

リンナイ社が最適な資本配分のもと市場で正しく評価される為に

2022年4月

免 責 事 項

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本資料の公開にあたって

- ダルトン・インベストメンツは機関投資家として約3年半にわたりリンナイ社株式を保有する長期株主です。我々の当初の見込みに違わず、リンナイは一貫して高いROICを維持・向上し、国内外共に事業の業容も着実に拡大してきました。結果、19年連続増配という上場企業の中でも稀な偉業にも敬意を表します。
- 又、我々はリンナイが持続可能な競争力を有する強いビジネスであると考えのみならず、経営陣が掲げる長期ビジョンにも共鳴します。世界中の消費者の生活の質の向上と、省エネ機器普及による地球環境問題への対応は欠かさざる重要社会課題です。
- 一方、我々は後述の問題意識から、長期的な株主価値向上の為に、資本政策の抜本的見直しをこれまで同社に要請してきました。しかしながら、同社と協議を重ねる中、経営陣の資本コストに対する意識の欠如を強く感じています。
- 現状の株価評価とバランスシートを放置することは、経営陣にとって不名誉であるのみならず、被買収リスクを高め（同社は実際、2008年に欧州企業から20%近くまで株式を買い進められた経緯があります）、全てのステークホルダーをリスクに晒すことにも繋がります。したがって、他の投資家に我々の問題意識を共有することを目的として本資料を公開します。

リンナイ社事業に対する弊社の見立て

- 稼ぎ頭の給湯器（耐用年数は約10年）事業は売上の主要ドライバーが更新需要であり、連結・単体ともに創業以来黒字の安定事業
- 各国市場でのトップシェアに裏付けされた高い技術力
- 70年代から徹底してきた生産合理化・内製化による高いコスト競争力
- 海外事業は売上の約半分を占め、エネルギー効率と利便性を売りにした製品拡販により中長期で着実な成長が見込まれる
- 国内は、市場規模の割に安全性への要求水準が厳しく新規参入への障壁が高いことから、日系企業数社による寡占となっており、現経営陣体制のもと推し進めてきた高付加価値商材へのシフトの効果が今後本格的に見込まれる
- 他の多くの日本企業同様、リーマン経営の結果、足元ではサプライチェーン混乱の影響を受け、受注残が増加

弊社が考えるリンナイの課題

- バランスシート上の必要現金は理解する一方、水準の妥当性について疑問。
- 全ての資金を想定資本コストが最も高い株主資本（現金）で調達する計画となっており、資本コストを意識しているように見受けられない。
- 高い現金創出能力を有するがゆえ、現行の株主還元政策では現金が積み上がり続け、資本効率低下の傾向は変わらない。
- ROEに対するコミットメントがない。

純資産の過半に値する必要現金水準は適切か

現行の資本政策で必要現金水準を設定しているが、その額は総資産の36%、純資産の53%を占め、過剰と言わざるを得ない。

- ・大規模災害を想定した復旧費用や従業員補償
- ・M&A 等、成長機会を逃さないための資金

1,800億円

災害対応準備
機動的資金
700億円

運転資金
1,100億円
(月商3ヶ月分)

- ✓ 下段の運転資金と重複するものと認識
- ✓ 具体的な計算根拠が不明
- ✓ 地震保険等によるリスクヘッジは実行済みか

- ✓ 災害対応準備・機動的資金700億円を別枠とするのであれば、月商2ヶ月分でも十分
- ✓ 5年後の目標売上高ベースでの月商3ヶ月分となっているが、より直近（2～3年後）の目標売上高ベースとし、都度見直すべき

出所：決算説明会資料

1%に満たない代替調達手段がある中、すべての資金需要を株主資本でカバーする必要があるのか

中計期間中の資金需要項目	金額 (億円)	資金調達手段	想定資本コスト (%)
災害対応準備、機動的資金	700	株主資本（手元現金）	8
運転資金	1,100	株主資本（手元現金）	8
基本シナリオの必要投資	800	株主資本（将来CF）	8
成長投資・戦略費用 （カーボンニュートラル投資）	500	株主資本（将来CF）	8
未定の成長投資・戦略費用 （中計の上限枠1,250億円との差額）	～750	株主資本（将来CF）	8

