers and steady growth.

The sales operations of these high-value-added cosmetic products are reinforced by the commitment of highly skilled POLA LADIES. Thanks to an exclusive contract with POLA, POLA LADIES offer only POLA brand products to their customers. POLA LADIES receive ongoing education and training in skincare and on new products, so they are much more knowledgeable about POLA brand products than sales personnel at other retail stores' beauty counters. In addition, each POLA LADY has her own individual customers, which allows POLA LADIES to get to know their customers and build strong relationships with them exclusively, giving POLA LADIES the opportunity to consult with their customers about their skin conditions on a continual basis.

The business model of POLA THE BEAUTY, which combines consulting, esthetic treatments, and high-value-added cosmetic products, and the skills of POLA LADIES who run POLA THE BEAUTY successfully realize the unique sales structure of POLA.

3
POLA's Competitiveness

Continuous Growth Backed by a Growing Number of POLA LADIES

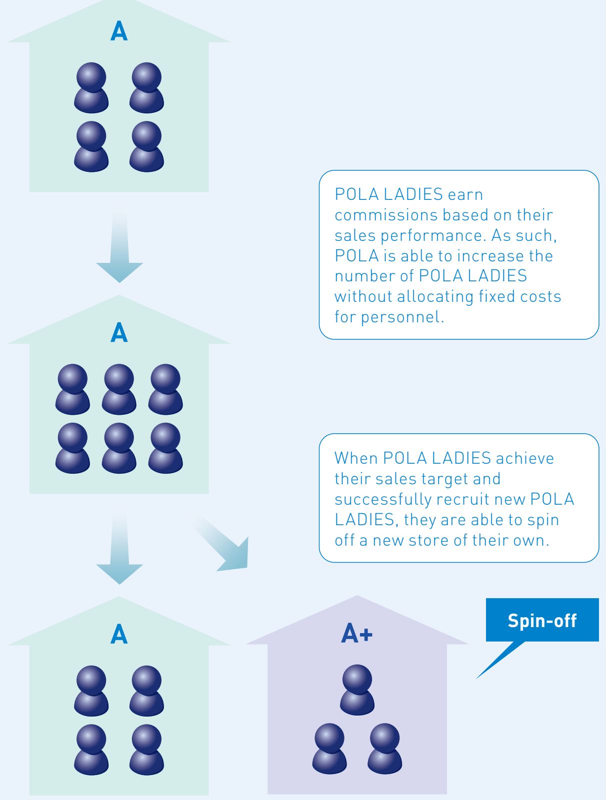
In consideration of profit and loss management, there are inherent limitations in the number of personnel who can be employed at any general retail store. At POLA THE BEAUTY stores, however, POLA LADIES earn commissions based on their sales performance. As such, POLA is able to increase the number of POLA LADIES without allocating fixed costs for personnel. Even the existing POLA THE BEAUTY stores are able to sustain continuous growth by increasing the number of POLA LADIES who bring in new customers.

Moreover, when POLA LADIES achieve their sales target and successfully recruit new POLA LADIES, they are able to spin off a new store of their own. This is a unique feature of POLA's sales channel. The number of stores is increasing while many domestic cosmetics specialty stores are forced to close because of a lack of successors.

POLA LADIES conduct business by actively engaging potential customers outside their stores, and as a result, they are able to cover a wider catchment area. This allows POLA to find prospective POLA THE BEAUTY locations in a way different from convenience stores and chain stores that open stores based on population density.

Therefore, there is still plenty of room for opening new POLA THE BEAUTY stores in Japan. POLA believes that it is possible to have 800 to 1,000 POLA THE BEAUTY stores in Japan without sacrificing the efficiency of one single store.

Flowchart Illustrating Increase in the Number of POLA LADIES



Comparison of the Number of Retail Stores in Different Industries

	POLA THE BEAUTY	Coffee-house chain A	Fast fashion retail chain B	Book-store chain C	Population of Japan (Unit: Thousands)
Total number of stores	572	965	845	919	127,799

These features of our competitiveness introduced here are the core elements that support the growth of POLA THE BEAUTY.

Thanks to the successful business model that maximizes the competitiveness of POLA THE BEAUTY, POLA has been able to achieve steady growth. As the source of growth in the POLA ORBIS Group, POLA will continue to make every effort to increase profits.

Jurlique

SPECIAL FEATURE 2

Becoming the No. 1 Natural Cosmetics Brand—Jurlique

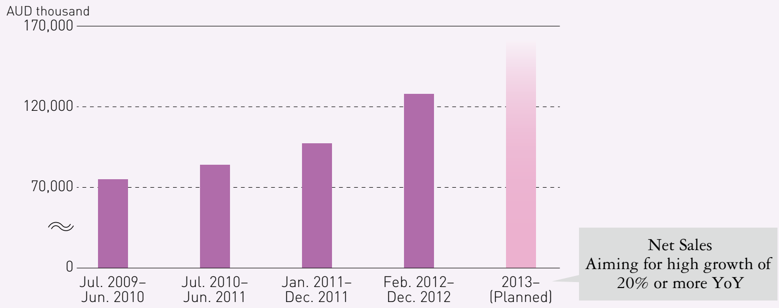
Jurlique joined the POLA ORBIS Group in February 2012.
We will now explain the fundamental concepts of the brand and the reason behind the high growth of Jurlique—a leading organic cosmetics brand recognized around the world.

nature+science=**beauty**

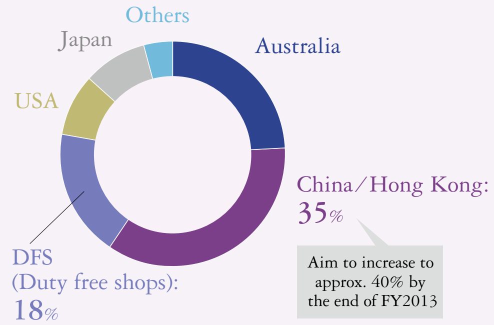
Brand Information

■ Company name	Jurlique International Pty Ltd
■ Foundation	1985
■ Location	Mount Barker, State of South Australia, Australia (Head office in suburban Adelaide)
■ Details of business	Selling cosmetics in 18 countries, using mainly organic ingredients
	A pioneer of organic cosmetics, maintaining a consistent focus on original concepts since the company's foundation

Jurlique Net Sales



Net Sales by Country (FY2012)



Focusing on Ingredients

Jurlique owns a farm in Adelaide, South Australia, and grows nearly all of the herbs that it uses for the ingredients in its cosmetic products. Jurlique maximizes the vitality of the plants through its unique method called biodynamic pesticide-free farming.

Ultimate Biodynamic Farming Unlocks the Full Potential of Nature

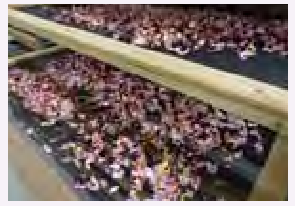
Jurlique's organic herbs are grown in the richest, purest soil while exposed to the harsh environment of Adelaide, where the temperature changes dramatically. Jurlique subscribes to the idea that "by nourishing the soil, the soil gives power to the plants that grow in it." Moreover, Jurlique does not use any chemical fertilizers. Instead, it uses its own original compost made from a mixture of hay and other materials. Herbs grown in rich soil are stronger and are more flavorful than herbs grown in other types of soil.

Note: Every year Jurlique's farm is certified as a biodynamic farm by the National Association for Sustainable Agriculture Australia (NASAA).

Preparing soil is an essential component of biodynamic farming. Jurlique's farm takes extra care and time to prepare soft and healthy soil.

Cow horns are stuffed with compost and buried under the ground to enhance the soil's nutrients.

Thanks to nature's rich gifts, roses that are grown on the farm have a bold scent.



Herbs picked one by one by hand are desiccated under controlled humidity and temperature.

Delivering the Highest Quality Cosmetic Products

Plants picked one by one by hand are finely categorized by harvest time, and are classified according to the soil's conditions, among other factors, and are organized with specific IDs. Jurlique consistently pursues the highest quality products by knowing when and where the best herbs were grown that year and utilizes such information for the next season.

Also, in order to ensure a stable supply of products, Jurlique maintains a three-year supply of herbs. These herbs are carefully stored to maintain their freshness and flavor, further ensuring Jurlique's brand value and quality.

Voice

We are devoted to realizing the highest quality cosmetics in the world and are actively engaged in research to find new ingredients.

We devote our undivided efforts and passion to grow our herbs, so we are confident that the herbs grown on this farm are of the highest quality. Furthermore, we are dedicated in our research to find new ingredients. In order to support the production of new cosmetic products, we are continually researching elements of plants and herbs that have not been used in cosmetics. Also, we make every effort to improve efficiency and reinforce our production to meet Jurlique's increasing sales.

Being able to watch our herbs grow and become cosmetic products that are loved by so many people gives us great joy and motivates us to sustain our farm operations.

Marc Intervera
Head of Jurlique Farm and Horticultural Specialist

Further Evolution of Organic Cosmetics

At Jurlique, they strive to reinforce such high-value-added offerings as anti-aging and skin-whitening products in their efforts to become a highly advanced organic cosmetics brand.

Nature + Science = Beauty

At Jurlique, they insist on using the natural ingredients extracted from the plants grown on their farm with the utmost care. In the production process, they pursue *Science* to develop their unique method and determine the composition of ingredients, which are extracted and condensed from the plants through which they derive their strong vitality. The integration of *Nature* and *Science* produces the highest quality cosmetics that realize the ultimate *Beauty*.

Reinforcing Anti-Aging and Skin-Whitening Features

Jurlique has reinforced its anti-aging and skin-whitening features that are not only natural and safe but are also effective in delivering distinct results and real satisfaction. In March 2011, Jurlique launched *Purely White*, a skin-whitening series with a unique ingredient called VitaBright KX. In autumn 2013, through synergies with POLA CHEMICAL, Jurlique plans to launch new products that have both the strengths of Jurlique, known for its natural ingredients, and POLA CHEMICAL, recognized for its expertise in anti-aging and skin-whitening.

Purely White series

Graceful Beauty series

Voice

Jurlique is becoming popular from Adelaide to Asia — and around the world.

Jurlique is a well established brand in Adelaide. I believe the reason why so many customers favor Jurlique is that it is an excellent brand that delivers distinct results while remaining *Natural*. We do not overly advertise in terms of TV commercials and such; in fact, many of our customers visit our stores through word of mouth. This is another quality of Jurlique.

Recently, there has been an increase in customers from China, South Korea, and Japan, and I can sense that Jurlique is becoming recognized all over the world.

Joanne Clayton
Store Manager, Rundle Mall (Adelaide)

Spotlight
Rapid Growth in China

Since the opening of the first store in 2009, Jurlique has been rapidly growing in China. With strength in its definitive brand concept, Jurlique has set out a growth strategy and has sustained a high growth rate.

Chinese Market Showing a Growing Interest in the Beauty of Bare Skin

The Chinese cosmetics market has been rapidly expanding over the past couple of years. Although the growth rate has been gradually slowing, the market is expected to see double-digit growth. Also, there is a significant amount of information regarding beauty delivered to consumers, and with an increasing number of consumers fully embracing beauty, an interest in the beauty of bare skin is growing. In light of this environment, the skincare market is expected to expand even further.

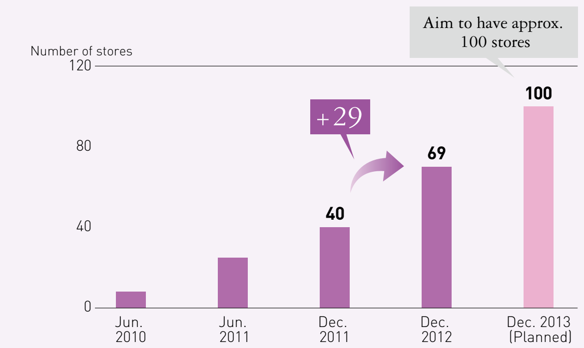
Jurlique's store in China

Jurlique Opens 29 Stores and Achieves a 70% Increase in Sales

Jurlique commenced sales in mainland China in 2009. In February 2012, Jurlique acquired its sales agent in China and accelerated its expansion. In fiscal 2012, Jurlique continued to expand and it opened 29 stores, which amounted to a 70% increase in sales from the previous fiscal year.

Jurlique aims to increase the number of stores in China to 100 and is planning to open 30 new stores in fiscal 2013. At the same time, it will work on further enhancing the level of its existing stores.

Number of Stores in China



Voice

Consumers who are becoming more aware of what they eat and their skincare needs are increasing, and as a result, an interest in Jurlique is growing.

Kevin Liu
China General Manager

Jurlique is highly regarded by Chinese consumers and is expanding in the Chinese market. Recently, Chinese consumers are becoming more aware of their dietary concerns as well as their skincare needs, particularly with regard to the ingredients in cosmetics and what they apply to their skin. As a result, many consumers appreciate Jurlique's cosmetic products that are made with organic herbs from Australia, where the environment is clean and pure.

We aim to become the No. 1 company in the natural cosmetics market in China, and with our unique customer appeal I see that happening soon.

AT A GLANCE

At a Glance

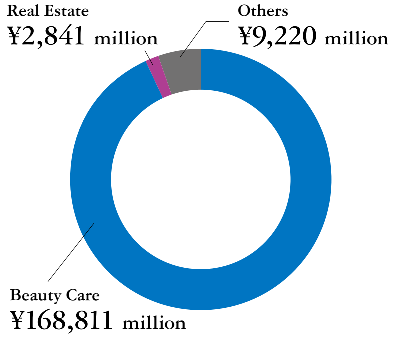
Consolidated Net Sales

¥180,873 million

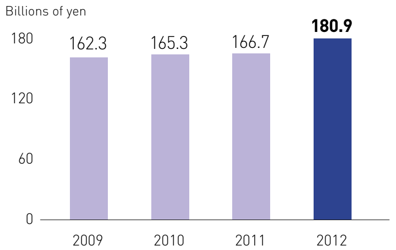
Consolidated Operating Income

¥13,520 million

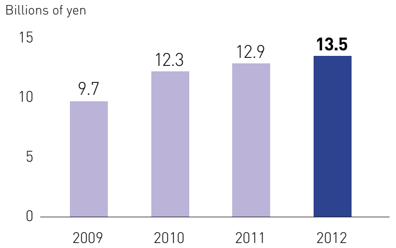
Net Sales Breakdown by Business Segment



Consolidated Net Sales



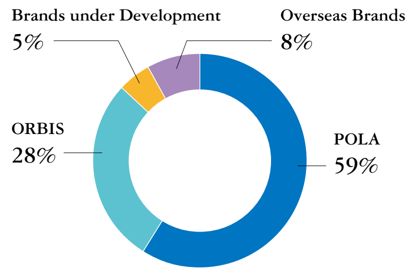
Consolidated Operating Income



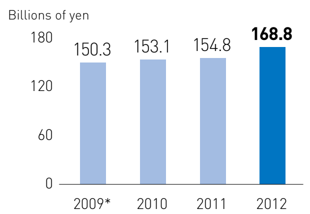
Beauty Care

Cosmetics business, emphasizing skincare products and services, and fashion business

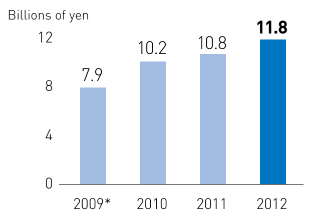
Net Sales Breakdown by Brand



Net Sales



Operating Income



* Amounts for fiscal 2009 are unaudited and provided for reference only.

Fiscal 2012 Operating Results

Buoyed by favorable sales of flagship brand POLA and a solid contribution from Jurlique, which came under the scope of consolidation in the first quarter of fiscal 2012, beauty care sales grew for the third consecutive year. On the profit front, the Company incurred costs associated with the acquisition of overseas brands, but successful efforts to boost the profitability of flagship brands led to a dramatic increase in profits.

POLA

P30

B.A series

ORBIS

P32

AQUA FORCE series

Brands under Development

P34

THREE

Overseas Brands

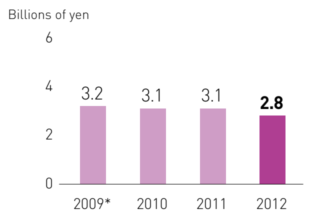
P34

Jurlique

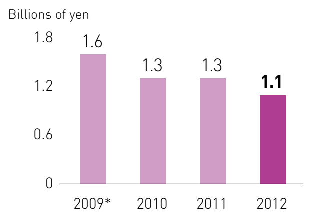
Real Estate

Leasing business utilizing portfolio assets effectively

Net Sales



Operating Income



* Amounts for fiscal 2009 are unaudited and provided for reference only.

Fiscal 2012 Operating Results

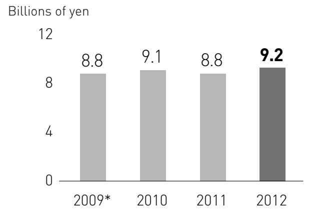
Despite concerted efforts to maintain rents and attract tenants, a persistent trend toward low rents led to a decline in net sales and operating income.

Brote Ookurayama

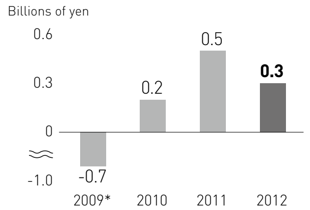
Others

Pharmaceuticals and building maintenance businesses

Net Sales



Operating Income (Loss)



* Amounts for fiscal 2009 are unaudited and provided for reference only.

Fiscal 2012 Operating Results

The pharmaceuticals business and building maintenance business both delivered solid contributions to this segment, underpinning increased sales. Operating income was down overall, owing to the exclusion of the commercial printing business from the scope of consolidation, effective from the third quarter of fiscal 2011. However, results from the pharmaceuticals business and building maintenance business marked year-on-year improvement in both businesses.

Note: The commercial printing business has been excluded from the scope of consolidation since FY2011 3Q.
(FY2011 1H results: Net sales: approx. ¥230 million; Operating income: ¥200 million)

Topical antifungal agent *Lulicon*

REVIEW OF OPERATIONS

Review of Operations

The POLA Brand

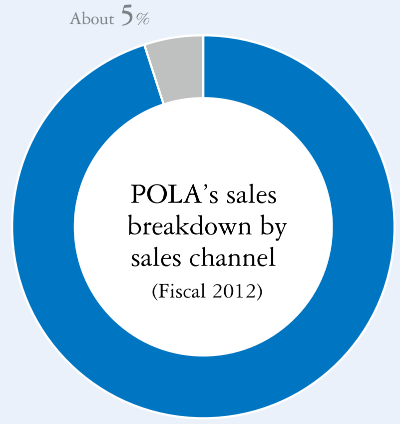
B.A series

POLA

High-prestige products
with personalized service
rooted in door-to-door sales

Overview of POLA's Operations

Products	Strength in anti-aging and whitening skincare products
Services	Consulting, skin analysis, and esthetic services
Sales Channels	• Door-to-door sales - New channel format (POLA THE BEAUTY and Esthe Inn) - Traditional door-to-door sales • Other (department stores, business use, and overseas)
Overseas Development	16 countries and regions including Russia, China, and Thailand

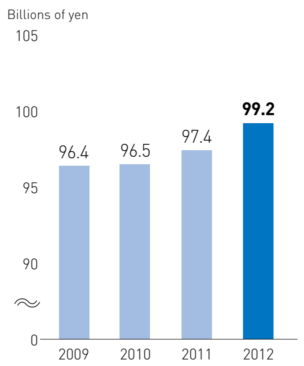


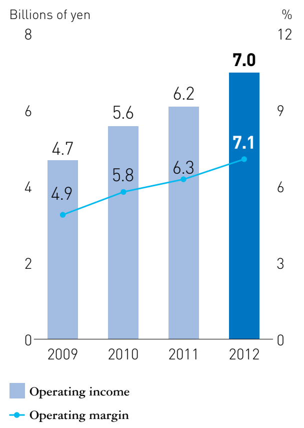
Net Sales

¥99,204 million
(Up 1.9%)

Operating Income

¥7,031 million
(Up 14.0%)





Notes: 1. Net sales and operating income are on a consolidated basis.
2. Amounts on pages 30 and 31 are unaudited and provided for reference only.

Products & Services

Strategy Success

Sales of *B.A* series

Up 9.1%

New customers

11.4% increase

POLA continued to enhance *B.A*, its popular anti-aging skincare series, and in fiscal 2012 added the *B.A Summer* series and *B.A The Eye Cream*. The tremendous market reception to these products raised the profile of the POLA brand even higher, leading to an 11.4% increase year on year in the number of new customers.

Sales per customer slipped 3.3% year on year, as the larger customer base spread sales thinner over the total, but purchases by existing customers were on a par with the previous fiscal year.

Sales Channels

Strategy Success

POLA THE BEAUTY stores

572 locations
(An increase of 39 stores)

POLA THE BEAUTY net sales growth

Up 9.1%

(Reference: Sales through Esthe Inn up 2.8%; sales through existing door-to-door channel down 8.2%)

Sales through POLA THE BEAUTY remained steady. POLA expanded the store network wider than initially planned, opening 39 new locations in fiscal 2012, which brought the total number of stores in operation to 572. Efforts were also made to invigorate the frontline sales structure. Sales grew 9.1% over the previous fiscal year, supported by the increase in stores, but even on an existing-store basis, sales remained high, at 8.4%, year on year.

The total number of sales offices, including POLA THE BEAUTY stores, reached 4,668 as of December 2012, up 115 from fiscal 2011, sustaining a stable growth trend.

Topics

Featured in newspapers and industry magazines, POLA attracts new customers with original events!

POLA ran events in collaboration with companies in other industries, such as car dealers and financial institutions. By offering hand treatments at these events, POLA broadened its approach to acquire new customers in the beauty care market, successfully targeting different consumer profiles that turned into store visits. These events were featured in newspapers and industry magazines, creating a synergistic effect that spurred an 11.4% jump year on year in the number of new customers in fiscal 2012.

