Financial strategy

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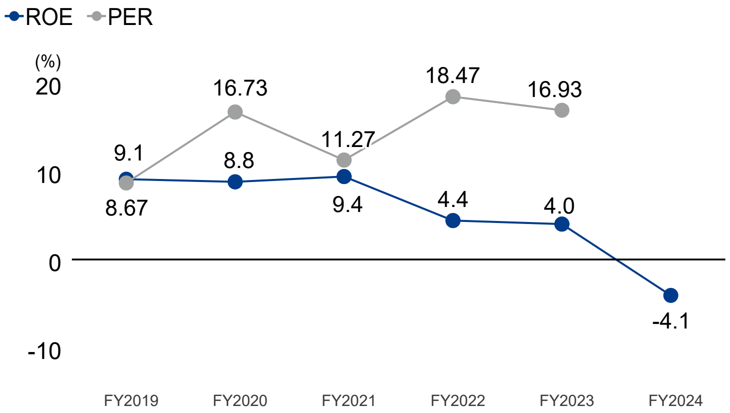
Message from the CFO

Our financial goal for this fiscal year is “revival.” In FY2024, we posted a loss for the first time since FY2001, which triggered significant concern among our stakeholders. We are currently undergoing a portfolio transformation, and as part of this process, we have recorded large special losses for three consecutive years since FY2022. In particular, the main reason for the loss in FY2024 was not only sluggish operating income but also impairment losses on fixed assets in the U.S. chloroprene rubber business. However, through these measures, we believe we have established a certain path toward securing sustainable growth. This fiscal year, our mission is to first return to a growth trajectory—in other words, to achieve a definite “revival.” Within this, I understand that my mission is to strongly promote rigorous business income management and pursuit of capital efficiency, thereby enhancing corporate value.

1. Short-term Strategies for Business Recovery and Portfolio Shift

In FY2024, net sales reached 400.3 billion yen and operating income was 14.4 billion yen, representing only a slight increase from the previous year, and business performance continues to remain sluggish. In addition, we recorded a special loss due to the impairment of fixed assets (about 16.1 billion yen) at DPE (Denka Performance Elastomer LLC), our U.S. chloroprene rubber manufacturing subsidiary, which had a significant impact on our results.
The factors behind the recent business stagnation are: (1) Poor performance in the U.S. chloroprene rubber business, (2) Delayed recovery of forward-looking investments in Electronics & Innovative Products, (3) Stagnant profits in Polymer Solutions, and (4) Increased company-wide cost burden.
Of these, for (1) the U.S. chloroprene rubber business, we began implementing fundamental measures in FY2024. While there is still a possibility of recording related disposal losses for several years to come, we will completely break away from the long-standing situation of continued operating losses. For (2) Electronics & Innovative Products, we have been proactively developing new products and expanding manufacturing capacity to address social issues such as “high-speed communication” and “growing power demand.” We are confident that further advances in generative AI

Return on Equity (ROE), Price Earnings Ratio (PER)



and next-generation high-speed communication will accelerate the recovery of these investments. For (3) Polymer Solutions, we will focus on restructuring the business, including collaboration with other companies and downsizing, while keeping a close eye on the entire value chain in line with the reorganization of ethylene crackers in the petrochemical industry.
First, we will implement measures capable of producing results in a reliable manner within our company, building a business structure that is not affected by market conditions. For (4) cost reduction, we are already running the "Best Practice Project" and will steadily build up each initiative one by one.
We recognize our capital cost as 7–8%, and our weighted average cost of capital (WACC) as 5–6%. Through these strategies, we aim to restore operating income to a record high 40 billion yen and bring ROE back to the capital cost level of 8% as soon as possible after FY2026.

