

Message from the CFO

By strengthening balance sheet management, TOK is fortifying its financial position to sustain value creation in a frank and open-minded culture, while focusing efforts on dialogue with stakeholders.



Yoichi Shibamura *Senior Executive Officer, Department Manager, Accounting and Finance Dept.*

Toward Enhancement of Corporate Value

■ Management Principles and Our Social Value

Since its establishment in 1940 as a fine chemicals manufacturer that develops and supplies high-purity chemicals, TOK has diversified into a broad range of fields, starting from functional materials for black and white TVs to high-performance printing materials, panel materials, and semiconductor microprocessing materials. TOK has seen great success from its long-running endeavor of contributing to society by developing quality products with outstanding technologies (not bulk chemicals) and encouraging thorough debate to this end among employees without regard to their rank or position.

For nearly 80 years, our four management principles have been passed down without changing, i.e., “Continue efforts to enhance our technology,” “Raise the quality levels of our products,” “Contribute to society,” and “Create a frank and open-minded business culture.” These management principles are evident in every aspect of development, manufacturing, and marketing. I believe TOK is a unique company among manufacturers above a certain size around the world, a “permanent venture company” with a culture of having a great time together developing technologies in a frank and open-minded environment in its DNA since its founding. Leveraging this DNA as much as possible, TOK is keen to further improve its social value by meeting expectations with chemicals to help solve climate change and issues in the era of 5G and IoT.

Management Principles

Continue efforts to enhance our technology

Raise the quality levels of our products

Contribute to society

Create a frank and open-minded business culture



Shigemasa Mukai
TOK founder

■ Focusing on Dialogue with Stakeholders while Ensuring a Financial Position that Facilitates Frank and Open-Minded Development

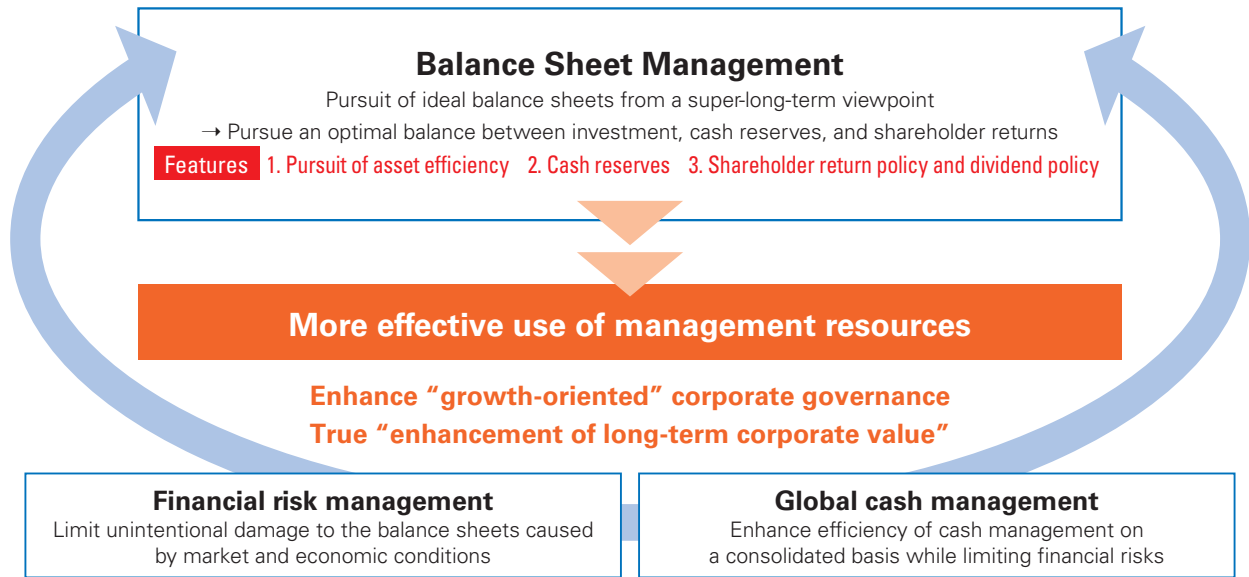
As the officer in charge of finance, I am concentrating my energies on ensuring the Company has a robust financial position that facilitates frank and open-minded development, while elevating our willingness to take on challenges and our venture spirit, with our DNA, as exemplified in our management principles, a driving force behind long-term sustainable growth and a source of social value. While taking the longer view instead of focusing on the short term, we are careful to base our analysis and decisions on an objective and cool-headed viewpoint when assessing investment returns and efficiency.

