

April 11, 2007

Sector: Apparel, Accessories & Luxury Goods

Company Research Report



**Polo Ralph Lauren Corp.**

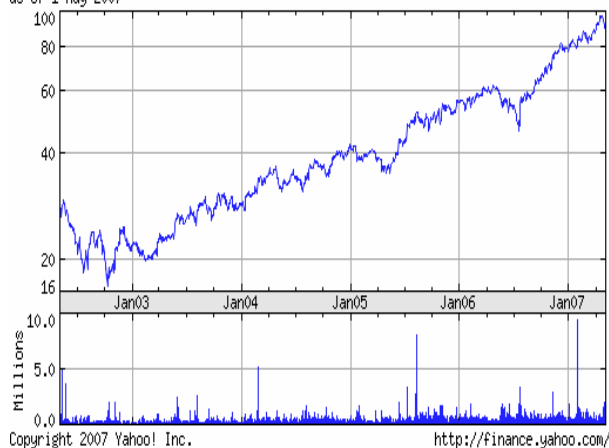
Timothy R. Carter  
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Index: S&P 500  
52-Wk Range: \$45.65 - 93.21

Actual Price:  
\$92.80 (as of: 4/11/07)

Target Price:  
\$86.05 (as of: 3/31/08)

POLO RALPH LAUREN CORP  
as of 1-May-2007



EPS

| Year | 2002   | 2003   | 2004   | 2005   | 2006   | 2007E  |
|------|--------|--------|--------|--------|--------|--------|
| EPS  | \$1.75 | \$1.76 | \$1.69 | \$1.83 | \$2.87 | \$3.73 |

Highlights

- For the five years ended FY 2006, RL had an average revenue growth rate of 11%; and a compounded annual growth rate (CAGR) of 8%.
- Co. acquired 3 businesses that it previously licensed, namely Polo Jeans, RL Footwear, and RL Children's wear.
- Co. recognized income from acquisitions, and allocated 75% of related costs to goodwill & intangibles.
- Independent auditor's report discloses material internal control and financial reporting weaknesses.

Key Statistics

|                         |                 |
|-------------------------|-----------------|
| 52-Week Price Range     | \$45.65 - 93.21 |
| Market Capitalization   | \$9.4B          |
| Shares Outstanding      | 105M            |
| Insider Ownership       | 0.42%           |
| Institutional Ownership | 89.50%          |
| Beta                    | 1.86            |
| P/E Ratio (ttm)         | \$24.98         |
| Price/Book (mrq)        | \$4.08          |
| Price/Sales (ttm)       | \$2.21          |
| Debt/Equity (mrq)       | 22              |
| ROA (ttm)               | 13.59%          |
| ROE (ttm)               | 18.22%          |
| Dividend Payout Ratio   | 6.00%           |

TTM - Trailing 12 Months

MRQ - Most Recent Quarter

## Company Profile and Analysis

Polo Ralph Lauren Corp. (RL) is a global retail Co. engaged in the design, marketing, and distribution of premium lifestyle products. The Co. is structured around three market segments, namely wholesale, licensing, and retail including polo.com. Some of its most recognizable brand names include Polo, Purple Label, Black Label, Chaps, RLX, Club Monaco and, Rugby, the latest sartorial concept.

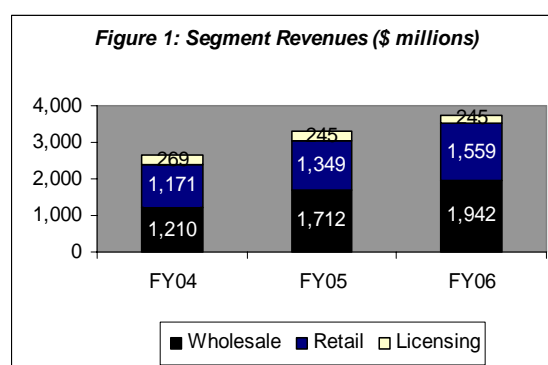
### Existing Global Operations and Expansion Pipeline

Ralph Lauren has existing operations in the United States, Europe, Japan, Australia, Pacific Rim/Korea, Canada, and South America. Expansion retail projects in Russia, Asia, Europe, and strategic locations throughout the U.S. are slated for 2007. In addition, RL plans to “grow” the new Rugby brand, a preppy, urban-oriented fashion concept. The Co. opened five Rugby retail stores in the U.S. in 2006 and plans to open an additional 50 stores within three years. Consistent with the Co. strategic growth plan, management has ploughed-back (and forward) greater than \$1 billion into the organization over the last five years to regain control over its licensed brands and to upgrade its infrastructure. The investment is intended to boost profits and reduce costs - via elevated product design (i.e., higher price points) and upgraded business intelligence capabilities.

### Market Segments

Ralph Lauren operates in three integrated business segments worldwide: wholesale, retail, and licensing. With multiple product lines, ranging from clothing and footwear to home furnishings and accessories, RL has a robust wholesale distribution operation,

servicing multiple, specialty and chain retail stores, including Ralph Lauren and polo.com. As of fiscal 2006, wholesale revenues of \$1.9 billion are the greatest, followed by retail sales of \$1.5 billion, and licensing sales of \$245 million. RL’s wholesale and retail operations produced double-digit sales growth between 2004 and 2006, resulting from acquisition and organic growth activities. Licensing revenues for the same period were slightly lower and flat, due to vendor license acquisitions and the resulting lost royalty payments.



