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Interview with Top Management

Toward becoming an all-embracing company for building materials that consistently pursues resolutions to social issues with technology, ideas, and passion.

Q What were the achievements and issues in fiscal year (FY) 2021, the second year of the medium-term management plan GP25 2nd Stage?

FY 2021 started with the uncertainties caused by the spread of COVID-19. Substantial changes were required in the business environment and in the behavior and recognition of people throughout the year, including lockdowns around the world, declarations of the states of emergency in Japan, postponement of the Tokyo 2020 Olympic and Paralympic Games, and the shift to working from home.

Under these circumstances, our business activities place the utmost priority on the assurance of safety and the prevention of the spread of infection for all stakeholders, including customers, business partners, employees, and their families. At the same time, we fully recognized that our daily lives depend on healthcare professionals and the many other professionals who provide support for society. We would like to express our gratitude to such people.

FY 2021 is the second year of the GP25 2nd Stage, the three-year medium-term management plan as the second step toward the achievement of GP25, which explains our goals for 2025. We just passed the turning point. At the beginning of the fiscal year, the impact of COVID-19 was particularly significant overseas. We faced many restrictions with the plant in New Zealand stopping operation for about one month due to the lockdown, and the plant in the United States forced to reduce production by 60%. However, economic activities gradually restarted in the second quarter going forward. In Japan, we strengthened proposals for home builders to enhance our presence in detached houses

for sale and steadily expanded apartment renovations in the metropolitan area. Because of the rapid recovery of the US housing market, our steady supply and input of new products through intra-group cooperation were successful, proving the effect of our efforts in the North America business, which went into full-scale operation through the M&A in FY 2020. As a result, our overseas net sales increased more than fourfold from FY 2016, when the long-term vision GP25 was launched. The share of overseas sales as part of overall sales increased from 6% to 23%, which represents steady progress in the revision of the business and market portfolio as one of the basic policies for the 2nd Stage.

Long-Term Vision GP25	▶P4
Medium-Term Management Plan GP25 2nd Stage	▶P30
Strategies by Business Segment and Market	▶P31-32

On the other hand, we have observed two issues. The first issue is the decreased profitability of MDF as the mainstay of the industrial materials business. MDF is the base material for buildings and furniture and signifies wood fiberboard molded with residual wood offcuts from afforested trees. We produce MDF at two plants in New Zealand and two plants in Malaysia. For MDF, multipurpose product selling prices have not recovered because of the difficulty in differentiating from competitors and because of the deteriorated market triggered by US-China trade friction, coupled with the decreased demand caused by COVID-19, which urgently calls for an improvement in profitability. The other issue is the lower growth in public and commercial buildings than our initial expectations despite focused efforts

in the non-housing market. Demand for accommodation and commercial facilities rapidly decreased after the loss of inbound tourists with people staying home due to the spread of COVID-19. The impact was particularly significant for tatami mats since orders had been increasing with the evaluation of their functionality, including durability and easy maintenance, and as Cool Japan products.

Q FY 2022 will be the final year of the medium-term management plan GP25 2nd Stage. How will it finish?

Despite substantial changes in the external environment, which had not been expected at the time of medium-term management planning, our basic strategies will not change for FY 2022. We will continue to increase market share in the new housing market and make up for the decrease in the overall markets of home renovation and non-housing public and commercial buildings, thereby maintaining the revenue structure in Japan while pursuing global growth. At the same time, we will carefully adapt to changes from the initial expectations and adjust our plans to grasp new demand by strengthening proposals for the new needs that have emerged because of COVID-19. Our performance forecast* as a commitment to shareholders and investors this fiscal year is set at 204 billion yen in net sales, the highest target since consolidation, 10.0 billion yen in operating profit, and 6.0 billion yen in profits attributable to owners of the parent. These figures for the performance forecast are different from the management goals in the medium-term management plan but will be maintained as stretch goals to be pursued toward the achievement of the further long-term vision GP25. *Forecast on May 14, 2021

- Differences between the management goals in the medium-term management plan and the performance forecast ▶P35
- Initiatives for Priority Markets ▶P36

As specific initiatives in Japan, we will continue to offer proposals both in new housing and in the renovation market, including the input of new products, by identifying specific changes in the required housing functions of securing workspace, preventing sound leaks and resonance, and achieving an ambience of comfort where people spend longer hours since working from home will become more common, whereas new housing starts will continue to decrease. The Japanese government launched incentive programs that include the green housing point system, which is applicable to many of our products. We will also strengthen our proposals in this aspect. In public and commercial buildings, we will increase the number of sales representatives at local branches to strengthen our sales structure. Because office functions are being reviewed as work styles become increasingly more diversified, we will proactively offer proposals concerning changes to the layout and application and improvements to the sound

environment in response to the rapid increase of online meetings. We developed building materials with an antiviral function in 2011 and released them in 2012 ahead of other companies in the industry. We see greater possibilities for an increase in the sales of these products to elderly facilities, medical facilities, and other institutions. As the ambience where people spend daily lives become more essential than ever, we will expand our scope of business and develop proposals as a manufacturer that contributes to production from the viewpoint of providing a safe, secure, healthy, and comfortable ambience.