ご提案

社債等による借入
コミットメントライン
（銀行融資枠）設定

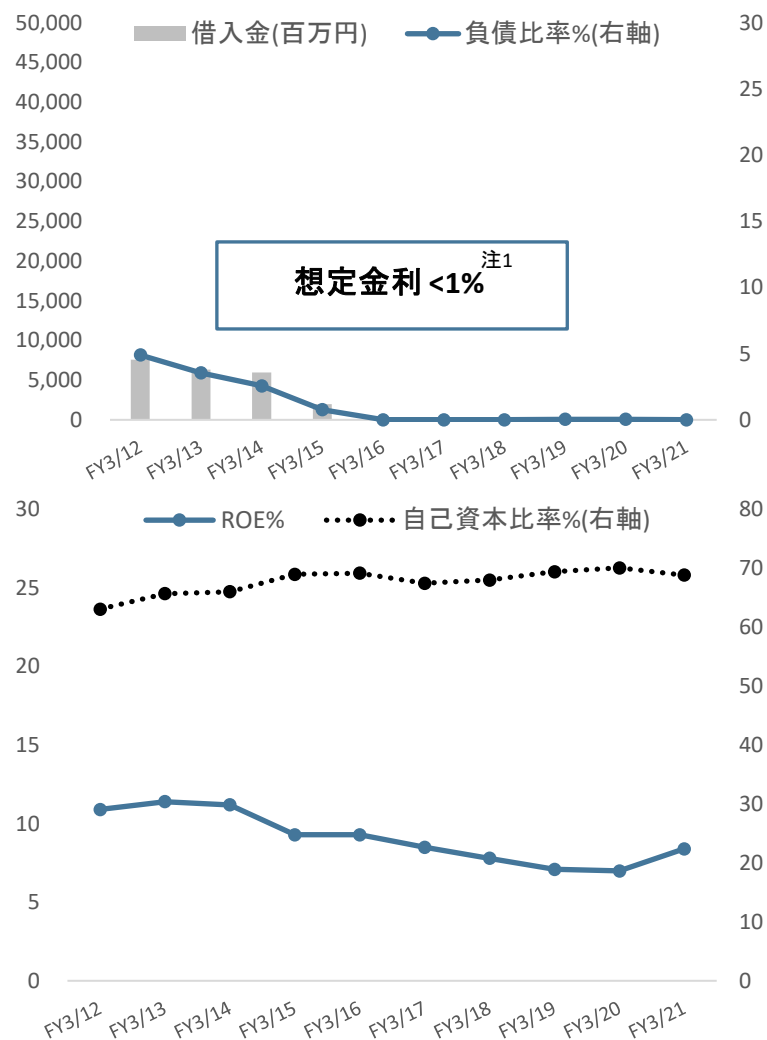
<1%^{注1}

出所：決算説明会資料

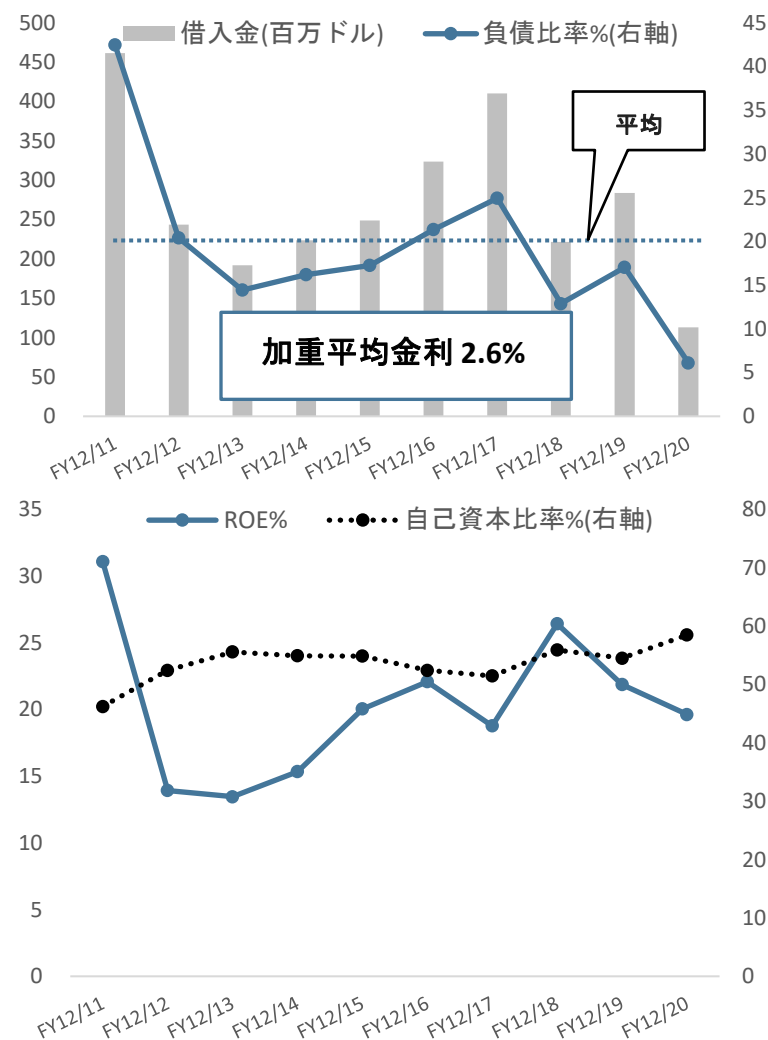
注記1) SDG債等の社債金利を前提に推定。

仮に競合の負債比率20%をベンチマークとした場合でも、700億円程度は借入により問題なく調達可能

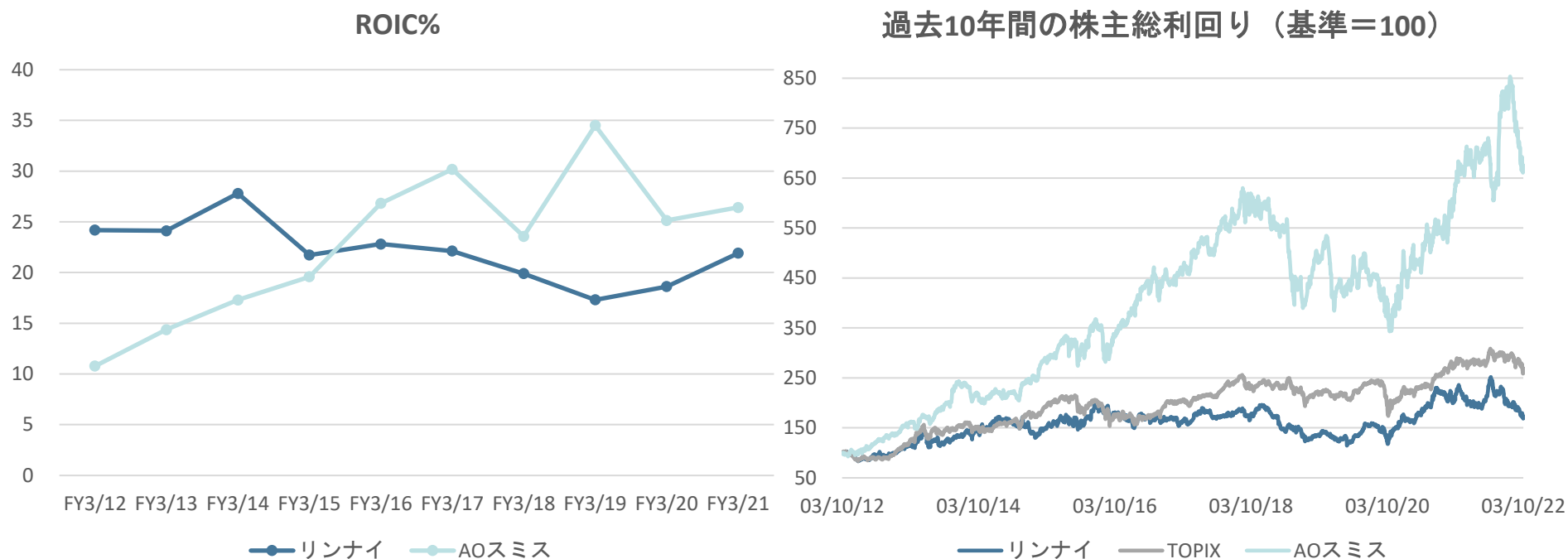
リンナイ



AOスミス

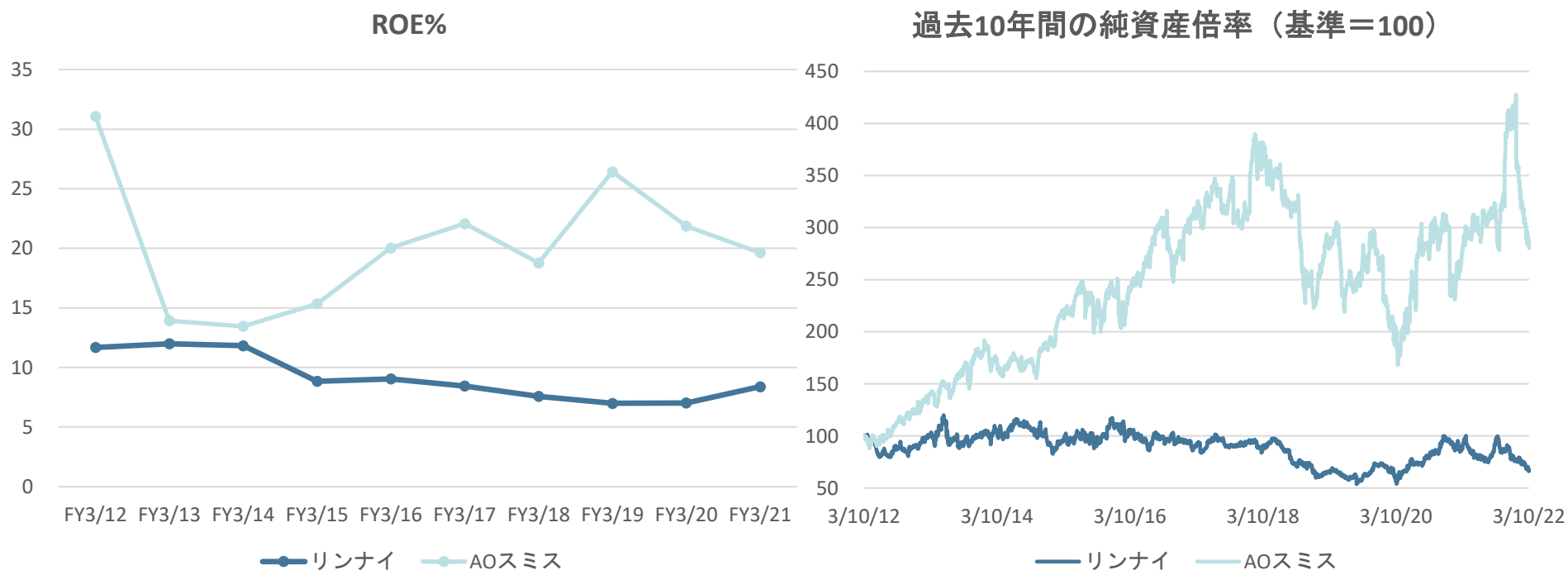


リンナイは高い現金創出力を有する一方、株主総利回り（TSR＝株価変化率+配当）は競合やTOPIXを著しく下回る



出所：有価証券報告書、AOスミス年次報告書、ブルームバーグ

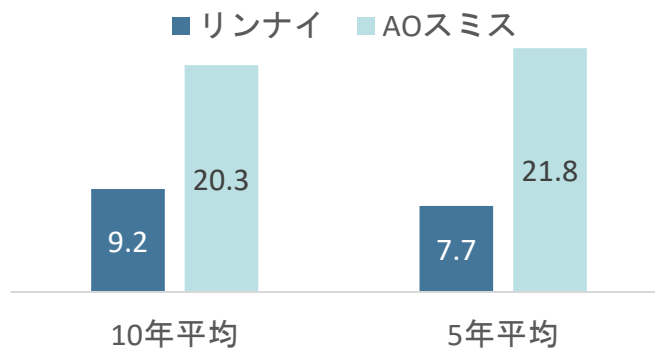
相対的に低いリンナイのROEが、市場からの低い評価（純資産倍率）につながっている



出所：有価証券報告書、AOスミス年次報告書、ブルームバーグ

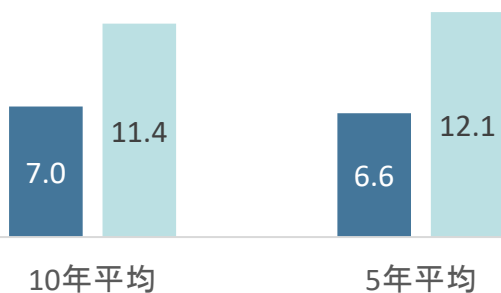
ROEの構成要素の内、利益率改善に向けては取組中と認識する一方、 バランスシートの効率性改善が課題