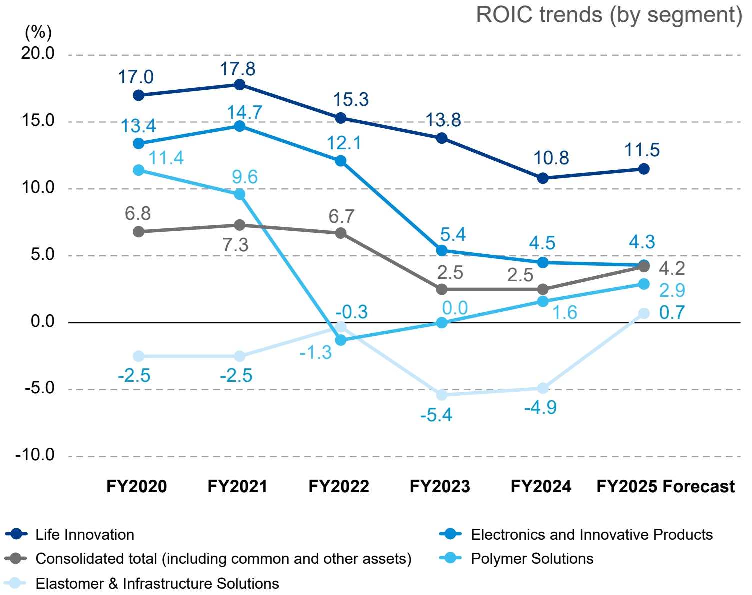
2. Portfolio Transformation and Clarification of Direction for Each Business Segment

In 2021, when we achieved record profits, our core businesses—Elastomer & Infrastructure Solutions and Polymer Solutions—generated steady cash flow despite low growth, while Electronics and Innovative Products and Life Innovation grew rapidly. With "revival" as our main theme, our urgent priority for this fiscal year is to return to this portfolio positioning.
In the future, we believe that our core businesses (Elastomer & Infrastructure Solutions and Polymer Solutions) can also shift to growth areas by leveraging environmental initiatives as growth drivers, and we will consider bold portfolio changes as necessary.

3. Measures for "Revival" (ROIC Improvement)

To quickly bring ROE back to the 8% level, our Company is united in working to improve capital profitability. Internally, we have introduced "ROIC" as a common measure of capital profitability and manage it by segment, individual business, and product using a "ROIC tree."
In investment decision-making, for projects aimed at improving profitability, such as growth investments and productivity enhancement investments, we use both the internal rate of return (IRR) set as a hurdle rate based on capital cost and weighted average cost of capital (WACC), and ROIC to comprehensively evaluate capital profitability before making decisions.
We are working to ensure that the concept of capital profitability becomes common knowledge throughout the Company, with ongoing internal education and other efforts. By raising awareness of capital profitability not only among management but throughout the company, we aim to improve ROIC and ROE and restore PBR to 1.0 as soon as possible.

■ Increase in ROIC together with Increased Operating Income



Financial Leverage

	"Mission 2030" Policy	FY2024 Results
D/E Ratio	0.6~0.8	0.73
Total shareholder return ratio	50%	92%

Utilize interest-bearing debt
Shareholder returns: 8-year average 50%.
Aim to maintain or increase dividends

No Change in Policy

Profitability ↑ × Efficiency ↑

(1) Business portfolio shift
▶ Structural reform of unprofitable businesses, conversion to cash cows
(2) Promotion of business strategies in each division
(3) ROIC management (CCC [inventory control, etc.])
(4) Careful selection of investments

Improvement of ROE, generation of cash

Measures to Achieve Management Conscious of Capital Cost and Stock Price

ROE ↑ > Capital Cost

PBR improvement (Price Book-value Ratio) = Profitability ↑ (Net income ratio) × Efficiency ↑ (Total asset turnover) × Financial Leverage × PER ↑

↑ Cash generation through business operations
- Business portfolio shift
- Enhancement of earning power
- Improvement of income ratio through thorough ROIC management by business
- Cost reduction through best practice utilization, etc.