REVIEW OF OPERATIONS

The ORBIS Brand

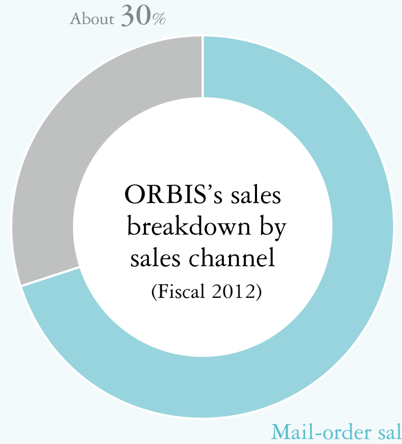
AQUA FORCE series

ORBIS

100% OIL-FREE skincare products with superb customer service via mail-order sales and retail stores

Overview of ORBIS's Operations

Products	100% OIL-FREE, fragrance-free, and pigment-free products
Services	"Fulfillment system" featuring free shipping and free returns and exchanges within 30 days
Sales Channels	• Mail-order (online and catalog) • Retail stores • Overseas sales
Overseas Development	Taiwan, South Korea, China, and Hong Kong

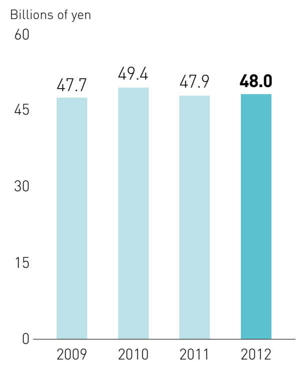


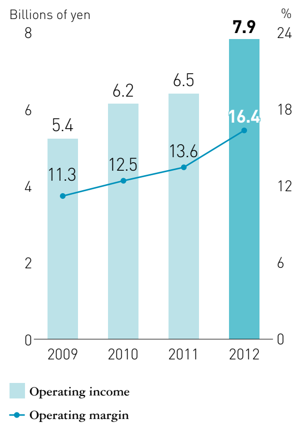
Net Sales

¥48,009 million
(Up 0.2%)

Operating Income

¥7,881 million
(Up 20.8%)





Notes: 1. Net sales and operating income are on a consolidated basis.
2. Amounts on pages 32 and 33 are unaudited and provided for reference only.

Products & Services

Strategy Success

Sales per customer

Mail-orders Up **7.8%**

Stores Up **1.0%**

Mail-order repeat ratio

Up **2.6 ppt**

ORBIS emphasized brand restructuring, with a focus on efforts to further enhance its skincare series and improve services, which was designed to reinforce customer loyalty and boost profitability. In fiscal 2012, ORBIS strengthened its selection of high-value-added skincare products and debuted *AQUA FORCE EXTRA*. The market's response exceeded expectations. Sales per customer soared, thanks to sales promotions of bundled products as well as brisk demand for high-priced products. Also, the ORBIS star shone brightly again in 2012, as the Japanese Customer Satisfaction Index survey—an evaluation conducted by Service Productivity & Innovation for Growth on behalf of the Ministry of Economy, Trade and Industry—ranked it the highest in customer satisfaction in the mail-order sales category for the second consecutive year.

Sales Channels

Strategy Success

Ratio of online sales to total sales

Up **2.4 ppt**

To strengthen online sales, ORBIS continued to update the product catalog on its website and further enhanced its one-to-one marketing system. By reducing paper-based marketing materials, ORBIS trimmed ¥260 million from catalog expenses. Store sales were brisk, rising above the previous fiscal year, when the aftereffects of the Great East Japan Earthquake dampened consumer spending. ORBIS showed improvement in both the number of customers and sales per customer.

Topics

Same-day delivery in some areas achieved through realignment of logistics into two-point east-west structure

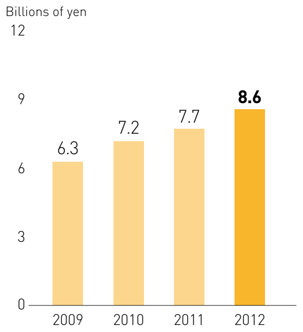
ORBIS realigned its three-point logistics structure in the Kanto region, centering on Tokyo, into a two-point east-west structure. This move made delivery operations more cost-effective and shortened the time needed to reach their end destinations. With the exception of some outer-lying islands, delivery has been expedited to the following day throughout Japan, and in some areas, same-day service is possible. ORBIS has always provided first-rate mail-order services and has taken these services to a higher level to improve the value of services to customers.

Brands under Development

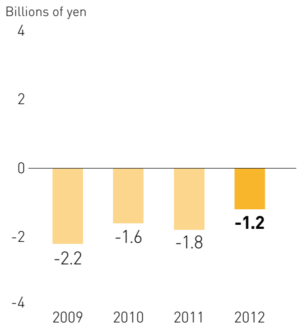
THREE

decencia

Net Sales



Operating Loss



Note: Amounts are unaudited and provided for reference only.

Net Sales

¥8,587 million
(Up 12.2%)

Operating Loss

¥1,202 million

Brands under development, particularly THREE, showed a considerable improvement over the previous fiscal year, with a huge increase in sales.

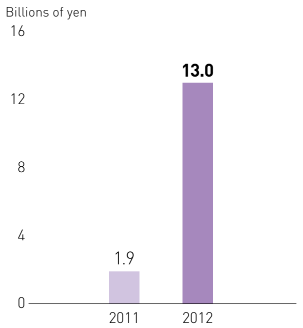
THREE added five new locations, mainly in large department stores, expanding its network to 19 locations in fiscal 2012. Paralleling higher sales, the loss position was not as deep as in fiscal 2011.

Overseas Brands

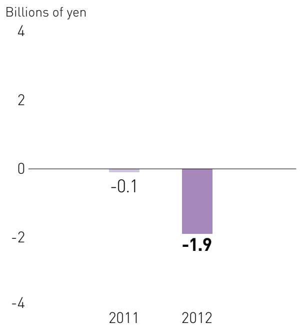
Jurlique

H2O PLUS

Net Sales



Operating Loss



Note: Amounts are unaudited and provided for reference only.

Net Sales

¥13,011 million
(Up 602.8%)

Operating Loss

¥1,897 million

Jurlique, which came under consolidation in February 2012, posted net sales of ¥10,018 million, in line with initial estimates. An operating loss of ¥1,185 million resulted, owing to an outlay of ¥1,886 million on acquisition-related costs of which ¥901 million was for one-time expenses, and also due to upfront investment in China, a market of outstanding growth opportunities.

H2O PLUS secured a new agent in China in February, which temporarily caused some setbacks including stalled shipments, and this led to net sales and operating income falling below initial estimates.

REVIEW OF OPERATIONS

Topics

POLA CHEMICAL Wins IFSCC Poster Award

The International Federation of Societies of Cosmetic Chemists (IFSCC) Congress is a biennial event for cosmetic chemists. At the 27th Congress, in 2012, POLA CHEMICAL INDUSTRIES INC. won the Poster Award, the first IFSCC award granted for the skin-whitening field.

The paper on which the winning poster was based analyzed the structure of dendrites, a cell structure linked to accumulation of melanin, the cause of uneven pigmentation, in the skin. POLA CHEMICAL's research team applied techniques to thoroughly analyze genetic conditions in humans in the quest to discover new factors that would control the number of dendrites. The team identified adrenomedullin (ADM) from more than 45,000 possible candidates as a melanocyte-activating factor, as it increased the number of dendrites.

Moving forward, the POLA ORBIS Group will continue to emphasize leading-edge research in the fields of anti-aging and skin-whitening to underpin the development of high-value-added products featuring proprietary ingredients.

Real Estate

Net Sales

¥2,841 million
(Down 8.0%)

Operating Income

¥1,139 million
(Down 11.3%)

Efforts were made to at least maintain if not raise rents by creating appealing office environments, particularly in buildings in urban areas such as Tokyo, and by reinforcing marketing capabilities to attract tenants to key buildings. Unfortunately, the downward trend in rents has caused segment performance to falter since the previous fiscal year.

Others

Net Sales

¥9,220 million
(Up 4.9%)

Operating Income

¥335 million
(Down 33.2%)

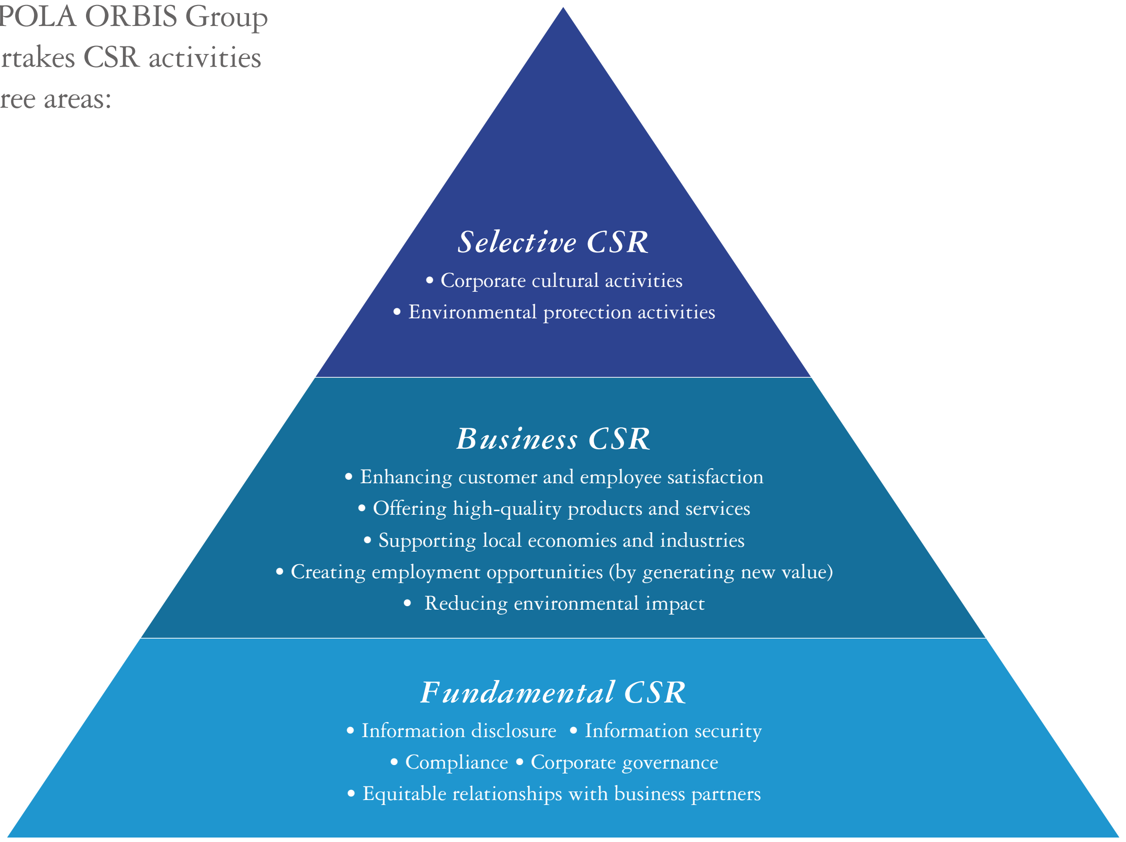
In the pharmaceuticals business, marketing efforts directed toward medical facilities specializing in dermatology yielded an increase in the number of customers for *Lulicon*, an antifungal agent for topical use. This underpinned a year-on-year increase in sales. In the building maintenance business, efforts to cultivate new demand prompted more order requests, which in turn buoyed business results for building maintenance, renovations, and subcontracting work.

Corporate Social Responsibility

Our efforts to secure and retain public trust

Perpetuating our long-held spirit to "find happiness in giving happiness," the POLA ORBIS Group strives to build a corporate brand that is loved and trusted by society. Our corporate social responsibility (CSR) activities reflect efforts to cultivate this spirit and fulfill our responsibilities as a good corporate citizen in contributing to society.

The POLA ORBIS Group undertakes CSR activities in three areas:



Fundamental CSR

Fundamental activities that all companies should carry out, such as compliance with laws, regulations and public morals, corporate governance related to the Group's operating structure, and information disclosure to meet corporate standards of accountability.

Business CSR

Programs implemented through our core business and in cooperation with stakeholders to support sustainable development, such as enhancing customer and employee satisfaction, providing high-quality products and services, supporting local economies and industries, and creating employment opportunities by generating new value.

Selective CSR

Active corporate culture and environmental protection programs that make significant contributions to society and enrich our core business.

Selective CSR

Activities that create a spiritually rich and beautiful tomorrow

Cultural activities

— Operation of Ginza gallery makes the arts more accessible —

At the POLA Museum Annex, in the POLA Ginza Building, admission to temporary exhibitions of modern art and other presentations is free throughout the year, to make the arts more accessible to the public. We support the creative activities of artists, especially young talent, by offering space in which to debut their works.

POLA Museum Annex

Business CSR

Fulfilling our social responsibility through our core business activities

Customer satisfaction

— Offering the pleasure of shopping via the Moving Salon Bus —

In 2011, POLA rolled out its Moving Salon, a department store on wheels that travels all over Japan. This novel shopping concept draws on POLA's nationwide network of door-to-door sales offices and an ability to anticipate demand through close local ties. Customers in sparsely populated areas without easy access to stores, particularly department stores, love to make their purchases in the luxurious atmosphere of the Moving Salon.

POLA held 370 events with its Moving Salon Bus in fiscal 2012.

Moving Salon Bus

Fundamental CSR

Corporate Governance

Basic Stance on Corporate Governance for the Group

Guided by the philosophy "Inspire all people and touch their hearts," the POLA ORBIS Group pursues a multi-brand strategy designed to enhance the overall corporate value of the Group with several original and distinctive brands within its scope and growing the associated businesses that control these brands. Essentially, each operating company in the Group manages itself autonomously and independently, while POLA ORBIS HOLDINGS INC., as the holding company, retains management control over each operating company with the aim of increasing shareholder value by ensuring sound and efficient management of overall Group operations.

Correspondingly, compliance is a priority for the Group and is an integral part of CSR activities. The Group will achieve enduring success by deepening its relationships with shareholders, business partners, and other stakeholders, fulfilling its corporate responsibilities to these stakeholders, and building bonds of trust with them and the community at large as a good corporate citizen. In addition, Group companies abide by the POLA ORBIS Group Action Platform (the "Action Platform"), which sets out regulations governing legal compliance, environmental protection, investor relations, and other matters. All executives and employees pledge to act in accordance with the Action Platform.

Should the Company consider transactions with controlling shareholders, the Board of Directors will thoroughly deliberate the necessity and fair value of any transaction before making a decision, in accordance with the aforementioned Action Platform, so that the interests of minority shareholders shall not be impaired.

Corporate Governance Structure

Outline

POLA ORBIS HOLDINGS has a Board of Directors and a Board of Corporate Auditors. The president of the Company is the chairman of the Board of Directors, and the full-time corporate auditor is the chairman of the Board of Corporate Auditors. The Company holds Group Strategy Meetings (management meetings) every month. A summary of the management and execution structure is provided below.

a. Board of Directors and executive structure

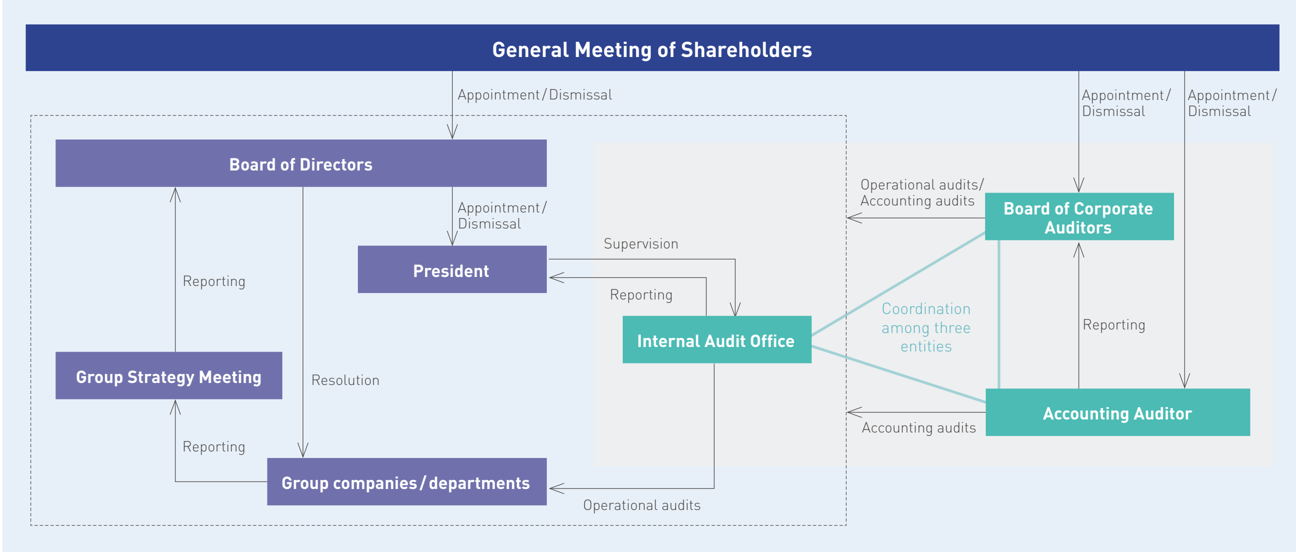
The Board of Directors, comprising seven directors, is responsible for improving the performance of the Group and operates under a structure that facilitates flexible decision making regarding the supervision of Group companies and responses to significant issues facing the Group. Directors are entrusted with the necessary authority to carry out these duties. Corporate auditors also attend meetings of the Board of Directors and offer their frank opinions.

Meetings of the Board of Directors are held at least once every month. In fiscal 2012, the Board of Directors met 24 times (including extraordinary meetings). The directors had a 100% attendance record. In addition to fulfilling their duties as set out by laws and regulations and the Company's Articles of Incorporation, directors use these meetings to pass resolutions and present reports on important management matters, such as the results of analyses comparing differences between monthly forecasts and actual performances and to ensure proper governance practices through the statement of opinions by directors and corporate auditors and subsequent discussion.

b. Group Strategy Meetings

Group Strategy Meetings are held with the aim of promoting profitability and supporting the development of the entire Group. Group Strategy Meetings are attended by the Company's directors and corporate auditors, as well as subsidiaries' presidents, directors, and others appointed through Board of Director resolutions. The meetings provide opportunities to hear about issues important to the Company and its subsidiaries and discuss pertinent themes.

Corporate Governance Structure



Reason for adopting this structure

As a pure holding company with operating companies responsible for multiple brands of cosmetics under its scope, POLA ORBIS HOLDINGS uses the aforementioned structure to clarify responsibilities for business operations. The Company seeks to reinforce governance through discussions in Group Strategy Meetings, where executives delve into management strategies and key issues, and through a basic approach that facilitates supervision of the execution of operations and decision making by the Board of Directors as well as the auditing function of the Board of Corporate Auditors. The Company will continue to operate under this structure as management deems it appropriate for implementing measures to enhance governance.

Implementation status of internal control system

Basically, internal controls are recognized as a process to be executed by all within a corporate organization to achieve four business objectives—effective and efficient operations, reliable financial reporting, activities in compliance with laws and regulations, and the safeguarding of assets—as set forth in "Standards for Management Assessment and Audit Concerning Internal Control Over Financial Reporting," issued by the Business Accounting Council. The policies for implementation of internal controls, as determined by the Company's Board of Directors are described as follows.

a. System to ensure efficient execution of duties by directors

In accordance with associated rules, the Board of Directors meets at least once a month, with extraordinary meetings held whenever circumstances warrant.

The Board executes its duties in accordance with rules defining the scope of official authority and the separation of duties, and carries out appropriate discussions, decision making, and reporting procedures in accordance with these rules as well as other rules, including those governing Group Strategy Meetings, affiliated company administration, budget control, and medium-term management planning and administration. In addition, Board of Directors' meetings provide an appropriate venue for discussions and decision making pursuant to important internal controls-related issues. The Group CSR Committee, which comprises a committee chair (the executive responsible for CSR), committee members (Group executives and outside experts), and a committee secretariat, carries out appropriate discussion of important issues related to compliance, risk management, and CSR, and executes decision-making procedures in accordance with rules defining the scope of official authority.

b. System for storing and managing information related to the execution of duties by directors

In accordance with document management rules, information regarding the execution of duties by directors, such as meeting proceedings and records of other meetings and discussions, are recorded on paper or electromagnetic media (hereafter “documents, etc.”) and stored appropriately. Requests by a director or corporate auditor to see such documents, etc., are promptly addressed.

c. Rules for controlling risk of loss, and other regulation systems
The Group CSR Committee is positioned directly below the Board of Directors so that risks related to business activities, from both strategic and operating perspectives, can be coordinated across the Group.

Each department adheres to risk management rules that keep business-related risks under control and will, should a crisis situation arise, establish a task force in accordance with rules for crisis control to quickly address the issue at hand.

d. Measures to establish and maintain a compliance system
The Group CSR Committee is positioned directly below the Board of Directors to coordinate a compliance system across the Group. This system is further complemented at Group companies by the establishment of a CSR Office or the assignment of someone to the role of Chief CSR Officer, depending on corporate size, to promote compliance practices within the respective company. Concurrently, efforts are made to deepen understanding of compliance issues through the distribution of a CSR handbook to all Group executives and employees, and everyone is required to submit a written pledge promising to uphold the Action Platform. A helpline has also been set up to raise awareness throughout the Group regarding compliance practices and to acquire a proper understanding of the related issues and also to encourage executives and employees to report potential violations or concerns.

e. Measures to ensure proper Group company operations
In accordance with rules governing Group Strategy Meetings, affiliated company administration, budget control and medium-term management planning and administration, preliminary discussions on important matters, budgets, and medium-term management plans for Group companies will take place at Group Strategy Meetings, and preliminary approval will be obtained from or notice be given to the Company’s Board of Directors. Approaches are also considered at Group Strategy Meetings to ensure that companies are thorough in their efforts to prevent unauthorized disclosure of the aforementioned information. In addition, measures will be taken to establish closer ties between Group companies so that the systems in a–d above are more fully integrated into Group companies.

f. System for employees to assist corporate auditors with their duties
When a corporate auditor requests an employee to assist with audit duties, a suitable department will be designated as the assisting office. A structure has also been established to complement auditing operations

Access to Helpline

The helpline was designed to raise awareness among executives and employees throughout the Group and to acquire a proper understanding of the compliance issues and also to encourage executives and employees to report potential violations or concerns in confidence.

By creating a Groupwide structure that allows all executives and employees throughout the Group to voice concerns or ask questions, the Company gains direct access to information on internal risks. This leads to steps that can minimize risks and prevent the occurrence of legal or regulatory violations.