ROE%



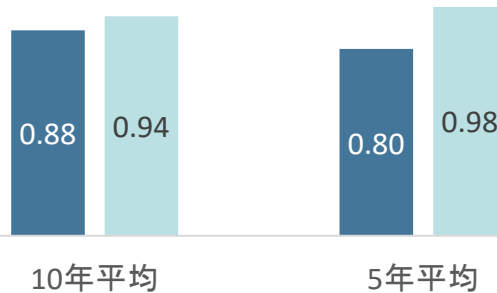
純利益率%

■ リンナイ ■ AOスミス



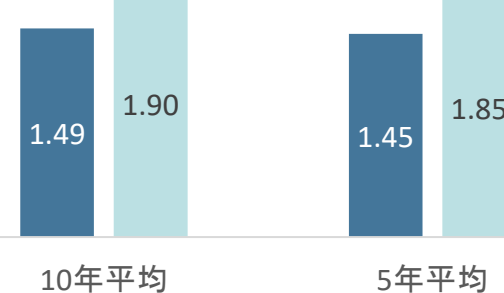
資産回転率x

■ リンナイ ■ AOスミス



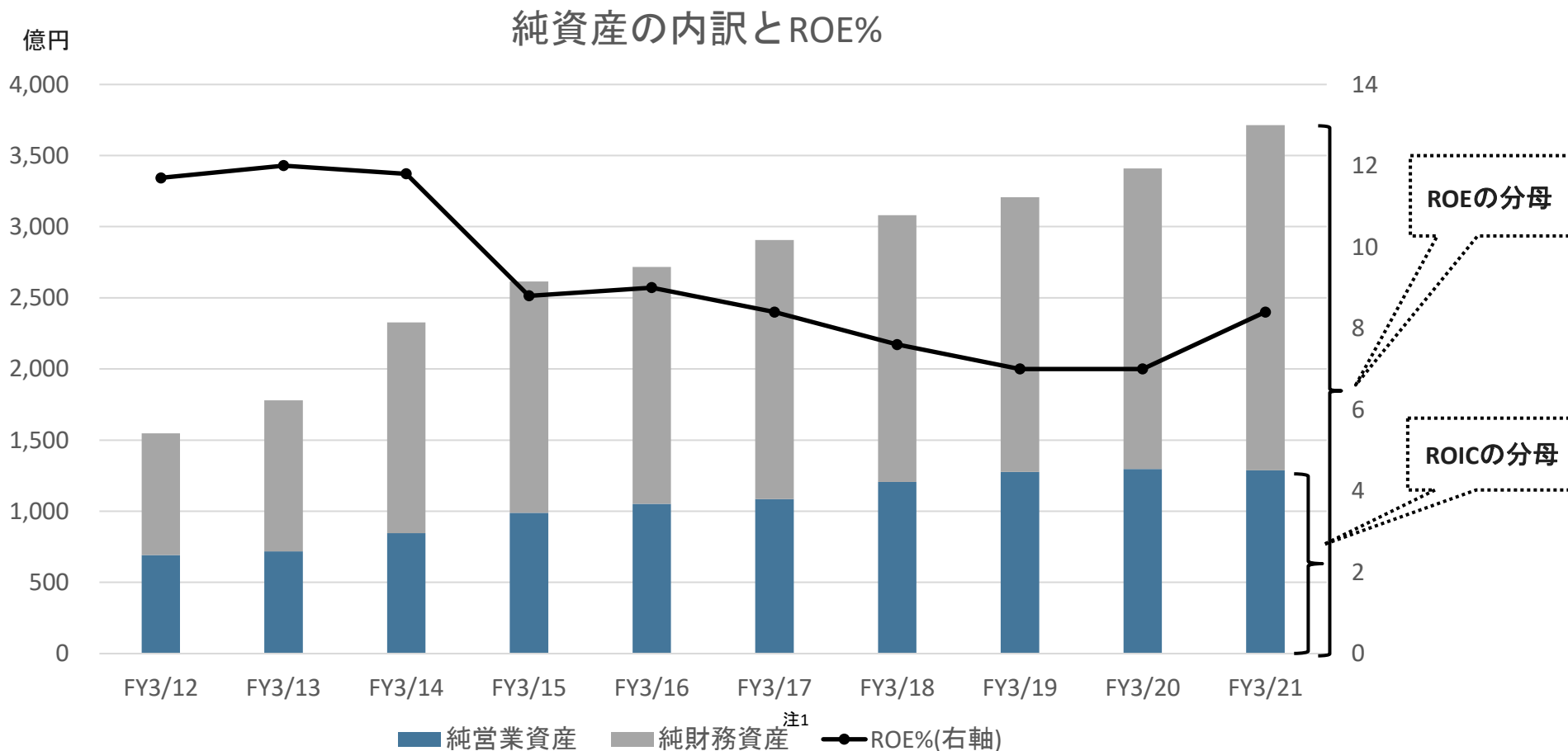
レバレッジx

■ リンナイ ■ AOスミス



出所：有価証券報告書、AOスミス年次報告書、ブルームバーグ

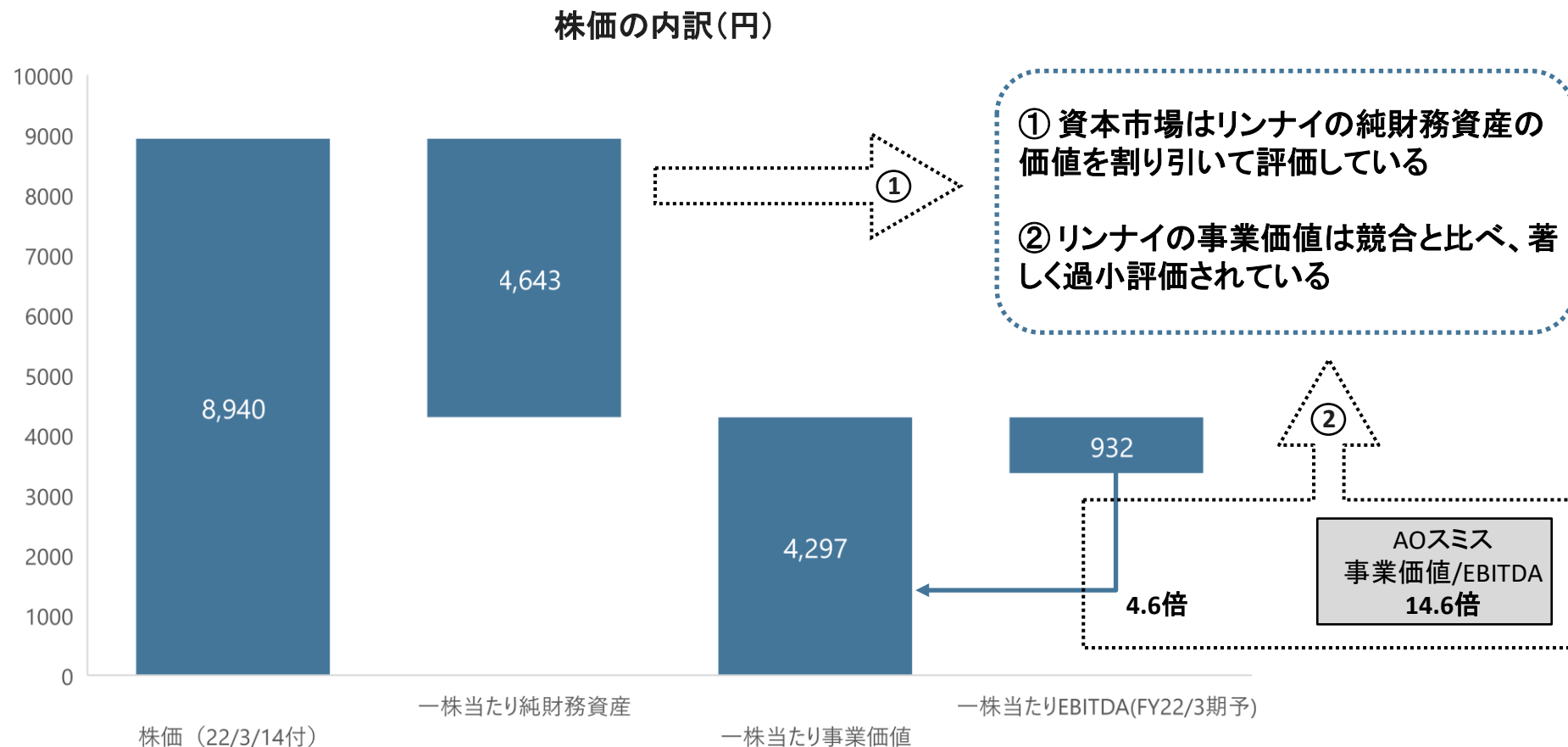
バランスシートが非効率である最大の要因は、不稼働の金融資産が積みあがってきた為



出所：有価証券報告書、ブルームバーグ

注記1) 純財務資産は、現金・有価証券・投資有価証券（持分法投資除く）の合計から、有利子負債を減算して算出。

ROE低迷の背景は、事業から創出される現金が事業に再投下されず、株主資本が金融資産へ配分され続けることにある



出所：有価証券報告書、AOスミス年次報告書、ブルームバーグ

株主資本の調達コストは年利8%程度

- コーポレートガバナンス・コードは、経営戦略や経営計画の策定・公表に当たっては、自社の資本コストを的確に把握した上で、収益計画や資本政策の基本的な方針を示すとともに、収益力・資本効率等に関する目標を提示することを求めています。
- 又、経済産業省から2014年に発行された「伊藤レポート」は以下を提言しています。

