Interview with the CEO

We will continue to build a more resilient business portfolio that responds to the rapidly changing external environment and contributes to sustainable growth for the HOYA Group.

Eiichiro Ikeda

Director, Representative Executive Officer, President & CEO

Fiscal 2023 saw a mix of various positives and negatives, including the impact of the weak yen. Could you share your thoughts on the year from a management perspective? Were there any particular challenges you perceived throughout the year?

During the fiscal year ended March 31, 2024 (fiscal 2023), the Information Technology business saw sluggish performance in glass substrates for hard disk drives (HDDs) and mask blanks for semiconductors as a result of inventory adjustments in the supply chain. However, the Life Care business remained robust, offsetting the decline in the Information Technology business. The weakening yen also provided a positive exchange rate effect, leading to record-high sales revenue and profits. This demonstrates the value of business portfolio management, which aims to stabilize overall performance by balancing weaker areas with stronger ones. In the Information Technology business, which experienced a revenue decline, we managed to maintain profit margins by controlling costs flexibly and promptly. We believe this achievement underscores our focus on both profitability and efficiency.

On the other hand, the system disruption caused by the cyberattack on March 30, 2024, highlighted challenges in our cybersecurity. The incident caused temporary shutdowns in a wide range of systems, including manufacturing and order processing systems, across multiple business units. We sincerely apologize for the significant inconvenience this incident caused our customers and business partners, as well as the concern it raised among our shareholders and other stakeholders. This system disruption occurred at the end of the fiscal year and did not affect our performance for fiscal 2023, but is impacting sales revenue, primarily in the Life Care business, in fiscal 2024. While systems have since been restored and normal business activities resumed, we've undertaken a comprehensive review of our cybersecurity measures in response to the incident. Based on the outcomes of this review, we are completely revamping not only our firewalls and other similar tools but our entire IT security infrastructure. While it's not possible to achieve "100% IT security" due to the constantly evolving nature of cyberattack methods, we are committed to preventing future incidents by staying abreast of new security technologies and continuously investing in IT.

It seems that despite the varying market trends across different businesses and products, the Group has managed to maintain overall profitability, largely thanks to its business portfolio management. Could you elaborate on the features of the business portfolio management approach and the systems that support it? Additionally, considering future changes in the external environment, do you foresee any challenges in the current business portfolio or areas that may need strengthening going forward?

As I mentioned earlier, during fiscal 2023, the robust performance of the Life Care business offset the downturn in the Information Technology business, enabling the Group to achieve solid overall growth. On the other hand, during the COVID-19 pandemic, it was the exact opposite scenario—the Life Care business was hit hard by lockdowns and other restrictions, but strong demand in the Information Technology business driven by remote work and other factors stabilized things for the Group as a whole.

The macro environment is always changing, and with the recent rise in geopolitical risks, it has become even more important to diversify the regions, markets, and customers we engage with. This diversification, which takes account of both risks and opportunities, is crucial for stabilizing our business performance.

We have always adapted our business portfolio flexibly to changes in the external environment through the acquisition of new businesses and the sale of others. This survival-of-the-fittest management approach has allowed us to build a robust portfolio by retaining our strongest businesses. However, because markets and businesses go through life cycles from growth to maturity and eventually decline, it's crucial to identify which stage each business or product in our portfolio is at and allocate management resources accordingly. To continuously develop our business portfolio, we prioritize acquiring businesses with medium- to long-term growth potential as a key task for the CEO. We actively pursue both internal development and M&A opportunities to this end.

Our business portfolio comprises more than 10 divisions that, in principle, operate independently. However, in October 2022 we reorganized these divisions into three internal companies under the themes of Eye Health, MedTech, and IT. When I was a division head, I observed that there was little collaboration between the divisions, and I felt that combining our individual expertise could lead to new business opportunities. Based on this idea, we are now promoting business development beyond existing frameworks under the unified themes of these internal companies.

With this system in place, we are focusing our attention on eye health and high-tech as areas with significant potential for structural growth. In eye health, the global rise in myopia and the increasing number of cataract patients due to aging populations are becoming major social issues. We aim to actively identify growth opportunities, including in areas not covered by our existing product range. In high-tech, advanced computing and data analytics technologies underpin modern society. We are continuously exploring innovative business opportunities, particularly around the materials and components that support these technologies behind the scenes.

Last, could you share your thoughts on any other future prospects, key initiatives, points to note, or messages you'd like to convey?

