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SUN SPORTSWEAR ANNUAL REPORT 1994



TO OUR SHAREHOLDERS

Sun Sportswear saw a number of significant changes in 1994. Our Women's and Girls' Division experienced rapid growth, becoming our largest division. New technology was brought on line to diminish the lead time in moving a garment from design to distribution. And the sales results of our Men's and Boys' Division declined.

Such a year of major transition inevitably brought with it a year of mixed results for Sun Sportswear. Our net sales grew 8% to \$113.2 million in 1994. But our earnings declined slightly to \$2.4 million in 1994, from \$2.7 million in 1993, as a result of higher operating costs.

WOMEN'S PRODUCTS LED SALES GROWTH — Our Women's/Girls' Division sales increased by 90% during the past year to \$68 million, accounting for 59% of our sales in 1994. The growth of this division resulted from its strong design and merchandising abilities, and a strong license portfolio. We anticipate continued growth in the Women's/Girls' Division, although at a slower rate than we experienced in 1994.

LICENSED GARMENTS GAIN SIGNIFICANCE — Sales of garments bearing licensed characters and trademarks contributed significantly to sales in 1994. Licensed products accounted for 76% of sales in 1994 versus 56% in 1993. Looney Tunes® (Warner Bros.) was once again our number one license. T-shirts, sweatshirts, baseball shirts and other apparel featuring Looney Tunes® and combination Looney Tunes®/Major League Baseball®, Looney Tunes®/National Football League® and Looney Tunes®/National Hockey League® accounted for 55% of total sales in 1994.

Our licenses with the Walt Disney Company were extremely important from mid-1994 on (especially for our Women's/Girls' Division) and will become even more important in the future. For example, our Lion King® (Disney) license brought in \$13 million in sales in 1994. Other Disney properties such as Aladdin® (Disney) and 101 Dalmatians® (Disney) were also strong contributors.

MEN'S SALES DECLINED — Our Men's and Boys' Division sales declined to \$47 million in 1994 from \$72 million in 1993. Besides a difficult winter retail environment, these sales were impacted by the National Hockey League® and Major League Baseball® strikes.

Further compounding Men's/Boys' sales difficulties was the loss of some long-time managers in this division and our International Purchasing Division in early 1994. We see this as an inevitable progression that affected our company's perfor-

mance in the short run — but will make us a stronger company in the future.

We believe we have now assembled a strong Men's/Boys' sales, design and merchandising team, headed by Senior Vice President Ken Schrang, that can rebuild this business. Ken is a strong leader and excellent sales manager. In addition, we have strengthened our Merchandise Manager and Designer positions. Realistically, we expect our new team to stabilize and begin growing the division by 1996.

OPERATING COSTS GREW — Operating costs increased to \$18.2 million in 1994 from \$15.9 million in 1993. Several factors impacted these costs, including: the downturn in Men's division sales; increased customer requirements for distribution services; and "learning-curve" costs associated with our new manufacturing information system (MIS).

To reverse this increase in operating costs — and to improve margins — we have made further investments in technology and are in the process of re-engineering our operations.

INVESTMENT IN TECHNOLOGY — Beginning in late 1993 and continuing to the present, Sun embraced a capital investment program to give us technological advantages. In 1995 these investments should start to lower operating costs and improve margins. For example, as of the first quarter of 1995, our new management information system was up and running. The system presently gives us better control of our inventory and later this year will help improve our manufacturing efficiencies.

In 1994 we began converting our entire art department to one that utilizes computer-aided design (CAD) equipment for the majority of our production. The conversion has reduced our art design costs, allowing us to dramatically increase the number of designs our artists can create. Currently, the CAD process is used to generate 95% of our art.

In addition, during first quarter 1995 we purchased a new 14-color press with a quick set-up capability. We now have 15 state-of-the-art screen printing presses with the capability of producing more than 100,000 units each day.