～日本企業はグローバルな投資家から認められるにはまずは第一ステップとして、最低限8%を上回るROEを達成することに各企業はコミットすべきである。もちろん、それはあくまでも「最低限」であり、8%を上回ったら、また上回っている企業は、より高い水準を目指すべきである～
- リンナイは26/3期にROIC19%を目標としている事を鑑みれば、適度なレバレッジを活用しながら相応のROE水準を目標とすべきです。

ご提案： ROE目標値の開示および現行資本政策の変更

リンナイは、最適な資本配分を行い長期的に株主価値を向上させるために、先ず下記の2点を実行すべきです。

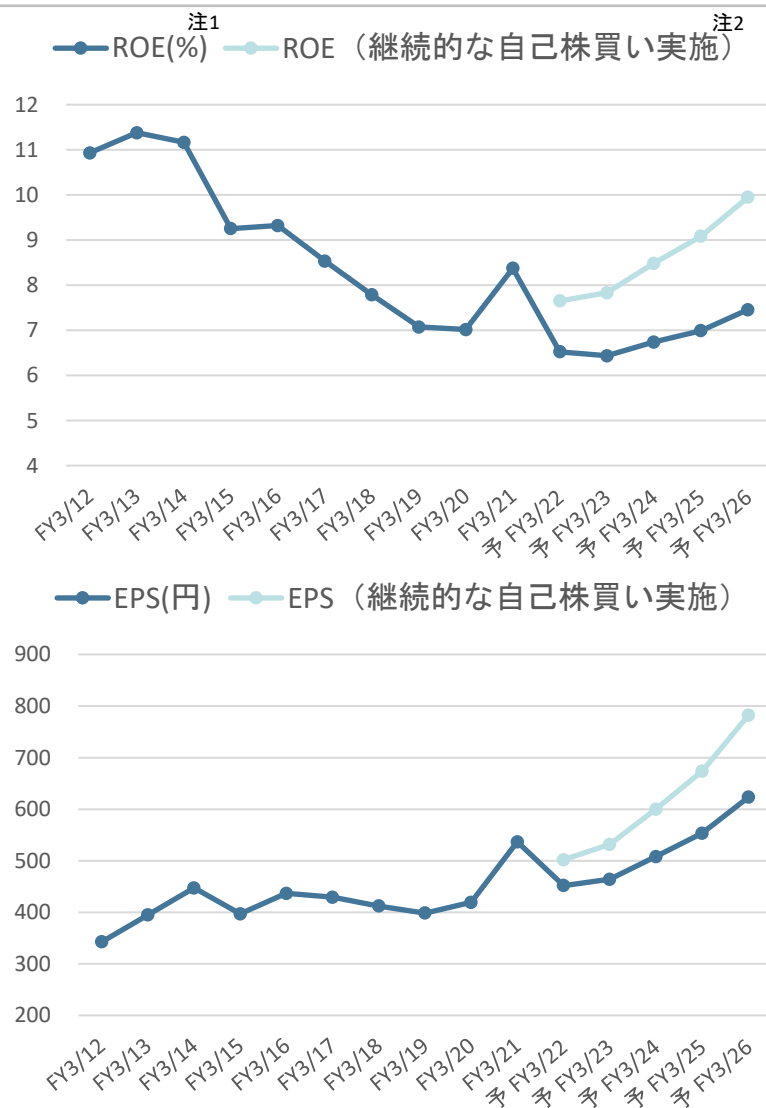
- ROE目標値の開示
- 2021年12月31日時点における余剰現金470億円^{注1}を原資とした自己株買い実施

加えて、下記の3点も今後の検討課題として提案します。

- 必要現金水準の見直し
- 資金需要項目の一部を、社債等の借入により調達
- 残りの中計期間にわたり、総還元性向の最低目標を現状の40%から引き上げ

注記1) 2021年12月31日時点の純財務資産から現行の必要現金1,800億円を控除して算出。

自己株買い効果の試算



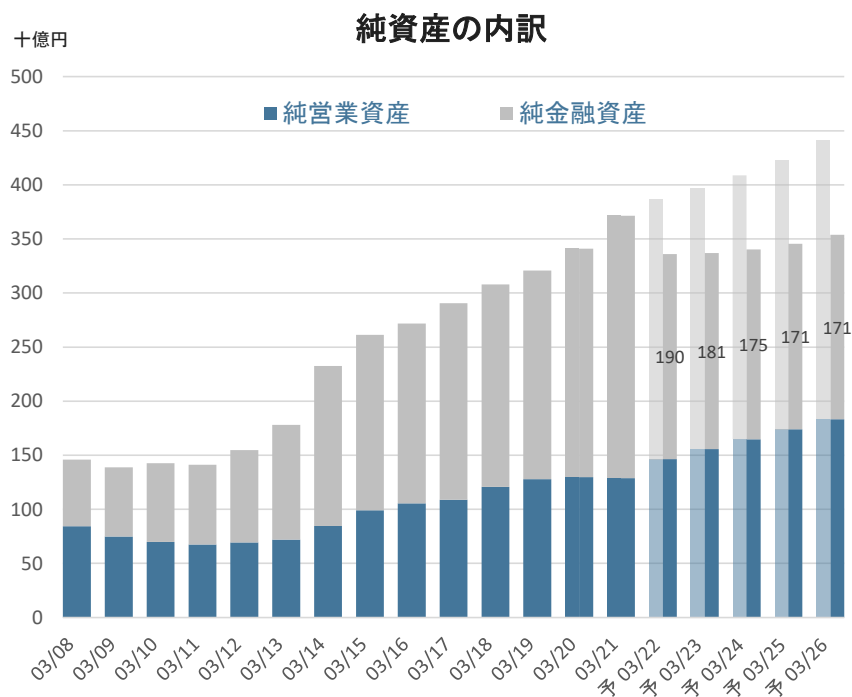
- 22/3期に追加で発行済株式の10%、以降每期追加で3%の自己株買いを想定。
- 自己株買いが無いケースでは継続的に資本コストを下回るROE（濃い青色）。
- 上記自己株買いによってROEは早期に資本コストを上回る水準に（薄い青色）。
- 一株当たり利益（EPS）の成長は大幅に加速。

出所：有価証券報告書、ブルームバーグ

注記1) 計画期のベースケースは、リンナイの中計目標値を基に弊社が推定。総還元性向は40%を想定。

注記2) 計画期における自己株買い取得時の株価は直近3年の純資産倍率平均1.5倍を基に推定。

自己株買い効果の試算（続き）



出所：有価証券報告書、ブルームバーグ

- 前項と同等の試算。
- 必要現金水準は1,700億円と仮定（26/3期目標売上高ベースでの月商4.5カ月分）。
- 自己株買いによって金融資産の増加ペースは抑制されるが、現行の必要現金水準とほぼ同程度の必要現金は維持。

最後に

事業経営と同等かそれ以上に資本配分の決断も経営の重要な責務です。リンナイ経営陣には、前述の我々の具体的提案に加え、下記の点を念頭に経営に取り組んで頂くことを要請します。

- 上場企業である以上、内部留保を含む株主資本も借入同様「調達」と認識
- 株主資本の調達コストは（目安として）年利8%程度と考える
- 1%に満たない代替調達手段がある中、すべての資金需要を株主資本でカバーする必要があるのか
- 事業投資と自社株買いは二律背反ではない。自社株買いも投資
- 実効的な自社株買い＝ターゲット株価を定めて・小分けに・時間をかけて

How Rinnai can unlock its value through optimal capital allocation

April 2022

1601CloverfieldBoulevard, Suite 5050N Santa Monica, CA 90404 | www.daltoninvestments.com

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Reasons for presenting this material publicly

- Having held shares of Rinnai for over 3 and a half years, Dalton Investments is a long-term institutional shareholder of the company. Consistent with our original expectations, Rinnai has consistently generated and improved upon its high ROIC, while expanding its businesses steadily in both domestic and overseas markets. This has allowed Rinnai to raise its dividends per share for 19 consecutive years, a remarkable achievement to which we pay our respect.
- We believe Rinnai has a robust business with a sustainable competitive advantage and we agree with its management's long-term strategic vision for the company. Improving the quality of life of the consumers around the world and helping resolve global environmental problems are essential social issues which Rinnai products can address.
- However, because of our concerns outlined in this presentation, we have requested for the company to perform a fundamental review of its capital policy. Based on a series of discussions with management, we realized a lack of focus on managing the company's cost of capital.
- We believe that leaving the company's current share price and balance sheet as they stand not only is dishonorable for the management, but also increases the risk of being acquired by another company (in fact, a European company undertook a series of purchases to acquire almost 20% of Rinnai in 2008), exposing all stakeholders to risk. Therefore, we present this material publicly to share our concerns with other shareholders.

