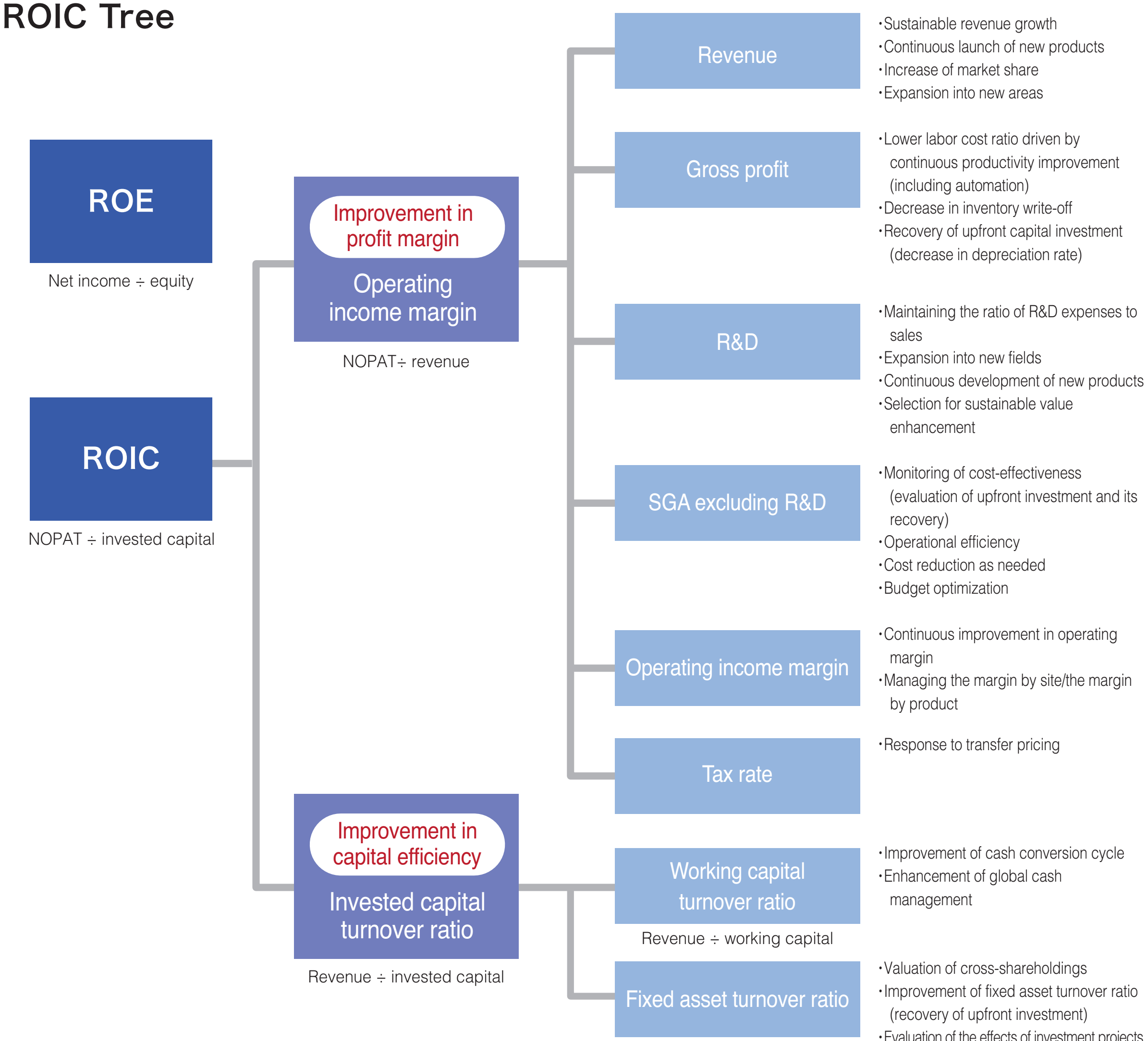
4-2 Financial Strategy

Basic Approach to Financial Strategy

Our Group will further strengthen the financial base by improving capital efficiency, etc., and aim to achieve sustainable growth, secure stable earnings, and increase corporate value by optimally allocating funds to aggressive growth investments and stable and continued shareholder returns.