In accordance with the Whistleblower Protection Act, the person in charge of the helpline as well as any individuals associated with this access point must strive to protect at all costs the privacy of anyone who reports a potential violation or asks for advice.

Helpline Structure

through enhanced contact with the Internal Audit Office (which serves as the Company’s internal audit department) and the Company’s accounting auditor (Ernst & Young ShinNihon LLC).

g. System under which directors and employees report to corporate auditors and other systems under which any report is made to corporate auditors
When directors or employees discover that laws and/or regulations have been broken or that the Company may potentially incur appreciable damages, they are expected to report the relevant issue to a corporate auditor without delay. When requested by a corporate auditor to report on the status of operations or assets, directors and employees must promptly do so. Corporate auditors make a concerted effort to attend meetings of the Board of Directors and other important meetings to learn the status of operations and assets from directors and employees. The Internal Audit Office also reports to the corporate auditors on the results of internal audits.

h. System to ensure that corporate auditors perform their audits effectively
In accordance with associated rules, the Board of Corporate Auditors meets at least once a month, with extraordinary meetings held whenever circumstances warrant. Corporate auditors make a concerted effort to attend Board of Directors’ meetings and other important meetings to collect information on the status of operations and assets. They also cooperate closely with the Internal Audit Office to ensure effective audit execution. Corporate auditors exchange opinions with the president, directors, and the accounting auditor periodically or as needed.

i. Basic approach and measures to exclude anti-social forces
As stated in the Action Platform, the Company is strictly opposed to any association with anti-social forces. In addition to the helpline, which enables anyone in the Group to express concerns in confidence about possible situations involving anti-social forces, Group companies coordinate with local police and gather outside information through membership in organizations, such as the Special Violence Prevention Association (*TOKUBOUREN*) and the Special Violence Prevention Council, and actively attend training sessions in an effort to prevent any association with anti-social forces whatsoever and eliminate any such relationships that are discovered to already exist. To complement these measures, a contingency manual has been prepared for Group companies and efforts are made to promote awareness of this reference source.

Basic guidelines for internal controls for financial reporting are presented below.

a. The Company ensures transparency of information and impartiality through the preparation of financial reports based on generally accepted accounting standards and the timely disclosure thereof.

b. The department in charge of financial reporting plays a vital role in the Company, which therefore seeks to improve inherent expertise in accounting and finance, and assign appropriate personnel and implement relevant training programs.

c. All executives and employees are well aware of the important role that internal controls play in financial reporting and strive within the scope of individual authority and responsibility to ensure that the following fundamental components of internal controls have been implemented and are operating effectively:
• Control environment
• Risk assessment and response
• Control activities
• Information and communication
• Monitoring
• IT support

d. Corporate auditors monitor and verify the appropriateness of financial reports as well as the implementation and operation status of internal controls, from an independent perspective.

Risk management system

To mitigate the various risks that influence the Group’s business activities and minimize losses, the Company has established risk management regulations to ensure sustained and stable business development. Risk management under normal conditions is the responsibility of the Board of Directors at each Group company, which discusses and decides on risk management matters, such as basic policy, annual targets, budget allocation, the composition of working groups, progress management, and the development of corrective measures and their follow-up.

Meanwhile, the Company has established crisis control regulations to provide a fundamental framework in the event of major risk events (crises) that have a significant impact on the Group's business and therefore require a prompt response. All executives and employees at Group companies must acknowledge the importance of crisis control in management and business activities when carrying out their duties.

Limited liability agreements

The Company enters into agreements with its outside corporate auditors that limit their liability for compensatory damages under Article 423, Paragraph 1 of Japan's Companies Act, in accordance with the Company's Articles of Incorporation and Article 427, Paragraph 1 of Japan's Companies Act. The liability of outside corporate auditors for compensatory damages under such agreements is limited to the amount set forth in the relevant laws and regulations. The aforementioned limited liability will only be recognized if the outside corporate auditor acted in good faith in executing his duties, even though such action invariably led to liability issues and if such liability does not lead to significant losses for the Company.

Internal Audits and Corporate Auditors' Audits

System of internal audits and corporate auditors' audits, and cooperation with the accounting auditor

a. Internal audits

The Company's Internal Audit Office has a staff of seven as of December 31, 2012, and is under the direct control of the president, separating it from other lines of business execution. From its independent and objective position, the Internal Audit Office strives to conduct highly effective internal audits to ensure sound and appropriate business operation at the Company and all Group companies. Specifically, through on-site audits at companies and in departments, the Internal Audit Office evaluates whether sufficient steps have been taken to address the potential circumstances (risks) most likely to occur in the course of business and to offer advice on corrective measures if need be. In addition, the Internal Audit Office cooperates with the accounting auditor on audits in the pursuit of highly effective audits.

b. Corporate auditor audits and the Board of Corporate Auditors

The Company's Board of Corporate Auditors comprises one full-time corporate auditor and two part-time outside corporate auditors as defined by Article 2-16 of Japan's Companies Act. The outside corporate auditors, Akio Sato, a lawyer, and Motohiko Nakamura, a certified public accountant and certified tax accountant, have considerable knowledge in their respective areas of expertise to deal with various issues concerning law as well as accounting, finance, and taxes.

The Board of Corporate Auditors meets at least once a month. In fiscal 2012, the Board of Corporate Auditors convened 16 times, including extraordinary meetings, and the Corporate Auditors had a 100% attendance record.

Corporate auditors are required to attend key meetings, such as the General Meeting of Shareholders, Board of Directors' meetings, and Group Strategy Meetings, where they receive updates from directors, employees, and the accounting auditor, and monitor the execution of duties by directors. In addition, at the beginning of the fiscal year, each corporate auditor receives from the accounting auditor an outline of the audit policies and important auditing items, and meets regularly, each quarter in principle, for an update on audit plans and the status of audits in progress. Corporate auditors also share information, as necessary, to raise the effectiveness of audits through the exchange of opinions or provision of materials from audits they have conducted themselves.

Cooperation on internal audits and corporate auditors' audits; status of three audit entities

Each corporate auditor receives an update from the Internal Audit Office on a monthly basis, in principle, regarding the status of internal audits, and works closely with the Internal Audit Office, mainly through the exchange of information, to facilitate these audits. At the Company, audits are also conducted with the participation of the accounting auditor, the Internal Audit Office, and corporate auditors. All three entities share their views on the content of audit reports and management issues, which contributes to the enhanced effectiveness and efficiency of the audit.

Relationship between internal audits and corporate auditors' audits and internal control department

Administration for the internal control department at the Company is handled by the CSR Promotion Division, and actual activities are the responsibility of the Internal Control Task Force. Members of the task force are chosen from numerous departments in the Company as well as from information system departments at some of the Company's subsidiaries. This ensures that internal controls are assessed from an independent and objective perspective. Assessment results are submitted to the Internal Control Committee, which is composed of Group Strategy Meeting members as well as the manager of the Internal Audit Office. Important issues are also conveyed to the Board of Directors and the Board of Corporate Auditors. As members of the Internal Control Committee, the manager of the Internal Audit Office and all corporate auditors receive reports on assessment results. They will discuss any shortcomings or seriously flawed decision making from a specialized, third-party standpoint and contribute to the improvement of the Company's internal control capabilities by indicating corrective measures to the company or department found lacking in some area of internal controls.

Outside Directors and Outside Corporate Auditors

Function and role that outside auditors fulfill in the Company's corporate governance efforts

The Company appoints two outside corporate auditors whose function and role is to reinforce governance by offering timely and pertinent advice from the third-party perspective of experts with wide-ranging thoughts on how to supervise the execution of business activities and decision-making processes within the Company. As described above, the Company seeks to enhance the auditing structure with three corporate auditors, including two outside corporate auditors, and this should be sufficient to monitor the execution of directors' duties. No outside directors are therefore appointed.

Thoughts on auditor independence and existence of personal, capital or business relationships, or any other interests between the Company and its outside corporate auditors

The Company has two outside corporate auditors. Neither of these corporate auditors has any personal connection to the Company's other executives—directors or the other corporate auditor—nor do any personal, capital relationships, or other interests exist between the Company and these outside corporate auditors. The Company therefore considers these outside corporate auditors to be fully independent of the Company.

Outside corporate auditor Akio Sato is a lawyer. He is the senior managing partner of Sato Sogo Law Office and concurrently holds positions as outside director and outside corporate auditor at several companies. No capital relationships, major business relationships, or special relationships exist between the Company and Sato Sogo Law Office or any of the companies at which Mr. Sato holds a concurrent position.

Outside corporate auditor Motohiko Nakamura is a certified public accountant. He is the senior managing partner of Central Public Accountant Nakamura Office and holds concurrent positions as a certified public accountant at Mai Tax Accountant Corporation and as an outside corporate auditor at another company. No capital relationships, major business relationships, or special relationships exist between the Company and the businesses at which Mr. Nakamura holds a concurrent position.

The Company does not have any particular criteria or policy regarding outside corporate auditors' independence from the Company—that is, POLA ORBIS HOLDINGS. However, both outside corporate auditors have been designated independent officers with virtually no chance of a conflict of interest arising between either of them and the Company's general shareholders. As such, the Company has notified the Tokyo Stock Exchange in its efforts to comply with the listing rules of this bourse.

Reasons for appointing outside corporate auditors

Akio Sato

Mr. Sato has been a member of various committees, including a task force for special research, a corporate lawyer, and an outside corporate auditor for major listed companies, and possesses the abundant experience and deep insights of a legal professional well-acquainted with various corporate issues. Therefore, the Company believes he has the necessary background and knowledge to suitably execute his duties as an outside corporate auditor of the Company. He sees issues from an expert's perspective, and at meetings, particularly those of the Board of Directors of the Company, he points out issues related to risks that may arise in the course of business and makes other remarks that are necessary to promote rational, balanced discussions about pertinent matters.

Motohiko Nakamura

Mr. Nakamura has been a director at the Japanese Institute of Certified Public Accountants, an expert advisor, and a member of the working group for the corporate IT controls study group formed by the Ministry of Economy, Trade and Industry. He possesses the abundant experience and deep insights of an accounting and tax professional well-acquainted with various issues concerning all matters related to corporate accounting, finance, and taxes. Therefore, the Company believes he has the necessary background and knowledge to suitably execute his duties as an outside corporate auditor of the Company. He sees issues from a specialized perspective, and at meetings, particularly those of the Board of Directors, he points out possible approaches, especially those that deal with financial risks to the Company, and makes other remarks that are necessary to promote rational, balanced discussions about these matters.

Outside corporate auditor attendance at meetings of the Board of Directors and Board of Corporate Auditors in fiscal 2012

Akio Sato	Board of Directors	All 24 meetings
	Board of Corporate Auditors	All 16 meetings
Motohiko Nakamura	Board of Directors	All 24 meetings
	Board of Corporate Auditors	All 16 meetings

Compensation for Directors and Corporate Auditors

Total compensation by executive category, total amount by type of compensation, and number of qualifying executives

Executive category	Total compensation (Millions of yen)	Breakdown of compensation by type (Millions of yen)				No. of qualifying executives
		Basic remuneration	Stock options	Bonuses	Retirement benefits	
Directors (Excluding outside directors)	205	154	25	17	8	8
Corporate auditors (Excluding outside corporate auditors)	19	16	—	2	—	2
Outside corporate auditors	13	13	—	—	—	2

Consolidated compensation from the Company by executive category

Since no single person receives more than ¥100 million of consolidated compensation, no applicable data is available for disclosure.

Key issues regarding the employee's salary portion for directors who concurrently serve as employees

Since no directors concurrently serve as employees, no applicable data is available for disclosure.

Policy for determining executive compensation amounts

Total compensation in each executive category, be it director or corporate auditor, is determined in line with the equity transfer plan drawn up when the Company was established. Remuneration for directors is set by the Board of Directors within the scope of total compensation, as stated above, based on Company regulations, and takes into account such factors as service level and contribution to the Company's business results. Remuneration for corporate auditors is set by the Board of Corporate Auditors within the scope of total compensation, as stated above, and reflects such factors as the job description of the individual and the responsibilities so carried.

With the objective to encourage directors to be more aware of their contributions to the improvement of the Group's business results over the medium to long term as well as enhanced corporate value, the Company introduced a stock-compensation-type stock options program, which was approved by an extraordinary meeting of the Board of Directors on March 30, 2012.

The retirement benefits system for directors that preceded the introduction of this program was subsequently abolished.

Communication with Shareholders

Approaches to encourage active participation at general meetings of shareholders and to facilitate the exercise of voting rights

Exercising voting rights via the Internet

A service that enables shareholders to exercise their voting rights via the Internet has been in place since fiscal 2010, commencing with the Fifth Annual General Meeting of Shareholders.

Other

To enable shareholders to gain a deeper understanding of the POLA ORBIS Group, POLA held a beauty seminar, which coincided with the annual general meeting of shareholders for fiscal 2012, and announced the results of the Nippon Bihada-ken Grand Prix (The All Japan Beautiful Skin Contest), conducted in early autumn 2012. This national contest employed POLA's own skin analysis system that identified which prefecture's women had the most beautiful skin.

IR activities

Creation/Announcement of disclosure policy

The Company formulated its disclosure policy as a basic policy, and provides an extensive array of information to stakeholders through its website and various other media formats.

Regular conference presentations for individual shareholders

The Company holds conference presentations for individual shareholders several times a year.

Regular conference presentations for analysts and institutional investors

Teleconferences are conducted every quarter. The Company also organizes financial conference presentations twice a year, one for the first half and one for the full year, and the president and designated executives describe noteworthy events and performance results.

Regular information meetings for overseas investors

Information meetings are held for overseas investors throughout the year.

IR materials posted on the Company's website

The Company uploads to its website a wide range of investor-oriented materials, including quarterly summaries of financial results, business reports, and other timely disclosure.

Public Relations & Investor Relations Division (IR Officer)

The Public Relations & Investor Relations Division handles matters related to investor relations (IR) and undertakes timely and appropriate disclosure of relevant materials.

A Director's Thoughts

Enhancing Corporate Governance to Reflect a Global Profile

Akira Fujii
Director

As the Group expands and becomes more global, POLA ORBIS HOLDINGS is earnestly striving to enhance its level of corporate governance. Management decisions based on the perspective of overall optimization of resources and thorough assessment of progress are the key characteristics of the Group's corporate governance.

All operating Group companies pursue activities independently, based on the multi-brand strategy articulated by POLA ORBIS HOLDINGS. Respective business strategies and investment plans are brought forward at Group Strategy Meetings, attended by the Group's directors and corporate auditors as well as the top executives of key subsidiaries. At these meetings, investment decisions and order of priority are determined from the perspective of overall optimization of resources.

The Group makes every effort to achieve its business forecasts disclosed to outside parties. In order to meet performance targets, top executives focus not only on the Group's business results but also on its management process. Key performance indicators are set and carefully examined in the management of each Group company. In addition, budget amendment criteria have been set internally and, should any discrepancy appear between business results and forecasts, management will act quickly to correct the situation through such steps as a recovery strategy or changes to the expense budget.

The governance structure at POLA ORBIS HOLDINGS highlights respect for the independence of each company to encourage brand growth as well as the merits of the holding company system.

An Outside Corporate Auditor's Thoughts

Achieving a High Standard of Corporate Governance

Motohiko Nakamura
Outside Corporate Auditor

Since assuming my position as an outside corporate auditor for POLA ORBIS HOLDINGS, I have attended various meetings, particularly those of the Board of Directors and Group Strategy Meetings, which bring the top executives of key subsidiaries together, as well as meetings of the Board of Corporate Auditors and corporate auditor liaison meetings, which involve corporate auditors from key subsidiaries. I offer my opinions at these and other meetings where my presence is required. In addition, I receive reports from the Company's accounting auditor and the Internal Audit Office, share my thoughts on the content, and strive to promote an atmosphere of cooperation and involvement. As an outside corporate auditor, I believe it is my duty to comment from the perspective of a third party, as someone external to the Company, and share these views through the exchange of opinions with executives at top-level meetings.

POLA ORBIS HOLDINGS is a pure holding company that fulfills its role at the top of the corporate pyramid by overseeing the activities of its operating companies, which now include the overseas subsidiaries that joined the Group in 2011 and 2012.

I can give the Company high marks from a corporate governance perspective for the clarity that management has brought to the Group's guiding philosophy and vision, for information sharing through quantification and visualization using such yardsticks as key performance indicators, and for fine-tuned responses to important issues.

Going forward, an even higher level of corporate governance will be required—a level that reflects the Group's organic structure and encompasses efforts to share the philosophy more deeply as the Group expands globally.

Directors and Corporate Auditors

Directors

Satoshi Suzuki
Representative Director, President

Motto:

Find happiness in giving happiness

Akira Fujii
Director

Motto:

Be yourself

Naoki Kume
Director

Motto:

What doesn't kill you makes you stronger

Hiroki Suzuki
Director

Motto:
He who does not pause to consider what is distant shall find sorrow near at hand

Yasuo Iwazaki
Director

Motto:

Creativity opens the door to new worlds

Takao Miura
Director

Motto:

Revere heaven, love mankind

Tsuneo Machida
Director

Motto:

Think globally, act locally

Corporate Auditors

Kuniaki Hoshi
Corporate Auditor

Motto:

Always aspire to something greater

Akio Sato
Outside Corporate Auditor

Motto:

Always do your best

Motohiko Nakamura
Outside Corporate Auditor

Motto:

Cool head, but warm heart

Note: Akio Sato and Motohiko Nakamura are Outside Auditors as stipulated in Article 2, Paragraph 16 of Japan's Companies Act.

Financial Section

Table of Contents

Five-Year Summary of Selected Financial Data

	Millions of yen (Except per share data)					Thousands of U.S. dollars*1 (Except per share data)
Years ended December 31	2008	2009	2010	2011	**2012**	**2012**
Operating Results						
Net sales*2	¥170,838	¥162,332	¥165,253	¥166,657	**¥180,873**	**$2,089,094**
Beauty Care		150,330	153,091	154,778	**168,811**	**1,949,780**
POLA		96,363	96,543	97,353	**99,204**	**1,145,810**
ORBIS		47,663	49,356	47,918	**48,009**	**554,506**
Brands under Development		6,304	7,192	7,654	**8,587**	**99,183**
Overseas Brands				1,851	**13,011**	**150,281**
Real Estate		3,216	3,102	3,089	**2,841**	**32,819**
Others		8,787	9,059	8,790	**9,220**	**106,495**
Operating income	10,868	9,706	12,270	12,853	**13,520**	**156,158**
Beauty Care		7,910	10,165	10,787	**11,812**	**136,438**
POLA		4,702	5,592	6,168	**7,031**	**81,218**
ORBIS		5,364	6,169	6,526	**7,881**	**91,033**
Brands under Development		(2,156)	(1,596)	(1,826)	**(1,202)**	**(13,892)**
Overseas Brands				(81)	**(1,897)**	**(21,921)**
Real Estate		1,598	1,304	1,283	**1,139**	**13,159**
Others		(696)	223	501	**335**	**3,872**
Operating margin (%)	6.4	6.0	7.4	7.7	**7.5**	
Net income	6,559	4,059	7,086	8,039	**6,681**	**77,170**
Financial Position						
Net assets	137,564	140,890	153,104	157,057	**164,896**	**1,904,556**
Total assets	180,664	181,909	187,771	193,027	**209,140**	**2,415,577**
Cash Flows						
Cash flows from operating activities	16,419	12,530	17,906	14,401	**17,592**	**203,193**
Cash flows from investing activities	(5,808)	(4,374)	(40,367)	(3,444)	**(39,625)**	**(457,674)**
Cash flows from financing activities	36	(1,125)	(2,789)	(4,093)	**(3,280)**	**(37,886)**
Cash and cash equivalents at end of year	61,803	68,817	43,507	50,246	**25,106**	**289,980**
Depreciation and amortization	4,602	4,973	5,361	5,374	**6,466**	**74,686**
Capital expenditure	5,655	8,639	6,245	5,048	**9,609**	**110,989**
Financial Indicators						
Equity ratio (%)	76.0	77.4	81.5	81.3	**78.8**	
Return on equity (%)	4.9	2.9	4.8	5.2	**4.2**	
Return on assets (%)	5.2	5.7	6.6	7.0	**7.3**	
Price-earnings ratio (times)*3	—	—	12.3	14.3	**20.5**	
Per Share Data						
Net income per share	127.91	79.16	137.36	145.43	**120.86**	**1.40**
Net assets per share	2,677.47	2,743.87	2,767.55	2,839.36	**2,980.48**	**34.42**
Cash dividends per share	20	20	40	45	**50**	**0.58**
Number of employees*4	3,603	3,713	3,773	3,812	**4,490**	
Average number of temporary-hired workers	2,103	1,906	1,872	1,864	**2,154**	

*1 Dollar amounts are shown for convenience only and are calculated based on the prevailing exchange rate of U.S.$1=¥86.58 as of December 31, 2012.
*2 Net sales do not include consumption taxes.
*3 The price-earnings ratio is not shown for fiscal 2008 and 2009 as the stock was not listed.
*4 The number of employees is the number of people working for the POLA ORBIS Group.

Management's Discussion and Analysis

Summary of Business Results

In fiscal 2012, ended December 31, 2012, the domestic cosmetics market showed signs of a recovery, but the encouraging trend was rather weak and, as a result, business conditions remained difficult. In light of this environment, the outlook for the domestic cosmetics market is uncertain. In the overseas cosmetics market, the expansion trend is expected to continue due to the growth in personal income supported by ongoing growth in internal demand in Asia, especially in China and India, as well as the recovery trend in the United States.

Within this market environment, the POLA ORBIS Group entered the second year of its three-year management plan launched in 2011, and persisted in its efforts to improve the profitability of domestic flagship brands while accelerating the growth of its brands under development. At the same time, the Group aggressively expanded into overseas markets, completing the acquisition of Jurlique International Pty Ltd, an Australian cosmetics company, in February 2012.

As a result of the aforementioned factors, consolidated net sales and operating income exceeded the levels posted in fiscal 2011.