Financial Strategy
- Maintain current level of financial leverage as a basic principle
- Improvement of total asset turnover through CCC improvement
- Control of cash outflow by carefully selecting investment projects

↑ Improving Future Growth Rates (Strengthening Intangible Assets as Growth Drivers)
- Strengthening R&D roadmap and structure
- IP landscape, patent value KPIs, IPL activities
- Initiatives for New Business Creation
- Process reform
- DX strategy (DX talent development [such as Digital Pilot])
- Human resources value creation (growth opportunities and psychological safety, an organization that takes on challenges, development system, health management, work style reform, DE&I)
- Promotion of GX (create business opportunities from decarbonization.)

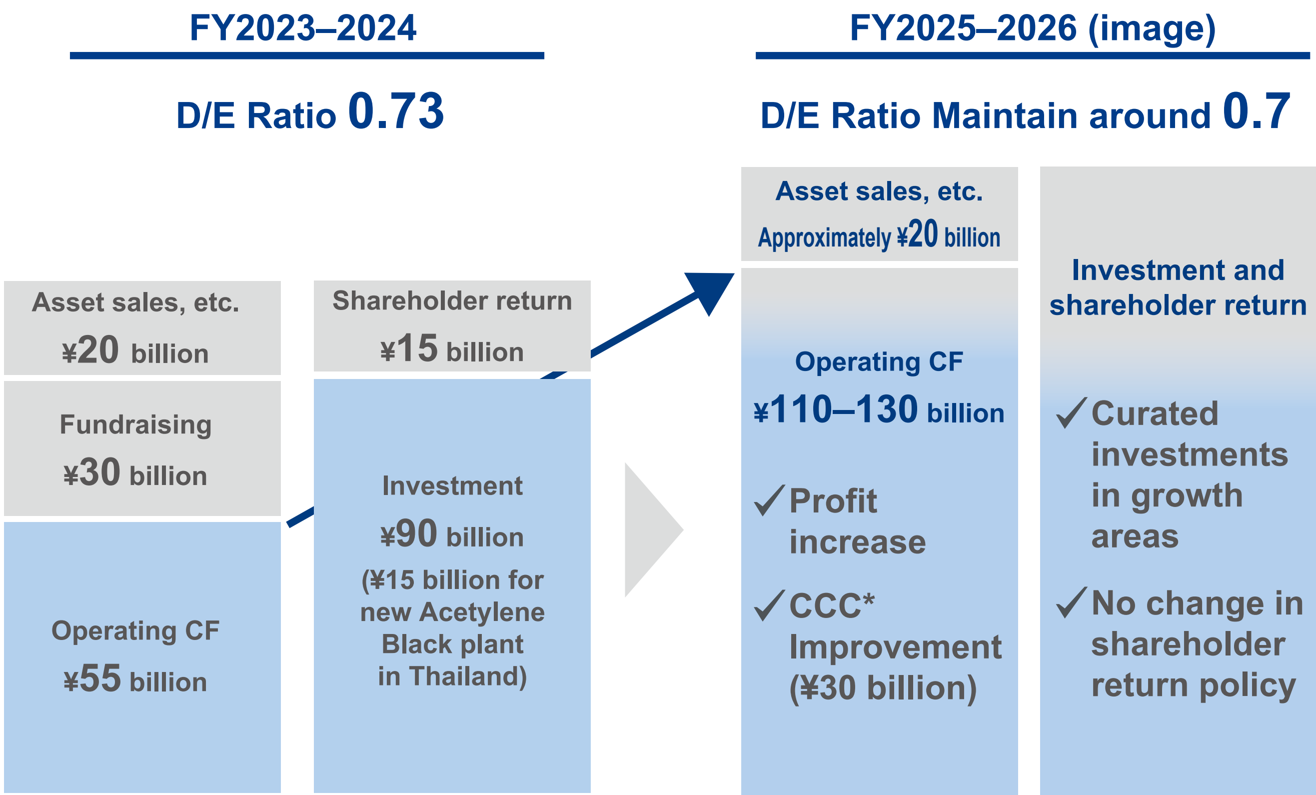
↓ Minimization of Capital Costs (Systems and Structures to Enhance Reliability)
- Promotion of sustainability management
- Safety, quality assurance, supply chain management
- Governance (improving management transparency and reliability)
- Dialogue with shareholders, investors, and stakeholders