### Competitive Landscape

RL has a market cap of \$9.4 billion, positioning the Co. as a top tier leader in the specialty retail space. RL’s top 3

| <i>Table 1:</i><br>As of April, 2007 | Ralph Lauren | Liz Claiborne | Jones Apparel | V.F. Corp |
|--------------------------------------|--------------|---------------|---------------|-----------|
| Market Cap (Mil)                     | \$9,440      | \$4,531       | \$3,496       | \$9,657   |
| 12-Mo. EPS                           | 2.87         | 2.46          | -1.32         | 4.72      |
| P/E Ratio                            | 26           | 18            | NM            | 18        |
| 1-Yr Price Change (%)                | 52%          | 9%            | -9%           | 50%       |
| ROE (%)                              | 16.50%       | 12.30%        | NM            | 17.60%    |
| NM- Not Material                     |              |               |               |           |

competitors include Jones of New York, Liz Claiborne, and V.F. Corp. An aggressive organic and acquisition growth strategy separates the Co. from its competition. RL acquired three major operations between

2004 and 2006 that were previously licensed by the Co.; partnered with Kohl's to distribute Chaps brand clothing exclusively to over 700 retail stores; opened six stores in 2006; and 11 international and domestic store openings are slated for 2007.

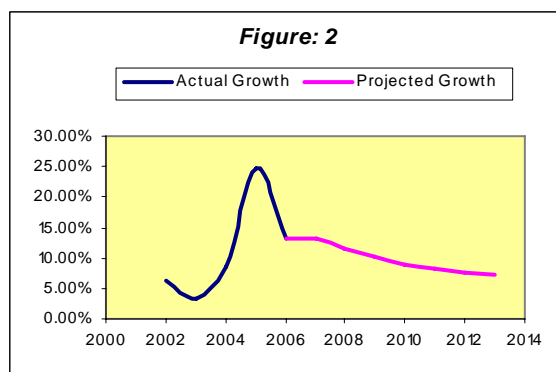
### Recent Acquisitions

On February 3, 2006, Ralph Lauren Co. acquired from Jones Apparel Group the "Polo Jean Business." RL paid \$260 million in cash for Polo Jeans, including \$5 million in transactions costs. On July 15, 2005, Ralph Lauren Co. acquired from Reebok International Ltd., all outstanding shares of Ralph Lauren Footwear Co. The Co. paid Reebok \$112 million in cash, including \$2 million in transactions costs, to regain control of its global "Footwear Business." On July 2, 2004, Ralph Lauren Co. acquired RL Children's Wear Co., LLC. The acquisition cost was \$264 million in cash, including transaction costs. Pursuant to the deal, RL regains exclusive control of its license to design, manufacture, and sell its children's wear clothing line.

### Financial Trends

Net revenues for fiscal 2006 were \$3,746 million, an increase of \$441 million, compared with \$3,305 million for fiscal 2005. The increase primarily reflects the acquisition of Polo Jeans, RL Footwear, and RL Children's Wear. In addition, the Co. successfully launched its Chaps fashion line; opened 11 new stores (to 289); and increased comparable retail store sales by \$73 million, or 6.5%. Cost of good sold (COGS) for fiscal 2006 were \$1,606 million, compared with \$1,519 million for fiscal 2005. *Despite extraordinary revenue growth – as a common size percentage of sales – COGS decreased from 45.9% in 2005 to 42.9% in 2006.* RL reports that the

COGS reduction reflects "sourcing efficiencies" and "reduced markdown activity." In addition to the reasons reported, the COGS decrease more than likely reflects acquisition activity and an asset reserve balance adjustment, which is discussed further herein.



Operating income for fiscal 2006 was \$517 million, an increase of \$217 million, compared with \$300 million for fiscal 2005. The increase is primarily the result of increased sales volume, greater contribution margins, lower COGS, and the absence of the \$100 million "Jones-Related Litigation" charge – recognized (not settled) in fiscal 2005. Earnings per common share (EPS) for fiscal 2006 were \$2.87, an increase of \$1.04, compared with \$1.83 for fiscal 2005. EPS growth largely results from higher net income associated with operating results and the absence the "Jones-Related Litigation" charge.

### Financial Exposure (Threats)

With regard to Sarbanes-Oxley (SOX) Section 404 compliance, Ralph Lauren Co. - with Deloitte & Touche - detected material internal control and financial reporting weaknesses as of fiscal year end 2006. The audit firm, Deloitte & Touche, reported that RL did not have the required operational controls and procedures to prevent and

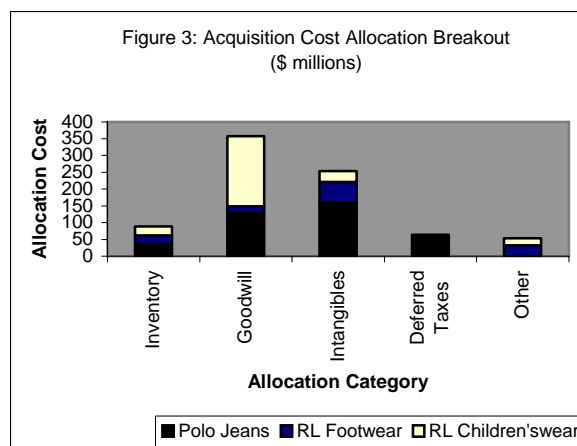
detect errors related to “tax accounting and disclosures.” Deloitte’s report concluded that RL’s material weaknesses were largely related to inadequate tax resources over an extended period, lack of training for tax personnel, and inadequate documentation related to the timely review of income tax accounts.

The most compelling caution sign surrounding RL’s financial statements – related to Deloitte’s audit report – is its acquisition activity between 2004 and 2006. Although the report does not charge RL of egregious financial reporting, it does raise serious concern over the accuracy of Co. financial statements during the same period. Between 2002 and 2006, Co. sales revenue and operating profit grew 58.5% and 67%, respectively. The bulk of the growth took place in 2004, 2005, and 2006; the growth rate in each of these years was 8.6%, 24.8%, and 13.3%, respectively.

