

CFO Message



Keeping Capital Costs Under Control to Achieve Our Goals, Epson 25 Renewed

Tatsuki Seki

Director, Managing Executive Officer
General Administrative Manager, Corporate Strategy and Management Control Division / Sustainability Promotion Office
CFO

Epson 25 Renewed presents a goal of future growth that emphasizes profitability, marking a departure from an excessive focus on revenue growth.

Accordingly, we have grouped our businesses into a growth area, mature area, and new area. In addition to executing strategies suited to each area, we will accelerate key environment, digital transformation, and co-creation strategies that span the areas. My role here is to ensure that we have the best possible financial strategy to support this effort.

New Performance Metrics to Keep Us On Course

To track the performance of investments under Epson 25 Renewed, we will use return on equity (ROE) as we have done in the past, but we will also use return on invested capital (ROIC). We once thought that inefficient investments were acceptable as long as they delivered revenue and profit. Recognizing our error, we now use ROIC to make sure we are spending our capital resources as efficiently as possible. Likewise, to track business performance over the medium and long term, we now use return on sales (ROS) instead of revenue. We stopped disclosing revenue because, given the uncertain business outlook, the assumptions underlying these forecasts could easily prove wrong. We consider a range of factors in addition to ROS, such as the performance and outlook in each business and whether we are on course to reach our goals. As announced in January 2021, we sold off our IC test handler business to Kanematsu. I doubt we could have made this decision if we had judged the business purely on revenue and profit. Keeping a close watch on capital efficiency will be particularly important for investments in co-creation (one of the key priorities).

Epson 25 Renewed sets the following goals for fiscal 2025: >11% ROIC, >13% ROE, and >10% ROS. These goals may seem daunting at first glance, but they are eminently achievable given that our existing investments are already bearing fruit. Key to success will be greater control over capital costs.

Consolidated Financial Targets	FY2020	FY2021	FY2023	FY2025
ROIC ¹	5.6%	6.4%	8% or more	11% or more
ROE ²	5.9%	8.5%	10% or more	13% or more
ROS ³	6.2%	6.5%	8% or more	10% or more

¹ ROIC = Profit for the year attributable to owners of the parent company / (equity attributable to owners of the parent company + interest-bearing liabilities)

² ROE = Profit for the year attributable to owners of the parent company / equity attributable to owners of the parent company
Equity attributable to owners of the parent company and interest-bearing liabilities are calculated using the average at the beginning and end of the period

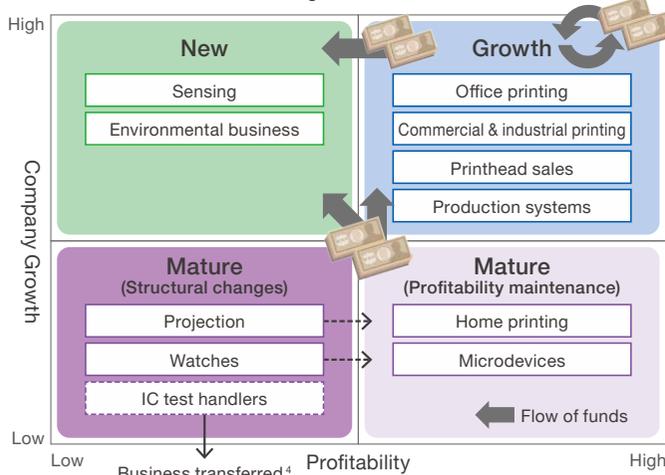
³ ROS = Business profit / revenue

CFO Message

Differentiated Investment Based on Contribution to Growth and Earnings

A key aim of Epson 25 Renewed is to improve capital efficiency. We do this by managing our business portfolio in a way that creates efficient capital circulation. We are no stranger to portfolio management, but until now we have only looked at the outcomes and fiscal viability of existing investments and the areas where spending is heavy. Since Epson 25 Renewed has given us a clearer idea of our financial priorities, we can now allocate capital in a more differentiated and targeted manner. Accordingly, we have grouped our businesses into the three areas based on growth and earnings. We prioritize spending on businesses in the new area that promise future growth and in the growth area. Meanwhile, we subject businesses in mature areas to a review to determine whether they are likely to deliver stable earnings or whether they need restructuring. Thus, in conjunction with the product lifecycle, we create a lifecycle for each business area by clarifying the position of the businesses, giving them the right budgets and goals, and then periodically reviewing them. We will consider, in addition to financial factors, business synergies and the social value the businesses produce. As well as tracking our overall ROIC, we will track business-specific ROIC to see how efficiently each business is performing. In this way, we are leveling-up portfolio management.