Dalton's understanding of Rinnai's business

- A primary sales driver of the Rinnai's cash-cow water heater (useful life is approximately 10 years) is replacement demand. Rinnai has a stable business which has been profitable every year on both a stand-alone and consolidated basis since the company's foundation.
- Rinnai's products remain leading technology proven by its leading share in various regional markets.
- The company has a high level of cost competitiveness earned through rationalization and insourcing of manufacturing process which the company has been carrying out intensely since the 1970's.
- Overseas sales account for a half of total sales, and expectations are for steady sales growth as the products are both energy efficient and convenient.
- The domestic market is an oligopoly made up of several Japanese companies, given the barriers to entry are high for new entrants due to strict safety standards. A shift to high-value-added products driven under the current management is expected to come to fruition at full scale going forward.
- Similar to many other Japanese companies, as a result of lean management, the company's order backlog has been increasing due to the effect of global supply chain disruption.

Dalton's understanding of Rinnai's issues

- We understand the need for required cash on the balance sheet; however, the appropriateness of the current high levels seems questionable.
- The current capital policy assumes all capital needs are financed by shareholders' equity (ie., cash) which has the highest cost of capital. Management does not seem conscious of this cost of capital.
- Because of Rinnai's robust cash generation ability, cash is expected to continue piling up under the current capital policy, and therefore, capital efficiency is expected to continue deteriorating.
- There is no commitment in ROE.

Is the current level of required cash, which accounts for a half of net assets, appropriate?

Rinnai sets a level of required cash under the current capital policy. We believe it is nothing short of excessive, as it accounts for 36% of total assets and 53% of shareholders' equity.

- Recovery costs and employee compensation in event of large-scale disaster
- Funding for growth opportunities, such as M&As

¥180.0 billion

Disaster preparedness
and response funds
¥70 billion

Working capital
¥110 billion yen
(Equivalent to
3 months of sales)

- ✓ Seems redundant given high working capital
- ✓ The rationale for the amount is not detailed or clear
- ✓ Has the company implemented a risk hedge such as earthquake insurance, etc.?

- ✓ 2 months of sales should suffice if the company sets aside disaster preparedness and response funds of JPY 70 billion
- ✓ The amount is 3 months of the target sales in 5 years; however, the amount should be based on the sales target of more recent year (ie., in 2-3 years)

Source: Earnings presentation materials

Does Rinnai need to utilize shareholders' equity for all capital needs, while alternative financing with below 1% cost of capital are available?

Capital Needs during Mid-term Business Plan	Amount (Y100M)	Financing	Assumed Cost of Capital (%)
Disaster Preparedness and Response	700	Equity (Cash on Hand)	8
Working Capital	1,100	Equity (Cash on Hand)	8
Necessary Investments for Basic Scenario	800	Equity (Future CF)	8
Growth Investments, Strategic Spending (Carbon Neutrality Investments)	500	Equity (Future CF)	8
Undecided Growth Investments, Strategic Spending (The remaining budget based on the upper limit of Y125B set in the business plan)	~ 750	Equity (Future CF)	8



Proposals

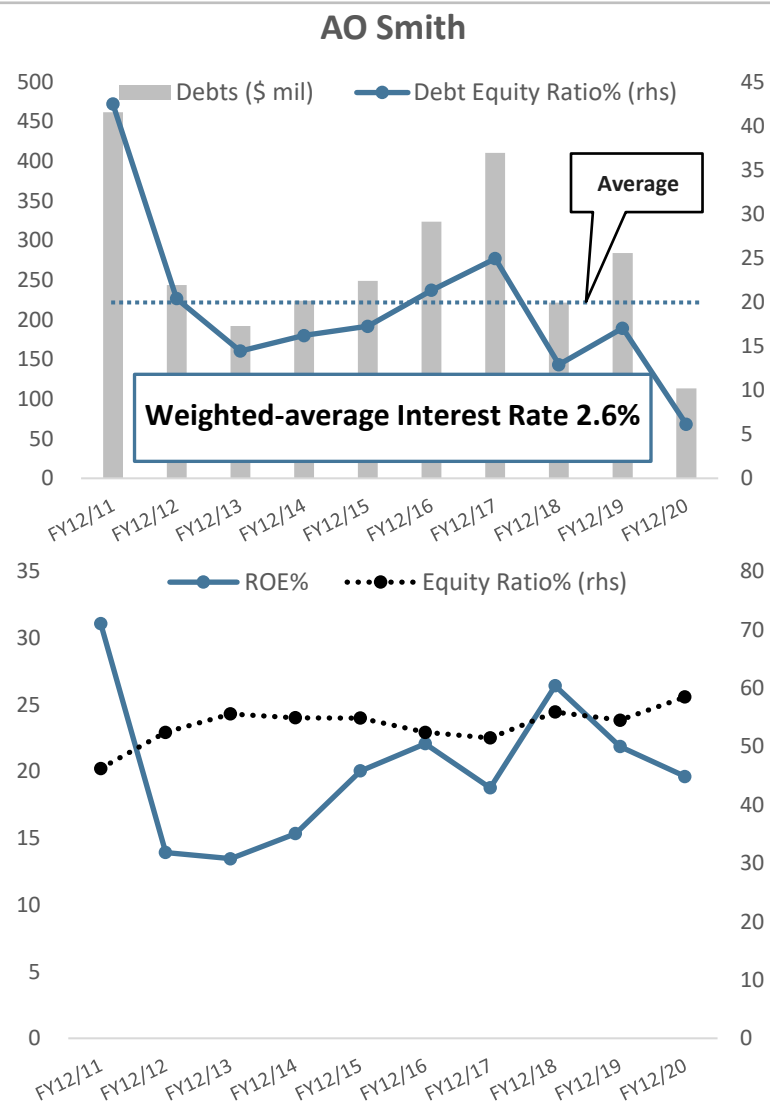
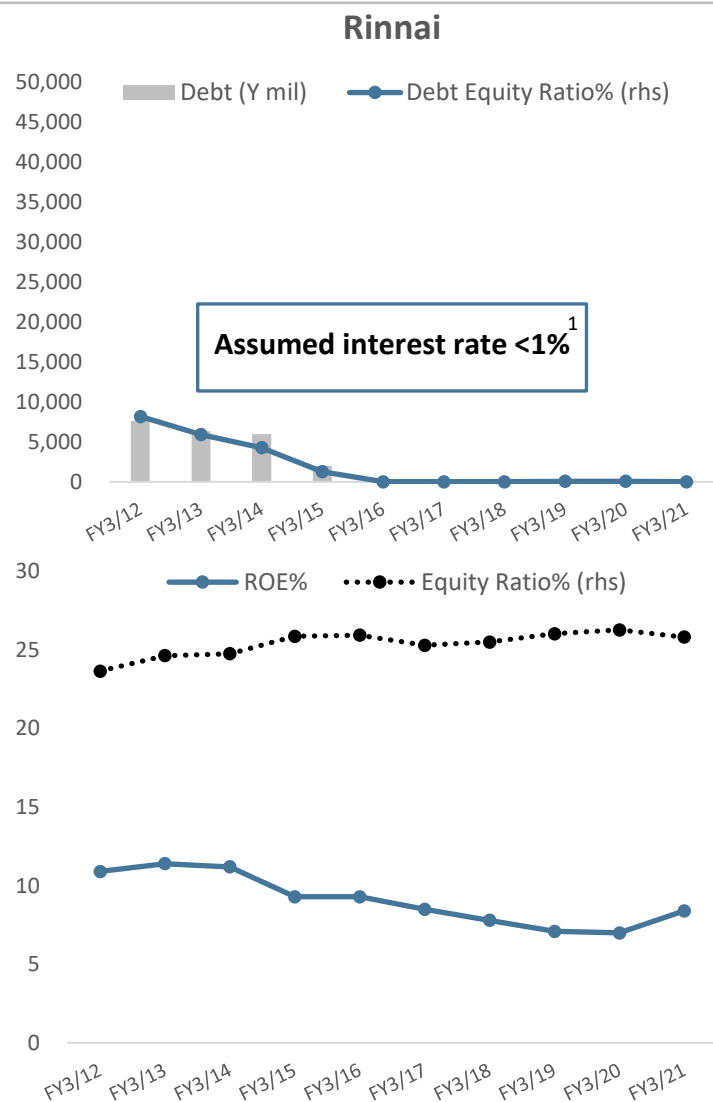
Utilization of Borrowing such as Bonds
Establishment of Commitment Line
(Credit Line by Bank)