RE-ENGINEERING EFFORTS UNDERWAY — Re-engineering efforts are also being focused on streamlining the company's sourcing, printing and distribution operations. During 1995, we will be re-engineering our entire operating process. For example, by partnering with "world-class" garment suppliers, we believe we can process orders more quickly for customers

and purchase garments more economically. To assist in these efforts, we have hired re-engineering and sourcing experts. While there will be short-term costs incurred with these consultants, overall we expect to see cost savings and improved customer responsiveness from these efforts beginning in late 1995.

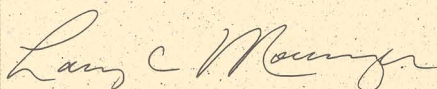
POSITIONED FOR THE FUTURE — Sun Sportswear believes the actions we are undertaking — complemented by our strong management team — will provide a sound foundation for our future.

Our investments in technology and our re-engineering efforts should help improve our gross margins and lower our operating costs later in 1995. Our Women's/Girls' Division is strong, as is our license portfolio. We have just added Pocahontas (© Disney) as a licensee. "Pocahontas" (© Disney) will be Disney's 1995 blockbuster summer movie and is expected to be a big revenue producer in the second, third and fourth quarters. We have also added Winnie the Pooh (© Disney) as a classic licensed property.

Further opportunity is foreseen in underdeveloped sales potential with national and regional retailers such as Sears, J.C. Penney, Mervyn's, Kohls and Fred Meyer. To expand our business with these retailers, we have added a Women's/Girls' Sales Specialist and Men's/Boys' Sales Specialist, each of whom will work directly with these retailers to identify and satisfy their needs.

The past year was one of accomplishment in the face of a difficult retail environment and internal changes. Our initial forecasts indicate 1995 will start out slowly. Nevertheless, we are excited about our future and are confident our leadership and resources we have assembled will produce gains later in 1995, and beyond.

Sincerely,



Larry C. Mounger
Chairman, President and
Chief Executive Officer
Sun Sportswear, Inc.





SERVING THE MASS-MERCHANT MARKET

Sun Sportswear serves the mass-merchandise retail market as one of the world's largest designers and manufacturers of imported casual sportswear for adults and children. Selling apparel to this huge marketplace requires quality products at low prices, sufficient capacity to quickly produce large quantities, and outstanding customer service that adds value to products — all Sun Sportswear's strengths.

During 1994, 88% of Sun's sales were to three of the nation's largest mass merchandisers — Target, Wal-Mart and Kmart — with the balance spread over another 27 customers such as Montgomery Ward, Hills Department Stores, Caldor, Bradlees and Sears.

Within this customer base, Sun Sportswear provides product in two major divisions: Women's and Girls', and Men's and Boys'. In 1994, Women's/Girls' accounted for 59% of sales, while Men's/Boys' accounted for 41% of all sales.

The Company's product mix includes T-shirts, tank-tops, sweatshirts, shorts, sweatpants, nightshirts and more detailed, fashion-oriented garments, such as button-front baseball jerseys, hooded tops and women's leggings. The vast majority of Sun's products are screen printed.

ANTICIPATING THE DEMANDS OF RETAIL SHOPPERS

Sun Sportswear is recognized for its ability to attract retail shoppers' interests. We accomplish this by offering a well-designed product line and fresh, attractive artwork that sells our screen printed goods.

To keep ahead of changing consumer demands and produce what shoppers want, company personnel monitor television shows, films, music and published media. Further, we stay abreast of available product licenses, hold focus groups and conduct field research on emerging trends, hot colors and unique fabrics. Armed with this information, Sun's large staff of 41 in-house artists produce "licensed" designs — designs that creatively use licensed characters and trade names, and "proprietary" designs — art owned by and unique to Sun Sportswear.

ADAPTING LICENSES TO WINNING PRODUCTS: Apparel bearing licensed designs has broad, growing market appeal, capitalizing on the popularity of characters such as Looney Tunes®, The Lion King (©Disney), Garfield (©Paws Inc), and trade names such as the National Wildlife Federation®. Sun's licensed Looney Tunes products were its biggest hit in 1994. Overall, licensed goods accounted for 76% of all sales in 1994.