That RL’s three-year extraordinary growth is more the result of acquisitions than organic growth is evidenced by several publicly reported events: the results of operations of its three acquisitions (i.e., Polo Jeans, RL Footwear, and RL Children’s Wear) is recognized as income, yet none of the acquisition costs are charged against income; the bulk of the acquisition costs are applied to goodwill & intangibles, excluding inventory; relative to sales COGS decreases; and relative to sales SG&A decreases. *Figure 3* illustrates the cost allocation of RL’s three acquisitions between 2004 and 2006. Total acquisition costs were approximately \$816 million, of which \$610 million (or 75%) was allocated to goodwill & intangibles; 44% allocated to goodwill; and 31% allocated to intangibles.

According to Howard Schilit, president of the Center for Financial Research and

Analysis (CFRA), “the new amortization rules [i.e., FAS 142] are likely to lead to new accounting tricks that attempt to allocate much of the acquisition price to goodwill. And, of course the plan will be not to amortize any of it, but rather to claim that no impairment has taken place. This trick will allow companies to keep most of the acquisitions on the balance sheet, rather than charging those costs against income.” To that end, in its 2006 independent audit report, Deloitte & Touche indicate that based on RL’s annual impairment testing between 2004 and 2006, impairment charges were deemed unnecessary. Moreover, as of fiscal end 2006, the Co. had \$251 million of finite-lived intangible assets on its balance sheet, which can be amortized up to 25 years! RL plans to amortize \$61 million as of fiscal year end 2011 and \$188 million thereafter. Clearly, in the short-term, RL has benefited disproportionately from its recent acquisition activity.



The Co. recognized a pending litigation charge – resulting in the perception of extraordinary revenue growth – when it shifted a future period special charge to a current period. In connection with the “Jones-Related Litigation,” RL recognized \$100 million on its statement of operations in 2005, however, remitted payment to Jones

Apparel Group in 2006—simultaneous with its acquisition of Polo Jeans from Jones.

The litigation commitment in 2005 was consistent with GAAP, yet remarkably timely. Recent acquisitions boosted Co. sales growth from 9.6% in 2004 to 24.8% in 2005. Consequently, by reporting the \$100 million charge in 2005, coupled with its stellar growth the same year, RL still recognized a 9.5% operating profit. Despite the remittance to Jones in 2006, the absence of the litigation charge from RL's 2006 income statement, coupled with its recent acquisitions, boosted operating profit, net income, and the stock price; between fiscal 2005 and 2006, operating profit and net income increased 72.4% and 61.8%, respectively; the stock price increased from \$38.80 to \$60.61 by fiscal year end 2006. On April 3, 2007, the stock price hit \$90.00.

## Corporate Governance

### *Recently Issued Accounting Standards*

The Federal Accounting Standards Board (FASB) in December 2004 issued FAS 123R, which addresses the method of accounting for stock-based compensation. FAS 123R is paramount to FAS123, which permitted companies applying APB 25 to disclose in their financial statements only the pro forma effect of stock-based compensation. Pursuant to FAS 123R, RL will have to treat all stock-based compensation as an expense, and recognize the fair value as of the grant date in its statement of operations.

RL will adopt FAS 123R effective fiscal 2007 (i.e., April 1, 2007), however. The new accounting standard will be applied “[to]...awards granted, modified, and settled by the Co. beginning on April 2, 2006,”

according to Deloitte's 2006 independent audit report. FAS 123R is expected to significantly impact future Co. income and earnings per share. As of April 1, 2006, RL had 8.2m stock options outstanding with a weighted average exercise price of \$28.69.

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# Appendix

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## 1 Industry Outlook

The outlook for the apparel, accessories & luxury goods market is positive. Retail sales grew by 5% in 2006. As of March 16, 2007, the S&P apparel, accessories & luxury goods index increased 5.1%, compared with previous year sales growth. Industry analysts report that recent growth is attributable to a trend toward career wear and dressy attire for men and women, particularly men. Consumers are split between either low-end or high-end luxury brands. At the high end, sales continue to grow, bolstered by a fashion conscious consumer with higher than average disposable income.

The long-term outlook in the mature apparel industry will remain highly competitive, resulting in deflationary pricing pressure. Accordingly, companies will continue to explore strategic growth options through sourcing efficiencies, merger & acquisition activity, broad product offerings, and licensing deals.

## 2 Corporate Valuation

### 2.1 DCF Model

Based on qualitative research and valuation analysis, RL's current stock price is overvalued—primarily the result of acquisition related top-line growth. For fiscal end 2007, Co. operating costs are expected to increase to better align with post-acquisition revenue growth. The 12-month target price for RL is \$86.05. The discounted cash flow (DCF) model assumes a starting growth rate of 13.3%, fading to 7% by 2013. Thereafter, the continuing value (CV) growth rate is 7%, assuming annual

GDP growth of 2-3%; price inflation of 2%; and organic growth of 2-3%. The estimated weighted average cost of capital (WACC) is 9.62%. The WACC reflects a debt-to-equity capital structure of 18:82 and a 1.2 beta. Sensitivity tables herein reflect the primary drivers of the target price, namely WACC, growth rate (g), and return on invested capital (ROIC). Moderate changes to the primary valuation drivers do not provide a compelling reason to adjust the 12-month target price.