Analysis of Operating Results: Comparison of Fiscal 2012 and Fiscal 2011

Net sales

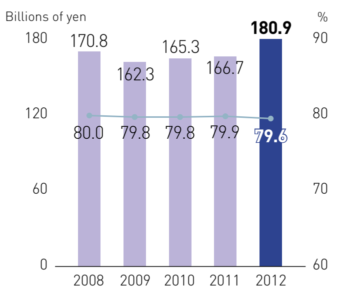
Net sales increased 8.5% year on year, to ¥180,873 million, mainly owing to brisk domestic sales underpinned by flagship brand POLA and the inclusion of sales from Jurlique, which was acquired in February 2012.

Cost of sales, and selling, general and administrative expenses

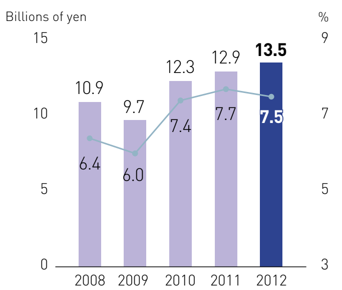
Cost of sales rose 10.4% year on year, to ¥36,946 million, reflecting the increase in net sales. Although cost of sales, particularly on flagship brands, decreased, the cost of sales ratio—cost of sales as a percentage of net sales—edged up 0.3 percentage point, to 20.4%, largely due to the consolidation of H2O PLUS HOLDINGS INC. and Jurlique and inventory valuation differences.

Selling, general and administrative expenses grew 8.4%, to ¥130,407 million, because of higher personnel costs and other increases associated with the consolidation of H2O PLUS and Jurlique as well as rising sales commissions and other increases at POLA, in line with higher sales. The ratio of selling, general and administrative expenses to net sales edged down 0.1 percentage point, to 72.1%, thanks to an aggressive Groupwide effort to curb costs through enhanced operating efficiency.

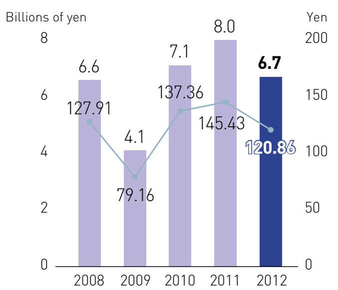
Net Sales and Gross Margin



Operating Income and Operating Margin



Net Income and Net Income per Share



Operating income

Operating income rose 5.2%, to ¥13,520 million, but the operating margin slipped 0.2 percentage point, to 7.5%, compared with fiscal 2011 results.

Income before income taxes and minority interests

Income before income taxes and minority interests jumped 27.1% year on year, to ¥14,311 million. This solid increase is largely due to the absence of two factors that eroded this line item in fiscal 2011, namely, a ¥954 million loss on adjustment for changes in accounting standard for asset retirement obligations and a ¥467 million loss on disaster.

Net income

Net income declined 16.9%, to ¥6,681 million, reflecting higher income taxes in line with higher taxable domestic income.

Consequently, net income per share dropped from ¥145.43 in fiscal 2011 to ¥120.86 in fiscal 2012. Return on equity followed suit, moving from 5.2% to 4.2%.

Business Segment Performance

Beauty Care

The Beauty Care segment consists of the flagship brands POLA and ORBIS; the brands under development, pdc, FUTURE LABO, ORLANE, decencia, and THREE; and the overseas brands Jurlique and H2O PLUS.

POLA aggressively promoted sales of its namesake brand through department store outlets and POLA THE BEAUTY stores, which integrate cosmetics, consulting, and esthetic treatments, and also endeavored to increase contacts with customers through expansion of its sales organization. In addition, POLA is striving to further enhance its sales techniques and consulting skills in order to boost customer satisfaction. In the domestic market, POLA introduced the *B.A Summer* series in March and April and *B.A The Eye Cream* in October, as new products featuring POLA's anti-aging technologies. Furthermore, POLA utilized its skin analysis technology and rolled out a campaign using its *APEX-i* Custom-Tailored Skincare Cosmetics. In overseas markets, POLA implemented measures to promote business growth, including the expansion of its sales organization in Thailand. As a result of the above, POLA's performance surpassed its results from the previous fiscal year.

ORBIS strove to improve profitability through various efforts that included increasing the rate of repeat purchases, renewing skincare cosmetics products, bolstering online sales, and streamlining sales costs. Within the domestic market, ORBIS introduced *"OIL-FREE STYLE,* WE ARE." as its new brand statement, and in August launched the new *AQUA FORCE EXTRA* line. Furthermore, ORBIS worked to strengthen its delivery services by establishing a two-point logistics structure, with a distribution center in eastern Japan and another in western Japan, which ensures next-day delivery nationwide. In the overseas market, ORBIS focused on promotional activities in China and implemented other measures to

Key Financial Indicators

	2012	2011	2010
Cost of Sales Ratio	**20.4%**	20.1%	20.2%
Gross Margin Ratio	**79.6%**	79.9%	79.8%
SG&A Ratio	**72.1%**	72.2%	72.4%
Personnel expenses	**14.9%**	14.3%	14.3%
Sales commissions	**25.0%**	26.1%	26.1%
Sales-related expenses	**18.8%**	19.7%	19.9%
Administrative and other expenses	**13.4%**	12.1%	12.1%
Operating Margin	**7.5%**	7.7%	7.4%
Net Income Margin	**3.7%**	4.8%	4.3%

increase brand awareness. As a reflection of the above, ORBIS generated results on a par with those in the previous fiscal year.

Sales of brands under development and overseas brands exceeded sales from the previous fiscal year. This reflected increasing domestic sales of THREE and decencia, an Asia-centered development of the H2O PLUS brand acquired in July 2011, and the inclusion of earnings from the Jurlique brand, purchased in February 2012.

As a result, net sales—sales to external customers—generated by the Beauty Care segment in fiscal 2012 amounted to ¥168,811 million, climbing 9.1% over fiscal 2011, and operating income reached ¥11,812 million, up 9.5%.

Real Estate

The Real Estate segment concentrates on the leasing of office buildings in major cities. Efforts are currently directed toward sustaining rent levels while also aiming for higher rents and raising occupancy rates by creating attractive office environments. Another area of emphasis is the rental residential properties business. This business highlights new-model condominiums perfect for families with young children. In fiscal 2012, measures to reinforce marketing capabilities and thereby maintain rents while attracting tenants were unable to offset a persistent trend toward lower rents, causing segment performance to falter.

As a result, net sales—sales to external customers—generated by the Real Estate segment for fiscal 2012 fell 8.0%, to ¥2,841 million, and operating income dropped 11.3%, to ¥1,139 million.

Others

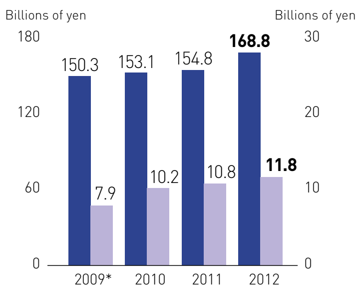
The Others segment currently comprises the pharmaceuticals and building maintenance businesses. The Group withdrew from the commercial printing business as of the third quarter of fiscal 2011.

The pharmaceuticals business operated by POLA PHARMA INC. draws on results accumulated by Group companies in research related to cosmetics and quasi-pharmaceuticals to develop and sell new drugs. Thus far, two products—*Lulicon*, an antifungal agent for topical use, and *DIVIGEL*, a treatment for menopausal symptoms—have successfully been brought to market. In addition, existing ethical pharmaceuticals, such as the laxative *Alosenn* and dermatological drugs, have been supplied to medical institutions including university hospitals throughout Japan. During fiscal 2012, POLA PHARMA continued sales activities, including visits to medical institutions, with a special focus on the field of dermatology. This led to a steady expansion of *Lulicon*'s market share, and results surpassed the year-earlier level.

The building maintenance business caters primarily to the needs of Group companies. In fiscal 2012, engaging in sales activities to sign up new customers and expand orders from outside the Group, the business generated an increase in orders received, underpinning a year-on-year improvement in performance.

As a result, net sales—sales to external customers—generated by the Others segment grew 4.9%, to ¥9,220 million. Operating income, however, fell 33.2%, to ¥335 million.

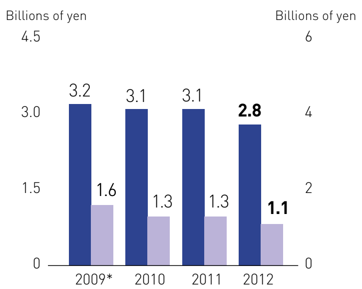
Beauty Care



Net sales (Left axis)
Operating income

* Amounts for fiscal 2009 are unaudited and provided for reference only.

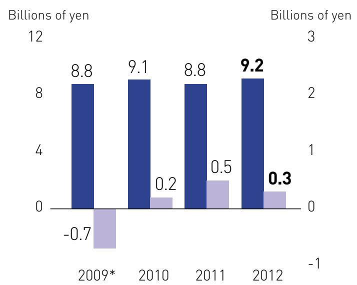
Real Estate



Net sales (Left axis)
Operating income

* Amounts for fiscal 2009 are unaudited and provided for reference only.

Others



Net sales (Left axis)
Operating income (loss)

* Amounts for fiscal 2009 are unaudited and provided for reference only.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Analysis of Financial Position

Assets, Liabilities, and Net Assets

Assets

As of December 31, 2012, total assets stood at ¥209,140 million, up 8.3% from December 31, 2011.

Total current assets settled at ¥88,844 million, down 20.0% from December 31, 2011, with key changes including a ¥1,389 million increase in short-term investments in securities due to the investment of surplus capital and a ¥28,127 million decrease in cash and deposits in line with an allocation of funds for the acquisition of Jurlique.

Net property, plant and equipment rose 12.1% from December 31, 2011, to ¥55,408 million. The primary factors contributing to the increase were a ¥2,011 million increase in construction in progress, mainly for residential properties for lease, and a ¥1,686 million increase in land from the purchase of property adjacent to a building owned by the Group in Aoyama, Tokyo.

Net intangible assets surged 226.9% from December 31, 2011, to ¥39,677 million, largely reflecting increases of ¥14,672 million in goodwill arising from the acquisition of Jurlique, ¥9,412 million in right of trademark, and ¥3,455 million in other intangible assets.

Total investments and other assets reached ¥25,209 million, up 23.7% from December 31, 2011, primarily reflecting an increase of ¥4,989 million in investments in securities.

Liabilities

As of December 31, 2012, total liabilities were ¥44,244 million, up 23.0% from December 31, 2011.

Total current liabilities climbed 30.7% from the end of the previous fiscal year, to ¥31,086 million, with key changes including an increase of ¥4,475 million in income taxes payable due to higher taxable domestic income.

Total non-current liabilities reached ¥13,157 million, up 8.0% from December 31, 2011.

Net assets

Total net assets amounted to ¥164,896 million, up 5.0% from December 31, 2011, reflecting net income of ¥6,681 million and an increase of ¥3,526 million in foreign currency translation adjustments as a result of the weakening yen, which were partly offset by dividends from retained earnings totaling ¥2,764 million.

Consequently, net assets per share grew ¥141.12 from December 31, 2011 to ¥2,980.48 as of December 31, 2012. The equity ratio dropped 2.5 percentage points, to 78.8%.

Cash Flows

The balance of cash and cash equivalents as of December 31, 2012, was ¥25,106 million, down ¥25,140 million from the end of the previous fiscal year.

Cash flows from operating activities

Net cash provided by operating activities rose 22.2% from the previous fiscal year, to ¥17,592 million. The primary components contributing to the increase in net cash were ¥14,311 million in income before income taxes and ¥6,466 million in depreciation and amortization. A major component offsetting the increase in net cash was ¥3,687 million in income taxes paid.

Cash flows from investing activities

Net cash used in investing activities amounted to ¥39,625 million compared with ¥3,444 million in the previous fiscal year. The main factors contributing to the increase in net cash used included outflows of ¥27,952 million due to the purchase of subsidiaries' stocks arising from the acquisition of Jurlique; ¥15,707 million due to the purchase of short-term investments in securities for investing surplus capital in line with investment plans; ¥15,565 million due to the purchase of investments in securities; and ¥6,742 million due to the purchase of property, plant and equipment, arising mainly from construction of residential properties for lease. Meanwhile, a cash inflow of ¥28,224 million in proceeds from sales and redemption of short-term investments in securities was generated.

Cash flows from financing activities

Net cash used in financing activities decreased 19.9% from the previous fiscal year, to ¥3,280 million. A key factor offsetting the decrease in net cash used was the application of ¥2,749 million in cash dividends paid.

Sources of funds and policy on fund liquidity

Sources of working capital and capital expenditure for Group operations are internal funds and bank loans. Of funds raised from external sources, interest-bearing debt reached ¥3,481 million as of December 31, 2012, up ¥418 million from a year earlier, due to a ¥233 million increase in short-term loans payable through repayment of overseas subsidiary bank loans and a ¥184 million increase in lease obligations. The Company introduced a cash management system in fiscal 2010 to boost fund efficiency for the whole Group by concentrating funding operations for subsidiaries at the Company.

The Company adheres to fund management regulations and standards to ensure appropriate application of operating funds and surplus funds. The balance of cash and deposits stood at ¥22,551 million as of December 31, 2012, down ¥28,127 million from a year earlier, primarily due to the use of funds for loans and investment, paralleling the acquisition of Jurlique.

Basic Policy on Profit Distribution and Dividends for Fiscal Years 2012 and 2013

Profit distribution is an underlying principle of the Company's management. As such, the Company's basic policy is to pay stable and ongoing dividends to all of its shareholders.

The Company distributes retained earnings twice a year, through an interim dividend and a year-end dividend. Based on Article 454, Paragraph 5 of Japan's Companies Act and the Company's Articles of Incorporation, the general meeting of shareholders is responsible for approving the year-end dividend, while the Board of Directors is responsible for approving the interim dividend.

Based on the aforementioned policy, the Company plans to use retained earnings to pay an annual dividend per common share of ¥50.00, comprising an interim dividend of ¥25.00 and a year-end dividend of ¥25.00 for fiscal 2012. Internal reserves will be invested to reinforce the Group's operating structure and support future business development. For fiscal 2013, taking into account consolidated earnings targets and other factors, the Company plans to pay an interim dividend of ¥25.00 per share and increase its year-end dividend by ¥5.00 per share to ¥30.00 per share, thereby paying an annual dividend of ¥55.00 per share.

Business Risks

For businesses and other aspects of the POLA ORBIS Group, risks that are considered to be critical for investors in making investment decisions are described below. As of December 31, 2012, forward-looking statements in this annual report are judgments made by the Group, unless otherwise noted.

1) Damage to brand value

The Group offers multiple brands, including POLA and ORBIS, among others. Through conscientious business management and the supply of products and services catering to customers' trust, the Group is working to maintain and enhance its brand image. However, the operating results and financial position of the Group could be adversely affected in the event that negative opinions and rumors about the Group's products and services are spread, trust is lost, and brand value is impaired.

2) Competition within the Group

In accordance with its multi-brand, multi-channel strategy, the Group develops new and existing brands by categorizing them by target customer segment (demographic base), price bracket, and sales channel, thereby preventing competition from occurring between brands. However, the operating results and financial position of the Group could be adversely affected in the event that competition occurs within the Group in the course of maximizing the values of existing brands and accelerating multi-brand evolution as the Group's strategy.

3) Securing sales partners (Sales managers and POLA LADIES)

POLA INC., the core of the Group's Beauty Care segment, operates its business through door-to-door sales based on consignment sales agreements. Securing sales partners based on consignment sales agreements is an important activity for business expansion and is something that POLA constantly works on. However, if regulations under the Act on Specified Commercial Transactions are tightened or the labor environment changes, sufficient human resources may not be available because implementation of measures for securing them may become difficult and the number of POLA LADY applicants may decrease. As a result, the operating results and financial position of the Group could be adversely affected.

4) Strategic investment activities

The Group makes strategic investments for overseas expansion concentrated in China, M&As, and new businesses. Information necessary for making decisions on strategic investment activities is collected and examined. However, the operating results and financial position of the Group could be adversely affected in the event that results initially intended are not achieved due to unexpected environmental changes, among other factors.

5) Cosmetics market environment

The domestic cosmetics market has reached maturity and the trend in product shipments has shifted from generally flat to a gradual decline. Against this backdrop, competition has increased due to the reorganization of corporate groups via M&A deals, new competitors entering the market from different industries, and the increasing influence of distributors and retailers through cooperation/integration. Consequently, the operating results and financial position of the Group could be adversely affected in the event that the Group cannot properly respond to unexpected changes in the competitive environment.

6) Research & development

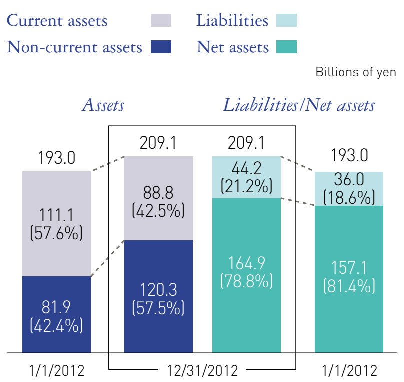
R&D is one source of the Group's competitive strength, and the Group intends to maintain its investment in this area. To carry out R&D effectively and efficiently, the Group implements R&D activities in accordance with an annual plan. If the development of a new product requires a long-term effort, the results may not be seen for some years. In some cases, when anticipated results cannot be achieved, an extension in the period of development or an increase in investment may be required; otherwise commercialization may not be achieved as a result. Furthermore, even after commercialization, the product may not necessarily be accepted by customers due to various factors that could create uncertainty about the product. If the initially intended results of R&D cannot be achieved as such, the operating results and financial position of the Group could be adversely affected.

7) Manufacturing and quality assurance

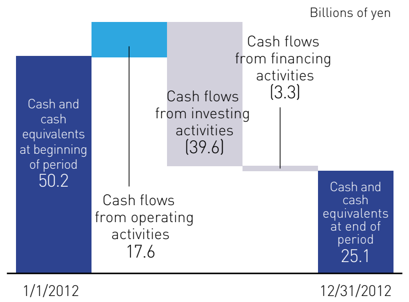
The Group works to secure the necessary volume of raw materials required for the manufacture of products at an appropriate price by using diversified sources of supply and by maintaining favorable relations with suppliers, based on overall supervision by divisions within the Group responsible for procuring raw materials. However, if an unexpected situation occurs resulting from external factors, the procurement of necessary raw materials could be disrupted.

The Group's cosmetics are manufactured at four locations: in Japan, at POLA CHEMICAL INDUSTRIES INC.'s Fukuroi Factory and Shizuoka Factory, both in Shizuoka Prefecture; in Australia, at Jurlique's Mount Barker Factory, in South Australia; and in the United States, at H2O PLUS's Chicago Factory, in Illinois. Pharmaceutical products are made at two locations: in Japan, at KAYAKU CO., LTD.'s Saitama Factory and Tokorozawa Factory, both in Saitama Prefecture. We are undertaking efforts to verify quality control and quality maintenance. However, should any problems arise in product quality, the operating results and financial position of the Group could be adversely affected.

Highlights of Consolidated Balance Sheet

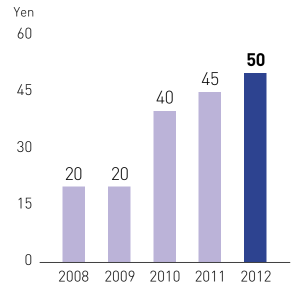


Overview of Consolidated Statement of Cash Flows



Note: The effect of exchange rate change on cash and cash equivalents is omitted. Any discrepancies due to this omission have been adjusted accordingly.

Cash Dividends per Share



8) Overseas business activities

The Group's main sales points are in Japan, but Group companies have expanded into Asia, particularly China, as well as the BRICS (Brazil, Russia, India, China, and South Africa), where market expansion is expected. The Group currently subscribes to a policy of further development overseas.

Since these overseas business activities contain the risk of social upheaval caused by unexpected economic/political uncertainty, labor problems, terrorism/war, infectious diseases, etc., the operating results and financial position of the Group could be adversely affected.

9) Currency exchange

The Group takes exchange rate risks into consideration for monetary materiality for settlement of foreign currency due to the increase in import/export transactions and loans to foreign subsidiaries as a result of expansion of overseas business activities. Additionally, since the figures denominated in the local currency of foreign consolidated subsidiaries are converted to yen when consolidated financial statements are prepared, changes in the exchange rate could affect the operating results and financial position of the Group.

10) Limit of protection for intellectual property rights

Although the Group takes steps to protect its intellectual property rights, third parties may infringe upon intellectual properties through means that exceed the Group's expectations. Consequently, the business activities of the Group could be adversely affected by the misappropriation of technologies and the creation of counterfeit goods.

11) Information security

The Group carefully manages the handling of confidential information, including personal information and R&D information, through the implementation of internal audits, the use of an information security system, the establishment of internal codes of conduct, and education initiatives by the division in charge of CSR and various committees. However, if such information were leaked for any reason, a claim for damage could be filed against the Group and the reputation of the Group could be tarnished. As a result, the businesses of the Group could be adversely affected.

12) Material litigation

Although lawsuits that could seriously affect the Group have not been filed in fiscal 2012, the operating results and financial position of the Group could be adversely affected in the event of material lawsuits in the future and judgments disadvantageous to the Group.

13) Disasters

The major production bases of the Group are the Fukuroi Factory and Shizuoka Factory of POLA CHEMICAL. Separate production lines have been installed for manufacturing different products at these factories, and backup manufacturing capacities between the factories are limited. Therefore, product supply could be affected in the event that manufacturing is disrupted or production capacity drops at either of these factories as a result of a natural disaster or other unforeseen event.

In addition, since both factories are close to each other, product supply could be interrupted for a long period in the event of a large-scale earthquake in the Tokai region.

Similarly, pharmaceutical products are produced at the Saitama Factory and Tokorozawa Factory of KAYAKU. Since both factories are close to each other, product supply may be interrupted for a long period in the event of a large-scale earthquake in the Kanto region.

Furthermore, unprecedented large-scale earthquakes as well as other natural disasters or accidents could occur in areas other than these two locations and interrupt the procurement of materials and components and the supply and sale of products, which could have an adverse effect on the operating results of the Group.

14) Spread of infectious diseases

If the spread of infectious diseases occurs, resulting in significant social impact, service and sales activities must be voluntarily suspended and sales offices must be closed because of the nature of daily face-to-face contact with customers and business partners. Consequently, the operating results of the Group could be adversely affected domestically and overseas.