Efficient Fund Circulation Through Business Portfolio



Clarify the role/importance of business areas according to product life cycles

Final decision made by also considering factors such as synergies between businesses and social value

Allocate funds and set targets according to business priority

Setting Area-specific Goals to Improve Overall ROS

For each business area, we set goals appropriate to how the area is positioned.

In the growth area, we aim to expand the businesses by leveraging Epson's assets. For example, the businesses will switch from analog to digital and use our inkjet technology to innovate. We do aim to raise the revenue growth rate of these businesses (targeting a compound annual growth rate of >15%), but we will also consider profitability when allocating budgets.

In the mature area, we will track ROS as part of an effort to maintain or increase the profitability of these businesses. In home printing and microdevices, we have maintained our target of 15% ROS, as we expect steady growth in these businesses. For the projection and watch businesses, which require restructuring, we have set a target of >10% ROS. The watch business was hit somewhat by Covid, so it may take time to recover. The projection business has restored profitability thanks to progress in restructuring. We will keep making improvements in both businesses.

Our priority in the new area is to launch startups, and we have set a target of ¥10 billion. We particularly want to achieve our targets in the environmental category, one of the strategic priorities of Epson 25 Renewed.

Through these area-specific strategies, we hope to achieve a total ROS of >8% by fiscal 2023, and an ROS of >10% by fiscal 2025.

Direction of Business Operations and Targets

	FY2021-FY2023	from FY2025	Targets
Growth	<ul style="list-style-type: none"> Office printing Commercial & industrial printing Printhead sales Production systems 	Growth strategies	FY2020→FY2025 revenue CAGR +15% or more
Mature	<ul style="list-style-type: none"> Projection Watches 	Structural changes	FY2020→FY2025 ROS improvement +10 pt or more
	<ul style="list-style-type: none"> Home printing Microdevices 	Profitability maintenance & improvement	Sustained ROS of 15% or more
New	<ul style="list-style-type: none"> Sensing Environmental business 	Business launch	FY2025 revenue ¥10 billion or more
		Growth strategies	

Group ROS targets | FY2023 **8%** or more | | FY2025 **10%** or more |

⁴ Concluded a business transfer agreement with Kanematsu Corp. on Jan. 28, 2021

CFO Message

Continuous and Stable Shareholder Returns Alongside Targeted Investment in Future Growth

Regarding cash allocation, we have budgeted ¥320 billion in cash flows from operating activities for the three-year period starting fiscal 2021. Of this, we have earmarked ¥180 billion for growth capital expenditure. While prioritizing spending on the growth and new areas, we will also invest in environmental initiatives, in digital infrastructure for streamlining business processes and saving labor, and in an outward-looking digital transformation—which will include using analytics to enhance the customer experience. The amount of expenditure will be less than what we have spent in the past. We completed a large spending program last year, and we have now created a product platform for the commercial and industrial sectors, which are set to grow.

As for shareholder returns, we remain committed to delivering a continuous and stable dividend, while repurchasing shares when necessary. Our benchmark for consolidated dividend payout ratio is 40%. We have also earmarked ¥70 billion to bolster our financial structure. To navigate these uncertain times, we need a shareholders' equity ratio of at least 50%, and to raise this to 55% in the longer term. In strengthening financial condition, we will consider a range of factors, including our financing needs.

3-year cumulative (FY2021-23)

Billions of yen



Green Bond-funded Environmental Investments to Become Carbon Negative and Underground Resource⁵ Free

Environmental Vision 2050 (updated in March 2021) commits us to becoming carbon negative and underground resource free. As our cash allocation demonstrates, we are stepping up environmental initiatives. We will spend some ¥100 billion on these initiatives up to 2030. The initiatives include decarbonization, closed resource loop, and environmental technology development. To give an example, PaperLab uses Dry Fiber Technology to turn waste paper into new paper, but we want to use this technology to recycle paper into other materials too. In another example, we recently teamed up with Euglena and NEC to develop a biomass plastic called pararesin. Together with these partners, we founded Pararesin Japan Consortium to promote the biomass plastic.

As well as making our own production facilities sustainable, we want our products to achieve a high level of environmental performance. Accordingly, we have committed to ecologically sustainable finance. In July 2020, we issued our first green bond. We used some of the funds to top up our cash on hand, which we had spent on buildings and facilities covered in the green bond program. We also used some of the money to fund R&D and capital expenditure for inkjet printers. Almost all of our activities can be covered by green bonds. We will combine our efficient, compact and precision technologies with co-creation through open innovation to improve the environmental performance of our products and business activities and to reduce environmental impacts across the value chain.