## Pro Forma Financial Statements

### POLO RALPH LAUREN CORP

In Millions U.S. \$

#### Income Statement

|   | Actual        |               |               |               |               | Projected     |               |               |               |               |               |               |               |  | CV <sup>∞</sup> |
|---|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|---------------|--|-----------------|
|   | 03/31/02      | 03/31/03      | 03/31/04      | 03/31/05      | 03/31/06      | 3/31/07E      | 3/31/08E      | 3/31/09E      | 3/31/2010E    | 3/31/2011E    | 3/31/2012E    | 3/31/2013E    | 3/31/2014E    |  |                 |
| Sales                                     | \$ 2,364      | \$ 2,439      | \$ 2,650      | \$ 3,305      | \$ 3,746      | \$ 4,246      | \$ 4,733      | \$ 5,210      | \$ 5,682      | \$ 6,153      | \$ 6,628      | \$ 7,113      | \$ 7,610      |  |                 |
| Costs of goods sold (COGS)                | 1,133         | 1,153         | 1,241         | 1,519         | 1,606         | 1,820         | 2,029         | 2,233         | 2,436         | 2,638         | 2,841         | 3,049         | 3,263         |  |                 |
| Sales, general and administrative expense | 838           | 817           | 1,050         | 1,385         | 1,497         | 1,696         | 1,891         | 2,081         | 2,270         | 2,458         | 2,648         | 2,842         | 3,040         |  |                 |
| Depreciation                              | 84            | 79            | 86            | 102           | 127           | 144           | 160           | 177           | 193           | 209           | 225           | 241           | 258           |  |                 |
| Operating profit                          | \$ 309        | \$ 391        | \$ 274        | \$ 300        | \$ 517        | \$ 586        | \$ 653        | \$ 718        | \$ 783        | \$ 848        | \$ 914        | \$ 981        | \$ 1,049      |  |                 |
| Interest expense                          | 19            | 14            | 10            | 11            | 13            | 25            | 24            | 27            | 30            | 32            | 35            | 38            | 40            |  |                 |
| Interest income                           | 0             | 0             | 0             | 0             | 0             | 0             | 4             | 8             | 15            | 23            | 32            | 44            | 57            |  |                 |
| Nonoperating income (Expense)             | (14)          | (103)         | 2             | 9             | (1)           | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             |  |                 |
| Earnings before taxes (EBT)               | \$ 276        | \$ 274        | \$ 266        | \$ 298        | \$ 503        | \$ 561        | \$ 632        | \$ 700        | \$ 769        | \$ 839        | \$ 911        | \$ 987        | \$ 1,066      |  |                 |
| Tax expense                               | 103           | 100           | 95            | 107           | 195           | 207           | 233           | 258           | 284           | 310           | 336           | 364           | 393           |  |                 |
| Net income before extraordinary items     | \$ 173        | \$ 174        | \$ 171        | \$ 190        | \$ 308        | \$ 354        | \$ 399        | \$ 442        | \$ 485        | \$ 529        | \$ 575        | \$ 623        | \$ 672        |  |                 |
| After-tax extraordinary income (Expense)  | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             | 0             |  |                 |
| <b>Net income (NI)</b>                    | <b>\$ 173</b> | <b>\$ 174</b> | <b>\$ 171</b> | <b>\$ 190</b> | <b>\$ 308</b> | <b>\$ 354</b> | <b>\$ 399</b> | <b>\$ 442</b> | <b>\$ 485</b> | <b>\$ 529</b> | <b>\$ 575</b> | <b>\$ 623</b> | <b>\$ 672</b> |  |                 |
| Dividends-- preferred                     | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          | \$ 0          |  |                 |
| Dividends-- common                        | \$ 0          | \$ 0          | \$ 15         | \$ 22         | \$ 21         | \$ 24         | \$ 26         | \$ 29         | \$ 32         | \$ 34         | \$ 37         | \$ 39         | \$ 42         |  |                 |
| <b>Additions to RE</b>                    | <b>\$ 173</b> | <b>\$ 174</b> | <b>\$ 156</b> | <b>\$ 169</b> | <b>\$ 287</b> | <b>\$ 330</b> | <b>\$ 373</b> | <b>\$ 413</b> | <b>\$ 453</b> | <b>\$ 495</b> | <b>\$ 538</b> | <b>\$ 583</b> | <b>\$ 630</b> |  |                 |

#### Balance Sheet

##### Assets

|  |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Cash                                   | \$ 245          | \$ 344          | \$ 352          | \$ 351          | \$ 286          | \$ 324          | \$ 361          | \$ 397          | \$ 433          | \$ 469          | \$ 505          | \$ 542          | \$ 580          |
| Inventory                              | 350             | 364             | 373             | 430             | 486             | 550             | 613             | 675             | 736             | 797             | 859             | 922             | 986             |
| Accounts receivable                    | 354             | 376             | 442             | 456             | 484             | 549             | 612             | 673             | 734             | 795             | 857             | 919             | 984             |
| Other short-term operating assets      | 60              | 83              | 120             | 178             | 123             | 140             | 156             | 171             | 187             | 202             | 218             | 234             | 250             |
| Short-term investments                 | 0               | 0               | 0               | 0               | 0               | 100             | 211             | 368             | 568             | 810             | 1,093           | 1,416           | 1,778           |
| <b>Total current assets</b>            | <b>\$ 1,008</b> | <b>\$ 1,166</b> | <b>\$ 1,287</b> | <b>\$ 1,414</b> | <b>\$ 1,379</b> | <b>\$ 1,662</b> | <b>\$ 1,953</b> | <b>\$ 2,285</b> | <b>\$ 2,659</b> | <b>\$ 3,074</b> | <b>\$ 3,532</b> | <b>\$ 4,033</b> | <b>\$ 4,579</b> |
| Net plant, property, & equipment (PPE) | 344             | 355             | 409             | 488             | 549             | 622             | 693             | 763             | 832             | 901             | 971             | 1,042           | 1,115           |
| Other long-term operating assets       | 398             | 470             | 544             | 763             | 1,098           | 1,244           | 1,387           | 1,527           | 1,665           | 1,803           | 1,942           | 2,084           | 2,230           |
| Long-term investments                  | 0               | 48              | 58              | 62              | 64              | 72              | 80              | 88              | 96              | 104             | 113             | 121             | 129             |
| <b>Total assets</b>                    | <b>\$ 1,749</b> | <b>\$ 2,039</b> | <b>\$ 2,298</b> | <b>\$ 2,727</b> | <b>\$ 3,089</b> | <b>\$ 3,601</b> | <b>\$ 4,113</b> | <b>\$ 4,663</b> | <b>\$ 5,252</b> | <b>\$ 5,883</b> | <b>\$ 6,557</b> | <b>\$ 7,280</b> | <b>\$ 8,053</b> |