We will also strive to contribute to all stakeholders by implementing management that is conscious of capital costs and maximizing corporate value. In order to realize returns that exceed the capital costs, we will improve return on capital (ROE and ROIC) using the ROIC tree and strengthen investment decision-making based on the capital costs.

ROIC Tree

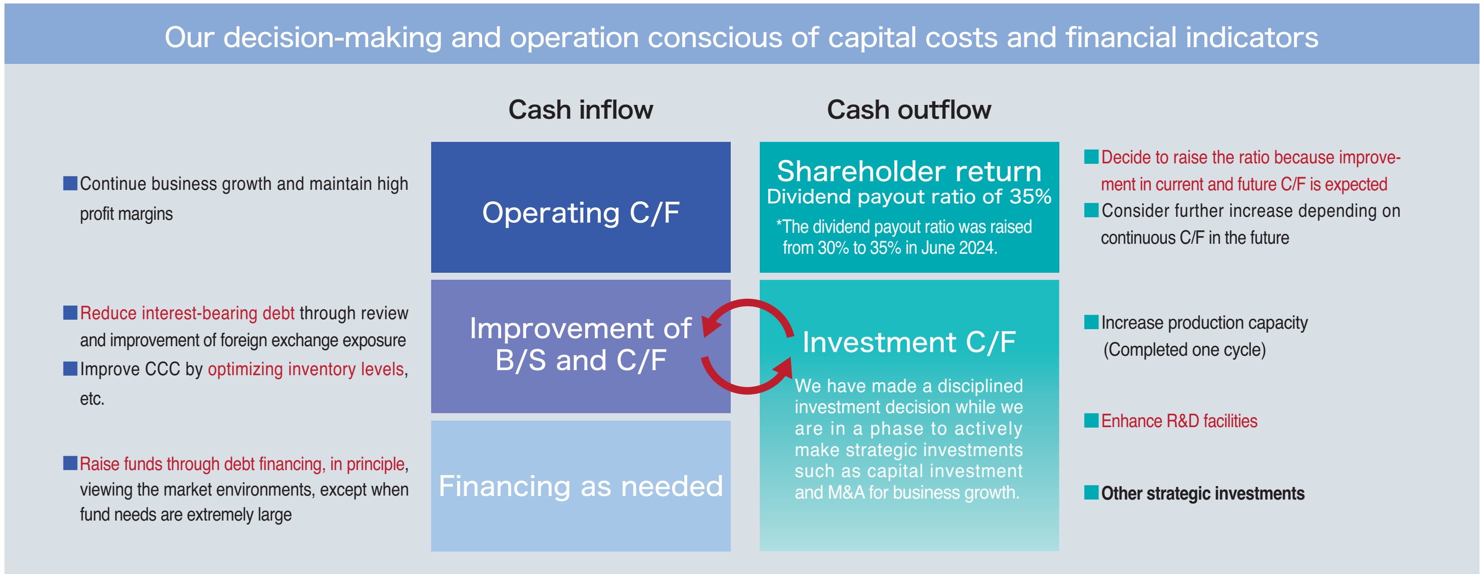


*Invested capital = shareholders' equity + interest-bearing debt, or working capital + fixed assets

*Working capital = trade and other receivables + inventories - trade and other payables