15) Risks in the pharmaceuticals business

In the pharmaceuticals business, an enormous investment in R&D is needed before a new pharmaceutical product can get to market. Despite this hurdle, the pharmaceuticals business achieved operating income in fiscal 2011 and has remained in the black, thanks to enhanced efficiency in the Group's investment process itself, mainly through joint development efforts with other companies on the new drug frontier. The Company aims to maintain the business's profitability and make every effort to increase its profits. However, a variety of potentially problematic risks could arise, such as a sudden change in the business environment, a delay in new pharmaceutical product development, and a shift in the management direction of partner companies involved in joint development with the Group's pharmaceuticals business. Such situations could return the business to an operating loss position, and if the loss expanded or persisted over a long period, it could adversely affect the operating results of the Group.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Fiscal 2013 Forecast

Guided by POLA ORBIS HOLDINGS INC., the Group will strive to respond swiftly to changes in the market environment by embracing business activities in line with its medium-term management plan and directing concerted efforts into building a corporate structure capable of supporting sustainable growth over the medium to long term. The Group will continue to work on its main strategic goals in its medium-term management plan, which are to improve the profitability of flagship brands and further promote the multi-brand strategy, increase growth potential through global business expansion (overseas expansion by leveraging the Group's strengths), and reinforce the operating structure. Through these activities, the Group will aim to achieve its consolidated earnings targets.

For the fiscal year ending December 31, 2013, the Group forecasts, on a consolidated basis, net sales of ¥188,500 million, up 4.2% year on year; operating income of ¥16,000 million, up 18.3%; and net income of ¥8,200 million, up 22.7%.

Significant Accounting Policies and Assumptions

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in Japan (Japanese GAAP). The preparation of consolidated financial statements requires management to select and apply certain accounting policies and make assumptions that affect the reported amounts and disclosure of assets and liabilities and of revenues and expenses. These assumptions are based on reasonable judgments taking into account historical performance and other factors. However, actual results could differ from these assumptions due to inherent uncertainties.

Fiscal 2013 Forecast (Consolidated)

(Millions of yen)	FY2013 Full Year	YoY Change Amount	YoY Change %
Net Sales	**188,500**	**7,626**	**4.2%**
Beauty Care	175,800	6,988	4.1%
Real Estate	3,000	158	5.6%
Others	9,700	479	5.2%
Operating Income	**16,000**	**2,479**	**18.3%**
Beauty Care	15,000	3,187	27.0%
Real Estate	1,200	60	5.3%
Others	300	-35	-10.5%
Reconciliations	-500	-732	—
Net Income	**8,200**	**1,518**	**22.7%**

Consolidated Balance Sheets

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	2012
Assets			
Current assets			
Cash and deposits (Notes 4, 6 and 19)	¥ 22,551	¥ 50,679	$ 260,473
Notes and accounts receivable – trade (Note 19)	22,684	20,719	262,010
Short-term investments in securities (Notes 4, 19 and 20)	19,801	18,412	228,709
Merchandise and finished goods	10,883	9,664	125,708
Work in process	1,493	1,648	17,244
Raw materials and supplies	4,901	4,351	56,612
Deferred tax assets (Note 16)	3,579	3,478	41,345
Other	3,073	2,208	35,503
Allowance for doubtful accounts	(125)	(69)	(1,449)
Total current assets	88,844	111,093	1,026,155
Property, plant and equipment (Note 14)			
Buildings and structures	59,680	57,120	689,310
Machinery, equipment and vehicles	12,449	11,834	143,790
Land	22,448	20,761	259,282
Leased assets	4,303	2,893	49,704
Construction in progress	2,328	317	26,890
Other	19,636	19,172	226,801
Total property, plant and equipment	120,846	112,099	1,395,777
Accumulated depreciation	(65,437)	(62,679)	(755,803)
Net property, plant and equipment	55,408	49,420	639,974
Intangible assets			
Goodwill, net (Note 23)	18,256	3,583	210,860
Right of trademark	11,841	2,429	136,767
Other intangible assets, net (Note 14)	9,579	6,124	110,646
Net intangible assets	39,677	12,137	458,273
Investments and other assets			
Investments in securities (Notes 19 and 20)	18,572	13,582	214,508
Long-term loans receivable	60	57	701
Deferred tax assets (Note 16)	3,137	3,415	36,234
Other	3,603	3,486	41,625
Allowance for doubtful accounts	(163)	(165)	(1,893)
Total investments and other assets	25,209	20,376	291,174
Total assets	¥209,140	¥193,027	$2,415,577

See notes to consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	2012
Liabilities and net assets			
Current liabilities			
Notes and accounts payable – trade (Note 19)	¥ 3,630	¥ 2,894	$ 41,931
Short-term loans payable (Notes 7 and 19)	1,733	1,500	20,025
Lease obligations (Note 7)	676	623	7,813
Accounts payable – other (Notes 19 and 21)	12,077	11,391	139,495
Income taxes payable	6,282	1,806	72,564
Provision for bonuses	1,504	1,561	17,372
Provision for directors' bonuses	42	45	490
Provision for sales returns	76	76	881
Provision for point program	1,629	1,605	18,825
Other	3,432	2,283	39,650
Total current liabilities	31,086	23,788	359,046
Non-current liabilities			
Lease obligations (Note 7)	1,071	939	12,377
Provision for retirement benefits (Note 9)	6,394	6,795	73,854
Provision for directors' retirement benefits	—	367	—
Provision for environmental measures	133	132	1,542
Deferred tax liabilities (Note 16)	1,305	317	15,074
Other	4,253	3,627	49,129
Total non-current liabilities	13,157	12,180	151,975
Total liabilities	44,244	35,969	511,021
Contingent liabilities (Note 8)			
Net assets (Note 10)			
Shareholders' equity			
Common stock			
Authorized: 200,000,000 shares			
Issued: 57,284,039 shares at December 31, 2012 and 57,284,039 shares at December 31, 2011	10,000	10,000	115,500
Capital surplus	90,718	90,718	1,047,797
Retained earnings	63,386	59,469	732,116
Treasury stock, at cost			
(2,000,000 shares at December 31, 2012 and 2,000,000 shares at December 31, 2011)	(2,199)	(2,199)	(25,400)
Total shareholders' equity	161,905	157,988	1,870,013
Accumulated other comprehensive income (Note 15)			
Unrealized gain (loss) on available-for-sale securities	331	(35)	3,829
Deferred gain (loss) on hedges	—	9	—
Foreign currency translation adjustments	2,535	(991)	29,289
Total accumulated other comprehensive income	2,867	(1,017)	33,118
Subscription rights to shares	40	—	471
Minority interests	82	86	954
Total net assets	164,896	157,057	1,904,556
Total liabilities and net assets	¥209,140	¥193,027	$2,415,577

See notes to consolidated financial statements.

Consolidated Statements of Income

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	**2012**
Net sales (Notes 18 and 22)	**¥180,873**	¥166,657	**$2,089,094**
Cost of sales (Notes 11, 12, 18 and 22)	**36,946**	33,461	**426,729**
Gross profit	**143,927**	133,196	**1,662,365**
Selling, general and administrative expenses (Notes 11, 13, 18 and 22)	**130,407**	120,342	**1,506,208**
Operating income	**13,520**	12,853	**156,158**
Other income (expenses) (Notes 14 and 18)			
Interest and dividend income	**510**	565	**5,894**
Interest expense	**(73)**	(53)	**(853)**
Foreign exchange gain (loss)	**544**	(121)	**6,284**
Equity in losses of affiliates	**(38)**	(24)	**(447)**
Gain on sale of subsidiary's stocks	**—**	529	**—**
Reversal of provision for directors' retirement benefits	**119**	—	**1,375**
Loss on disposal of non-current assets	**(222)**	(389)	**(2,569)**
Impairment loss	**(194)**	(754)	**(2,244)**
Loss on disaster	**—**	(467)	**—**
Loss on adjustment for changes of accounting standard for asset retirement obligations	**—**	(954)	**—**
Other, net	**147**	71	**1,699**
	791	(1,597)	**9,140**
Income before income taxes and minority interests	**14,311**	11,255	**165,297**
Income taxes (Note 16)			
Current	**7,358**	3,492	**84,994**
Deferred	**287**	(266)	**3,319**
	7,646	3,226	**88,314**
Income before minority interests	**6,665**	8,029	**76,984**
Minority interests in net loss of consolidated subsidiaries	**(16)**	(10)	**(187)**
Net income	**¥ 6,681**	¥ 8,039	**$ 77,170**

Per share information (Note 24)	Yen		U.S. dollars (Note 3)
Basic net income per common share	**¥120.86**	¥145.43	**$1.40**
Diluted net income per common share	**120.82**	—	**$1.40**
Weighted average common shares outstanding	**55,284,039**	55,284,039	**—**
Cash dividends declared per common share	**¥ 50.00**	¥ 45.00	**$0.58**

See notes to consolidated financial statements.

Consolidated Statements of Comprehensive Income

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	**2012**
Income before minority interests	**¥ 6,665**	¥8,029	**$ 76,984**
Other comprehensive income (Note 15)			
Unrealized gain (loss) on available-for-sale securities	**367**	(246)	**4,240**
Deferred gain (loss) on hedges	**(9)**	9	**(109)**
Foreign currency translation adjustments	**3,540**	(521)	**40,895**
Share of other comprehensive income of associates accounted for using the equity method	**(1)**	—	**(20)**
Total other comprehensive income (Note 15)	**3,896**	(758)	**45,006**
Comprehensive income	**¥10,561**	¥7,270	**$121,989**
Comprehensive income attributable to:			
Owners of the parent	**¥10,565**	¥7,287	**$122,037**
Minority interests	**¥ (4)**	¥ (16)	**$ (48)**

See notes to consolidated financial statements.

Consolidated Statements of Changes in Net Assets

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

		Millions of yen							
	Common shares (Thousands)	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Accumulated other comprehensive income (Note 15)	Subscription rights to shares	Minority interests	Total net assets
Balance at January 1, 2011	57,284	¥10,000	¥ 90,718	¥54,746	¥(2,199)	¥ (264)	—	¥103	¥ 153,104
Dividends from retained earnings				(3,317)					
Net income				8,039					8,039
Disposal of treasury stock									
Retirement of treasury stock									
Change in scope of consolidation									
Accumulated other comprehensive income									
Change in unrealized gain (loss) on available-for-sale securities						(246)			(246)
Deferred gain (loss) on hedges						9			9
Foreign currency translation adjustments						(515)			(515)
Minority interests								(16)	(16)
Balance at January 1, 2012	57,284	10,000	90,718	59,469	(2,199)	(1,017)	—	86	157,057
Dividends from retained earnings				**(2,764)**					**(2,764)**
Net income				**6,681**					**6,681**
Disposal of treasury stock									
Retirement of treasury stock									
Change in scope of consolidation									
Accumulated other comprehensive income									
Change in unrealized gain (loss) on available-for-sale securities						**367**			**367**
Deferred gain (loss) on hedges						**(9)**			**(9)**
Foreign currency translation adjustments						**3,526**			**3,526**
Subscription rights to shares							**¥40**		**40**
Minority interests								**(4)**	**(4)**
Balance at December 31, 2012	**57,284**	**¥10,000**	**¥90,718**	**¥63,386**	**¥(2,199)**	**¥2,867**	**¥40**	**¥ 82**	**¥164,896**

See notes to consolidated financial statements.

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

	Thousands of U.S. dollars (Note 3)							
	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Accumulated other comprehensive income (Note 15)	Subscription rights to shares	Minority interests	Total net assets
Balance at at January 1, 2012	$ 115,500	$ 1,047,797	$ 686,872	$ (25,400)	$(11,748)	—	$1,001	$ 1,814,022
Dividends from retained earnings			**(31,927)**					**(31,927)**
Net income			**77,170**					**77,170**
Disposal of treasury stock								
Retirement of treasury stock								
Change in scope of consolidation								
Accumulated other comprehensive income								
Change in unrealized gain (loss) on available-for-sale securities					**4,240**			**4,240**
Deferred gain (loss) on hedges					**(109)**			**(109)**
Foreign currency translation adjustments					**40,736**			**40,736**
Subscription rights to shares						**$471**		**471**
Minority interests							**(48)**	**(48)**
Balance at December 31, 2012	**$115,500**	**$1,047,797**	**$732,116**	**$(25,400)**	**$33,118**	**$471**	**$ 954**	**$1,904,556**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	**2012**
Cash flows from operating activities			
Income before income taxes and minority interests	**¥14,311**	¥11,255	**$165,297**
Adjustments to reconcile income before income taxes and minority interests to net cash flows from operating activities:			
Depreciation and amortization	**6,466**	5,359	**74,686**
Impairment loss	**194**	754	**2,244**
Amortization of goodwill	**829**	91	**9,585**
Gain on sale of subsidiary's stocks	**—**	(529)	**—**
Gain on sales of non-current assets	**(2)**	(3)	**(31)**
Loss on disposal of non-current assets	**222**	389	**2,569**
Loss on disaster	**—**	467	**—**
Loss on adjustment for changes of accounting standard for asset retirement obligations	**—**	954	**—**
Increase (decrease) in allowance for doubtful accounts	**15**	5	**183**
Increase (decrease) in provision for retirement benefits	**(402)**	(425)	**(4,653)**
Increase (decrease) in other provisions	**(413)**	(168)	**(4,772)**
Interest and dividend income	**(510)**	(565)	**(5,894)**
Interest expense	**73**	53	**853**
Foreign exchange loss (gain)	**(660)**	95	**(7,626)**
Equity in losses of affiliates	**38**	24	**447**
Changes in operating assets and liabilities:			
Decrease (increase) in notes and accounts receivable – trade	**(1,007)**	(1,215)	**(11,638)**
Decrease (increase) in inventories	**571**	62	**6,596**
Increase (decrease) in notes and accounts payable – trade	**359**	(388)	**4,154**
Increase (decrease) in consumption taxes payable	**(78)**	(210)	**(907)**
Decrease (increase) in other assets	**184**	(47)	**2,130**
Increase (decrease) in other liabilities	**471**	476	**5,443**
Other	**132**	112	**1,534**
Subtotal	**20,796**	16,547	**240,200**
Interest and dividends received	**565**	637	**6,529**
Interest paid	**(81)**	(36)	**(947)**
Income taxes paid	**(3,687)**	(2,339)	**(42,588)**
Payments for loss on disaster	**—**	(407)	**—**
Net cash provided by operating activities	**¥17,592**	¥14,401	**$203,193**

See notes to consolidated financial statements.

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

Years ended December 31

	Millions of yen		Thousands of U.S. dollars (Note 3)
	2012	2011	2012
Cash flows from investing activities			
Payments into time deposits	¥ (2,231)	¥ (1,281)	$ (25,770)
Proceeds from withdrawal of time deposits	2,415	989	27,896
Purchase of short-term investments in securities	(15,707)	(30,897)	(181,428)
Proceeds from sales and redemption of short-term investments in securities	28,224	48,800	325,999
Purchase of property, plant and equipment	(6,742)	(2,421)	(77,870)
Proceeds from sales of property, plant and equipment	34	1,310	401
Purchase of intangible assets	(1,785)	(1,641)	(20,619)
Purchase of investments in securities	(15,565)	(9,476)	(179,784)
Proceeds from sales of investments in securities	17	19	197
Payments for disposal of non-current assets	(191)	(448)	(2,210)
Purchase of long-term prepaid expenses	(77)	(76)	(900)
Payments for lease and guarantee deposits	(226)	(171)	(2,616)
Proceeds from collection of lease and guarantee deposits	198	162	2,294
Purchase of investments in subsidiaries resulting in change in scope of consolidation (Note 4)	(27,952)	(8,923)	(322,854)
Proceeds from sale of investment in subsidiary resulting in change in scope of consolidation	—	629	—
Other	(35)	(17)	(409)
Net cash used in investing activities	(39,625)	(3,444)	(457,674)
Cash flows from financing activities			
Net increase (decrease) in short-term loans payable	215	(254)	2,489
Cash dividends paid	(2,749)	(3,300)	(31,755)
Repayments of lease obligations	(746)	(538)	(8,620)
Net cash used in financing activities	(3,280)	(4,093)	(37,886)
Effect of exchange rate changes on cash and cash equivalents	172	(124)	1,997
Net increase (decrease) in cash and cash equivalents	(25,140)	6,738	(290,369)
Cash and cash equivalents at beginning of year (Note 4)	50,246	43,507	580,349
Cash and cash equivalents at end of year (Note 4)	¥25,106	¥50,246	$289,980

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

POLA ORBIS HOLDINGS INC. and Consolidated Subsidiaries

Note 1 Summary of Significant Accounting Policies

1.1. Basis of presentation

The accompanying consolidated financial statements of POLA ORBIS HOLDINGS INC. (the “Company”) and its consolidated subsidiaries (collectively, the “Group”) have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Law and its related accounting regulations, and in conformity with accounting principles generally accepted in Japan (“Japanese GAAP”), which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards – (“IFRS”).

Certain amounts in the consolidated financial statements of the prior years have been reclassified to conform to the current year’s presentation for comparative purposes. For the convenience of readers outside Japan, certain presentations in the consolidated financial statements filed with the Director of the Kanto Local Finance Bureau in Japan have been reclassified and rearranged.

1.2. Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. All companies included in the scope of consolidation have a fiscal year ending December 31.

Under the control or influence concept, those companies in which the Company, directly or indirectly, can control over their operations are consolidated, and those companies over which the Company has the ability to exercise significant influence are accounted for using the equity method. All significant inter-company balances, transactions and material unrealized profit included in assets resulting from the inter-company transactions have been eliminated in consolidation.

43 subsidiaries were included in the scope of consolidation at December 31, 2012 (29 at December 31, 2011). One affiliated company was accounted for using the equity method at December 31, 2012 and December 31, 2011.

Changes in significant subsidiaries in fiscal 2012 compared to fiscal 2011 are as follows:

Jurlique International Pty Ltd. (“Jurlique”) and its 11 consolidated subsidiaries were included in the scope of consolidation following the acquisition of its all outstanding shares. The two special purpose companies (SPCs)—Pola Orbis Jurlique Holdings Pty Ltd and Pola Orbis Jurlique Pty Ltd, established for acquiring all outstanding shares in Jurlique, were also included in the scope of consolidation.

1.3. Unification of accounting policies applied to foreign subsidiaries

In accordance with Practical Issues Task Force (PITF) No. 18, “Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements” (Issued by the Accounting Standards Board of Japan (ASBJ) on May 17, 2006), the Company and its consolidated subsidiaries use uniform accounting policies and procedures for like transactions and other events in similar circumstances in preparing consolidated financial statements. Financial statements of foreign consolidated subsidiaries prepared in accordance with either IFRS or accounting principles generally accepted in the United States (“U.S. GAAP”) are accepted except for certain items, which are adjusted to comply with Japanese GAAP. The adjustments include the following:

1. Amortization of goodwill
2. Scheduled amortization of unrecognized actuarial gains or losses of pensions directly recorded in shareholders’ equity
3. Expensing capitalized development cost of R&D
4. Cancellation of the fair value model accounting for property, plant, and equipment and investment properties and incorporation of the cost model accounting
5. Exclusion of minority interests from net income, if contained

1.4. Business combination

The purchase method of accounting is used to account for acquired businesses. Assets and liabilities of consolidated subsidiaries are evaluated using the full fair value method at the acquisition date. The difference between the cost of purchased businesses and the fair value of their net assets is recorded as goodwill or negative goodwill (i.e. bargain purchase) after the purchased businesses’ identifiable assets and liabilities are measured at their fair value at the acquisition date. Goodwill is amortized using the straight-line method over 20 years. Negative goodwill is recognized in profit or loss in the period in which the business combination took place.

1.5. Scope of cash and cash equivalents on consolidated statements of cash flows

Cash and cash equivalents consist of cash on hand, cash in banks which can be withdrawn at any time, and short-term investments with a maturity of three months or less when purchased which can easily be converted to cash and are subject to little risks of changes in value.

1.6. Inventories
Inventories held for sale in the ordinary course of business are stated at cost. The cost of merchandise, finished goods, work in process and raw materials is determined on the monthly moving average method, and the cost of supplies is determined on the last purchase price method.

The carrying amount of inventories on the balance sheets is written down to net realizable value if it is lower than the carrying amount.

1.7. Investments in securities
Securities are classified into held-to-maturity or available-for-sale securities depending on management's intent. Held-to-maturity securities are recorded at amortized cost using the straight-line method.
Marketable securities classified as available-for-sale securities are recorded at fair value. Unrealized holding gains or losses on available-for-sale securities are reported as a component of net assets. Cost of securities sold is determined using the moving average method.

Non-marketable securities classified as available-for-sale securities are recorded at cost which is determined using the moving average method. Investments in limited partnerships (investments defined as securities under Article 2.2 of the Financial Instruments and Exchange Law of Japan) are recorded at net equity based on the most recently available financial statements to the reporting date specified in the partnership agreement.

1.8. Property, plant and equipment, excluding leased assets
Property, plant and equipment are stated at cost.

Depreciation of property, plant and equipment of the Company and its domestic consolidated subsidiaries is calculated using the declining balance method, except for buildings (excluding building fixtures) acquired after April 1, 1998, for which depreciation is calculated using the straight-line method. Depreciation of property, plant and equipment of the foreign consolidated subsidiaries is calculated using the straight-line method based on the local accounting standards of each country.

The primary useful lives are as follows:
Buildings and structures 10—50 years
Machinery and equipment, vehicles 7—15 years

Property, plant and equipment with acquisition cost greater than ¥100,000 and less than ¥200,000 are depreciated by the straight-line method over 3 years.

1.9. Intangible assets, excluding leased assets
Intangible assets are amortized using the straight-line method. Software for internal use is amortized using the straight-line method over its estimated useful life of 5 years.

1.10. Leases
Finance leases that do not transfer ownership are capitalized and depreciated using the straight-line method over the lease term with zero residual value. However, finance leases entered into on or prior to December 31, 2008 are not capitalized but accounted for using a method similar to that for operating lease transactions, and corresponding information is provided in the notes to the accompanying consolidated financial statements.

Lease transactions other than finance lease transactions are accounted for as operating leases and the related payments are charged to income as they incurred.