⁵ Non-renewable resources such as oil and metals

Responding to TCFD Recommendations



Climate change is greatly impacting society and Epson sees it as a significant societal problem. The goal of the Paris Agreement is to achieve decarbonization and limit the global average temperature to well below 2°C above pre-industrial levels and try to limit the temperature increase to 1.5°C. To achieve this, Epson is working to reduce total emissions in line with a 1.5°C scenario¹ by 2030. Furthermore, Epson coordinated the revision of Environmental Vision 2050 with the announcement of the Epson 25 Renewed Corporate Vision. To attain our goals of becoming carbon negative and underground resource free² by 2050, we are working to decarbonize and to close the resource loop. We are also providing products and services that reduce environmental impacts and developing environmental technologies. Since Epson declared its support for the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) in October 2019, it has disclosed information (on governance, strategy, risk management, and metrics and targets) based on the TCFD framework so as to enable good communication with shareholders, investors, and a broad spectrum of other stakeholders. Epson has decided to disclose the level of financial impact in 2021 in a quantitative manner for the first time.

¹ Target for reducing greenhouse gas emissions aligned with the criteria under the Science Based Targets initiative (SBTi) ² Non-renewable resources such as oil and metals

Scenario Analysis Findings

We analyzed scenarios based on the TCFD framework to quantitatively assess the financial impact of climate-related risks and opportunities on Epson's strategy. In a 1.5°C scenario in which there is rapid decarbonization of society, we found that there is transitional risk of an increase in operating costs due to market changes, policies, and legislation, but we expect to limit the financial impact by strengthening products and services based on inkjet technology and paper recycling technology.

Epson will spend 100 billion yen over a period of 10 years ending in 2030 to accelerate decarbonization, close the resource loop, and develop environmental technology. The solution to climate-related risks aligns with the materialities we have set of achieving sustainability in a circular economy and advancing the frontiers of industry and will lead to opportunities for business expansion with Epson's low environmental impact products and services that save electricity and reduce waste. These products and services will help to mitigate customers' environmental impact and control climate change.

Based on the results of these analyses, Epson will continue to try to maximize its opportunities while addressing recognized risks in order to achieve decarbonization, which we believe is a rational goal both for society and for Epson.

On the other hand, even in a 4°C scenario in which global warming has advanced because the world failed to take additional measures, we found that the impact of physical risks on our domestic and overseas sites due to the damages arising from weather extremes would be small.

Main Climate Change Initiatives

FY2019

- Declared support for the TCFD recommendations
- Studied risks of natural disasters caused by climate change (2°C scenario and 4°C scenario)

FY2020

- Qualitatively disclosed the financial impact based on the disclosure recommendations of the TCFD framework (2°C scenario)
- Studied risks of natural disasters caused by climate change (1.5°C scenario)

FY2021

- Revised Environmental Vision 2050 and set clear objectives, including becoming carbon negative
- Quantitatively disclosed the financial impact based on the disclosure recommendations of the TCFD framework (1.5°C scenario)

Governance

Important matters related to climate change are supervised by the board of directors, which receives reports at least once a year after deliberations by the Sustainability Strategy Council, which formulates medium- to long-term strategy for the Epson Group's sustainability activities and reviews the status of implementation as the president's advisory body.

In addition, Seiko Epson's president and representative director, the individual who has the highest responsibility and authority for climate-related issues, delegates responsibility for climate-related issues to the Sustainability Director, who heads the Sustainability Promotion Office and manages and promotes climate change initiatives, including TCFD.

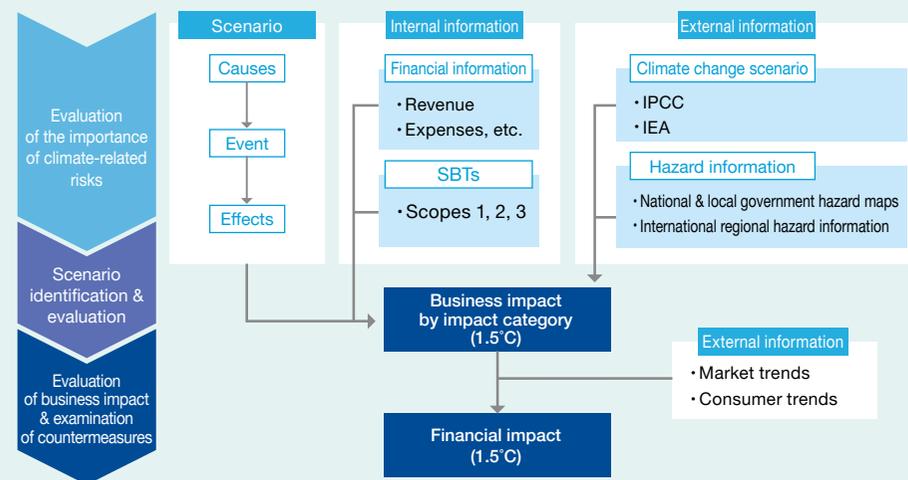


Responding to TCFD Recommendations

Strategy

Epson has determined that achieving sustainability in a circular economy and advancing the frontiers of industry are material matters in its value creation story. To achieve these, we will further reduce greenhouse gas (GHG) emissions by leveraging our efficient, compact, and precision technologies to drive innovation.