Capital allocation

Based on the strategies incorporated in the Medium-Term Management Plan “ASAHI Going Beyond 1000”, in addition to the growth of existing business (cardiovascular and non-cardiovascular fields), we are also promoting the launch of new business and are actively laying the groundwork for further growth, exceeding the final-year target of 110 billion yen in revenue under the Medium-Term Management Plan.
In particular, in the medical device field, which is our strategic business area, we are actively promoting up-front investments such as acquisition of shares and alliances, including M&A, capital investments, and R&D investments. Amid this backdrop, while emphasizing the balance between growth and financial strategies, we consider capital allocation providing for discipline and distribution of funds for cash flow for growth as follows.
This capital allocation was reviewed flexibly through dialogue with institutional investors.
As the source of funds is cash on hand and operating cash flows, we strive to improve our ability to generate funds and efficiency.
To improve the ability to generate funds, we evaluate major investments and new product and business projects using the evaluation methods with capital cost and cash flow such as the net present value (NPV) method and the internal rate of return (IRR) method. To improve fund efficiency, we consolidate surplus funds of our Group companies in Japan, the United States and Europe into Asahi Intecc using a global cash management system. In addition, the use of the cash management system enables us to centrally manage assets and liabilities denominated in foreign currencies, thereby reducing exchange rate risks.
If we need external financing, we will procure funds through the method we consider most appropriate, such as borrowing from a financial institution, based on various conditions such as the amount, timing, and duration.



Our Group's Key Management Indicators and Capital Costs

Our Group's key management indicators are revenue, operating income, and operating income ratio. The operating income ratio is currently set at 20%, and the EBITDA (operating income + amortization of goodwill + depreciation) ratio, which is the key performance of management, is set at 30%. We intend to improve these ratios and set new targets and to present them at the disclosure stage of the new Medium-Term Management Plan.

As for financial indicators, we have used ROE (return on equity) and ROIC (return on invested capital) as noteworthy indicators. ROE and ROIC (calculated using working capital + fixed assets as invested capital) are both set at a basic level of over 10% in addition to exceeding the cost of capital, and we aim to improve them. We believed that the use of shareholders' equity plus interest-bearing debt as invested capital did not accurately reflect the actual situation of our Group because our interest-bearing debt increased owing to foreign currency borrowings for the purpose of currency hedging. Therefore, we calculated ROIC using working capital plus fixed assets as invested capital. However, owing to the recent rise in interest rates on foreign currency borrowings, we reviewed our foreign exchange exposure and significantly reduced our foreign currency borrowings. Therefore, for future ROIC, we will apply and disclose the approach using shareholders' equity + interest-bearing debt as invested capital, too, as a closely watched indicator, in addition to the current approach using working capital + fixed assets.

The weighted average cost of capital (WACC) of our Group is considered to be 6.3% as of FYE June 2024. We have periodically revised the WACC taking into account risk-free rates and stock market trends.

For major investments and new products and business projects, the NPV (net present value) method and IRR (internal rate of return) method using the capital costs are applied.

Our ROIC = NOPAT ÷ (working capital + fixed assets)

NOPAT = Operating profit x (1 - statutory tax rate (currently 30.6%))

Working capital = Current assets - current liabilities
= Trade and other receivables + inventories + accrued income
- trade and other payables - account payables - advances received

Fixed assets = Fixed assets on the balance sheet

Typical ROIC (liability-based ROIC) = NOPAT÷ (interest-bearing debt + shareholders' equity)

NOPAT = Operating profit x (1 - statutory tax rate (currently 30.6%))

Interest-bearing debt = Total amount of borrowings

Shareholders' equity = Equity (Net assets - non-controlling interests)

Changes in management indicators

	Basic Level	FYE June 2022	FYE June 2023	FYE June 2024	Factors
Operating income margin	-	19.6%	20.0%	20.6%	
EBITDA margin	30% (standard)	29.2%	29.7%	29.6%	
ROE	10% or more	10.2%	10.4%	11.2%	Increased owing to improved profits regardless of increase in equity capital
Asset-based ROIC	10% or more	10.9%	10.7%	12.1%	Increased owing to decrease in inventories and increase in advances received
Liability-based ROIC	-	9.1%	9.0%	10.1%	Increased owing to improved profits
WACC	-	5.0%	5.5%	6.3%	See the below.