1.11. Impairment on non-current assets
The Group reviews non-current assets for impairment whenever events or changes in circumstances based on external or internal sources of information indicate that the carrying amount may not be recoverable. When such events or changes in circumstances occur, a recoverability test is required to be performed. An individual asset or asset group is impaired if its carrying amount exceeds the amount to be recovered through use or sale of such asset or asset group.

1.12. Retirement benefits
The Company and its domestic consolidated subsidiaries have defined benefit plans including a cash balance plan, lump sum retirement payment plan to cover the majority of their employees (including corporate officers).

For the employees (including corporate officers) of certain foreign consolidated subsidiaries, defined contribution pension plans and lump sum retirement payment plans are provided.

Certain subsidiaries may make an additional lump sum retirement payment, which is expensed as incurred.

The retirement benefit attributable to each year is calculated by assigning the same amount of pension benefits to each year of service. Provision for retirement benefits, accrued as the future payments of pension benefits for employees (including corporate officers), is stated based on the estimated amount of projected benefit obligation and the pension plan assets at the fiscal year end. Prior service cost is amortized by the straight-line method over a certain period (10 years), within the average remaining service period of the employees.

Unrecognized actuarial gains or losses are amortized from the following year after the recognition by the straight-line method over a certain period (10—14 years), within the average remaining service period of the employees.

1.13. Directors' retirement benefits
(Supplementary information)
Directors' retirement benefits, which had been accrued at the fiscal year end based on the internal regulations of the Company and its domestic subsidiaries, were terminated in accordance with the resolution of the annual meeting of shareholders and the board meeting on March 29, 2012.

The total balance of ¥378 million (U.S. $4,368 thousand) in "Provision for directors' retirement benefits" was reversed and the future payments amounting to ¥253 million (U.S. $2,929 thousand) arising in the period before the termination was included in "Accounts payable—other" and "Other" under "Non-current liabilities" as of December 31, 2012.

1.14. Allowance for doubtful accounts
The Company and its domestic consolidated subsidiaries record allowance for doubtful accounts based on historical loss ratio for general receivables, and based on individual assessment of uncollectible amounts for certain receivables. Foreign consolidated subsidiaries mainly estimate unrecoverable amounts on an individual basis.

1.15. Provisions
Provisions for directors' and employees' bonuses
Provisions for directors' and employees' bonuses are stated at the estimated amounts of the bonuses to be paid to directors and employees, in accordance with their services provided during the fiscal year.
Provision for sales returns
Provisions are set up to cover future losses arising from sales returns based on the past return ratios.
Provision for point program
Provisions are set up to cover future discounts and commemorative gifts under point program plans based on the estimated future outflows.
Provision for environmental measures
Provisions are set up to cover the estimated charges for disposal of waste (polychlorinated biphenyl (PCB)).

1.16. Research and development costs
The costs for research and development are charged to income as incurred.

1.17. Income taxes
Income taxes are accounted for using the asset and liability approach. Deferred tax assets and liabilities are recognized in the accompanying consolidated financial statements with respect to the differences between financial reporting and the tax bases of the assets and liabilities, and measured using the enacted tax rates and laws which will be in effect when the differences are expected to reverse.

1.18. Per share information
Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average common shares outstanding during the period. The number of shares used in the computations was 55,284 thousand shares for fiscal 2012 (55,284 thousand shares for fiscal 2011). Diluted net income per share is computed for fiscal 2012 due to the dilutive effect of subscription rights to shares arising from stock options, which were adopted by the Group in the current fiscal year. The Company did not have securities or contingent stock agreements with potentially dilutive effect during fiscal 2011.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends applicable to the respective years, including dividends to be paid after year-end.

1.19. Foreign currency translation
Receivables and payables of the domestic consolidated subsidiaries denominated in foreign currencies are translated into yen at year-end exchange rates, and differences arising from the translation are included in the accompanying consolidated statements of income.
All assets and liabilities of the foreign consolidated subsidiaries are translated into yen at year-end exchange rates, while revenue and expenses are translated at the average exchange rate for the year. Adjustments to translate those accounts into Japanese yen are presented as foreign currency translation adjustments and minority interests in net assets of the accompanying consolidated balance sheets.

1.20. Amortization method and period of goodwill
Goodwill is amortized using the straight-line method over 20 years.

1.21. Other important items related to the preparation of the consolidated financial statements

1.21.1 Accounting method for consumption tax and local consumption tax

The tax-exclusion accounting method is applied for consumption tax and local consumption tax.

1.21.2 Application of consolidated tax system

The consolidated tax system is applied.

Note 2 Changes in Accounting Policies and Disclosures

2.1. Newly adopted accounting policies and disclosures

Newly adopted accounting policies and disclosures in fiscal 2012

2.1.1 Accounting Standard for Accounting Changes and Error Corrections

Effective from January 1, 2012, the "Accounting Standard for Accounting Changes and Error Corrections" (ASBJ Statement No. 24, issued on December 4, 2009) and "Guidance on Accounting Standard for Accounting Changes and Error Corrections" (ASBJ Guidance No. 24, issued on December 4, 2009) were adopted by the Group to account for accounting changes and corrections of prior period errors.

2.2. Accounting standards issued but not yet adopted

From the viewpoint of improvements to financial reporting and international convergence, the ASBJ has been deliberating the establishment of a revised accounting standard for retirement benefits, "Accounting Standard for Retirement Benefits" (ASBJ Statement No. 26, issued on May 17, 2012) and "Guidance on Accounting Standard for Retirement Benefits" (ASBJ Guidance No. 25, issued on May 17, 2012), which mainly focus on (a) how actuarial gains and losses and prior service cost should be accounted for, (b) how projected benefit obligations and current service costs should be determined and (c) enhancement of disclosures.

This revised accounting standard, though not yet adopted by the Group, will be introduced and made effective from the end of fiscal 2014. The resulting impacts on future consolidated financial statements are being examined.

Note 3 U.S. Dollar Amounts

The accompanying consolidated financial statements are presented in yen, and solely for the convenience of readers outside Japan, certain amounts have been translated into U.S. dollars at the rate of U.S. $1= ¥86.58, the approximate rate of exchange prevailing at December 31, 2012. This translation should not be construed as a representation that all amounts shown could be converted into U.S. dollars at such a rate.

Note 4 Cash Flow Information

4.1. Cash and cash equivalents consist of the following:

	Millions of yen		Thousands of U.S. dollars
December 31	**2012**	2011	**2012**
Cash and deposits	**¥22,551**	¥50,679	**$260,473**
Short-term investments in securities	**19,801**	18,412	**228,709**
Less:			
Time deposits with maturities exceeding three months	**(1,445)**	(1,432)	**(16,693)**
Stocks and bonds with maturities exceeding three months	**(15,801)**	(17,412)	**(182,509)**
Cash and cash equivalents	**¥25,106**	¥50,246	**$289,980**

4.2. Cash flows from business combination

In fiscal 2012, the Company acquired all outstanding shares in Jurlique. The assets and liabilities at the acquisition date, reconciliation from acquisition cost to net cash used for the purchase of investment in subsidiary are as follows:

	Millions of yen
Current assets	**¥ 2,927**
Non-current assets	**27,651**
Current liabilities	**(3,285)**
Non-current liabilities	**(2,809)**
Acquisition cost	**¥24,484**
Accounts payable – other associated with the acquisition of shares in Jurlique	**(183)**
Repayments of loans payable of Jurlique	**3,694**
Cash and cash equivalents of Jurlique	**(43)**
Net cash used for purchase of investment in Jurlique	**¥27,952**

In fiscal 2011, the Company acquired all outstanding shares in H2O PLUS HOLDINGS INC. ("H2O PLUS"). The assets and liabilities at the acquisition date, reconciliation from acquisition cost to net cash used for the purchase of investment in subsidiary are as follows:

	Millions of yen
Current assets	¥1,029
Non-current assets	8,935
Current liabilities	(857)
Non-current liabilities	(933)
Acquisition cost	8,174
Repayments of loans payable of H2O PLUS	838
Cash and cash equivalents of H2O PLUS	(89)
Net cash used for purchase of investment in H2O PLUS	¥8,923

4.3. Significant non-cash transactions

Assets and liabilities related to finance lease transactions newly recorded are ¥892 million (U.S. $10,309 thousand) in fiscal 2012 (¥800 million in fiscal 2011).

Asset retirement obligations newly recorded were ¥438 million (U.S. $5,066 thousand) in fiscal 2012 (¥1,374 million in fiscal 2011 due to the adoption of the accounting standard for asset retirement obligations).

Note 5 Items Related to Affiliated Companies

Items related to affiliated companies are as follows, except for those stated separately:

	Millions of yen		Thousands of U.S. dollars
December 31	**2012**	2011	**2012**
Investments in securities (stock)	**¥20**	¥57	**$232**
(Of which, investments in joint ventures)	**¥20**	¥57	**$232**

Note 6 Pledged Assets

Assets pledged as collateral for operating transactions are as follows:

	Millions of yen		Thousands of U.S. dollars
December 31	**2012**	2011	**2012**
Cash and deposits	**¥33**	¥41	**$382**

Note 7 Short-term and Long-term Debt

Short-term and long-term debt consists of the following:

December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Short-term loans payable	**¥1,733**	¥1,500	**$20,025**
Lease obligations-current portion	**676**	623	**7,813**
Lease obligations-long term	**¥1,071**	¥ 939	**$12,377**

The weighted average interest rates of short-term loans payable and lease obligations are as follows:

December 31	2012	2011
Short-term loans payable	**0.62%**	0.65%
Lease obligations-current portion	**2.41%**	2.25%
Lease obligations-long term	**2.57%**	2.23%

At December 31, 2012, the annual maturities of lease obligations for the subsequent 5 years are as follows:

Years ending December 31	Millions of yen	Thousands of U.S. dollars
2013	**¥676**	**$7,813**
2014	**543**	**6,277**
2015	**288**	**3,331**
2016	**133**	**1,540**
2017	**61**	**713**

Note 8 Contingent Liabilities

Contingent liabilities consist of the following:

December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Guarantees of loans			
Employees' mortgages	**¥253**	¥334	**$2,932**
Total	**¥253**	¥334	**$2,932**

Note 9 Retirement Benefits

9.1. Provision for retirement benefits consists of the following:

December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Projected benefit obligation	**¥12,120**	¥12,444	**$139,988**
Fair value of plan assets	**(5,694)**	(5,356)	**(65,768)**
Unfunded retirement benefit obligation	**6,425**	7,087	**74,219**
Unrecognized prior service cost	**288**	378	**3,334**
Unrecognized actuarial losses	**(320)**	(670)	**(3,700)**
Provision for retirement benefits	**¥ 6,394**	¥ 6,795	**$ 73,854**

9.2. The components of net periodic retirement benefit costs are as follows:

Years ended December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Service cost	**¥741**	¥758	**$8,560**
Interest cost	**174**	178	**2,014**
Expected return on plan assets	**(79)**	(77)	**(914)**
Amortization of prior service cost	**(89)**	(89)	**(1,032)**
Amortization of actuarial losses	**74**	98	**866**
Additional lump-sum payment	**4**	7	**57**
Net periodic retirement benefit costs	**¥826**	¥876	**$9,551**

Retirement benefit costs of certain consolidated subsidiaries which apply the simplified method were included in "Service cost."

9.3. Assumptions used in accounting for the above plans are as follows:

Years ended December 31	2012	2011
Discount rate	**1.50%**	1.50%
Expected rate of return on plan assets	**1.50%**	1.50%

Note 10 Net Assets

Information regarding changes in net assets is summarized as follows:

10.1. Shares issued and outstanding / Treasury stock

Thousands of shares	Common stock: Shares issued	Common stock: Treasury stock
Balance at January 1, 2011	57,284	2,000
Increase	—	—
Decrease	—	—
Balance at January 1, 2012	57,284	2,000
Increase	—	—
Decrease	—	—
Balance at December 31, 2012	57,284	2,000

10.2. Subscription rights to shares

Year ended December 31, 2012

Name of company	Details of subscription rights to shares	Type of shares issued	Number of shares issued: At beginning of fiscal 2012	Number of shares issued: Increase	Number of shares issued: Decrease	Number of shares issued: At end of fiscal 2012	Balance at December 31, 2012: Millions of yen	Balance at December 31, 2012: Thousands of U.S. dollars
POLA ORBIS HOLDINGS INC.	**Stock options**	—	—	—	—	—	**¥40**	**$471**
	Total		—	—	—	—	**¥40**	**$471**

There were no subscription rights to shares at December 31, 2011.

10.3. Dividends

Dividends paid

Year ended December 31, 2012

Resolution	Type of shares	Millions of yen Total dividends	Thousands of U.S. dollars Total dividends	Yen Dividends per share	U.S. dollars Dividends per share	Record date	Effective date
Annual Meeting of Shareholders on March 29, 2012	**Common stock**	**¥1,382**	**$15,963**	**¥25**	**$0.29**	**December 31, 2011**	**March 30, 2012**
Board of Directors' Meeting on July 30, 2012	**Common stock**	**¥1,382**	**$15,963**	**¥25**	**$0.29**	**June 30, 2012**	**September 13, 2012**

Year ended December 31, 2011

Resolution	Type of shares	Millions of yen Total dividends	Yen Dividends per share	Record date	Effective date
Annual Meeting of Shareholders on March 30, 2010	Common stock	¥2,211	¥40.00	December 31, 2010	March 31, 2011
Board of Directors' Meeting on July 29, 2011	Common stock	¥1,105	¥20.00	June 30, 2011	September 12, 2011

Dividends with the record date in fiscal 2012 and the effective date in fiscal 2013

Year ended December 31, 2012

Resolution	Type of shares	Source of dividends	Millions of yen Total dividends	Thousands of U.S. dollars Total dividends	Yen Dividends per share	U.S. dollars Dividends per share	Record date	Effective date
Annual Meeting of Shareholders on March 28, 2013	**Common stock**	**Retained earnings**	**¥1,382**	**$15,963**	**¥25**	**$0.29**	**December 31, 2012**	**March 29, 2013**

Dividends with the record date in fiscal 2011 and the effective date in fiscal 2012

Year ended December 31, 2011

Resolution	Type of shares	Source of dividends	Millions of yen Total dividends	Yen Dividends per share	Record date	Effective date
Annual Meeting of Shareholders on March 29, 2012	Common stock	Retained earnings	¥1,382	¥25.00	December 31, 2011	March 30, 2012

Note 11 Research and Development Costs

Research and development costs of ¥3,747 million (U.S. $43,285 thousand) and ¥3,629 million were expensed for fiscal 2012 and 2011, respectively, as incurred, and included in selling, general and administrative expenses and cost of sales.

Note 12 Cost of Sales

Provision for sales returns included in cost of sales consists of the following:

Years ended December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Reversal of provision for sales returns	**¥76**	¥90	**$884**
Provision for sales returns	**¥76**	¥76	**$881**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 13 Selling, General and Administrative Expenses

Selling, general and administrative expenses mainly consist of the following:

Years ended December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Sales commission	**¥ 45,240**	¥ 43,477	**$ 522,526**
Promotion expenses	**17,491**	16,676	**202,028**
Advertising expenses	**7,293**	7,373	**84,242**
Packing and transportation expenses	**4,845**	4,438	**55,963**
Salaries, allowances and bonuses	**20,763**	17,882	**239,820**
Welfare expenses	**3,220**	2,869	**37,198**
Retirement benefit expenses	**692**	733	**8,003**
Provision for bonuses	**1,306**	1,331	**15,092**
Provision for point program	**1,622**	1,602	**18,743**
Depreciation and amortization	**4,546**	3,345	**52,508**
Amortization of goodwill	**829**	91	**9,585**
Other	**22,554**	20,521	**260,501**
Total	**¥130,407**	¥120,342	**$1,506,208**

Note 14 Other Income (Expenses)

14.1. Loss on disposal of non-current assets mainly consists of the following:

Years ended December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Buildings and structures	**¥ 71**	¥ 54	**$ 829**
Removal and demolition	**81**	255	**938**
Others	**69**	79	**803**
Total	**¥222**	¥389	**$2,569**

14.2. Reversal of provision for directors' retirement benefits of ¥119 million (U.S. $1,375 thousand) in fiscal 2012 arose from the termination of directors' retirement benefits approved by the annual meeting of shareholders and the board meeting on March 29, 2012. For further information, refer to "1.13. Directors' retirement benefits" in Note 1 "Summary of Significant Accounting Policies".

14.3. Impairment loss consists of the following:

Years ended December 31	Millions of yen 2012	Millions of yen 2011	Thousands of U.S. dollars 2012
Domestic			
Stores	**¥ 44**	¥ 47	**$ 517**
Offices	**8**	17	**103**
Idle assets	**—**	—	**—**
Office buildings for lease	**—**	102	**—**
Non-current assets held for sale	**—**	550	**—**
Overseas			
Stores	**6**	36	**77**
Offices	**—**	—	**—**
Other intangible assets (agency contracts)	**133**	—	**1,547**
Total	**¥194**	¥754	**$2,244**

(1) Background of recognizing impairment loss
For the non-current assets held for sale, and those asset groups of stores and offices for which operating losses have been continually recorded and whose estimated amount of future cash flows fell below their book value, impairment losses are recognized under other expenses by reducing their book value to recoverable value.

Impairment losses from agency contracts arising from the decision-making of terminating contracts with agents are recorded under other expenses by reducing the book value to recoverable value.

(2) Grouping method of assets
Stores and offices are grouped by store and office respectively, mainly on a basis of business departments whose income and expenditure are continually being examined.

Office buildings for lease and non-current assets held for sale are grouped by individual property unit.

Agency contracts are grouped by agent.

(3) Calculation methods of recoverable value
The recoverable value of stores and offices is measured by the value in use based on the present value of future cash flows, while offices scheduled for closure are measured by the fair value less costs to sell relying on the amount to be sold.

The recoverable value of office buildings for lease is measured by the higher amount of the value in use based on the present value of future cash flows and the fair value less costs to sell relying on the real estate appraisal, while non-current assets held for sale are measured by the fair value less costs to sell based on the real estate appraisal or the amount to be sold.

Agency contracts are measured by the value in use based on the present value of future cash flows.

The value in use of stores, offices and agency contracts is assessed at zero because the future cash flows can not be expected.

Note 15 Information on Consolidated Statements of Comprehensive Income

Reclassification adjustments and tax effects for each component of other comprehensive income are as follows:

	Millions of yen	Thousands of U.S. dollars
Year ended December 31	2012	2012
Unrealized gain or loss on available-for-sale securities		
Amount arising during the year	¥ 381	$ 4,405
Reclassification adjustment	5	64
Amount before tax effect	386	4,470
Tax effect	(19)	(230)
Unrealized gain or loss on available-for-sale securities, net of tax	¥ 367	$ 4,240
Deferred gain or loss on hedges		
Amount arising during the year	¥ (15)	$ (184)
Amount before tax effect	(15)	(184)
Tax effect	6	75
Deferred gain or loss on hedges, net of tax	¥ (9)	$ (109)
Foreign currency translation adjustments		
Amount arising during the year	¥3,540	$40,895
Share of other comprehensive income of associates accounted for using the equity method		
Amount arising during the year	¥ (1)	$ (20)
Total other comprehensive income	¥3,896	$45,006

Note 16 Income Taxes

16.1. Deferred tax assets and liabilities consist of the following:

	Millions of yen		Thousands of U.S. dollars
December 31	2012	2011	2012
Deferred tax assets:			
Provision for bonuses	¥ 562	¥ 594	$ 6,499
Provision for retirement benefits	2,260	2,400	26,104
Loss on valuation of inventories	604	621	6,982
Impairment loss	14,370	14,435	165,984
Loss on valuation of investments in securities	302	302	3,491
Provision for point program	601	637	6,951
Unrealized inter-company profit	1,222	1,024	14,119
Tax loss carry-forwards	8,227	7,864	95,032
Enterprise tax payable	373	226	4,309
Asset retirement obligations	667	487	7,711
Other	1,065	1,172	12,302
Less valuation allowance	(22,750)	(22,345)	(262,767)
Total deferred tax assets	7,507	7,422	86,716
Deferred tax liabilities:			
Unrealized gain on available-for-sale securities	(183)	(163)	(2,124)
Restoration cost for asset retirement obligations	(263)	(124)	(3,038)
Goodwill, trademark rights and other intangible assets	(1,627)	(535)	(18,800)
Other	(21)	(22)	(249)
Total deferred tax liabilities	(2,096)	(847)	(24,211)
Deferred tax assets, net	¥5,411	¥6,575	$62,505

16.2. The reconciliations between the statutory tax rate and the effective tax rate are as follows:

Years ended December 31	2012	2011
Statutory income tax rate	40.7%	40.7%
Expenditure not allowable for income tax purposes (Entertainment expense, etc.)	1.5	1.3
Per capita inhabitants' tax	0.3	0.4
Increase (decrease) in valuation allowance	9.4	(10.7)
Amortization of goodwill	2.4	0.3
Adjustments to the book values of investments	—	(4.6)
Tax credits for research and development costs	(1.8)	(2.3)
Reduction in deferred tax assets at reporting date due to revision of tax law	1.0	3.8
Other	(0.1)	(0.3)
Effective income tax rate	53.4%	28.7%

Note 17 Leases

(As a lessee)

17.1. Finance leases that do not transfer ownership

17.1.1. Accounting treatment for the finance leases entered into on or after January 1, 2009

The finance leases entered into on or after January 1, 2009 are capitalized. They primarily consist of interior and furniture and fixtures for retail stores included in buildings and structures or other property, plant and equipment, and are depreciated using the straight-line method over the lease term with zero residual value. Interest expense is calculated as the difference between the aggregate lease payments and the acquisition cost of leased assets, allocated over the lease term using the effective interest method.

17.1.2. Accounting treatment for the finance leases entered into on or prior to December 31, 2008

The finance leases entered into on or prior to December 31, 2008 are not capitalized but accounted for using a method similar to that applicable to operating lease transactions.

If such leases were capitalized, their depreciation or amortization would be determined on the straight-line method over the lease term with zero residual value and interest expense would be calculated as the difference between the aggregate lease payments and the acquisition cost of leased assets, allocated over the lease term using the effective interest method.