##### Liabilities and Equity

|   |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |                 |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Accounts payable (AP)                       | \$ 177          | \$ 181          | \$ 189          | \$ 184          | \$ 202          | \$ 229          | \$ 255          | \$ 281          | \$ 307          | \$ 332          | \$ 358          | \$ 384          | \$ 411          |
| Accruals                                    | 172             | 209             | 316             | 438             | 361             | 409             | 456             | 502             | 547             | 593             | 639             | 685             | 733             |
| Other operating current liabilities         | 10              | 9               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               |
| All short-term debt                         | 33              | 101             | 0               | 0               | 280             | 61              | 68              | 74              | 81              | 88              | 95              | 102             | 109             |
| <b>Total current liabilities</b>            | <b>\$ 392</b>   | <b>\$ 500</b>   | <b>\$ 505</b>   | <b>\$ 622</b>   | <b>\$ 844</b>   | <b>\$ 699</b>   | <b>\$ 779</b>   | <b>\$ 858</b>   | <b>\$ 935</b>   | <b>\$ 1,013</b> | <b>\$ 1,091</b> | <b>\$ 1,171</b> | <b>\$ 1,253</b> |
| Long-term debt                              | 285             | 248             | 277             | 293             | 24              | 328             | 365             | 402             | 438             | 475             | 511             | 549             | 587             |
| Deferred taxes                              | 0               | 0               | 66              | 0               | 21              | 24              | 26              | 29              | 32              | 34              | 37              | 39              | 42              |
| Preferred stock                             | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               | 0               |
| Other long-term liabilities                 | 74              | 81              | 34              | 136             | 151             | 171             | 190             | 209             | 228             | 247             | 266             | 286             | 306             |
| <b>Total liabilities</b>                    | <b>\$ 751</b>   | <b>\$ 830</b>   | <b>\$ 882</b>   | <b>\$ 1,051</b> | <b>\$ 1,039</b> | <b>\$ 1,221</b> | <b>\$ 1,361</b> | <b>\$ 1,498</b> | <b>\$ 1,634</b> | <b>\$ 1,769</b> | <b>\$ 1,906</b> | <b>\$ 2,045</b> | <b>\$ 2,188</b> |
| Par plus PIC Less treasury (and other adju) | 217             | 254             | 304             | 396             | 482             | 482             | 482             | 482             | 482             | 482             | 482             | 482             | 482             |
| Retained earnings (RE)                      | 781             | 955             | 1,111           | 1,280           | 1,567           | 1,897           | 2,270           | 2,683           | 3,136           | 3,631           | 4,169           | 4,752           | 5,382           |
| Total common equity                         | \$ 998          | \$ 1,209        | \$ 1,415        | \$ 1,676        | \$ 2,050        | \$ 2,380        | \$ 2,753        | \$ 3,165        | \$ 3,619        | \$ 4,114        | \$ 4,652        | \$ 5,235        | \$ 5,865        |
| <b>Total liabilities and equity</b>         | <b>\$ 1,749</b> | <b>\$ 2,039</b> | <b>\$ 2,298</b> | <b>\$ 2,727</b> | <b>\$ 3,089</b> | <b>\$ 3,601</b> | <b>\$ 4,113</b> | <b>\$ 4,663</b> | <b>\$ 5,252</b> | <b>\$ 5,883</b> | <b>\$ 6,557</b> | <b>\$ 7,280</b> | <b>\$ 8,053</b> |



**POLO RALPH LAUREN CORP**

**Common Size Ratios For Historical Financial Statements**

***Ratios to calculate operating profit***

|                        | Average | Trend | Most Recent | 2006  | 2005  | 2004  | 2003  | 2002  |
|------------------------|---------|-------|-------------|-------|-------|-------|-------|-------|
| Sales growth rate      | 11.2%   | 22.0% | 13.3%       | 13.3% | 24.8% | 8.6%  | 3.2%  | 6.2%  |
| COGS / Sales           | 46.2%   | 42.7% | 42.9%       | 42.9% | 45.9% | 46.8% | 47.3% | 47.9% |
| SGA / Sales            | 38.1%   | 43.3% | 40.0%       | 40.0% | 41.9% | 39.6% | 33.5% | 35.4% |
| Depreciation / Net PPE | 22.3%   | 21.2% | 23.1%       | 23.1% | 20.9% | 21.0% | 22.2% | 24.4% |

***Ratios to calculate operating capital***

|   |       |       |       |       |       |       |       |       |
|---|-------|-------|-------|-------|-------|-------|-------|-------|
| Cash / Sales                            | 11.2% | 8.5%  | 7.6%  | 7.6%  | 10.6% | 13.3% | 14.1% | 10.4% |
| Inventory/ Sales                        | 14.0% | 12.3% | 13.0% | 13.0% | 13.0% | 14.1% | 14.9% | 14.8% |
| Accts. rec. / Sales                     | 14.7% | 13.0% | 12.9% | 12.9% | 13.8% | 16.7% | 15.4% | 15.0% |
| Other short term operating assets/Sales | 3.8%  | 4.9%  | 3.3%  | 3.3%  | 5.4%  | 4.5%  | 3.4%  | 2.5%  |
| Net PPE / Sales                         | 14.8% | 14.9% | 14.6% | 14.6% | 14.8% | 15.4% | 14.6% | 14.5% |
| Other long-term oper. assets / Sales    | 21.8% | 30.4% | 29.3% | 29.3% | 23.1% | 20.5% | 19.3% | 16.8% |
| Accts. pay./ Sales                      | 6.6%  | 4.8%  | 5.4%  | 5.4%  | 5.6%  | 7.1%  | 7.4%  | 7.5%  |
| Accruals / Sales                        | 10.1% | 13.0% | 9.6%  | 9.6%  | 13.3% | 11.9% | 8.6%  | 7.3%  |
| Other current liabilities / Sales       | 0.2%  | -0.2% | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.4%  | 0.4%  |