To reiterate, in the two years following the COVID-19 pandemic, the Life Care business compensated for a downturn in the Information Technology business. However, as of September 2024, the situation has shifted significantly. Due to the system disruption and an economic slowdown in the Chinese market, growth in the Life Care business is expected to slow slightly in fiscal 2024. Conversely, the Information Technology business is anticipated to experience robust growth, driven by the recovery of inventory levels for extreme ultraviolet (EUV) mask blanks and glass substrates for HDDs.

Demand for EUV mask blanks has significantly increased, fueled by the development of next-generation nodes. While we expect heightened competition in the medium term, we aim to maintain our leading position and high market share in next-generation products. Regarding glass substrates for HDDs, the exponential increase in data generation, particularly that related to generative AI, underscores the growing importance of cost-competitive HDDs. With the normalization of supply chain inventory levels that occurred by the end of 2023, demand for glass substrates for HDDs in fiscal 2024 is expected to match the peak levels seen in fiscal 2021. In response to these developments, we are enhancing capacity in both businesses.

As demonstrated, while the performance of individual businesses may fluctuate, our business portfolio management is enabling continued, stable growth for the Group as a whole. We will continue to optimize our business portfolio to respond flexibly to the rapidly changing external environment and ensure sustainable growth for the Company. We sincerely appreciate the continued support and encouragement of all our shareholders, investors, and other stakeholders.

Interview with the CFO

When making various management decisions, I always try to think in numerical terms and strive to enhance corporate value.

Ryo Hirooka

Director, Representative Executive Officer & CFO

2024 marks your 12th year as CFO of the HOYA Group. What have you valued most in your role?

I make a wide variety of decisions in our daily business operations, and I try to think of everything in terms of numbers. I think it's essential for a CFO to look at things from the perspective of "What does this initiative mean for us in terms of numbers? Is it really going to contribute to enhancing our corporate value?" For instance, when I hear abstract terms like "strategic investment" used in management meetings, I see that as my cue to exercise caution and to further quantify exactly how this investment is going to increase corporate value for us.

Following the March 2023 recommendations by the Tokyo Stock Exchange, there has been a surge in activities aimed at improving capital efficiency among listed companies in Japan. This Company has prioritized capital efficiency in our management for over 20 years. What are we doing to improve it even further? Which key metrics are we focusing on?

Long before I became CFO, the Company already had a solid foundation, including a quarterly budget management system established by my predecessors. This has allowed us to improve capital efficiency in our daily operations in an organic way, without the need for any special measures. Rather than specific initiatives, I think it's more important to use rigorous financial metrics when making important decisions, for example. Our metrics are multifaceted, but the payback period for cash-based investments is one that we prioritize. Profitability is the cornerstone of our cash generation, making profit margin an essential metric. It does vary by business, but in our Life Care business, for instance, we use a profit margin of 20% as an implicit benchmark. Based on this benchmark, we consider the payback period on a cash flow basis, taking into account tax rates and other factors. Of course, some investments, like updating existing facilities, can be recouped quickly, while others, like M&A investments, may take longer. In any case, it's essential to make decisions on the premise of recovering the invested capital on each and every project. Maintaining cost awareness in our everyday business activities also aids in improving capital efficiency.

In addition to pursuing profitability and payback periods for each project, do you also consider methods such as increasing financial leverage to improve capital efficiency?

To be frank, I find little value in such technical maneuvers. While we are not averse to taking on debt, and borrowing to fund acquisitions that exceed our equity is certainly possible, such options should only be considered when there is a genuine opportunity for growth. In my view, altering our capital structure through financial leverage without a specific purpose is putting the cart before the horse. I intend to remain steadfast on this point going forward.

You mentioned capital structure. Our Company currently holds over 520 billion yen in cash and deposits. What do you see as being an appropriate level for our cash reserves, and how do you envision allocating future cash flows?

More than 80% of our cash and deposits are held in foreign currencies such as US dollars and euros. Due to yen’s recent depreciation, these amounts seem very large when converted back into yen. That said, we recognize that our current level of cash and deposits is quite substantial relative to our operational requirements, and we aim to prevent excessive accumulation. Regarding allocation, with our operating cash flow consistently exceeding 200 billion yen annually, we plan to allocate 50 to 60 billion yen for capital expenditure and about 40 billion yen for dividends, with the exact amounts depending on currency exchange trends. In the absence of M&As, our standard policy is to return the remaining funds to our shareholders through share buybacks.

From a CFO's perspective, what do you consider to be the main management challenges facing the Company?

Acquiring businesses with medium to long-term growth potential is a recognized challenge among our management team. There has been an increase in discussions about expanding our business domains, especially through M&As. Our existing businesses are highly profitable, and it’s exceedingly rare to find M&A opportunities that meet the payback period criteria for internal investments I mentioned earlier. Viewed in isolation, M&As can be seen as fundamentally diluting corporate value. These are complex issues with no clear-cut answers, but our approach is to seek out assets that can offer synergies with our existing operations, and where any negative impacts can be absorbed by the Group as a whole.