In my dialogue with shareholders, investors and other stakeholders, I make a concerted effort to convey TOK’s unique traits and strengths as a long-run R&D-driven company and as a company that always strives to be a global niche top company. As we embed various messages in our financial capital strategy, I intend to continue dialogue with stakeholders so they become long-run supporters.

■ Taking a “Growth-Oriented” Approach to Corporate Governance

I focus on “growth-oriented” corporate governance as the CFO in ESG initiatives for sustainable enhancement in corporate value. During the “TOK Medium-Term Plan 2021,” I believe my primary mission is to strengthen the balance sheet management that began during the previous medium-term plan, simultaneously managing financial risks on a worldwide basis while managing cash on a global basis. We are in position to bring about true “enhancement of long-term corporate value” with due consideration paid to our stakeholders, including shareholders, investors, customers, employees, and local communities.

“The trinity” of balance sheet management, financial risk management, and global cash management



Financial Capital Strategy in the Medium-Term Plan

■ Review of the “TOK Medium-Term Plan 2018”

TOK saw two major successes with its financial strategies during the “TOK Medium-Term Plan 2018.”

The first success was changing the end of the fiscal year to December, starting in fiscal 2017. Previously, the TOK Group ended its fiscal year in March, presenting in its consolidated results at the domestic companies including the parent company ending their fiscal years on March 31, and overseas subsidiaries ending their fiscal years on December 31 (with a three-month delay). However, with the overseas sales ratio up to nearly 80%, and in light of the globalization of business and international division of operations over the past few years, management decided to unify the end of the fiscal year to December for both domestic and overseas companies in 2017 to improve transparency in the disclosure of results. This has enhanced our accountability to investors, while also accelerating and fine-tuning consolidated management.

The second success was plotting a path forward for strengthening balance sheet management. Details about this measure were disclosed at the same time as the “TOK Medium-Term Plan 2021.” From the initial stages of the previous medium-term plan, however, TOK has been advancing measures with an eye on the balance sheets and a strong awareness of the capital cost. Specifically, the Company implemented a ¥10 billion share buyback in 2017. Then in the following year, the Company essentially swapped equity for debt as a result of long-term debt financing to raise ¥10 billion for capital investments, taking a major step forward in strengthening balance sheet management.

Over the three years of the previous medium-term plan, TOK stepped up efforts to return value to shareholders, which exceeded the total amount of free cash flow during this period when including share buybacks. Our financial capital strategy in the “TOK Medium-Term Plan 2021” serves as a clarification of management’s stance on strengthening shareholder returns while focusing more on the balance sheets.

■ Background to Major Shift in the Financial Capital Strategy

There are two factors behind our major shift in the financial capital strategy in the “TOK Medium-Term Plan 2021.”

The first factor entails a major turning point for the TOK Group approaching in the business environment. As various innovations are likely to emerge in the electronics industry, its main domain, from the advent of 5G and IoT, TOK is continuing to make swift and bold investments as a “permanent venture company” with the intention of sustaining growth toward its vision of a “100-year company” in 2040. Maintaining distinctive growth over the long run will hinge on our decision that a new financial capital strategy based on balance sheet management with a long-term viewpoint is necessary.

The second factor is major changes on Japan’s capital market, as demonstrated by the creation of two new codes*. Viewing these major trends as an opportunity to change itself, TOK reassessed how it will genuinely work for investors and other stakeholders with a strong awareness of the capital cost. Amid these major changes, management came to better understand the importance of having a new financial capital strategy based on balance sheet management from the standpoint of how to better serve its long-run investors that have been supporting and encouraging TOK, a long-run R&D-driven company.

* The two new codes are Japan’s Stewardship Code in 2014 and the Corporate Governance Code in 2015.

Policies on cash reserves

As a long-run R&D-driven company, TOK will calculate **cash reserves from the standpoint of securing the necessary funds.**

- Develop technologies in anticipation of a super-long time frame
- Continuously tackle challenges over a super-long time frame
- Respond rapidly when the unexpected happens (restoration, rebuilding, etc. from major disasters)

$$\text{Cash reserves} = \text{Working capital} + \text{Investment reserves} + \text{Risk reserves}$$

Financial Capital Strategy in the TOK Medium-Term Plan 2021

In 2019, TOK announced and started its new financial capital strategy, and its intention of pursuing an optimal balance between investments, cash reserves, and shareholder returns. Management is delighted that these new policies have been positively received by our shareholders and investors. We made a significant pivot in strategy with a target of 3.5% for DOE, and many of our shareholders and investors have agreed with this new policy.