***Ratios to calculate operating taxes***

|                              |       |       |       |       |       |       |       |       |
|------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|
| Deferred taxes/Net PPE       | 4.0%  | 6.3%  | 3.8%  | 3.8%  | 0.0%  | 16.1% | 0.0%  | 0.0%  |
| Average tax rate (Taxes/EBT) | 36.9% | 37.5% | 38.8% | 38.8% | 36.1% | 35.7% | 36.5% | 37.5% |
| Marginal tax rate            | 36.9% | 37.5% | 38.8% | 38.8% | 36.1% | 35.7% | 36.5% | 37.5% |

***Dividend and debt ratios***

|  |       |       |       |       |       |       |       |       |
|--|-------|-------|-------|-------|-------|-------|-------|-------|
| Dividend policy: growth rate                 | 8.4%  | 19.8% | -4.1% | -4.1% | 46.2% | 0.0%  | 0.0%  | 0.0%  |
| Long-term debt / market value of firm        | 14.1% | 1.9%  | 1.3%  | 1.3%  | 15.4% | 16.4% | 16.3% | 21.1% |
| Preferred stock / market value of firm       | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  |
| Coupon rate on preferred stock               | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  | 0.0%  |
| Perm. Short-term debt / market value of firm | 4.7%  | 10.0% | 14.5% | 14.5% | 0.0%  | 0.0%  | 6.6%  | 2.4%  |

***Ratios to calculate rest of income statement and balance sheet***

|                               |       |      |      |      |      |      |       |       |
|-------------------------------|-------|------|------|------|------|------|-------|-------|
| Nonop. inc. / Sales           | -0.9% | 0.8% | 0.0% | 0.0% | 0.3% | 0.1% | -4.2% | -0.6% |
| Extr. inc. / Sales            | 0.0%  | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0%  | 0.0%  |
| Long-term investments / Sales | 1.5%  | 2.5% | 1.7% | 1.7% | 1.9% | 2.2% | 2.0%  | 0.0%  |
| Other long-term liab. / Sales | 3.2%  | 3.9% | 4.0% | 4.0% | 4.1% | 1.3% | 3.3%  | 3.1%  |

**POLO RALPH LAUREN CORP**

In Millions U.S. \$

| DCF Value Drivers                                      | <=====Actual |              |              |              |              | Projected=====> |              |              |              |              |              |              |              | CV <sup>∞</sup> |
|--|--------------|--------------|--------------|--------------|--------------|-----------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|-----------------|
|  | 2002         | 2003         | 2004         | 2005         | 2006         | 2007E           | 2008E        | 2009E        | 2010E        | 2011E        | 2012E        | 2013E        | 2014E        |                 |
| <b>Free Cash Flow</b>                                  |              |              |              |              |              |                 |              |              |              |              |              |              |              |                 |
| Marginal tax rate                                      | 37%          | 37%          | 36%          | 36%          | 39%          | 37%             | 37%          | 37%          | 37%          | 37%          | 37%          | 37%          | 37%          |                 |
| Reported income tax expense                            | 103          | 100          | 95           | 107          | 195          | 207             | 233          | 258          | 284          | 310          | 336          | 364          | 393          |                 |
| Taxes reported but not paid                            | <u>0</u>     | <u>0</u>     | <u>66</u>    | <u>(66)</u>  | <u>21</u>    | <u>3</u>        | <u>3</u>     | <u>3</u>     | <u>3</u>     | <u>3</u>     | <u>3</u>     | <u>3</u>     | <u>3</u>     |                 |
| Actual taxes paid                                      | 103          | 100          | 29           | 173          | 174          | 204             | 231          | 256          | 281          | 307          | 334          | 362          | 391          |                 |
| Plus tax saved due to net interest expenses            | 7            | 5            | 4            | 4            | 5            | 9               | 7            | 7            | 6            | 4            | 1            | (2)          | (6)          |                 |
| Minus tax paid on non-operating income                 | <u>(5)</u>   | <u>(38)</u>  | <u>1</u>     | <u>3</u>     | <u>(0)</u>   | <u>0</u>        | <u>0</u>     | <u>0</u>     | <u>0</u>     | <u>0</u>     | <u>0</u>     | <u>0</u>     | <u>0</u>     |                 |
| Tax on operating income                                | 116          | 143          | 32           | 174          | 179          | 213             | 238          | 263          | 287          | 311          | 335          | 359          | 385          |                 |
| Net operating profit after taxes (NOPAT)               | <u>193</u>   | <u>248</u>   | <u>242</u>   | <u>126</u>   | <u>337</u>   | <u>372</u>      | <u>414</u>   | <u>456</u>   | <u>497</u>   | <u>538</u>   | <u>579</u>   | <u>621</u>   | <u>665</u>   |                 |
| NOPAT adjusted for extraordinary income                | 193          | 248          | 242          | 126          | 337          | 372             | 414          | 456          | 497          | 538          | 579          | 621          | 665          |                 |
| Operating current assets                               | 1,008        | 1,166        | 1,287        | 1,414        | 1,379        | 1,562           | 1,742        | 1,917        | 2,091        | 2,264        | 2,439        | 2,617        | 2,800        |                 |
| Operating current liabilities                          | <u>359</u>   | <u>399</u>   | <u>505</u>   | <u>622</u>   | <u>563</u>   | <u>638</u>      | <u>711</u>   | <u>783</u>   | <u>854</u>   | <u>925</u>   | <u>996</u>   | <u>1,069</u> | <u>1,144</u> |                 |
| Net operating working capital                          | 649          | 767          | 782          | 791          | 815          | 924             | 1,030        | 1,134        | 1,237        | 1,339        | 1,443        | 1,548        | 1,656        |                 |
| Operating long term capital                            | 741          | 825          | 953          | 1,251        | 1,647        | 1,866           | 2,080        | 2,290        | 2,497        | 2,704        | 2,913        | 3,126        | 3,345        |                 |
| Operating capital (adjusted for impaired assets)       | <u>1,391</u> | <u>1,592</u> | <u>1,735</u> | <u>2,042</u> | <u>2,462</u> | <u>2,790</u>    | <u>3,110</u> | <u>3,424</u> | <u>3,734</u> | <u>4,043</u> | <u>4,356</u> | <u>4,674</u> | <u>5,001</u> |                 |
| Investment in operating capital (Current - Prior yr.)  | N/A          | 201          | 143          | 308          | 420          | 328             | 320          | 314          | 310          | 310          | 312          | 318          | 327          |                 |
| <b>Free Cash Flow</b> (including extraordinary income) | N/A          | <u>47</u>    | <u>99</u>    | <u>(182)</u> | <u>(83)</u>  | <u>44</u>       | <u>94</u>    | <u>142</u>   | <u>187</u>   | <u>228</u>   | <u>267</u>   | <u>303</u>   | <u>338</u>   |                 |
| <b>Return on Invested Capital (ROIC)</b>               | N/A          | 17.8%        | 15.2%        | 7.2%         | 16.5%        | 15.1%           | 14.9%        | 14.7%        | 14.5%        | 14.4%        | 14.3%        | 14.3%        | 14.2%        |                 |
| <b>Growth Rates</b>                                    |              |              |              |              |              |                 |              |              |              |              |              |              |              |                 |
| Growth in Sales  | N/A          | 3.2%         | 8.6%         | 24.8%        | 13.3%        | 13.3%           | 11.5%        | 10.1%        | 9.1%         | 8.3%         | 7.7%         | 7.3%         | 7.0%         |                 |
| Growth in NOPAT  | N/A          | 28.4%        | -2.5%        | -48.1%       | 168.4%       | 10.4%           | 11.4%        | 10.0%        | 9.0%         | 8.2%         | 7.7%         | 7.3%         | 7.0%         |                 |
| Growth in Operating Capital                            | N/A          | 14.5%        | 9.0%         | 17.7%        | 20.6%        | 13.3%           | 11.5%        | 10.1%        | 9.1%         | 8.3%         | 7.7%         | 7.3%         | 7.0%         |                 |
| <b>WACC</b>  | 9.62%        | 9.62%        | 9.62%        | 9.62%        | 9.62%        | 9.62%           | 9.62%        | 9.62%        | 9.62%        | 9.62%        | 9.62%        | 9.62%        | 9.62%        |                 |