Last, could you describe the kind of CFO you aspire to be?

As a corporate executive, I value integrity. While it's perhaps human nature for self-interest to occasionally influence our thoughts, I always try to go back to the question “Will this benefit the Company?” when making decisions. I also try to avoid confining myself to traditional CFO responsibilities, but instead consider issues from a broader management perspective.

Interview with the CSO

Driving ESG initiatives forward to enhance corporate value

Tomoko Nakagawa
Executive Officer, Chief Sustainability (ESG) Officer (CSO)

Fiscal 2022 saw significant progress made, including our first TCFD (Task Force on Climate-Related Financial Disclosures) disclosure. In fiscal 2023, your second year as CSO, what were the key activities you focused on?

In my first year as CSO in fiscal 2022, we laid the groundwork for our ESG efforts by establishing an internal framework and implementing a system for Group-level environmental data collection.

In fiscal 2023, we focused on actually collecting environmental data, expanding the number of businesses covered by TCFD, calculating Scope 3 data, and preparing for the European CSRD (Corporate Sustainability Reporting Directive).

Due to the diversity of our products and services and the differing environments in which our businesses operate, our ESG challenges and priorities vary by division. To enrich ESG activities within each division, discussions were needed to identify their specific ESG issues and put in place relevant targets and effective measures. Consequently, fiscal 2023 was a year of building collaborative relationships with each division.

Additionally, to promote knowledge sharing across the HOYA Group and raise awareness of cross-divisional cooperation and Group-wide ESG activities, we launched the “ESG Awards.” These awards recognize ESG initiatives that contribute to enhancing corporate value for the entire Group. We received approximately 50 submissions showcasing various global initiatives. It was a source of immense pride to see how proactively involved our employees are in ESG activities, and it provided a wonderful opportunity for sharing best practices across the Group. It reaffirmed just how important ESG activities are to enhancing our resilience to the environmental changes affecting our businesses, and to improving the competitiveness of our Group companies. We plan to continue with these internal activities going forward.

For Scope 1 and Scope 2 CO_2 emission reductions, we are steadily pursuing strategies to achieve our interim targets of 60% renewable energy use and a 60% reduction in CO_2 emissions (compared to fiscal 2021) by fiscal 2030. Initiatives include installing solar panels on company buildings, reviewing our energy contracts, and procuring non-fossil certificates. As a result, our renewable energy ratio improved from 2% in fiscal 2022 to 14% in a single year. We will continue to advance our renewable energy adoption by exploring procurement methods in various countries and gathering the latest information.

On the other hand, Scope 3 remains a significant challenge. In fiscal 2023, we began calculating Scope 3 emissions company-wide, starting with the disclosure of major emission sources. Since the value chain varies by business, the trends, challenges, and countermeasures for Scope 3 emissions also differ. Moving forward, we need to address each business individually while also tackling issues common to all of them—specifically, expanding the calculation categories and engaging with suppliers to collect primary data and implement emission reduction activities, particularly for Category 1 (Purchased Goods and Services). Our goal is to advance our Scope 3 initiatives and aim for SBT (Science Based Target) certification, which targets a 1.5°C limit for global warming based on scientific evidence.

ESG covers a very broad range of areas. Among those, what particular challenges do you see at this current time?

As mentioned, understanding, disclosing, and setting reduction targets for Scope 3 emissions, along with obtaining SBT certification, is a major challenge in the Environmental agenda.

In the Social agenda, we introduced a global employee evaluation system in fiscal 2022, creating a common standard across the Group. After a year, we feel that the qualities and competencies we expect from employees are becoming well understood internally. Additionally, HR conducts ongoing employee engagement surveys, using the results to engage in dialogue with employees in each business unit and implement improvement measures to create a better workplace environment.

Diversity & Inclusion (D&I) is also crucial in enhancing corporate value. In particular, we recognize the need to increase the presence of women, including female engineers, in the Information Technology sector. We are considering initiatives such as talks by our female external directors with engineering experience to share their insights within the Company.

Promoting ESG requires considering not only this Company but the entire value chain, and that presents a major but vital challenge. Reducing Scope 3 emissions is part of that challenge, and we must also update our supply chain management to include human rights due diligence, given the global nature of our supply chain. We recently revised our Supplier Code of Conduct and must now implement initiatives to enhance its effectiveness. We need to move forward in a manner compliant with the European Corporate Sustainability Due Diligence Directive (CSDDD) as we evolve our current efforts.

Finally, could you sum up fiscal 2023 and share your outlook for the future?