In our global business, North America will remain a profit driver as the largest market in the world for wood housing. New housing starts in the US decreased to an annual rate of approximately 1.0 million in April and May 2020 but rapidly recovered to more than 1.5 million in July onward and has remained steady. The number of new housing starts is nearly twice that of Japan, and the demand in North America is extremely large considering residence areas. In addition, the population will continue to increase by more than 2 million every year on a medium-term and long-term basis, which suggests robust housing needs. We will endeavor to maintain a steady supply by leveraging our integrated supply structure from the veneer plant in Canada with its abundant forest resources to the LVL plant in the US, while increasing the share of the high-added value products of preservative LVL and high-strength LVL in the product mix, thereby effectively grasping the vigorous demand in the market.

We will pursue rationalization and streamlining for MDF by restructuring plants as a manufacturer. For any rapid cost increases that cannot totally be offset, we will incorporate the increase into selling prices through discussions with customers. We will also accelerate the development of specialty MDF with high added value by leveraging our technological power and improve our product mix, thereby improving profitability. Ultra-lightweight MDF, which was developed at our plant in New Zealand, has been popular with customers in the US and other countries. Through our plant in Malaysia, we are also promoting proposals for the MDF fully produced with acacia chips from trees afforested by our company over 20 years. Because MDF offers excellent size stability, we are expanding its application to new uses from conventional flooring to use as a base material for interior doors. MDF is capable of effectively using wood materials. Although it is impacted by market conditions on a short-term basis, it has high potential with global demand expected on a medium-term and long-term basis. We will expand its application and propose substitute demand by sharing its value as a sustainable material with our customers.

- Global markets ▶P37-38
- Public and commercial buildings ▶P39-40
- Home renovation market ▶P41-42



Q | What are the investment approach and key points in financial strategies?

In FY 2021, we invested in carefully selected BCP measures, safety measures, and IT systems linked to the enhancement of the management foundation but suspended growth investments that assumed sales increases while prioritizing cash flow in the midst of uncertainties caused by the COVID-19 pandemic. However, we have not changed our approach to proactive investments, including M&A, for favorable items that will contribute to medium-term and long-term growth strategies and increased competitiveness, while we will carefully monitor trends in material and resource inflation. Our focused investment target is the global industrial materials business with the key areas of North America and Asia. In North America, we are considering an expansion into new products that will exercise synergistic effects by utilizing sales channels for LVL. We will increase the capacity of MDF and further enhance our presence in Asia and other regions.

We will continue to reduce cross-shareholdings and strengthen management on the balance sheet of each manufacturing division, thereby achieving the balance sheet goal targets in the medium-term management plan. In FY 2021, we generated cash by reducing cross-shareholdings with key business partners. We plan to steadily reduce cross-shareholdings from the viewpoint of asset rationalization down to a share of approximately 10% versus net assets.

We will enhance shareholder return with a dividend payout ratio of 30% or higher and provide stable dividends as the basic policy by balancing investments for medium-term and long-term growth with financial soundness.

Financial strategies ▶P45-46

Capital Policy/Shareholder Return ▶P73

Q | Next, what is the approach concerning ESG management and sustainability? First, what are the initiatives for E: Environment?

As an environmental initiative, we set the reduction rate for CO₂ emissions as one of the management goals under the medium-term management plan. In FY 2021, our domestic CO₂ emissions were reduced by 35% versus FY 2014 from a production decrease combined with the stable use of renewable energy, which focused on wood biomass boilers that had synergistic effects with our main business. Therefore, we will be able to achieve a reduction of 26% as our initial goal for FY 2022. We will set a stretched reduction target in the next medium-term management plan with the goal of making an additional contribution under the carbon neutrality target for 2050 and a new reduction target by 2030 as set by the Japanese government. We will also examine the introduction of in-house carbon pricing as an internal investment decision and business evaluation in consideration of the substantial influence of these elements on our business activities. Among these efforts, we will promote information disclosure in accordance with the Task Force on Climate-Related Financial Disclosures (TCFD) as part of the revised Corporate Governance Code 2021.

At the same time, as the momentum increases for a circular economy, we believe it is necessary to fundamentally review our processes from development and procurement from the viewpoint of reducing after-sales product disposal based on our experience in business and our contributions to a resource-recycling society.

Recycling of Waste Materials ▶P49

Initiatives toward the CO₂ Emissions Reduction ▶P50

Q | What is the priority regarding S: Society?

Among the many requirements under S: Society, the highest priority is placed on human resources. Human resources are the source of technology, ideas, and passion, which comprise the mission in our group corporate philosophy. We believe that the maximization of the value of human resources will lead to improvements in our corporate value. We promote diversity, work-style reform, and human resource development in order to provide a workplace where employees are happy. With regard to diversity, we promote a workplace environment where human resources with diverse personalities and values can fully achieve their potential with a particular focus on female employees as the most familiar goal. However, the promotion of females to managers and directors, an indicator that draws external attention, is insufficient, and we consider it an important requirement. We have enhanced the systems to support the combination of work with childcare and long-term care, provided training opportunities, and reformed the corporate culture to help female employees. As the share of female recruits has been increasing recently, we expect that these initiatives will take effect on a medium-term basis.