Acquisition cost, accumulated depreciation or amortization, accumulated impairment loss and net book value of such leases would be as follows:

	Millions of yen							
	2012				2011			
December 31	Acquisition cost	Accumulated depreciation/ amortization	Accumulated impairment loss	Net book value	Acquisition cost	Accumulated depreciation/ amortization	Accumulated impairment loss	Net book value
Buildings and structures	—	—	—	—	¥ 413	¥ 354	¥ 3	¥ 55
Other property, plant and equipment, including tools, furniture and fixtures	¥209	¥159	—	¥50	1,116	922	9	183
Total	¥209	¥159	—	¥50	¥1,529	¥1,277	¥12	¥238

	Thousands of U.S. dollars			
	2012			
December 31	Acquisition cost	Accumulated depreciation/ amortization	Accumulated impairment loss	Net book value
Buildings and structures	—	—	—	—
Other property, plant and equipment, including tools, furniture and fixtures	$2,424	$1,839	—	$586
Total	$2,424	$1,839	—	$586

Future lease payments are as follows:

	Millions of yen		Thousands of U.S. dollars
December 31	2012	2011	2012
Due within 1 year	¥28	¥208	$329
Due after 1 year	38	194	442
Total	¥66	¥402	$771

Balance of allowance for impairment loss on leased assets is as follows:

	Millions of yen		Thousands of U.S. dollars
December 31	2012	2011	2012
Allowance for impairment loss on leased assets	¥0	¥5	$9

Lease payments, reversal of impairment loss on leased assets, depreciation and amortization, interest expense and impairment loss are as follows:

	Millions of yen		Thousands of U.S. dollars
Years ended December 31	2012	2011	2012
Lease payments	¥215	¥627	$2,494
Reversal of impairment loss on leased assets	5	21	66
Depreciation and amortization	191	568	2,208
Interest expense	9	27	114
Impairment loss	0	1	8

17.2. Operating lease transactions

Future lease payments under non-cancelable operating lease arrangements are as follows:

	Millions of yen		Thousands of U.S. dollars
December 31	2012	2011	2012
Due within 1 year	¥14	¥ 7	$163
Due after 1 year	19	3	228
Total	¥33	¥11	$391

Note 18 Investment and Rental Property

18.1. Overview

The Group owns office buildings and residential properties for lease in Tokyo and other areas. Net rental income was ¥1,377 million (U.S. $15,914 thousand) in fiscal 2012, (¥1,504 million in fiscal 2011) (rental income is recorded under sales and other income, while rental expenses are recorded under cost of sales, selling, general and administrative expenses, and other expenses). No impairment loss and loss on disaster was recognized in fiscal 2012, while impairment loss of ¥606 million and loss on disaster of ¥83 million were recorded under other expenses in fiscal 2011.

18.2. Fair value of investment properties

The carrying amount on the consolidated balance sheets, net changes, the fair value of these properties, and the method used for calculating the fair value of investment and rental properties are as follows:

December 31, 2012	Millions of yen		
	Carrying amount		Fair value
Balance at January 1, 2012	Net increase	Balance at December 31, 2012	At December 31, 2012
¥ 21,980	**¥3,319**	**¥25,299**	**¥42,812**

December 31, 2011	Millions of yen		
	Carrying amount		Fair value
Balance at January 1, 2011	Net increase	Balance at December 31, 2011	At December 31, 2011
¥ 24,067	¥(2,087)	¥21,980	¥41,381

December 31, 2012	Thousands of U.S. dollars		
	Carrying amount		Fair value
Balance at January 1, 2012	Net increase	Balance at December 31, 2012	At December 31, 2012
$253,869	**$38,342**	**$292,212**	**$494,480**

1. The carrying amounts present acquisition cost less accumulated depreciation and accumulated impairment loss.
2. Components of change

Increase:

In fiscal 2012: Acquisition of office buildings and residential properties for lease: ¥3,355 million (U.S. $38,757 thousand)
Refurbishment of office buildings for lease: ¥277 million (U.S. $3,200 thousand)

In fiscal 2011: Refurbishment of office building for lease: ¥185 million.
Transfer due to changes in the use of properties: ¥146 million.

Decrease:

In fiscal 2012: Depreciation on office buildings and residential properties and other properties for lease:
¥438 million (U.S. $5,069 thousand)

In fiscal 2011: Sales of office building and idle assets: ¥1,222 million.
Impairment loss and non-recurring depreciation on office buildings and idle assets: ¥621 million.
Depreciation on office buildings and residential properties for lease: ¥571 million.

3. Method for calculating fair values

The fair values of major properties are determined by the amounts using appraisal certificates provided by independent real estate assessors. For other properties, however, the fair value of land is determined by the amount adjusted using the indices considered to properly reflecting market price, and the fair values of depreciable assets such as buildings are determined by the carrying amounts on the consolidated balance sheets. For the properties acquired in fiscal 2012, the fair values are determined at the carrying amounts due to minimal fluctuation on fair values.

Note 19 Financial Instruments

19.1. Overview of financial instruments

19.1.1. Policies on financial instruments

The Group only utilizes low risk, short-term financial instruments for cash management, and it raises funds through borrowings from banks and by issuing corporate bonds in the capital market. Derivatives are utilized only to the extent necessary to hedge foreign currency risk arising from transactions denominated in foreign currencies. The Group does not enter into derivative transactions for speculative or trading purposes.

19.1.2. Description of financial instruments, risks and risk management policy

Trade receivables such as notes and accounts are exposed to customers' credit risk. In order to manage such risk, the Group manages payment dates and outstanding balances by individual customer and review customers' credit status on a regular basis in accordance with credit management policy.

Investments in securities consist of financial instruments with low risk such as held-to-maturity debt securities, but some of them are exposed to the risk of fluctuations in market price. The Group reviews the prices on a quarterly basis in order to manage such risk.

Notes and accounts payable – trade and accounts payable – other are due within one year. The interest-bearing liabilities mainly include short-term loans payable and lease obligations. Short-term loans are mainly funding for operating transactions, and lease obligations are mainly funding for capital investments. Loans payable with floating interest rates are exposed to the risk of interest rate fluctuations but they are all short-term in nature.

The Group executes and manages derivative transactions in accordance with the internal policy governing the authorization of transactions. The use of derivatives is limited only to the extent necessary to hedge foreign exchange risk, and also the counterparties are limited to financial institutions with high credit standing in order to mitigate credit risk.

Furthermore, trade payables and interest-bearing liabilities are exposed to liquidity risk, but the Group manages such risk by, for example, preparing the cash management schedule on a monthly basis.

19.1.3. Supplementary information on fair value of financial instruments

Fair value of financial instruments is based on the quoted price in the active market. A reasonable valuation technique is used if a quoted price is not available. The values may change under different assumptions as such calculation incorporates variable factors. Also, the contract amounts disclosed in "Derivative transactions" do not represent market risk related to derivative transactions. For detailed information on derivative transactions, see Note 21 "Derivative transactions."

19.2. Fair value of financial instruments

The carrying amount, fair value of financial instruments and the difference between them consist of the following:

	Millions of yen		
	2012		
December 31	Carrying amount	Fair value	Difference
Assets			
(i) Cash and deposits	**¥22,551**	**¥22,551**	**—**
(ii) Notes and accounts receivable – trade (*1)	**22,559**	**22,559**	**—**
(iii) Investments in securities:			
Held-to-maturity securities	**35,363**	**35,366**	**¥3**
Available-for-sale securities	**2,817**	**2,817**	**—**
Total assets	**¥83,292**	**¥83,295**	**¥3**
Liabilities			
(i) Notes and accounts payable – trade	**¥ 3,630**	**¥ 3,630**	**—**
(ii) Short-term loans payable	**1,733**	**1,733**	**—**
(iii) Accounts payable – other	**12,077**	**12,077**	**—**
Total liabilities	**¥17,441**	**¥17,441**	**—**

	Millions of yen		
	2011		
December 31	Carrying amount	Fair value	Difference
Assets			
(i) Cash and deposits	¥ 50,679	¥ 50,679	—
(ii) Notes and accounts receivable – trade (*1)	20,650	20,650	—
(iii) Investments in securities:			
Held-to-maturity securities	29,312	28,694	¥(617)
Available-for-sale securities	2,446	2,446	—
Total assets	¥103,089	¥102,471	¥(617)
Liabilities			
(i) Notes and accounts payable – trade	¥ 2,894	¥ 2,894	—
(ii) Short-term loans payable	1,500	1,500	—
(iii) Accounts payable – other	11,391	11,391	—
Total liabilities	¥ 15,786	¥ 15,786	—
Derivative transactions (*2)	¥ 15	¥ 15	—

	Thousands of U.S. dollars		
	2012		
December 31	Carrying amount	Fair value	Difference
Assets			
(i) Cash and deposits	**$260,473**	**$260,473**	**—**
(ii) Notes and accounts receivable – trade (*1)	**260,561**	**260,561**	**—**
(iii) Investments in securities:			
Held-to-maturity securities	**408,453**	**408,489**	**$36**
Available-for-sale securities	**32,545**	**32,545**	**—**
Total assets	**$962,032**	**$962,068**	**$36**
Liabilities			
(i) Notes and accounts payable – trade	**$ 41,931**	**$ 41,931**	**—**
(ii) Short-term loans payable	**20,025**	**20,025**	**—**
(iii) Accounts payable – other	**139,495**	**139,495**	**—**
Total liabilities	**$201,451**	**$201,451**	**—**

(*1) Notes and accounts receivable-trade are presented net of allowance for doubtful accounts.
(*2) Receivables and payables arising from derivative transactions are presented on a net basis, with net payables presented in parenthesis.

1. Calculation method of fair value of financial instruments and information about securities

Assets

(i) Cash and deposits, (ii) Notes and accounts receivable – trade

Carrying value is used for fair value as they are short term in nature; the fair value approximates the carrying value.

(iii) Investments in securities

The fair value of stock is determined on the quoted price on stock exchanges and the fair value of debt securities is determined on the quoted prices provided by financial institutions. For the short-term investments in securities, their fair values approximate carrying value.

For notes related to securities by holding purpose, refer to Note 20 "Investments in securities."

Liabilities

(i) Notes and accounts payable – trade, (ii) Short-term loans payable and (iii) Accounts payable – other

Carrying value is used for fair value as they are short term in nature; the fair value approximates the carrying value.

2. Financial instruments for which fair values are not readily available consist of the following:

	Millions of yen		Thousands of U.S. dollars
	2012	2011	2012
December 31	Carrying amount	Carrying amount	Carrying amount
Unlisted stock	**¥ 23**	¥ 60	**$ 270**
Capital contribution to investment in a limited partnership	**168**	175	**1,948**
Total	**¥192**	¥236	**$2,218**

These financial instruments are not included in "(iii) Investments in securities" as their fair values are unavailable and future cash flows are not determinable.

3. Redemption schedule of monetary receivables and investments in securities with maturities at December 31, 2012 and 2011 are as follows:

	Millions of yen			
	2012			
December 31	Due within 1 year	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and deposits	**¥22,551**	**—**	**—**	**—**
Notes and accounts receivable – trade	**22,559**	**—**	**—**	**—**
Investments in securities				
Held-to-maturity debt securities (corporate bonds)	**1,000**	**—**	**—**	**—**
Held-to-maturity debt securities (other)	**17,800**	**¥16,500**	**—**	**—**
Available-for-sale securities with maturities (other)	**1,003**	**165**	**—**	**—**
Total	**¥64,914**	**¥16,665**	**—**	**—**

	Millions of yen			
	2011			
December 31	Due within 1 year	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and deposits	¥50,679	—	—	—
Notes and accounts receivable – trade	20,650	—	—	—
Investments in securities				
Held-to-maturity debt securities (corporate bonds)	800	¥ 1,000	—	—
Held-to-maturity debt securities (other)	16,612	10,900	—	—
Available-for-sale securities with maturities (other)	1,008	—	¥167	—
Total	¥89,751	¥11,900	¥167	—

	Thousands of U.S. dollars			
	2012			
December 31	Due within 1 year	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and deposits	**$260,473**	**—**	**—**	**—**
Notes and accounts receivable – trade	**260,561**	**—**	**—**	**—**
Investments in securities				
Held-to-maturity debt securities (corporate bonds)	**11,550**	**—**	**—**	**—**
Held-to-maturity debt securities (other)	**205,590**	**$190,575**	**—**	**—**
Available-for-sale securities with maturities (other)	**11,586**	**1,913**	**—**	**—**
Total	**$749,760**	**$192,488**	**—**	**—**

4. For the repayment schedule of lease obligations at December 31, 2012, refer to Note 7 "Short-term and Long-term Debt."

Note 20 Investments in Securities

20.1. Marketable securities classified as held-to-maturity securities consist of the following:

	Millions of yen					
	2012			2011		
December 31	Carrying amount	Fair value	Difference	Carrying amount	Fair value	Difference
Securities with fair value exceeding carrying amount						
Corporate bonds	**¥ 1,000**	**¥ 1,002**	**¥ 2**	¥ 1,800	¥ 1,826	¥ 26
Other	**16,104**	**16,182**	**77**	4,800	4,821	21
Subtotal	**17,104**	**17,184**	**79**	6,600	6,648	47
Securities with carrying amount exceeding fair value						
Corporate bonds	**—**	**—**	**—**	—	—	—
Other	**18,259**	**18,182**	**(76)**	22,712	22,046	(665)
Subtotal	**18,259**	**18,182**	**(76)**	22,712	22,046	(665)
Total	**¥35,363**	**¥35,366**	**¥ 3**	¥29,312	¥28,694	¥(617)

	Thousands of U.S. dollars		
	2012		
December 31	Carrying amount	Fair value	Difference
Securities with fair value exceeding carrying amount			
Corporate bonds	**$ 11,550**	**$ 11,574**	**$ 24**
Other	**186,011**	**186,909**	**898**
Subtotal	**197,561**	**198,483**	**922**
Securities with carrying amount exceeding fair value			
Corporate bonds	**—**	**—**	**—**
Other	**210,892**	**210,006**	**(886)**
Subtotal	**210,892**	**210,006**	**(886)**
Total	**$408,453**	**$408,489**	**$ 36**

20.2. Marketable securities classified as available-for-sale securities consist of the following:

	Millions of yen					
	2012			2011		
December 31	Carrying amount	Acquisition cost	Difference	Carrying amount	Acquisition cost	Difference
Securities with carrying amount exceeding acquisition cost						
Stock	**¥1,817**	**¥1,312**	**¥505**	¥ 593	¥ 133	¥459
Other	**—**	**—**	**—**	—	—	—
Subtotal	**1,817**	**1,312**	**505**	593	133	459
Securities with acquisition cost exceeding carrying amount						
Stock	**0**	**0**	**(0)**	852	1,178	(326)
Other	**1,000**	**1,000**	**—**	1,000	1,000	—
Subtotal	**1,000**	**1,000**	**(0)**	1,852	2,178	(326)
Total	**¥2,817**	**¥2,312**	**¥505**	¥2,446	¥2,312	¥133

	Thousands of U.S. dollars		
	2012		
December 31	Carrying amount	Acquisition cost	Difference
Securities with carrying amount exceeding acquisition cost			
Stock	**$20,991**	**$15,155**	**$5,836**
Other	**—**	**—**	**—**
Subtotal	**20,991**	**15,155**	**5,836**
Securities with acquisition cost exceeding carrying amount			
Stock	**5**	**7**	**(3)**
Other	**11,550**	**11,550**	**—**
Subtotal	**11,555**	**11,557**	**(3)**
Total	**$32,545**	**$26,712**	**$5,833**

Unlisted stock of ¥23 million (U.S. $270 thousand) at December 31, 2012 (¥60 million at December 31, 2011) and capital contribution to investment in a limited partnership of ¥168 million (U.S. $1,948 thousand) at December 31, 2012 (¥175 million at December 31, 2011) were carried in the accompanying consolidated balance sheets. They are not included in "available-for-sale securities" in the above table as quoted price is unavailable and their fair value is not readily determinable. Refer to "2. Financial instruments for which fair values are not readily available" in Note 19 "Financial Instruments".

20.3. Available-for-sale securities sold during fiscal 2012 and 2011 consist of the following:

	Millions of yen					
	2012			2011		
Years ended December 31	Amount sold	Aggregate gains on sales of securities	Aggregate losses on sales of securities	Amount sold	Aggregate gains on sales of securities	Aggregate losses on sales of securities
Stock	**—**	**—**	**—**	¥14	—	¥14
Other	**—**	**—**	**—**	—	—	—
Total	**—**	**—**	**—**	¥14	—	¥14

	Thousands of U.S. dollars		
	2012		
Year ended December 31	Amount sold	Aggregate gains on sales of securities	Aggregate losses on sales of securities
Stock	**—**	**—**	**—**
Other	**—**	**—**	**—**
Total	**—**	**—**	**—**

Note 21 Derivative Transactions

There were no derivative transactions applicable to fiscal 2012.

Derivative transactions related to a foreign currency to which hedge accounting was applied as of December 31, 2011 consist of the following:

			Millions of yen		
December 31			2011		
Accounting method	Hedging instruments	Hedged item	Contract amount	Maturity over 1 year	Fair value (1)
Deferred hedge accounting basis	Foreign currency options (2)				
	Sell (Put)				
	Australian dollar	Forecasted foreign currency transaction	¥12,812	—	¥ (1)
	Purchase (Call)				
	Australian dollar	Forecasted foreign currency transaction	13,326	—	17
	Total		¥26,138	—	¥15

(1) The fair value is determined on the quoted prices provided by financial institutions.
(2) No premium is paid to the broker in the foreign currency options.

Note 22 Segment Information

22.1. General information about reportable segments

A reportable segment is a component of the Group for which discrete financial information is available and whose operating results are regularly reviewed by the Board of Directors to make decisions about resources to be allocated to the segment and assess its performance. The Group primarily develops, manufactures and markets cosmetics and related products. It promotes a multi-brand strategy of holding a range of brands and winning market share for each of its high profile brands in order to satisfy the diversifying needs of its customers based on their values. Comprehensive strategies are planned and products are marketed by each brand name in Japan and overseas. In addition to its cosmetics business, a variety of businesses is conducted to contribute to the Group's profits.

Therefore, reportable segments consist of the Beauty Care business, the Group's core business, and the Real Estate business, which indirectly supports the Group's core business. The Beauty Care business manufactures and markets cosmetics and health foods and sells fashion items (women's underwear, women's apparel and jewelry) under the following brand names: *POLA, ORBIS, pdc, FUTURE LABO, ORLANE, decencia, THREE, H2O PLUS and Jurlique.* The Real Estate business is engaged in the leasing of office buildings and residential properties.

22.2. Calculation method for net sales, income (loss), assets and other items by reportable segment

The accounting policies and measures for the Group's reportable business segments are generally the same as described in Note 1 "Summary of Significant Accounting Policies". Segment income is based on operating income. The amounts of inter-segment unrealized profit and transfer are calculated based on prevailing market prices.

22.3. Information about net sales and income (loss) by reportable segment

	Millions of yen						
	2012						
	Reportable Segments						
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others (Note 1)	Subtotal	Reconciliations (Note 2)	Consolidated total (Note 3)
Net sales							
Sales to external customers	¥168,811	¥2,841	¥171,653	¥9,220	¥180,873	—	¥180,873
Inter-segment sales or transfers	76	628	705	3,277	3,983	¥(3,983)	—
Total	168,888	3,470	172,358	12,498	184,857	(3,983)	180,873
Segment income	11,812	1,139	12,952	335	13,287	232	13,520
Segment assets	163,165	29,838	193,003	10,742	203,746	5,393	209,140
Other items							
Depreciation and amortization	5,364	593	5,957	265	6,223	242	6,466
Amortization of goodwill	829	—	829	—	829	—	829
Increase in property, plant and equipment and intangible assets	¥ 5,683	¥3,736	¥ 9,419	¥ 228	¥ 9,648	¥ (38)	¥ 9,609

Notes: 1. "Others" comprises business operations that are not categorized as reportable segments and include the pharmaceuticals and building maintenance.
2. Reconciliations consist of the following:
(1) The segment income reconciliation of ¥232 million (U.S. $2,688 thousand) includes intersegment transaction eliminations of ¥2,378 million (U.S. $27,472 thousand) minus corporate expenses of ¥2,145 million (U.S. $24,784 thousand), not allocated to each segment. Corporate expenses are primarily the Company's administrative expenses not allocated to reportable segments.
(2) The segment assets reconciliation of ¥5,393 million (U.S. $62,299 thousand) includes corporate assets of ¥56,666 million (U.S. $654,494 thousand), not allocated to each segment, minus intersegment eliminations of ¥51,272 million (U.S. $592,195 thousand). Corporate assets are primarily the Company's financial assets and assets in the administrative division not allocated to reportable segments.
(3) Reconciliations of depreciation and amortization, and increases in property, plant and equipment, and intangible assets are those related to corporate assets and intersegment eliminations.
3. Segment income is adjusted for operating income reported in the consolidated statements of income.
4. Amortization and increase in long-term prepaid expenses are included in depreciation and amortization, and increases in property, plant and equipment, and intangible assets, respectively.