4. Dialogue with Capital Markets

We position dialogue with shareholders and investors as a key management initiative, with the aim of reducing capital costs and increasing corporate value in a sustainable manner. We strive to enhance disclosure and engage in two-way communication regarding our business strategy, financial strategy, portfolio review, and efforts to strengthen our management foundation.
Specific items include progress on fundamental measures in the chloroprene rubber business and their impact on performance, clear disclosure of financial strategies including capital allocation, performance recovery measures such as the Best Practice Project, and growth scenarios for new products such as "SNECTON" in Electronics and Innovative Products, thereby enhancing the content of earnings briefing materials. In addition, from FY2025, we have been holding new management briefings to outline the execution status of the management plan separately from financial results announcements.
In addition to these activities, we have established a system to share feedback from shareholders and investors with all directors, all division heads, and relevant departments, with the aim of verifying management execution from the perspective of shareholders and investors and identifying areas for improvement.
By leveraging insights gained through these dialogues in management, we will achieve short-term performance improvements in a steady manner while striving to balance future profitability and social value, and work to enhance corporate value.

5. Capital Allocation

The Management Plan "Mission 2030," launched in FY2023, is centered on a growth strategy of making strategic investments in business areas aligned with megatrends. Accordingly, from the outset, we have been active in utilizing interest-bearing debt and increased financial leverage to make aggressive investments and pave the way for growth in line with the management plan. However, as business performance has lagged behind initial expectations, we have worked to maintain financial discipline by carefully selecting and postponing investments at an early stage last fiscal year.
Shareholder returns are positioned as one of the most important management priorities, and we will continue our policy of "maintaining and increasing dividends per share, aiming for a total shareholder return ratio of 50% over the eight-year management plan."
Since the start of the management plan, we have controlled the D/E ratio at around 0.6 to 0.8 times, and will continue to promote our growth strategy while maintaining financial discipline and striving to enhance corporate value.



* Cash Conversion Cycle

TOPIC [Approach to Capital Investment]

To prioritize and select investments, we are clearly aware of the capital cost when making decisions for equipment investments, and make decisions with the weighted average cost of capital (WACC) in mind. We also adopt the internal rate of return (IRR) and ROIC as an investment criterion for our strategic and growth investment to curate the investment projects.

- **Strategic investment**: Investments that contribute to growth in key areas, Investments that contribute to process reform (production, research, operations), Investments primarily aimed at energy saving and carbon neutrality, etc.
- **Growth investment**: Investments to increase profit, excluding strategic investments

	Strategic investment	Growth investment
IRR15%≦	Investable	Investable
	Determined strategically	In principle, difficult to invest
	In principle, not feasible to invest	

* IRR is set as pre-tax internal rate of return

6. Raising Funds through Sustainable Finance

Denka is also looking to raise funds through ESG and SDGs initiatives. In the last five years (FY2020 to FY2024), approximately 50% of our long-term funds were procured through sustainable finance, which we will continue to actively utilize in the future.

[Examples of Fundraising through Sustainable Finance]

Signed a "Mizuho Positive Impact Finance" Loan Agreement with Mizuho Bank

Mizuho Positive Impact Finance is a loan based on the Principles for Positive Impact Finance, which comprehensively analyzes and evaluates the impact (both positive and negative) of corporate activities on the environment, society, and the economy, and aims to provide ongoing support for such activities. Among our initiatives, themes such as employment, climate, and zero emissions were evaluated both qualitatively and quantitatively.