However, the reason for this approach to balance sheet management stems from TOK's belief that business growth over the long run is its overriding imperative. Considering the competitive landscape and the Company's position within it lately, management believes a fair amount of cash reserves are necessary for the future. In this regard, I believe we must continue dialogue to clearly explain our policy on cash reserves to shareholders and investors.

As explained earlier, TOK's approach to cash reserves considers that all of our business rivals in cutting-edge fields are multifaceted divisions of large-scale companies. Although we are confident that our technological development capabilities and ability to collaborate closely with customers as a B-to-B

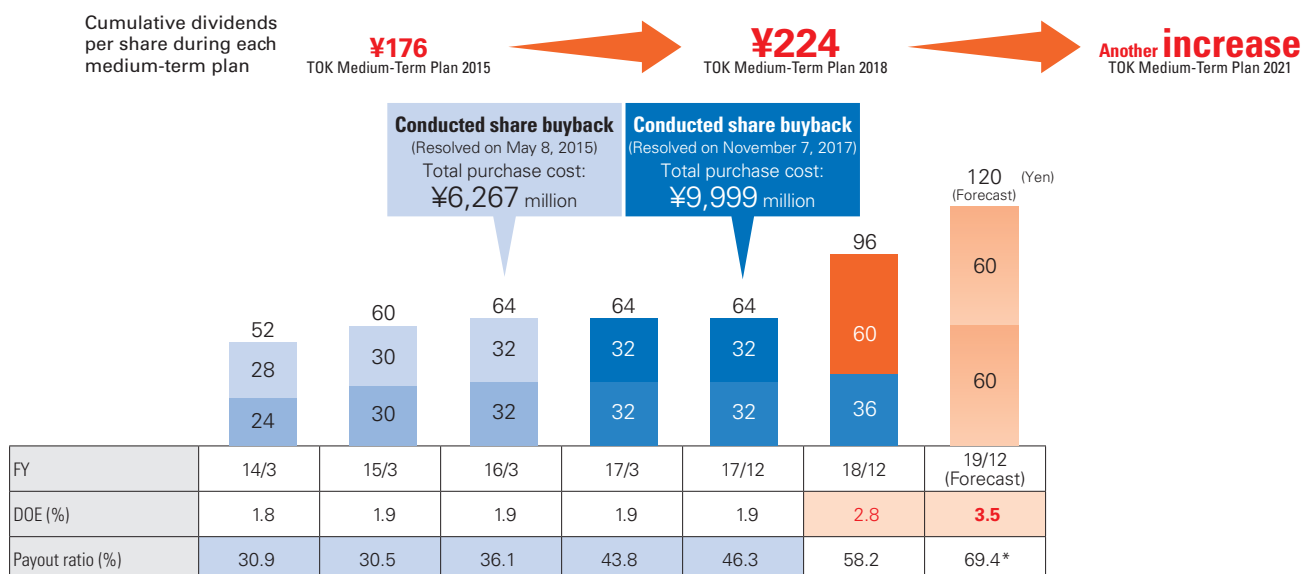
company are better than rivals, we must have a relatively large amount of cash reserves to ensure TOK has the capacity to invest on a par with rivals and keep pace with the competition in terms of development and investments. Management pays due consideration to investment and asset efficiency by gauging and pursuing asset efficiency with ROIC and IRR indicators, and by focusing more efforts on periodic reviews of reasons for cross shareholdings.

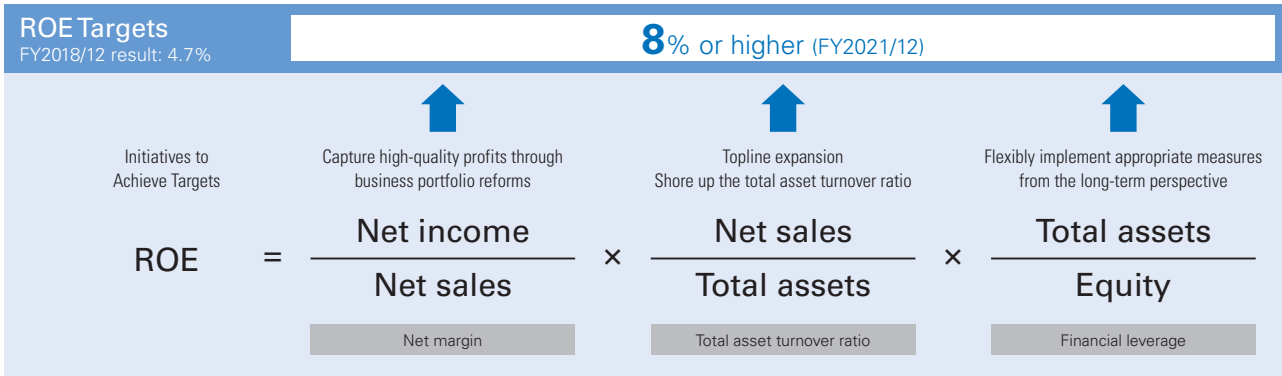
Improving ROE

The Company targets an ROE of 8% or higher by the fiscal year ending December 31, 2021 in the "TOK Medium-Term Plan 2021." To achieve this target, management aims to increase the net margin by generating high-quality profits through a reform of its business portfolio.