	Millions of yen						
	2011						
	Reportable Segments						
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others (Note 1)	Subtotal	Reconciliations (Note 2)	Consolidated total (Note 3)
Net sales							
Sales to external customers	¥154,778	¥3,089	¥157,867	¥8,790	¥166,657	—	¥166,557
Inter-segment sales or transfers	100	659	759	5,781	6,541	¥(6,541)	—
Total	154,878	3,748	158,627	14,571	173,199	(6,541)	166,657
Segment income	10,787	1,283	12,071	501	12,573	280	12,853
Segment assets	111,405	28,512	139,917	10,367	150,285	42,742	193,027
Other items							
Depreciation and amortization	4,339	637	4,977	282	5,260	113	5,374
Amortization of goodwill	91	—	91	—	91	—	91
Increase in property, plant and equipment and intangible assets	¥ 4,516	¥ 273	¥ 4,790	¥ 193	¥ 4,983	¥ 64	¥ 5,048

Notes: 1. "Others" comprises business operations that are not categorized as reportable segments and include the pharmaceuticals, building maintenance and printing businesses.
2. Reconciliations consist of the following:
(1) The segment income reconciliation of ¥280 million includes inter-segment transaction eliminations of ¥2,351 million minus corporate expenses of ¥2,071 million, not allocated to each segment. Corporate expenses are primarily the Company's administrative expenses not allocated to reportable segments.
(2) The segment assets reconciliation of ¥42,742 million includes corporate assets of ¥88,517 million, not allocated to each segment, minus inter-segment eliminations of ¥45,775 million. Corporate assets are primarily the Company's financial assets and assets in the administrative division not allocated to reportable segments.
(3) Reconciliations of depreciation and amortization, and increases in property, plant and equipment, and intangible assets are those related to corporate assets and intersegment eliminations.
3. Segment income is adjusted for operating income reported in the consolidated statements of income.
4. Amortization and increase in long-term prepaid expenses are included in depreciation and amortization, and increases in property, plant and equipment, and intangible assets, respectively.
5. Depreciation and amortization in the Beauty Care segment includes non-recurring depreciation on non-current assets of ¥15 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Thousands of U.S. dollars						
	2012						
	Reportable Segments						
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others (Note 1)	Subtotal	Reconciliations (Note 2)	Consolidated total (Note 3)
Net sales							
Sales to external customers	$1,949,780	$32,819	$1,982,599	$106,495	$2,089,094	—	$2,089,094
Inter-segment sales or transfers	886	7,263	8,149	37,858	46,007	$(46,007)	—
Total	1,950,665	40,082	1,990,747	144,353	2,135,101	(46,007)	2,089,094
Segment income	136,438	13,159	149,598	3,872	153,470	2,688	156,158
Segment assets	1,884,567	344,630	2,229,197	124,081	2,353,278	62,299	2,415,577
Other items							
Depreciation and amortization	61,954	6,860	68,815	3,072	71,887	2,799	74,686
Amortization of goodwill	9,585	—	9,585	—	9,585	—	9,585
Increase in property, plant and equipment and intangible assets	$ 65,643	$43,152	$ 108,795	$ 2,643	$ 111,438	$ (449)	$ 110,989

22.4. Information related to reportable segment

22.4.1. Sales information by product and service

	Millions of yen			
	2012			
Year ended December 31	Cosmetics	Fashion	Others	Total
Sales to external customers	¥155,849	¥ 12,962	¥ 12,061	¥ 180,873

	Millions of yen			
	2011			
Year ended December 31	Cosmetics	Fashion	Others	Total
Sales to external customers	¥141,453	¥ 13,324	¥ 11,879	¥ 166,657

	Thousands of U.S. dollars			
	2012			
Year ended December 31	Cosmetics	Fashion	Others	Total
Sales to external customers	$1,800,068	$ 149,711	$ 139,314	$2,089,094

22.4.2. Information by geographical area

Information by geographical area is omitted, as both sales and assets of the domestic segment account for more than 90% of the total sales and assets of all segments for fiscal 2012 and 2011.

22.4.3. Information by customer

Information by customer is omitted, as there are no external customers for which sales account for more than 10% of net sales presented in consolidated statements of income for fiscal 2012 and 2011.

22.5. Information about impairment loss of non-current assets by reportable segment

	Millions of yen					
	2012					
	Reportable Segments					
Year ended December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Impairment loss	¥194	—	¥194	—	—	¥194

	Millions of yen					
	2011					
	Reportable Segments					
Year ended December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Impairment loss	¥101	¥649	¥751	—	¥3	¥754

	Thousands of U.S. dollars					
	2012					
	Reportable Segments					
Year ended December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Impairment loss	**$2,244**	**—**	**$2,244**	**—**	**—**	**$2,244**

22.6. Information about amortization and balance of goodwill by reportable segment

	Millions of yen					
	2012					
	Reportable Segments					
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Amortization of goodwill	**¥ 829**	**—**	**¥ 829**	**—**	**—**	**¥ 829**
Goodwill	**¥18,256**	**—**	**¥18,256**	**—**	**—**	**¥18,256**

	Millions of yen					
	2011					
	Reportable Segments					
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Amortization of goodwill	¥ 91	—	¥ 91	—	—	¥ 91
Goodwill	¥3,583	—	¥3,583	—	—	¥3,583

	Thousands of U.S. dollars					
	2012					
	Reportable Segments					
Year ended or at December 31	Beauty Care	Real Estate	Subtotal	Others	Reconciliations	Total
Amortization of goodwill	**$ 9,585**	**—**	**$ 9,585**	**—**	**—**	**$ 9,585**
Goodwill	**$210,860**	**—**	**$210,860**	**—**	**—**	**$210,860**

No gains arising from negative goodwill were recognized in fiscal 2012 and 2011.

Note 23 Business Combination

Business Combination—Acquisition of Jurlique

On November 30, 2011, the Company's Board of Directors approved a definitive agreement to acquire all outstanding shares in Jurlique, an Australia-based leading developer, manufacturer and marketer of natural organic skin and body care products, mainly operating in Asia, the United States and Europe. In addition, the Board also approved a resolution to establish two special purpose companies (SPCs) in Australia for acquiring all outstanding shares in Jurlique. The two SPCs were established on December 19, 2011. Following their establishment, the procedure for investing in the two SPCs was finalized on January 31, 2012. The acquisition of shares in Jurlique was completed on February 3, 2012.

23.1. Outline of business combination

23.1.1. Name and main business of acquired company

a. Name: Jurlique International Pty Ltd.
b. Business: Manufacturing and marketing of cosmetics products
c. Capital: A$72,133 thousand (At February 3, 2012)

23.1.2. Names of selling investor groups and individuals

a. JJHP, LLC
b. CPH Products Pty Limited
c. Ulrike Klein Investments Pty Limited
d. Other entities and Directors of Jurlique

23.1.3. Reason for business combination

To become a highly profitable global company—the Company's long-term strategic goal—by strengthening its global business base through the acquisition of Jurlique, which has 11 subsidiaries in five countries, and has developed retail points of distribution in 20 countries and regions, mainly in Asia, the United States and Europe. (The information is as of February 3, 2012.)

23.1.4. Date of business combination

February 3, 2012

23.1.5. Legal method used for business combination

Purchase of shares in cash

23.1.6. Names of companies and percentage of voting rights after business combination

a. Jurlique International Pty Ltd 100%

23.1.7. Identification of acquirer

Pola Orbis Holdings Inc. retains 100% voting rights of Jurlique and its 11 subsidiaries by acquisition of shares in Jurlique.

23.2. Operating period of acquired company included in accompanying consolidated financial statements

February 4, 2012–December 31, 2012

23.3. Breakdown of acquisition cost

		Millions of yen
Purchase consideration	Cash	¥23,763
Expenses directly related to acquisition	Advisory fees	¥ 721
Acquisition cost		¥24,484

23.4. Information regarding allocation of acquisition cost

23.4.1. Breakdown and amounts of assets received and liabilities assumed on the combination date

	Thousands of Australian dollars
Current assets	A$ 36,027
Non-current assets	340,461
Total assets	**A$376,489**
Current liabilities	40,439
Non-current liabilities	34,574
Total liabilities	**A$ 75,013**

23.4.2. Significant intangible assets excluding goodwill after allocation consist of the following:

	Thousands of Australian dollars
Right of trademark (non-amortization)	A$102,000
Customer-related intangible assets (weighted average amortization over 12 years)	A$ 39,008

23.4.3. Reason for and amount of goodwill incurred, and amortization method and period

a. Amount of goodwill recognized	¥15,177 million
b. Reason for recognition	Due to future excess earning potential, including synergies expected in future business development
c. Amortization method and period	Straight-line method over 20 years.

23.5. Estimated impact on the consolidated results for fiscal 2012 assuming the business combination had been completed as of the beginning of fiscal 2012 and its calculation method

	Millions of yen
Net sales	¥821
Operating loss	¥ (70)

(Calculation Method and Significant Assumptions for the Estimated Amounts)

(1) The estimated impact is the difference between the net sales and operating income (loss) of the acquired companies assuming the business combination had been completed as of the beginning of fiscal 2012 and the net sales and operating income (loss) included in the consolidated statements of income. The advisory fees relating to the combination paid by Jurlique and 11 other companies have not been included in the difference.

(2) The estimated amounts in Japanese yen shown above are converted using the average exchange rate from January 1, 2012 to January 31, 2012, ¥80.21 to A$1.

(3) The estimated amounts above are not audited.

Note 24 Per Share Information

For fiscal 2012 and 2011, basic net income per share is computed based on the net income available for distribution to shareholders of common stock and the weighted average common shares outstanding. Diluted net income per share is computed for fiscal 2012 due to the dilutive effect of subscription rights to shares arising from stock options, which were issued by the Group in the fiscal year ended December 31, 2012. The Company did not have securities or contingent stock agreements with potentially dilutive effect during fiscal 2011.
Net assets per share are computed based on the net assets excluding subscription rights to shares and minority interests, and common shares outstanding at year-end.

24.1. Net income per share and assumptions used for calculations are as follows:

	Millions of yen		Thousands of U.S. dollars
Years ended December 31	2012	2011	2012
Numerator:			
Net income attributable to common stock	¥6,681	¥8,039	$77,170
Denominator:			
Weighted average number of common stock outstanding (thousands of shares)	55,284	55,284	55,284
	Yen		U.S. dollars
Basic net income per share	¥120.86	¥145.43	$1.40
	Millions of yen		Thousands of U.S. dollars
Adjustment for Numerator:			
Adjustment of net income	—	—	—
Adjustment for Denominator:			
Increase in the number of common stock (thousands of shares)	16	—	16
(Of which, subscription rights to shares)	(16)	—	(16)
	Yen		U.S. dollars
Diluted net income per share	¥120.82	—	$1.40

24.2. Net assets per share and assumptions used for calculations are as follows:

	Millions of yen		Thousands of U.S. dollars
At December 31	2012	2011	2012
Numerator:			
Total net assets	¥164,896	¥157,057	$1,904,556
Amount deducted from total net assets	123	86	1,425
(Of which, subscription rights to shares)	(40)	—	(471)
(Of which, minority interests)	(82)	(86)	(954)
Net assets attributable to common stock	¥164,773	¥156,971	$1,903,131
Denominator:			
Common shares issued (thousands of shares)	57,284	57,284	57,284
Treasury stock (thousands of shares)	2,000	2,000	2,000
Common shares outstanding used in the calculation of net assets per share (thousands of shares)	55,284	55,284	55,284
	Yen		U.S. dollars
Net assets per share	¥2,980.48	¥2,839.36	$34.42

Note 25 Related Party Transactions

There were no related party transactions in fiscal 2012 and 2011.

Note 26 Stock Options

On February 28, 2012, the Company's Board of Directors approved a resolution under which the directors' retirement benefit plan was terminated and a stock-based compensation plan to the directors of the Company and its subsidiaries was introduced. This resolution was also approved at the Annual Meeting of Shareholders on March 29, 2012.

26.1. Share-based compensation expenses of ¥40 million (U.S. $471 thousand) arising from stock options are included in selling, general and administrative expenses in fiscal 2012. There were no stock option plans in effect in fiscal 2011.

26.2. Details of the stock options

26.2.1 Information on the stock options

	Subscription rights to shares issued in 2012
Date of approval	March 30, 2012
Grantees	7 directors of the Company and 7 directors of subsidiaries
Type and number of shares granted	Common stock: 29,700 shares
Grant date	April 16, 2012
Preconditions to exercising rights	Resignation of the positions as directors in both the Company and the subsidiaries
Service period required	Not specified
Exercisable period	April 17, 2012 -April 16, 2042

26.2.2 Information on and changes to the stock options

The number of existing stock options at the end of fiscal 2012 (December 31, 2012) is presented below.

a. Number of stock options

	Subscription rights to shares issued in 2012
Date of approval	March 30, 2012
Non-vested	(shares)
Outstanding as of December 31, 2011	—
Granted	29,700
Forfeited	850
Vested	—
Outstanding as of December 31, 2012	28,850
Vested	(shares)
Outstanding as of December 31, 2011	—
Vested	—
Exercised	—
Forfeited	—
Outstanding as of December 31, 2012	—

b. Price information

	Subscription rights to shares issued in 2012	
Date of approval	March 30, 2012	
Exercise price	¥ 1	$ 0.01
Average stock price at the time of exercise	—	—
Fair value of stock options on the grant date	¥1,832	$21.15

26.3 Method used for estimating the fair value of stock options

The Company uses the Black-Scholes model for estimating the fair value of stock options.
Main basic assumptions used in the estimation are as follows:

	Subscription rights to shares issued in 2012
Volatility of stock prices (*1)	26.34%
Estimated remaining period (*2)	15 years
Estimated dividend (*3)	¥45.00 per share
Risk free rate (*4)	1.47%

(*1) Because it is less than 2 years since its listing, the Company uses the stock price information of other peer companies to calculate the volatility for part of the period.
(*2) As making a reasonable estimation is difficult due to insufficient data available, the estimated remaining period is measured based on the assumption that the subscription rights to shares would be exercised in the middle of the exercisable period.
(*3) The amount of the estimated dividend is based on the actual dividends in fiscal 2011.
(*4) The risk free rate is calculated based on the yield of government bonds corresponding to the estimated remaining period.

26.4 Method used for estimating the exercise of rights of the stock option

As is difficult to make a reasonable estimation for the future forfeited shares, the Company adopted the method of reflecting the actual number of forfeited shares only.

Note 27 Significant Subsequent Events

On February 13, 2013, the Company's Board of Directors approved a resolution under which the two plants of POLA CHEMICAL INDUSTRIES INC. (a consolidated subsidiary) are to be integrated.

27.1. Reasons for Integration

In line with the Group's consideration of establishing optimal production systems to radically enhance productivity, manufacturing in the Shizuoka Plant will be terminated and its functions transferred to the Fukuroi Plant.

27.2. Overview of Shizuoka Plant

(1) Location:	Suruga-ku, Shizuoka-shi, Shizuoka
(2) Business:	Cosmetics manufacturing
(3) Site area:	44,953 m²
(4) Book value of property, plant and equipment:	¥1,953 million (At December 31, 2012)
(5) Number of employees (including temporary staff):	336 (At February 1, 2013)

27.3. Schedules (appointed)

Manufacturing in the Shizuoka Plant will be terminated in fiscal 2014, with its functions being transferred to the Fukuroi Plant.

27.4. Impact on Performance

The impact on future performance is currently being carefully examined.

Independent Auditor's Report

ERNST & YOUNG

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Independent Auditor's Report

The Board of Directors
Pola Orbis Holdings Inc.

We have audited the accompanying consolidated financial statements of Pola Orbis Holdings Inc. and its consolidated subsidiaries, which comprise the consolidated balance sheet as at December 31, 2012, and the consolidated statements of income, comprehensive income, changes in net assets, and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information, all expressed in Japanese yen.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in Japan, and for designing and operating such internal control as management determines is necessary to enable the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. The purpose of an audit of the consolidated financial statements is not to express an opinion on the effectiveness of the entity's internal control, but in making these risk assessments the auditor considers internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pola Orbis Holdings Inc. and its consolidated subsidiaries as at December 31, 2012, and their consolidated financial performance and cash flows for the year then ended in conformity with accounting principles generally accepted in Japan.

Convenience Translation

We have reviewed the translation of these consolidated financial statements into U.S. dollars, presented for the convenience of readers, and, in our opinion, the accompanying consolidated financial statements have been properly translated on the basis described in Note 3.

Ernst & Young ShinNihon LLC

March 22, 2013
Tokyo, Japan

A member firm of Ernst & Young Global Limited

History

1929	Shinobu Suzuki founds the business in Shizuoka Prefecture.
1940	POLA CHEMICAL INDUSTRIES INC. is established (incorporated).
1946	POLA Cosmetics, Inc. is established (incorporated).
1954	The Shizuoka Factory is completed.
1961	The Yokohama Factory is completed. Fuji Printing, Ltd. (currently P.O. MEDIA SERVICE INC.) is established.
1964	The Yokohama R&D Center is completed.
1971	POLA Real Estate Inc. is established and the real estate business is launched.
1976	The POLA Research Institute of Beauty & Culture is established.
1977	The Fukuroi Factory is completed.
1979	The POLA Foundation for the Promotion of Traditional Japanese Culture is established.
1983	POLA CHEMICAL becomes a major investor in KAYAKU CO., LTD. and enters the pharmaceuticals business.
1984	ORBIS Inc. is established and the mail-order sales business is launched.
1986	POLA GTS Inc. (currently P.O. TECHNO SERVICE INC.) is established and the building maintenance business is launched. POLA CHEMICAL wins an award at the 14th IFSCC (International Federation of Societies of Cosmetic Chemists) Congress held in Barcelona, Spain.
1987	ORBIS starts full-fledged business activities (in the Tokyo metropolitan area).
1988	ORBIS first publishes its nationwide catalog.
1993	POLA Daily Cosme Inc. (currently pdc INC.) is established and the personal cosmetics business is launched.
1994	POLA CHEMICAL wins the highest award at the 18th IFSCC Congress held in Venice, Italy.
1996	POLA CHEMICAL wins an award at the 19th IFSCC Congress held in Sydney, Australia. The Pola Art Foundation is established.
1997	ORBIS receives ISO9001 certification. The Shizuoka and Fukuroi factories receive ISO9002 certification.
1998	POLA wins the highest award at the 20th IFSCC Congress held in Cannes, France. The Shizuoka and Fukuroi factories receive ISO9001 certification.
1999	ORBIS The Net (EC site) opens.
2000	POLA's corporate message, "Consulting First," is delivered. The first retail store "ORBIS THE SHOP" at Marui department store, in Ikebukuro, Tokyo opens. The Shizuoka and Fukuroi Factories receive ISO14001 certification.
2002	New business announcement by POLA aimed at "A thorough commitment to customer first," "Selection and concentration of businesses," and "Reform of corporate culture and management." The POLA Museum of Art opens at Sengokuhara in Hakone, and the POLA Museum Annex opens in Ginza.
2004	The Fukuroi Factory receives the Prime Minister's Award, recognizing it as an Outstanding Green Plant.
2005	POLA THE BEAUTY premium esthetic salons are launched. ORBIS acquires the Privacy Mark, certifying the proper handling of personal information.
2006	POLA ORBIS HOLDINGS INC. is established and the Group transitions to a pure holding company system. P.O. REAL ESTATE INC. is established and carries on the real estate business. The Group becomes a major investor in the FUTURE LABO group, and the TV mail-order sales business is launched.
2007	POLA Cosmetics, INC. is renamed to POLA INC. The pharmaceutical company POLA PHARMA INC. is established. ORLANE JAPON INC. is established through a joint venture with Orlane S.A. of France. decencia INC. is established.
2008	ACRO INC. is established. POLA CHEMICAL wins the highest award at the 25th IFSCC Congress held in Barcelona, Spain.
2010	POLA ORBIS HOLDINGS INC. is listed on the Tokyo Stock Exchange First Section.
2011	The Group acquires all outstanding shares in H2O PLUS HOLDINGS INC. P.O. MEDIA SERVICE INC. is sold to an outside party.
2012	The Group acquires all outstanding shares in Jurlique International Pty Ltd. POLA CHEMICAL wins the Poster Award at the 27th IFSCC Congress held in Johannesburg, South Africa.

Corporate Information *(As of December 31, 2012)*

Company name	POLA ORBIS HOLDINGS INC.
Foundation	September 29, 2006
Capital	¥10 billion
Number of employees	4,490 (for the Group); 76 (for the Company) Full-time employees (Excluding those on loan to other companies, including those on loan from other companies)
Fiscal year-end	December 31
General meeting of shareholders	March
Business description	Business management of the entire Group
Head office	2-2-3 Nishigotanda, Shinagawa-ku, Tokyo 141-0031, Japan (Business activities conducted at 1-7-7 Ginza, Chuo-ku, Tokyo)
Stock listing	Tokyo Stock Exchange, First Section
TSE code	4927
Share register	1-4-5 Marunouchi, Chiyoda-ku, Tokyo Mitsubishi UFJ Trust and Banking Corporation

Major Group companies (As of March 31, 2013)

Beauty Care business

- POLA INC.
- ORBIS Inc.
- POLA CHEMICAL INDUSTRIES INC.
- Jurlique International Pty Ltd
- H2O PLUS HOLDINGS INC.
- pdc INC.
- FUTURE LABO INC.
- MEDI LABO INC.
- ORLANE JAPON INC.
- decencia INC.
- ACRO INC.

Real Estate business

- P.O. REAL ESTATE INC.

Other businesses

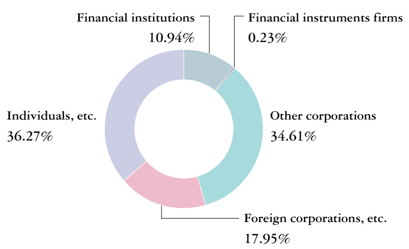
- POLA PHARMA INC.
- KAYAKU CO., LTD.
- P.O. TECHNO SERVICE INC.

Stock Information *(As of December 31, 2012)*

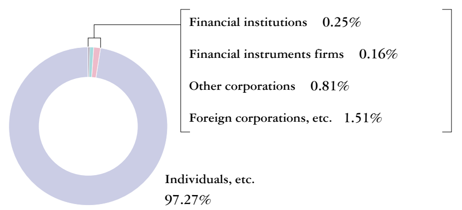
Total number of authorized shares	200,000,000 shares
Total number of issued shares	57,284,039 shares
Number of shareholders	12,560

Composition of shareholders

By number of shares



By number of shareholders



Principal shareholders

Shareholders	Number of shares held (Thousands)	Percentage of shareholding (%)
The Pola Art Foundation	19,654	35.6
Satoshi Suzuki	12,758	23.1
Japan Trustee Services Bank, Ltd. (Trust Account)	2,069	3.7
The Bank of New York Treaty JASDEC Account	1,287	2.3
The Master Trust Bank of Japan, Ltd. (Trust Account)	1,272	2.3
Naoko Nakamura	1,192	2.2
The Chase Manhattan Bank, N.A. London S.L. Omnibus Account	1,094	2.0
POLA ORBIS HOLDINGS Employees' Stockholding	1,010	1.8
Goldman Sachs International	868	1.6
Northern Trust Co AVFC Re Northern Trust Guernsey. Irish Clients.	553	1.0

Notes: 1. The number of shares is rounded down to the nearest thousand shares.
2. In addition to the above, the Company holds 2,000 thousand shares of treasury stock.
3. The percentage of shareholding is calculated by deducting shares of treasury stock.

POLA ORBIS HOLDINGS INC.

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