<1%¹

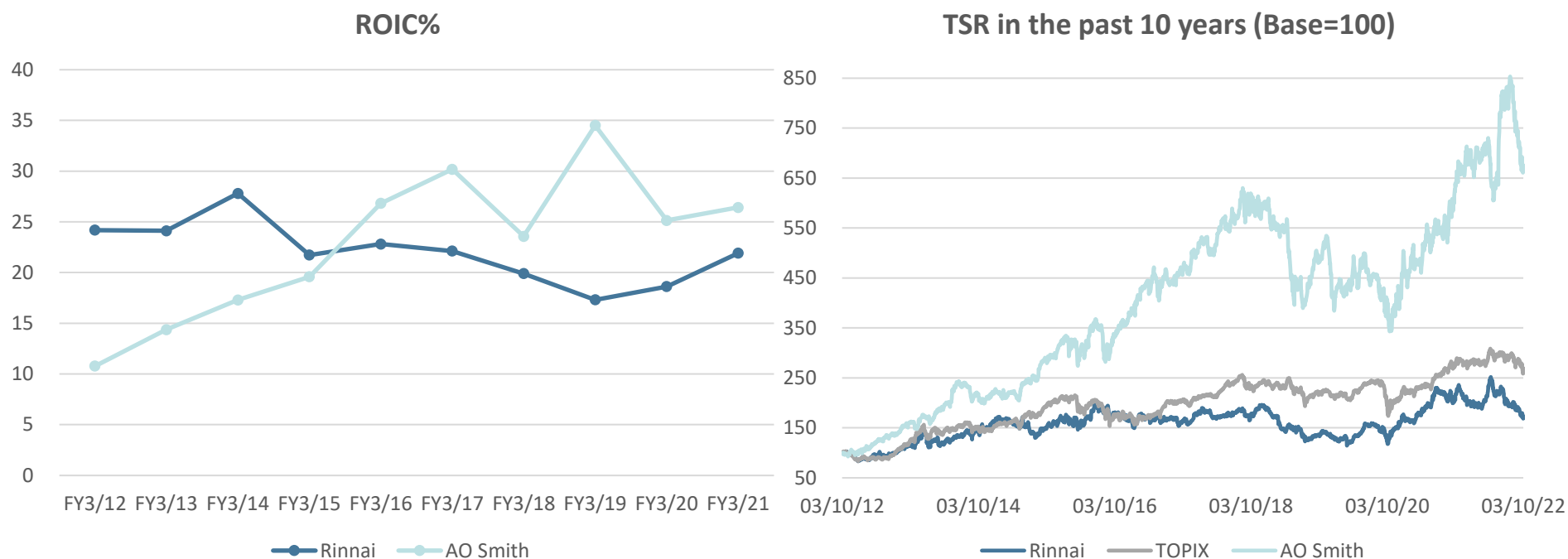
Source: Earnings presentation materials

Note 1) Estimated based on assumed interest rates of bonds such as SDG bonds

Based on a peer's debt-to-equity ratio of 20%, we believe that Rinnai can borrow about JPY 70 billion without any issues

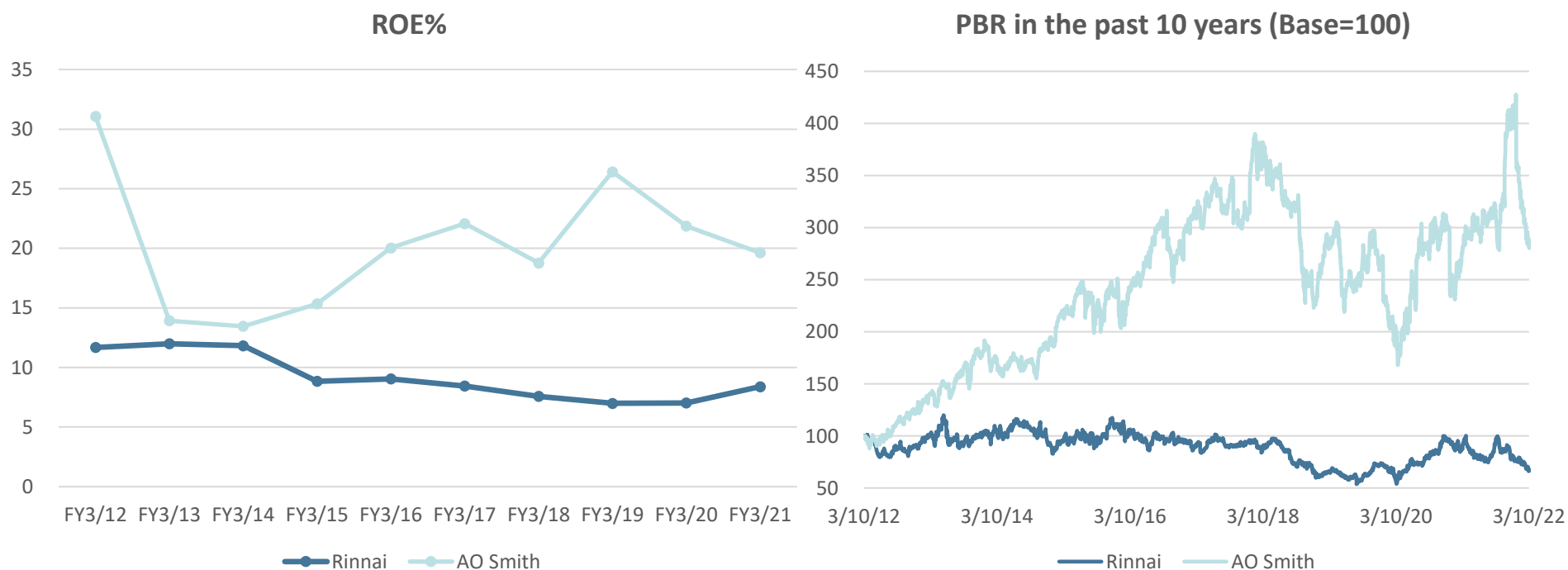


While Rinnai has robust cash generation ability, the company lags behind its peer and TOPIX significantly in Total Shareholder Return (TSR = stock price fluctuation % + dividends)



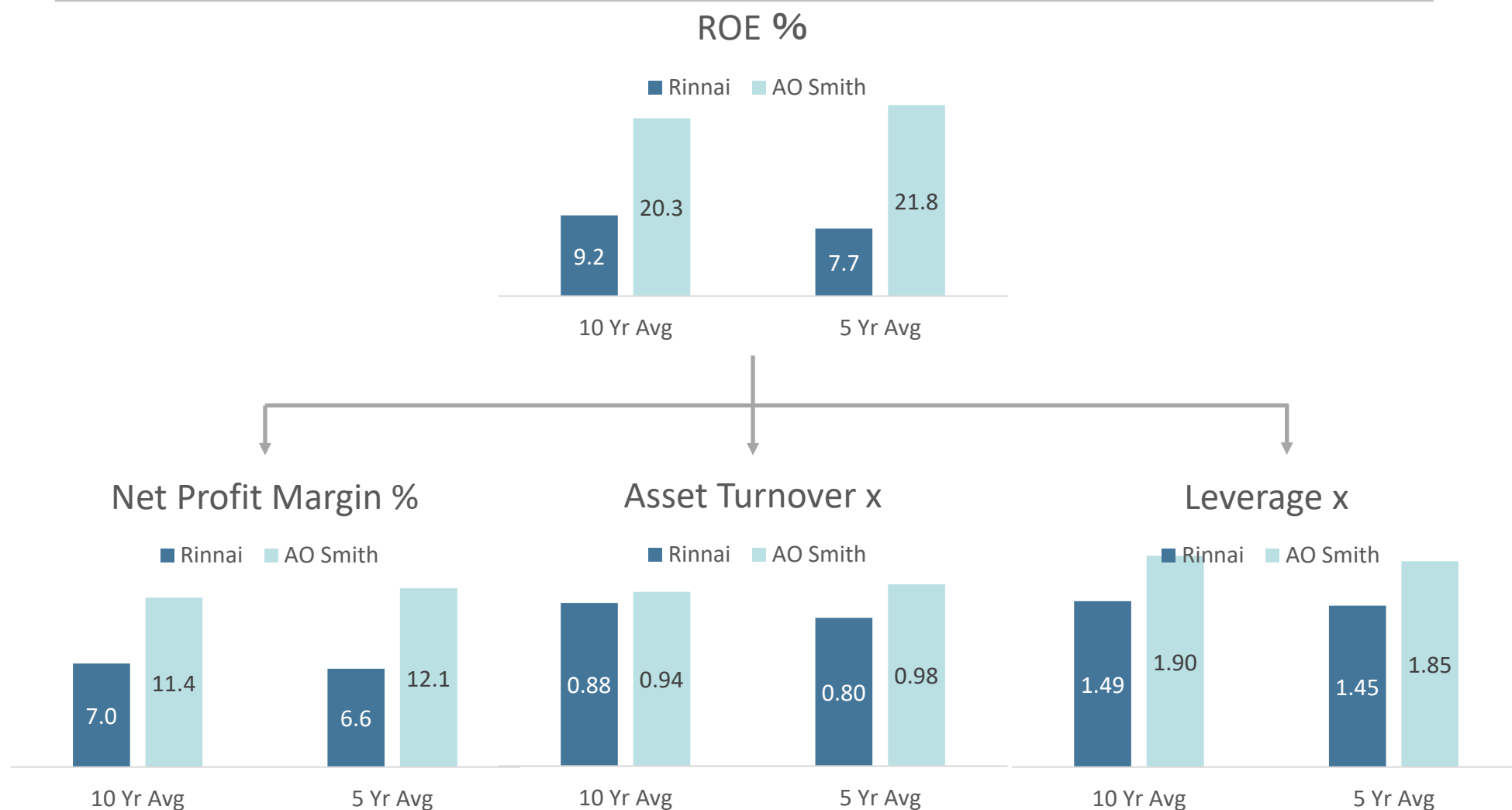
Source: Rinnai's annual filing, AO Smith's annual filing, Bloomberg