Fiscal 2023 was a year where various disclosure frameworks for non-financial information were further developed and clarified. Moving forward, it will be essential to comply with international non-financial disclosure frameworks such as those from the ISSB (International Sustainability Standards Board) and the European CSRD. In preparation, we are currently reviewing and improving our internal information collection processes, controls, and IT systems. While building these processes is a significant challenge, enhancing our disclosures will provide an opportunity to increase transparency regarding our business activities, achievements, and initiatives, fostering better dialogue with our stakeholders. To underscore our Group's commitment to implementing this effectively, our Compensation Committee has increased the weighting of ESG targets from 10% to 25% within our long-term incentive evaluation criteria for executive officers. We have also incorporated non-financial KPIs into the compensation structure for business unit leaders responsible for implementing these initiatives. This will ensure ESG activities are integrated across management and operations to enhance corporate value. We sincerely appreciate the continued support of our stakeholders throughout this process.

[Special Feature] Interviews with Independent Directors:

Perspectives

Lead Independent Director
Chairperson of the Audit Committee, Member of the Nomination Committee, Member of the Compensation Committee, Member of the Healthcare Compliance Committee

Insights from Hiroaki Yoshihara

Q

In last year's Integrated Report, you commented that "it is most urgent for HOYA to create the businesses that will drive clear growth for the future." From your perspective as the lead independent director, how do you view the progress HOYA has made in creating and acquiring new businesses?

The Company's strategy for the growth of each of its businesses in the near future is very clear. Meanwhile, a roadmap for medium- to long-term growth strategies is being drawn up under the in-house-company structure introduced in October 2022. The Board of Directors are engaged in ongoing discussions and are verifying a strategy that balances profitability and growth over the medium to long term. This review is founded on a firm awareness of HOYA's management resources, such as its technological and production capabilities, human capital, and its positioning with the customers and markets it serves.

Independent Director
Chairperson of the Nomination Committee, Member of the Compensation Committee, Member of the Audit Committee, Member of the Healthcare Compliance Committee

Insights from Yasuyuki Abe

Q

I believe succession planning for the CEO and other key positions within the Company is an important point. From your perspective as Chairperson of the Nomination Committee, are there any issues you are aware of, including from the perspective of leadership development?

In my view, it is critical for the key members who will lead the future of HOYA to understand the history of the Company from its establishment in 1941 to today, as well as the current strengths of HOYA. On top of that, the Nomination Committee will provide advice on the development of human resources who can lead the company's growth in the future.

Independent Director
Member of the Nomination Committee, Member of the Compensation Committee, Member of the Audit Committee

Insights from Takayo Hasegawa

Q

I have heard that since you took office as CEO of SWCC Corporation, you have been promoting internal reforms using ROIC (return on invested capital) as a yardstick. How do you rate HOYA's management from the standpoint of efficiency?

I think it is very commendable that HOYA has a well-functioning business division system in terms of securing profits, and that it conducts business activities with a strong awareness of year-on-year growth by setting high profit margin targets. ROIC is also exceptionally high, and since most of the businesses are generating returns well above WACC (weighted average cost of capital), this metric does not appear to be suitable for HOYA. Although the Tokyo Stock Exchange has raised ROIC as a major indicator, I think it is critical to consider KPIs that match the characteristics of a company and its growth. As such, I believe that HOYA's method of adopting a hurdle rate is reasonable in light of its current business situation.

Independent Director
Chairperson of the Healthcare Compliance Committee, Member of the Nomination Committee, Member of the Compensation Committee, Member of the Audit Committee

Insights from Mika Nishimura

Q

Technological innovations in the field of health care, such as the deployment of robotics and AI, are underway. Given your extensive experience in the life science field, what are your expectations for the growth potential of HOYA's Life Care business?

In life sciences, medical devices are increasingly married to AI-based predictive or personalized algorithms to help clinicians optimize patient management. For HOYA, many of our life care devices are based on our unique optical technology. With such rich imaging data coupled with patient information, I can see a future where AI-based models will help identify who is at risk for further disease progression and create tailored solutions for each individual.

Independent Director
Chairperson of the Compensation Committee, Member of the Nomination Committee, Member of the Audit Committee

Insights from Mototsugu Sato

Q

It has been a year since you were appointed as an Independent Director of the Company. How would you evaluate HOYA's global business development reflecting back on your own global management experience?

The HOYA Group's business portfolio strategy is exhaustive, and its global businesses are optimally rolled out locally based on market needs. Also, decisions are made quickly and appropriately with sound delegation of authority. On the other hand, I would like to see the Company expand and develop management talent who can lead businesses and cross-functional functions from a Group perspective across business domains.