N/A - Prior year required data not included in analysis.

**POLO RALPH LAUREN CORP**

In Millions U.S. \$

**DCF Valuation Drivers**

|                |        |
|----------------|--------|
| WACC           | 9.62%  |
| CV ROIC        | 14.22% |
| CV Growth Rate | 7.00%  |

Most Recent FY End

03/31/06

| DCF Valuation Model  | CV              |                 |                 |                 |                  |                  |                  |                  |                  |        |
|--|-----------------|-----------------|-----------------|-----------------|------------------|------------------|------------------|------------------|------------------|--------|
|  | 2006            | 2007E           | 2008E           | 2009E           | 2010E            | 2011E            | 2012E            | 2013E            | 2014E            |        |
| Free Cash Flow   |                 | 44              | 94              | 142             | 187              | 228              | 267              | 303              | 338              |        |
| Horizon value  |                 | ●—————▶         |                 |                 |                  |                  |                  |                  |                  | 13,793 |
| Present value of operations  | 7,591           | 8,277           | 8,979           | 9,700           | 10,447           | 11,223           | 12,036           | 12,891           | 13,793           |        |
| Present value of operations adjusted for half-year convention          | 7,948           | 8,666           | 9,401           | 10,156          | 10,937           | 11,751           | 12,602           | 13,496           | 14,441           |        |
| Value of investments   | <u>64</u>       | <u>172</u>      | <u>292</u>      | <u>456</u>      | <u>664</u>       | <u>914</u>       | <u>1,205</u>     | <u>1,537</u>     | <u>1,908</u>     |        |
| Total value of firm  | 8,011           | 8,838           | 9,693           | 10,613          | 11,602           | 12,665           | 13,807           | 15,033           | 16,349           |        |
| Value of all debt, preferred stock, and other nonoperating liabilities | <u>455</u>      | <u>559</u>      | <u>623</u>      | <u>686</u>      | <u>748</u>       | <u>810</u>       | <u>873</u>       | <u>936</u>       | <u>1,002</u>     |        |
| Value of equity  | <u>7,556</u>    | <u>8,279</u>    | <u>9,070</u>    | <u>9,927</u>    | <u>10,854</u>    | <u>11,855</u>    | <u>12,934</u>    | <u>14,097</u>    | <u>15,347</u>    |        |
| Number of shares   | 105             | 105             | 105             | 105             | 105              | 105              | 105              | 105              | 105              |        |
| <b>Estimated Price Per Share, FY End</b>                               | <b>\$ 71.69</b> | <b>\$ 78.55</b> | <b>\$ 86.05</b> | <b>\$ 94.18</b> | <b>\$ 102.98</b> | <b>\$ 112.48</b> | <b>\$ 122.72</b> | <b>\$ 133.74</b> | <b>\$ 145.61</b> |        |

