



TSE Explanatory Material b)

*The Eighth Council of Experts Concerning
the Follow-up of Market Restructuring*

Exchange & beyond
Tokyo Stock Exchange, Inc.

February 15, 2023



- In order to encourage management to be more conscious of cost of capital and stock prices, TSE plans to request the following actions for all listed companies in the Prime and Standard Markets. (notification to be made in the spring of 2023)

Note: Specify in the notice that adequate actions are required especially in cases where PBR is below 1x, except in cases where it is due to temporary effects such as a deterioration in market conditions.

Contents of Request to Encourage Management to be More Conscious of Cost of Capital and Stock Prices (Draft)

Analysis of Current Conditions

- Properly identify the company's cost of capital and capital efficiency (ROE, ROIC, etc.)
- Analyze and evaluate those statuses and market valuation (stock price, market capitalization, PBR, PER, etc.) at the board of directors meetings, etc.

- (Examples of perspectives on analysis and evaluation)
- Whether the company has achieved capital efficiency that exceeds its cost of capital, and if not, the reasons why.
 - Even if the company has achieved capital efficiency that exceeds its cost of capital, if the company's market valuation is not sufficient (e.g., PBR is less than 1x), the reasons why, etc.

Planning & Disclosure

- Consider and develop policies, targets, planning periods, and specific initiatives for improving capital efficiency and market valuation.
- Disclose the details of these initiatives, along with current evaluations, to investors in an easy-to-understand manner.

- Target indicators are set by each company based on its own situation.
- If a company considers that it has already achieved a sufficient level and that there is no need for improvement, it should disclose its evaluation.
- In addition to disclosure using the new format to be provided by TSE, companies can also present their initiatives in the disclosure of management strategies and management plans in accordance with the CG Code Principle 5.2 (in either case, the fact that disclosure is being made should be indicated in the CG Report).

Implementation of Initiatives

- Promote management conscious of cost of capital and stock prices based on the disclosed plan

- Engage in proactive dialogue with investors based on the disclosure

Conduct an analysis of progress and update disclosures every year (at least once a year).

Japan's Corporate Governance Code (Revised June 2021)

Principle 5.2 Establishing and Disclosing Business Strategies and Business Plans

When establishing and disclosing business strategies and business plans, **companies should articulate their earnings plans and capital policies, and present targets for profitability and capital efficiency after accurately identifying the company's cost of capital. Also, companies should provide explanations that are clear and logical to shareholders with respect to the allocation of management resources, such as reviewing their business portfolio and investments in fixed assets, R&D, and human capital, and specific measures that will be taken in order to achieve their plans and targets.**

Supplementary Principle 5.2.1

In formulating and announcing business strategies, etc., companies should clearly present the basic policy regarding the business portfolio decided by the board and the status of the review of such portfolio.

Guidelines for Investor and Company Engagement (Revised June 2021)

1. Management Decisions in Response to Changes in the Business Environment

1.2 Does management accurately identify the company's cost of capital, reflecting risks associated with the business in an appropriate manner? Does management manage the business with a recognition of the company's cost of capital by setting targets on profitability and capital efficiency to generate sustainable growth and increase corporate value over the mid- to long-term? Does management clearly explain why they decided upon such targets? Does the company achieve returns which cover the cost of capital on a mid- to long-term basis?

1.4 Does management understand the business environment and business-related risks appropriately and make decisions decisively, such as restructuring the company's business portfolio, including investment in new businesses with higher growth potential and exit from or sale of existing businesses, based on the company's business strategies and business plans? Is a policy on reviewing a business portfolio clearly established, and is the review process effective?