The market's low evaluation (Price-to-Book Ratio) is attributable to the relatively low level of Rinnai's ROE



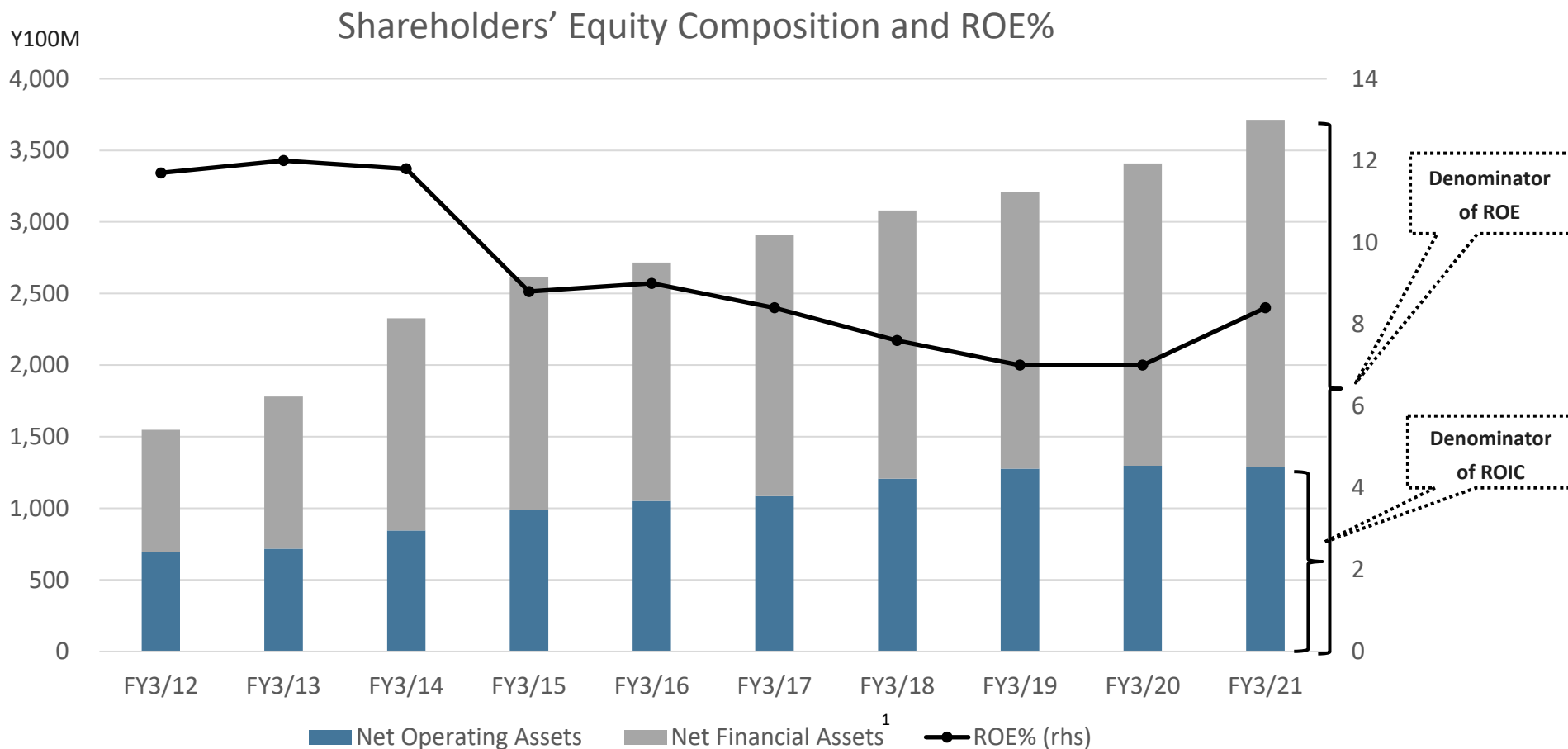
Source: Rinnai's annual filing, AO Smith's annual filing, Bloomberg

Among the components of ROE, we understand that Rinnai is engaged in improving the profitability; however, enhancing the efficiency of the balance sheet remains an area for improvement



Source: Rinnai's annual filing, AO Smith's annual filing, Bloomberg

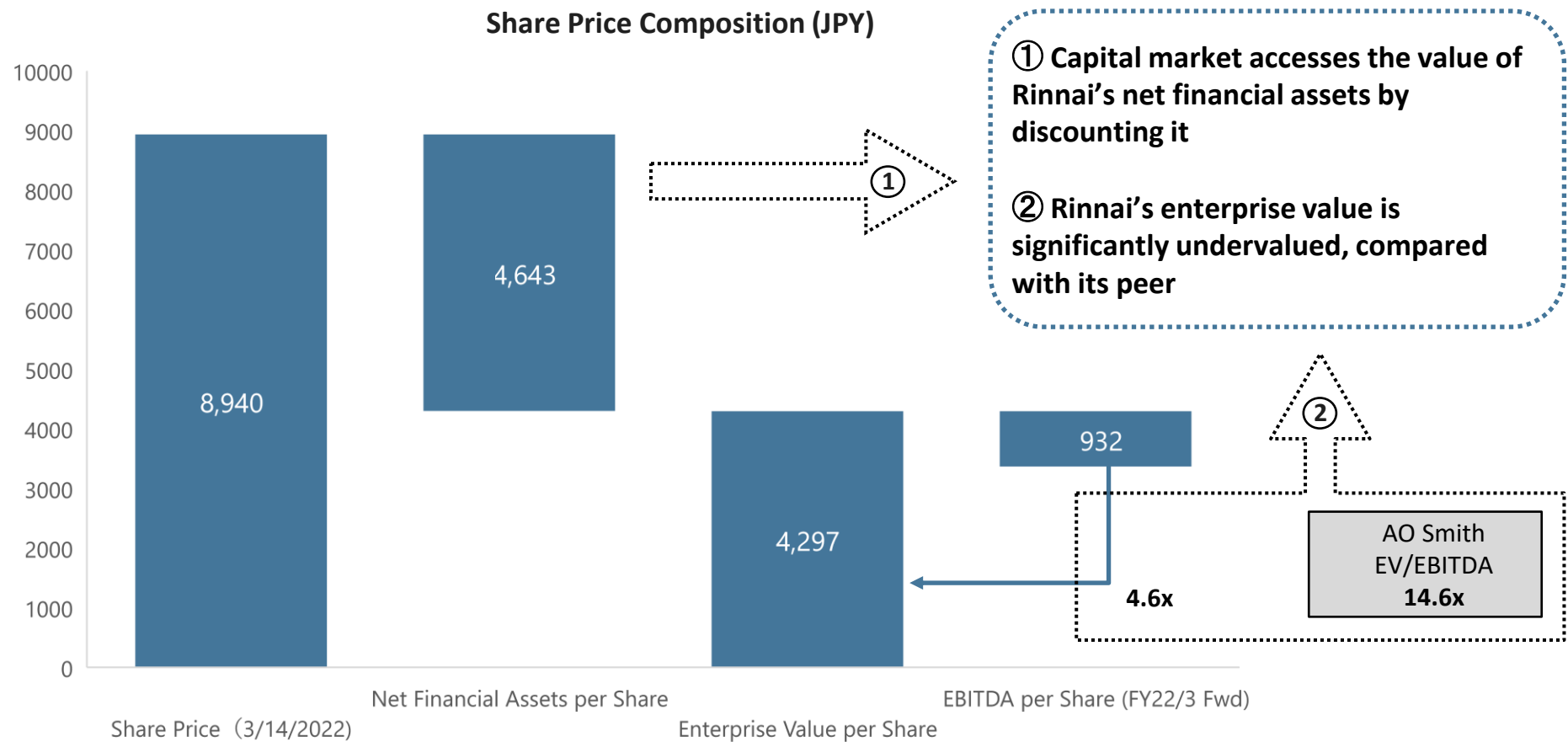
The primary reason for the inefficient balance sheet is the idle financial assets which have been piling up over years



Source: Rinnai's annual filing, Bloomberg

Note 1) Net financial assets is calculated as a sum of Cash, Short-term Securities, and Long-term Securities (excluding Investments in Equity Affiliates), less Interest-bearing Debts.