For now, the Company will carry on with structural reforms while expanding investment. The three years of the "TOK Medium-Term Plan 2021" are positioned as an interim period for reaping benefits from past initiatives to advance and add higher value to products in the photoresists for semiconductor front-end processes and high-purity chemicals field. TOK aims to increase the net margin to around 10% by the fiscal year

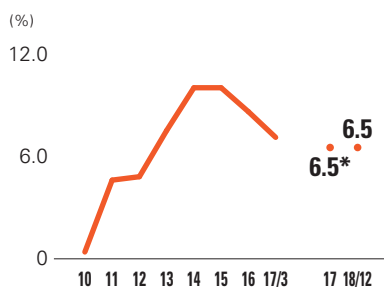
Shareholder returns and dividends per share



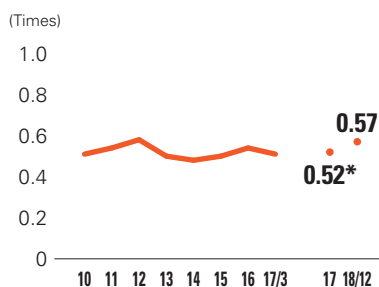


10-year trends of ROE-related indicators and ROE

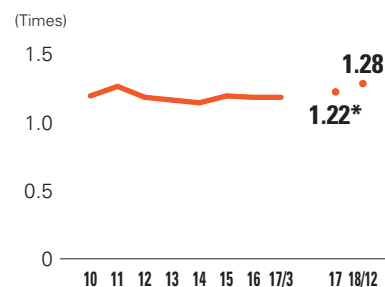
Net margin (%)



Total asset turnover ratio (Times)



Financial leverage (Times)



* The fiscal year ended December 31, 2017 was an irregular nine-month period due to a change in fiscal year-end.

ending December 31, 2021 if earnings stay within its best-case scenario target range. The Company projects the total asset turnover ratio will improve to 0.7 times in its aim to strengthen and instill balance sheet management. As a result of swapping equity for debt during the previous medium-term plan, financial leverage was 1.28 times (equity ratio of 78.0%), and we believe this level can be maintained or increased to a certain degree. With this as a possible scenario, the Company aims to achieve an ROE of 8% or higher by responding in a proper and timely manner to changes in the business environment, investment conditions, and financial situation. Our policy of targeting a DOE of 3.5% is also a moderate measure for the denominator towards ROE growth, and we are also taking flexible measures toward share buybacks and from the standpoint of measure for the denominator.

■ Evolving Global Cash Management

As a part of balance sheet management, TOK is concentrating on evolving global cash management. Overseas operations have expanded thanks to deepening our strategy of building close relationships with customers, and the international division of operations has accelerated between Japan and overseas subsidiaries, and among overseas subsidiaries. Consequently, the flow of money within the Group has become more diverse and complicated on a worldwide basis, necessitating a more thorough approach to cash management to effectively deploy capital throughout the Group.

Of the surplus funds at overseas subsidiaries, the portion excluding cash reserves for investments and necessary working capital is in principle concentrated at the parent company, while a parent-subsidiary finance scheme is also being created

for unexpected situations. We are working to quickly create this scheme because it will also serve as a means of controlling financial risks related to fluctuations in foreign exchange rates and liquidity, in addition to being an effective way to strengthen balance sheet management on a consolidated basis.

■ Strengthening Tax Governance on a Worldwide Basis

In addition to focusing on global cash management, TOK is strengthening tax governance on a worldwide basis. We are creating an appropriate tax governance system with the parent company as a control tower that gathers know-how about taxation on a consolidated basis and for each entity, with the intention of addressing issues in international taxation including problems associated with transfer price taxation and strengthening base erosion and profit shifting (BEPS) measures in advanced countries. As its first step, the TOK Group is researching taxation and tax customs in all regions where it conducts business, while also assessing conditions in product markets, to formulate a transfer price policy. At the same time, TOK aims to improve collaboration among sites with the parent company as a control tower, and qualitatively improve its tax governance systems at domestic and overseas sites.