FY2015 Tokuyama Corporation Investor Meeting (May 12, 2016)
Q&A (Excerpts)

Participants:
Hiroshi Yokota, Representative Director, President and Executive Officer
Akihiro Hamada, Director, Managing Executive Officer, General Manager of Financial Div.

1. Questions regarding the Medium-Term Management Plan and efforts to lay the "Cornerstone for the Group's Revitalization

Q1: The new management plan, as the "Cornerstone for the Group's Revitalization," seems to be a clear departure from the previous Medium-Term Management Plan 2017 announced in July 2015. What is the thought process behind this new management plan?

A1: Sweeping revisions to the management plan became necessary after Tokuyama incurred major impairment losses on two occasions. On reviewing the overall situation, we identified two major problems: 1) new businesses were not taking off, and 2) in existing businesses, the potential of our plants was not being fully realized despite abundant resources, such as inexpensive electricity and port infrastructure at the Tokuyama Factory. Believing our organizational culture was to blame for these problems, we embarked on a sweeping review of the management plan.

Q2: The Medium-Term Management Plan 2017 targeted operating income of ¥34 billion in FY2017, while the "Cornerstone for the Group's Revitalization" targets operating income of ¥36 billion in FY2020, giving the impression that targets have been pushed back. Why?

A2: We realized that the operating result of FY2015 was beyond our reach, owing to relatively favorable conditions in terms of coal prices, domestic naphtha prices and the foreign exchange rate staying above ¥100/$. Under the previous management plan, we took a bottom-up approach to formulating our forecasts without conducting a thorough analysis of conditions. Our new management plan was created with a much better understanding of external conditions and the issues we are facing. Through various reforms, we now aim for operating income of ¥36 billion, a respectable target.

Q3: The management plan projects an improvement of ¥12.2 billion in operating income at Tokuyama Malaysia Sdn. Bhd. Please explain the factors that will drive this improvement.

A3: Tokuyama Malaysia Sdn. Bhd. posted an operating loss of ¥10.2 billion in FY2015. We aim for the company to turn a profit of ¥2 billion in FY2018, an improvement of ¥12.2 billion. This reflects a decrease in depreciation expenses as a result of the recognition of impairment losses.

Q4: Are cash costs on the decline at Tokuyama Malaysia Sdn. Bhd.?

A4: We plan to reduce cash costs further by cutting costs and increasing production volume.

2. Questions regarding classified (preferred) shares

Q5: Can you provide us with the scheme of classified shares you plan to issue?

A5: Page 77 of the results presentation materials provides an overview of shares classifications. We plan to issue ¥20 billion in Class A shares. The preferred dividend yield and monetary redemption premium are as shown in the presentation materials. A key point is the put option, as shown at the bottom of the table. This put option is exercisable by the underwriter Japan Industrial Solutions (JIS), conferring the right to receive cash and Class B shares or common shares in exchange for the Class A shares. In principle, these put options cannot be exercised for three years. We intend to repay this ¥20 billion with cash over the three-year period. If the targets in our new management plan are achieved, we will be able to repay this ¥20 billion with cash within three years.

Once three years have passed, JIS will have two options. In the event that this ¥20 billion is not redeemed and JIS exercises its right to receive cash and Class B shares, the principal portion of the ¥20 billion will be repaid with cash. For the remaining ¥4.4 billion premium portion, at maximum, we will issue Class B shares with put options for conversion into common shares. Although the theoretical maximum dilution is about 9%, these put options cannot be exercised for three years. Moreover, Tokuyama's rights take preference in the contract so that even if JIS exercises its option to convert the shares into common shares, Tokuyama would seek to redeem the shares for cash within the constraints of the amount available for distribution. We thus believe there is a rather low probability of the Class A shares being converted into common shares.

In addition, there are conditions that would allow JIS to convert all of the Class A shares into common shares. In this case, maximum dilution would be as much as 41%, but Tokuyama's rights take preference so that even if JIS exercises this option, Tokuyama would redeem the shares for cash within the constraints of the amount available for distribution.

In any case, we believe there is a very high probability of redeeming the ¥20 billion within three years.

Q6: Please explain the Class C shares.

A6: Tokuyama has certain rights with regard to the Class C shares. After two years have passed, if the amount available for distribution is more than the remaining balance of Class A shares + ¥40 billion, Tokuyama can convert Class A shares into Class C shares, which has lower dividend yields and redemption premiums. For example, if ¥20 billion in Class A shares remains after two years have passed, and the amount available for distribution is at least ¥60 billion, Tokuyama can convert the Class A shares into Class C shares. We would naturally like to see a transfer as rights occur in the event of a balance.

3. Questions regarding earnings forecasts

Q7: Regarding the semiconductor-grade polycrystalline silicon business, Tokuyama seems to have a bullish outlook with plans to restart operations at plants. What are your thoughts regarding the future?

A7: We do not expect much growth in the market for semiconductor-grade polycrystalline silicon in 2016. However, the structure of the market is changing. Quality requirements for polycrystalline silicon have increased sharply alongside miniaturization. By differentiating on quality, we believe a certain share of the market can be secured, even if growth is not strong, although it depends on strategy.

Q8: Would it be correct to assume that costs at plants being restarted for semiconductor-grade polycrystalline silicon will be largely the same as at existing plants that have been in operation to date?

A8: Yes, that is correct.

Q9: Tokuyama aims to increase the volume of cement exports quite a bit. Another cement producer has stated that it expects tough conditions in the export market. How will Tokuyama increase exports of cement?

A9: We plan to expand sales, centered on shipments of clinker which is powdered into cement on site, such as at Tokuyama Nouvelle Calédonie S.A. in New Caledonia.