Scenario Analysis of Climate-Related Risks and Opportunities	Epson identified and evaluated scenarios in the categories of transition risk, physical risk, and opportunity to evaluate the importance of climate-related risks and opportunities. Six risks and opportunities were singled out for evaluation. We evaluated the business impact and financial impact of each on the basis of the scenarios corresponding to temperature increase of 1.5°C presented by the Intergovernmental Panel on Climate Change (IPCC) and the International Energy Agency (IEA) as well as on the basis of internal and external information. The results of the evaluation of climate-related risks and opportunities based on this scenario analysis are as follows:
---	---



Climate-Related Risks and Opportunities in a 1.5°C Scenario

The results of evaluating climate-related risks and opportunities based on scenario analysis are as follows.

Category		Evaluated risks & opportunities	Actualization	Business impacts			Financial impact
Transition risks	Market changes Policy & laws and regulations	<ul style="list-style-type: none"> Paper demand 	Short-term	Impact	<ul style="list-style-type: none"> We were unable to detect a strong relationship between climate change and the change in paper demand, but demand for printing and communication paper is assumed to be on a declining trend. Even if that shift to paperless advances further due to changes in trends due to COVID-19 (such as the contraction of office printing because of decentralization), we expect that the financial impact from the strengthening of products and services based on inkjet technology and paper recycling technology (reduction of printing costs, reduction of environmental impacts, increase of ease of printing, appeal using usefulness of paper information) will be limited. 		Small
		(Initiatives in Environmental Vision 2050) <ul style="list-style-type: none"> Decarbonization Closed resource loop Environmental technology development 	Short-term	Impact	<ul style="list-style-type: none"> "Decarbonization" of products and services as well as the supply chain and advanced initiatives in "resource recycling" are needed to respond to "climate change" and "resource depletion," which are social issues shared globally. Scientific and specific solutions are necessary to develop environmental technologies linked with the rapid decrease of environmental impacts. 	Response to risks <ul style="list-style-type: none"> Decarbonization <ul style="list-style-type: none"> Renewable energy use Supplier engagement Closed resource loop <ul style="list-style-type: none"> Effective use of resources Extend product service lives Environmental technology development <ul style="list-style-type: none"> Dry fiber technology applications Material recycling (metal, paper) Energy-saving facilities Carbon-free logistics Greenhouse gas removal Minimize production losses Naturally derived (plastic-free) materials CO₂ absorption technology 	Invest a total of approximately ¥100.0 billion by 2030
Physical risks	Acute	<ul style="list-style-type: none"> Damage to business sites due to floods, etc. 	Long-term	Impact	<ul style="list-style-type: none"> Based on the results of the latest FY2021 risk assessment for 36 sites (17 sites in Japan and 19 sites overseas), the changes in future operational risks due to flooding (rivers overflowing) and high tides are limited. Short-term climate change risks to the supply chain will be addressed in line with our business continuity plans. 		Small
	Chronic	<ul style="list-style-type: none"> Damage to business sites due to rising sea levels 					
Opportunities	Products and services	(Initiatives in "Environment Vision 2050") <ul style="list-style-type: none"> Customer environmental impact mitigation 	Short-term	Assumed scenarios	<ul style="list-style-type: none"> The need for environmentally friendly products and services will increase due to the introduction of a carbon tax, soaring electricity prices, rising waste disposal costs, sustainable production amounts, and reduced resource use. 	Business opportunities <ul style="list-style-type: none"> For the growth areas of "Epson 25 Renewed," a CAGR (compound annual growth rate) of 15% is expected for revenue growth by providing 1) office printing, commercial & industrial printing and printhead sales utilizing inkjet technology to achieve a reduction of environmental impacts, increased work productivity and reduction of printing costs and 2) production systems with expanded use of new production devices to achieve a reduction of environmental impacts. 	Large CAGR of 15% is expected in growth areas until 2025
		<ul style="list-style-type: none"> Environmental business 	Short-term	Assumed scenarios	<ul style="list-style-type: none"> Market growth is expected in the field of combatting global warming and the field of waste treatment and effective utilization of resources. Due to the shift to a circular economy, market growth is expected for recycled plastics, high-performance Bio-based plastic, Bio-based plastic and metal recycling. 	Business opportunities <ul style="list-style-type: none"> As effective solutions for combatting global warming and responding to the shift to a circular economy, generate revenue by upcycling (enhancing functionality), eliminating plastics (packing and molding materials), creating new high-value-added materials and carrying out other measures through the establishment of technologies, such as applications of dry fiber technology, including paper recycling, development of naturally derived materials (elimination of plastics) and recycling of raw materials (metal and paper recycling). 	Medium