**Value-Based Performance Metrics**

|                                   |       |       |       |       |       |       |       |       |       |
|-----------------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| <i>Economic Value Added (EVA)</i> | 141   | 135   | 146   | 157   | 168   | 179   | 190   | 202   | 215   |
| <i>Market Value Added (MVA)</i>   | 5,486 | 5,876 | 6,291 | 6,732 | 7,204 | 7,707 | 8,246 | 8,822 | 9,440 |

**POLO RALPH LAUREN CORP**

Sensitivity Analysis

| DCF Valuation Drivers |        |
|-----------------------|--------|
| WACC                  | 9.62%  |
| CV ROIC               | 14.22% |
| CV Growth Rate (g)    | 7.00%  |

|   |       | WACC   |        |        |        |        |       |       |       |       |        |        |
|---|-------|--------|--------|--------|--------|--------|-------|-------|-------|-------|--------|--------|
|   |       | 9.15%  | 9.24%  | 9.33%  | 9.43%  | 9.52%  | 9.62% | 9.72% | 9.81% | 9.91% | 10.01% | 10.11% |
| g | 6.66% | 91.98  | 88.54  | 85.31  | 82.26  | 79.39  | 76.68 | 74.14 | 71.73 | 69.44 | 67.27  | 65.20  |
|   | 6.72% | 94.39  | 90.77  | 87.37  | 84.18  | 81.18  | 78.34 | 75.69 | 73.18 | 70.80 | 68.54  | 66.39  |
|   | 6.79% | 96.96  | 93.14  | 89.57  | 86.22  | 83.07  | 80.10 | 77.33 | 74.71 | 72.23 | 69.88  | 67.65  |
|   | 6.86% | 99.71  | 95.68  | 91.91  | 88.38  | 85.07  | 81.96 | 79.06 | 76.33 | 73.74 | 71.29  | 68.97  |
|   | 6.93% | 102.66 | 98.39  | 94.41  | 90.69  | 87.21  | 83.94 | 80.90 | 78.04 | 75.34 | 72.78  | 70.36  |
|   | 7.00% | 105.83 | 101.30 | 97.08  | 93.16  | 89.49  | 86.05 | 82.86 | 79.85 | 77.02 | 74.35  | 71.83  |
|   | 7.07% | 109.22 | 104.40 | 99.93  | 95.77  | 91.89  | 88.27 | 84.91 | 81.76 | 78.80 | 76.00  | 73.37  |
|   | 7.14% | 112.88 | 107.74 | 102.98 | 98.57  | 94.46  | 90.64 | 87.10 | 83.79 | 80.68 | 77.75  | 75.00  |
|   | 7.21% | 116.86 | 111.35 | 106.27 | 101.58 | 97.22  | 93.18 | 89.44 | 85.95 | 82.68 | 79.61  | 76.72  |
|   | 7.28% | 121.17 | 115.26 | 109.83 | 104.82 | 100.19 | 95.90 | 91.94 | 88.26 | 84.81 | 81.58  | 78.55  |
|   | 7.36% | 125.89 | 119.52 | 113.68 | 108.32 | 103.38 | 98.82 | 94.62 | 90.72 | 87.08 | 83.68  | 80.49  |

|      |        | ROIC   |        |        |        |        |        |        |        |        |        |        |
|------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|      |        | 13.53% | 13.66% | 13.80% | 13.94% | 14.08% | 14.22% | 14.37% | 14.51% | 14.65% | 14.80% | 14.95% |
| WACC | 9.15%  | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 | 105.83 |
|      | 9.24%  | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 | 101.30 |
|      | 9.33%  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  | 97.08  |
|      | 9.43%  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  | 93.16  |
|      | 9.52%  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  | 89.49  |
|      | 9.62%  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  | 86.05  |
|      | 9.72%  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  | 82.86  |
|      | 9.81%  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  | 79.85  |
|      | 9.91%  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  | 77.02  |
|      | 10.01% | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  | 74.35  |
|      | 10.11% | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  | 71.83  |

|      |        | g     |       |       |       |       |       |       |       |       |       |       |
|------|--------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
|      |        | 6.66% | 6.72% | 6.79% | 6.86% | 6.93% | 7.00% | 7.07% | 7.14% | 7.21% | 7.28% | 7.36% |
| ROIC | 13.53% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 13.66% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 13.80% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 13.94% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.08% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.22% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.37% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.51% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.65% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.80% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |
|      | 14.95% | 76.68 | 78.34 | 80.10 | 81.96 | 83.94 | 86.05 | 88.27 | 90.64 | 93.18 | 95.90 | 98.82 |

Condensed WACC

**Weighted Average Cost of Capital**

In Millions

WACC =====> 9.62%

WACC as of: 11-Apr-2007

| <b>Market Value of Equity</b> |    |       |        |
|-------------------------------|----|-------|--------|
| Common Shares Outstanding     |    | 105   |        |
| Current Stock Price           | \$ | 92.80 |        |
| Market Capitalization         | \$ | 9,781 | 82.22% |

| <b>Market Value of Preferred Stock</b> |       |
|--|-------|
| Target Preferred Stock                 | 0.00% |

| <b>Market Value of Debt</b> |        |
|-----------------------------|--------|
| Target Short-Term Debt      | 2.78%  |
| Target Long-Term Debt       | 15.00% |

**Rates**

| CAPM                    |        | Comments                     |
|-------------------------|--------|------------------------------|
| Beta                    | 1.2    |                              |
| Risk-Free Rate          | 4.85%  | 10-Year Treasury Bond Yield. |
| Risk Premium            | 5.00%  |                              |
| Cost of Equity          | 10.85% |                              |
| Cost of Preferred       | 0.00%  |                              |
| Bond Rating Spread      | 1.00%  |                              |
| Cost of Long-Term Debt  | 5.9%   |                              |
| Cost of Short-Term Debt | 8.25%  |                              |
| Tax Rate                | 36.91% |                              |

**WACC** 9.62%

Capital Structure