Regarding work-style reform, the COVID-19 pandemic destroyed fixed ideas concerning the place, time, and method of work while making work from home and remote work more common. In our company, we regard these movements not as provisional countermeasures against COVID-19 but as the new normal, and we will establish flexible work styles as regular parts of the system and culture so that employees amidst the life events of childcare and long-term care can exercise their skills and potential as the source of corporate growth without interruption. We will also focus on the development of global human resources as we pursue expansion from the domestic housing market to the non-housing market and to the global market.

The COVID-19 pandemic has renewed our recognition of

the importance of life and health. We will further strengthen and upgrade health management as the foundation of human resources to exercise their skills and reach their potential. We have supported employees in quitting smoking and paid allowances to employees with a proactive attitude toward health promotion. We will continue promoting these initiatives to bring smiles to employees and their families as the source of their energy.

Human Resources

▶ P51-53

Q | The governance structure has been reformed lately. What is the plan for G: Governance?

With the approval of shareholders on June 25, 2021, we became a company with an audit and supervisory committee. The aims are to strengthen the supervisory function of the Board of Directors, expedite the decision-making process, and develop and upgrade the next generation of management. Under the new structure, directors and audit and supervisory board members were reduced from 12 to 9, and their independence was secured with outside directors accounting for more than one-third of the members. The operating structure also changed in April with the establishment of the position of operating officer. By clarifying the division of roles with executive officers, we will flexibly and proactively allocate and promote human resources to executive officers from the viewpoint of leadership development so that they can undertake reform and growth in the allocated business domains by serving in key positions in the R&D division, manufacturing division, sales division, and administrative division. We will also further enhance the governance system by responding to the revised Corporate Governance Code 2021 and by envisioning market reorganization under the Tokyo Stock Exchange in FY 2023.

Governance

▶ P55-68





Q | Finally, what is the medium-term and long-term direction of DAIKEN CORPORATION?

In the integrated report for the last year, our medium-term and long-term strategies are formulated with a focus on changes and a return to the origin by reconfirming our strengths and envisioning the post-COVID-19 era. We have four major strengths: (1) research and development capabilities accumulated since our foundation to pursue the possibilities of sustainable industrial materials and a safe, secure, healthy, and comfortable ambience; (2) product deployment capabilities to create industrial and building materials with a variety of features that differ from industrial materials, thereby proposing new lifestyles and industrial standards; (3) a customer base with a wide variety of professional clients, including the housing industry, construction industry, and various manufacturers; and (4) an integrated system for developing industrial and building materials, as well as installation work and construction for creating ambiances. To pursue the sustainable improvement of corporate value through these strengths, we redefined materiality (material issues to cope with) by identifying risks and opportunities that may have a significant influence on our medium-term and long-term management strategies. One of them is the pursuit of the sustainable use of wood resources. Our company has been engaged in this materiality as a key business since our foundation. This pursuit also leads to countermeasures against climate change and contributions to the SDGs, which are urgent global issues.

Wood as a product absorbs CO₂, fixates it as carbon, and continuously preserves it in the growth process. By appropriately felling wood and planting new trees in accordance with the growth cycle, the CO₂ absorption function of forests can be maximized. Since our foundation, we have achieved comfortable lives for people and preserved an increasing amount of carbon by using industrial materials

and building materials for the ambience of life based on the functions of wood as a recyclable resource.

Recently, we received feedback through discussions with investors, for example, "It seems that the felling and utilization of trees are misunderstood as unfavorable conducts," and "It would be favorable if DAIKEN CORPORATION could be introduced in a more understandable way as a company that contributes to carbon neutrality, featuring its commitment to the diverse use of wood." This feedback renewed our recognition of the importance of clarifying the significance of businesses that we had taken for granted and communicating it to shareholders, investors, customers, the entire industry, and other stakeholders.

Based on these ideas, we began to examine the commercialization of new wood materials to fully use domestic timber, which requires early utilization following the felling of the trees, by leveraging our technology. We have endeavored to reduce the use of natural lauan wood, for which protection has been urged because of concerns with regard to depletion. In the coming years, we intend to eliminate the use of natural lauan wood by commercializing these new materials. Although many issues need to be resolved, we will continuously endeavor to achieve a resolution by joining technology, ideas, and passion in our company and jointly creating value through cooperation with various stakeholders.

We will continue endeavoring to stay a company that contributes to society through these businesses. We sincerely ask for your continued support.

Group Corporate Philosophy	▶P3
Process of Creating Value	▶P15-16
Business Models and Strengths	▶P17-18
Risks, opportunities, and material issues (materiality)	▶P19-20
Pursuit of Sustainable Use of Wood Resources	▶P21-22