Breakdown of capital cost

		FYE June 2022	FYE June 2023	FYE June 2024
Disclosed capital cost		5.0%	5.5%	6.3%
(1) Weighted cost of equity	Share ratio (approx. 99%) x (a + b x c)	4.90%	5.52%	6.28%
Risk-free rate: a	Adjusted 10 year JGB interest rate average for five periods	0.07%	0.14%	0.35%
β value: b	Calculated based on the five-year average of five-year monthly beta and two-year weekly beta, and adjusted for future value calculation	0.824	0.913	1.000
Market risk premium: c	Matching the average cost of equity of Japanese companies with estimates from analyst reports of companies employing them	6%	6%	6%
(2) Weighted cost of debt	Debt ratio (approx. 1%) x cost of debt x (1- corporate tax rate) Cost of debt: five-period average of SWAP five-year rate + Spread (0.5%)	0.01%	0.01%	0.01%

International Taxation

As we expand globally, international taxation is becoming increasingly important.

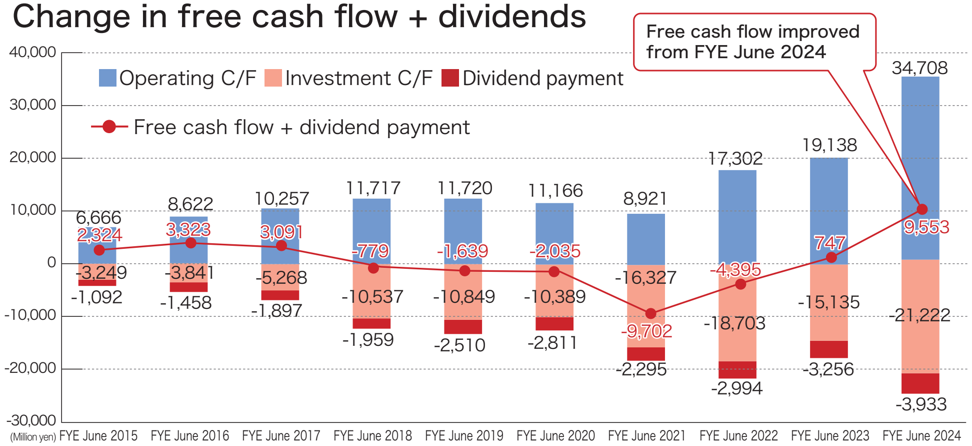
As for the taxation issues, with the support of outside experts such as tax accountants, we work in good faith to address tax issues and ensure transparency and credibility with tax authorities in the countries where we operate. With respect to transfer prices, we strive to manage them appropriately so that they become arm's-length prices by complying with local tax laws and OECD guidelines. For transactions with high transfer price tax risk, we reduce tax risk by utilizing the APA (Advance Pricing Agreement) system.

Shareholder Return

Our Group is developing its business on a global scale and is constantly striving to increase its corporate value. We recognize that returning profits to shareholders is one of our key issues, and our basic policy is to pay dividends on a stable and continuous basis from a long-term perspective, taking into account consolidated performance and other factors.
In the past few years, free cash flow temporarily declined owing to active investment in facilities and M&As, as well as an increase in inventories resulting from compliance with the relevant pharmaceutical regulations. However, in view of the fact that the upfront investment in capital investment and the increase in inventories have run their course and that further business expansion will enable cash flow from operating activities to cover the cash flow of investments and the payment of dividends in the future, we reviewed the consolidated dividend payout ratio considering it is important to further improve the return of profits to shareholders and to expand our shareholder base. From the payment of dividends from retained earnings for the fiscal year ended June 2024, we have decided to raise the consolidated dividend payout ratio from a target of 30% to a target of 35%. If cash flow is expected to remain stable in the future, we will flexibly consider reviewing the dividend payout ratio.
We have determined the amount of the current dividends by comprehensively taking into account the consolidated performance for the current fiscal year, future business prospects, the level of internal reserves, and other factors from a long-term perspective, while aiming for a consolidated dividend payout ratio of 35%. We allocate retained earnings to R&D, capital investments, and business investments, which are essential for future growth. This way, the company will endeavor to improve its business performance and strengthen its financial position.

See page 139 for the financial summary.

Change in free cash flow + dividends



Change in dividend per share and consolidated dividend payout ratio