The Company is constantly searching for new licensed opportunities and has recently strengthened its portfolio of licenses with the addition of Winnie the Pooh (© Disney); Peanuts®; Disney's 1995 movie, "Pocahontas" (© Disney); and Warner Brothers' 1995 movie, "Batman Forever" (™ and © DC Comics).

In addition, Sun Sportswear's strong reputation for quality artwork and mass-merchant customer satisfaction attract other key licensors as new licensing opportunities become available.

PROPRIETARY DESIGNS GIVE BALANCE: Sun's creative artists constantly produce original proprietary designs. Our strong reputation for these unique designs gives us an edge with our mass merchants. In 1994, proprietary designs accounted for 24% of our overall sales, and we believe they will continue to be an important part of our future business.

Sun has developed several proprietary design "brand names". These include GUTS®, U.S.A. Unique Sportswear Attitude™ and Epic®.

TAILORING SERVICES FOR MASS-MERCHANT NEEDS

Sun Sportswear's success is tied to the satisfaction of its retail mass-merchandise customers. That satisfaction is based on three major ingredients:

- providing quality, low-cost products that sell on the retail floor;
- offering customized apparel and value-added services;
- fulfilling orders in a complete and timely manner.

SELL-THROUGH IS KEY: The retail "sell-through" rate of Sun Sportswear's adult and children's casual sportswear is high. It results from an attractive selection of creative designs, using both licensed and proprietary artwork, and competitive pricing. Being able to move large quantities of inventory quickly for our retail customers — through high retail sell-through — drives our success in the mass-merchandising market.

QUALITY DEMANDS GROWING: There is growing demand for quality in value-priced garments, ranging from minimal garment shrinkage to long-lasting color. Mass-merchandise shoppers want products they can depend on and wear confidently.

To assure our apparel quality, we are developing a select core of "blank" garment vendors — suppliers who have demonstra-

ted their willingness to adhere to our quality requirements. We regularly visit these factories to monitor and test garment quality. In addition, before a screen printing run begins, we conduct extensive testing to determine the printability of our designs on various garment fabrics and colors.

CUSTOMIZING APPAREL: Sun has seen increasing consumer acceptance of "store-branded" merchandise. To that end, Sun works closely with store buyers to develop exclusive art and garment designs for each merchant — often with the customer's label sewn in.

PROVIDING VALUE-ADDED SERVICES: Serving customers is more than supplying quality salable products. It also encompasses pre-shipment assistance that enhances the value of our products to the retailer. Sun Sportswear's in-house professionals are experts at customizing activities that speed the flow of goods from us to the retail sales floor, such as attaching customer sales tags to the finished goods and placing the apparel on hangers and in see-through plastic bags.

MEETING DELIVERY SCHEDULES: Understanding the importance of keeping salable product on the retail floor for its customers, Sun Sportswear works diligently to assure timely delivery. The enormous capacity of our state-of-the-art screen printing facility — 28 million units annually — allows us to screen print large orders with remarkable speed and slash the lead time for custom-order detailing.

In addition, Sun maintains a large stock of blank inventory to quickly fill "at once" orders. We've also developed the ability to electronically receive orders from our retail customers.

KEEPING OUR OPERATIONS EFFECTIVE & EFFICIENT

To help assure our continued ability to anticipate retail shoppers' demands and tailor services for our mass merchants, we constantly seek ways to make our operations more effective and efficient. During 1994 we made significant investments in new production technology. We also take pride in the environmentally sound methods we have always employed in our operations.

COMPUTERS SPEED DESIGN: During 1994 we completed the installation of a computer-aided design (CAD) system that makes the mechanics of the art-design process easier and quicker, while freeing up more "creative" time. Using the new CAD system, the color and look of an initial design can be

altered in just moments. A design now moves to the final stage in a fraction of the previous time. With the new system, artists can create many more designs while decreasing overall production costs.