A low ROE is accounted for by the company's continuous allocation of shareholders' equity to financial assets, not reinvesting cash to its business



Source: Rinnai's annual filing, AO Smith's annual filing, Bloomberg

The cost to finance by equity is ~ 8% per annum

- The Japan Corporate Governance Code requires companies to articulate their earnings plans and capital policies when establishing and disclosing business strategies and business plans, and to present targets for profitability and capital efficiency after accurately identifying the company's cost of capital.
- Also, “the Ito Review” published in 2014 by the Ministry of Economy, Trade and Industry presents the following:
 - ~ ...the first step in receiving recognition from global investors is for a company to commit to achieving a minimum ROE of 8%. Companies should further strive to achieve a higher ROE appropriate to their specific business and that will contribute to sustainable growth.~
- Given that Rinnai aims to achieve ROIC of 19% in FY3/26, the company should target a reasonable level of ROE, utilizing an appropriate amount of leverage.

Our proposals: Disclosure of target ROE and a revision of the current capital policy

To increase its long-term equity value through optimal capital allocation, Rinnai should implement the following two actions first:

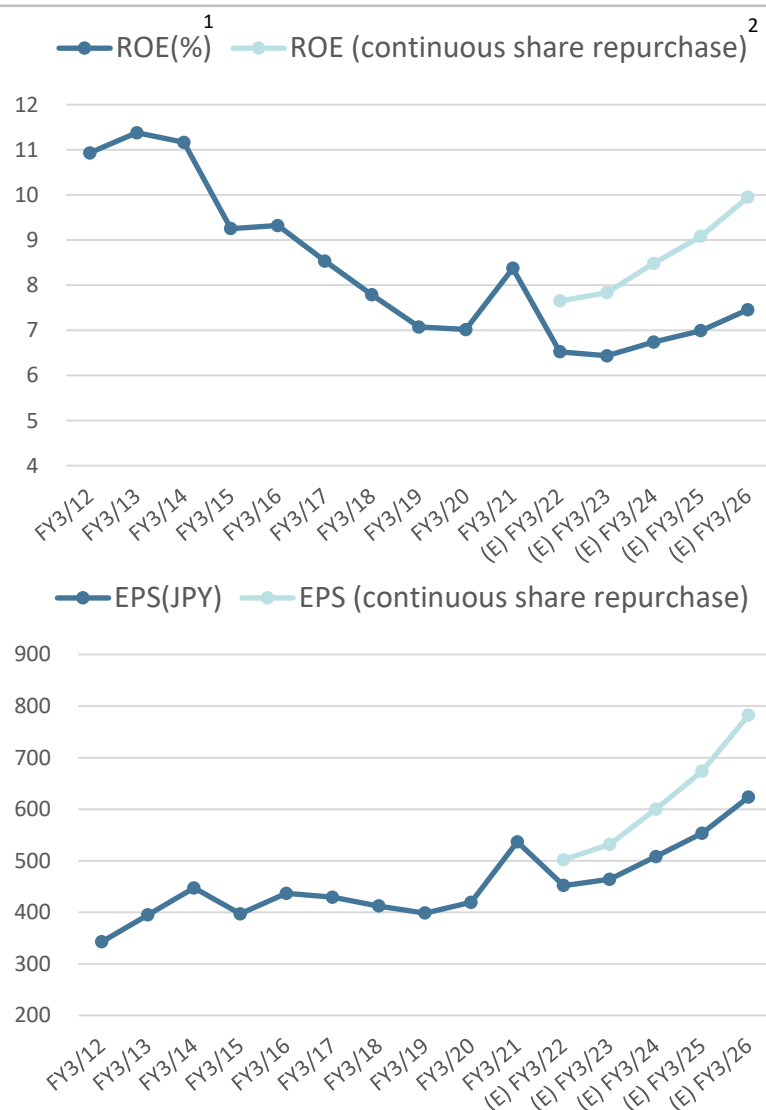
- Disclosure of target ROE
- Share repurchase of JPY 47 billion¹ based on the excess cash as of December 31, 2021

Additionally, we propose the following three actions as a future agenda:

- Reevaluation of the level of required cash
- Utilization of borrowing such as bonds
- Increase of Total Payout Ratio from the current 40% for the remaining period of the mid-term business plan

Note 1) The amount was calculated as net financial assets as of December 31, 2021 less required cash of JPY 180 billion set under the current capital policy.

Pro Forma estimate of the effects of a share repurchase



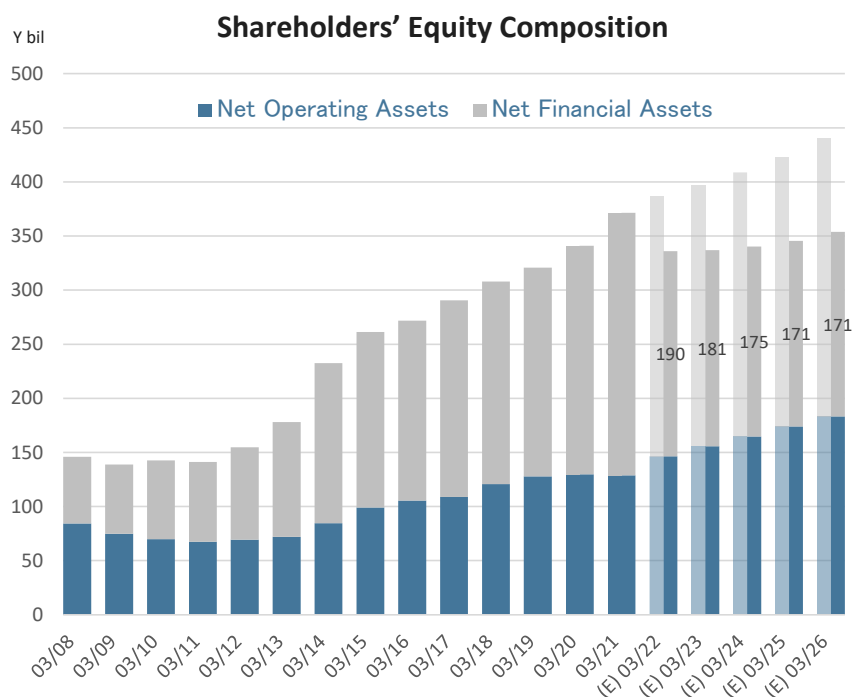
- Assumptions of a 10% buy back of outstanding shares additionally in FY3/22, and 3% annually thereafter.
- ROE is expected to stay below cost of equity consistently under the base case scenario which assumes no share repurchase (dark line).
- ROE is expected to exceed cost of equity early under the scenario with the above share repurchases (light line).
- The growth of EPS is expected to accelerate significantly.

Source: Rinnai's annual filing, Bloomberg

Note 1) The base case scenario during the projection period is estimated by Dalton based on the company's Mid-term Business Plan. Total payout ratio is assumed to be 40% under the base case scenario.

Note 2) The share prices utilized to estimate the amount of share repurchases during the projection period are based on the average Price-to-Book Ratio over the last 3 years of 1.5x.

Pro Forma estimate of the effect of a share repurchase (Cont'd)



Source: Rinnai's annual filing, Bloomberg

- Same assumptions as the last page.
- Hypothetically set JPY 170 billion as a level of required cash (equivalent to 4.5 months of sales for FY3/26.)
- Share repurchase moderates the accumulation of financial assets, while maintaining the level of required cash that is nearly as high as the company's current estimate.

Conclusion

For management, capital allocation is a responsibility that is equally important as/or more important than business operations. In addition to the detail proposals described previously, we request that Rinnai management run the company by bearing in mind the below:

- For publicly listed companies, shareholders' equity including retained earnings, same as debts, should be considered financed
- The cost to finance by equity is about 8% per annum
- Does a company need to utilize shareholders' equity for all capital needs, while alternative financing with below 1% cost of capital are available?
- A company can conduct investments in its own business and share repurchase simultaneously. Share repurchase is also an investment
- Effective share repurchase programs should be based on a pre-determined target price, and conducted in steps over time