OPERATIONS ARE ENVIRONMENTALLY SOUND: The safe, environmentally sound operation of our facility is important to us and our customers. We employ non-toxic plastisol and water-based inks for screen printing. Non-toxic citrus-based solvents are used to clean our equipment. We recycle nearly half of our solid waste, and the fresh air supply in our plant is scrubbed every two minutes.



FINANCIAL HIGHLIGHTS

Year Ended December 31
(In thousands, except share amounts)

| | 1994 | 1993 | 1992 |
|-------------------------------------|-----------|-----------|----------|
| Net sales | \$113,213 | \$104,772 | \$70,645 |
| Net income (Loss) | \$2,449 | \$2,737 | (\$517) |
| Net income (Loss per share) | \$0.43 | \$0.49 | (\$0.09) |
| Weighted average shares outstanding | 5,722,121 | 5,611,996 | 5,609,00 |
| Total assets | \$62,384 | \$42,247 | \$40,278 |
| Shareholder's equity | \$29,750 | \$26,820 | \$23,902 |

BOARD OF DIRECTORS AND MANAGEMENT

Larry C. Mounger, Chairman and Director

Chairman, President and
Chief Executive Officer
of Sun Sportswear, Inc.

James H. Williams, Director

Executive Vice President
of Bank of America

Paul R. Rollins, Jr., Director

Senior Vice President
of Seafirst Bank

James A. Walsh, Director

Retired President of Allied Stores

Robert A. Pene, Director

Principal in Wiley, Pene and Company

L. Kaye Counts, Director

Executive Vice President and
Chief Operating Officer
of Sun Sportswear, Inc.

Sandra L. Teufel

Senior Vice President
Women's and Girls' Division
of Sun Sportswear, Inc.

Kenneth R. Schrang

Senior Vice President
Men's and Boys' Division
of Sun Sportswear, Inc.

Kevin C. James

Senior Vice President and
Chief Financial Officer
of Sun Sportswear, Inc.

SHAREHOLDER INFORMATION

FORM 10-K, FORM 10-Q AND ANNUAL REPORTS: Copies of the Company's Form 10-K and Form 10-Q reports as filed with the Securities and Exchange Commission and the Company's Annual Report to Shareholders are available to shareholders (without charge) upon request to:

Mr. Kevin James
Senior Vice President and Chief Financial Officer
Sun Sportswear, Inc.
6520 South 190th Street
Kent, WA 98032

STOCK MARKET INFORMATION: The Company's common stock trades on The Nasdaq Stock Market under the symbol SSPW.

As of March 13, 1995, the number of shareholders of record was approximately 143. The number of beneficial shareholders was approximately 2,000.

INDEPENDENT PUBLIC ACCOUNTANTS

Price Waterhouse LLP
1001 Fourth Avenue Plaza
Suite 4200
Seattle, WA 98154

TRANSFER AGENT AND REGISTRAR

U.S. Stock Transfer Corporation
1745 Gardena Avenue, 2nd Floor
Glendale, CA 91204

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U.S.A. Unique Sportswear Attitude™ is a trademark owned by Sun Sportswear, Inc.

Disney's Pocahontas(® Disney) is a copyrighted property of The Walt Disney Company.

Disney's Pooh(® Disney) is a copyrighted property of The Walt Disney Company.

Snoopy® is a Peanuts character created by Charles M. Schulz. United Features Syndicate Inc. owns the copyright and all proprietary rights to the Peanuts characters.

Bugs Bunny and Tweety are Looney Tunes characters. Looney Tunes are copyrighted characters and trademarks owned by Warner Bros., a Time Warner Entertainment Company, LP.

Garfield(® Paws) is a copyrighted character created by Jim Davis. Paws, Inc. owns the copyright and all proprietary rights to the character Garfield.

Batman Forever is a Warner Brothers movie using the Batman(™ and © DC Comics) character owned by DC Comics.

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