Actualization Short term: ≤ 10 years Medium term: 10-50 years Long term: > 50 years **Financial Impact** Small: ≤ 1 billion yen Medium: 1-10 billion yen Large: >10 billion yen

Responding to TCFD Recommendations

Risk Management

As the environment in which we operate grows more complex and uncertain, effectively dealing with risks that could have a significant impact on corporate activities will be essential in order to carry out business strategies and business objectives.

Epson sees climate-related issues as risks that could significantly impact management and manages them appropriately.

Metrics and Targets

Under Environmental Vision 2050, in order to achieve the medium- and long-term greenhouse gas (GHG) emission reduction targets validated by the Science Based Targets initiative (SBTi), we are actively working to reduce environmental impacts throughout the value chain. We are doing so primarily by improving the environmental performance of our products, utilizing renewable energy, and enhancing our business activities, based on our efficient, compact, and precision technologies.

The current targets validated by the SBTi correspond to the 2°C target. In FY2021, we plan to update the reduction targets to those that correspond to the 1.5°C target, which is the target in Environmental Vision 2050.

Climate-Related Risk Identification, Assessment and Management Process

1. Study	2. Identify & assess	3. Manage
<ul style="list-style-type: none"> Study risks of natural disasters caused by climate change at major sites worldwide. Research social trends. 	<ul style="list-style-type: none"> Identify risks and opportunities from the policies and actions of Epson 25 Renewed and Environmental Vision 2050. Evaluate scenario analysis through the Sustainability Strategy Council and board of directors. 	<ul style="list-style-type: none"> Effectively manage risks through the Sustainability Strategy Council and the board of directors.



GHG Reduction Targets (reduction targets in line with "SBT 1.5°C Scenario")

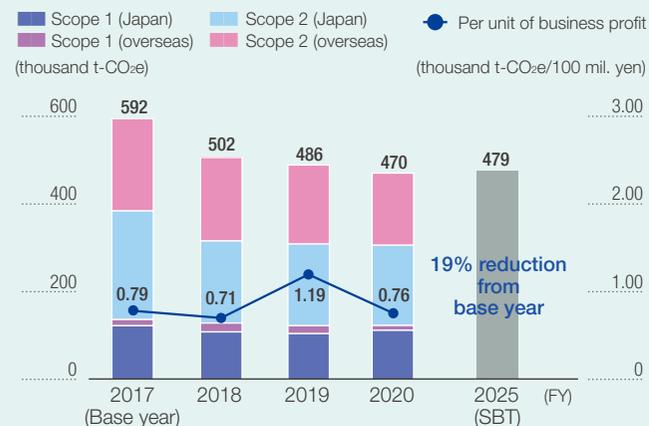
Scopes 1, 2, 3	Reduce GHG emissions by 55% compared to FY2017 by FY2030.
----------------	---

Scope 1: Direct emissions from the use of fuel, etc., by the reporting company

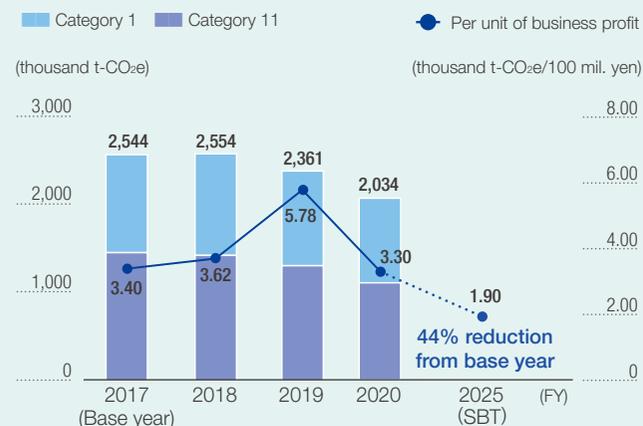
Scope 2: Indirect emissions from purchased energy

Scope 3: Emissions from the reporting company's value chain

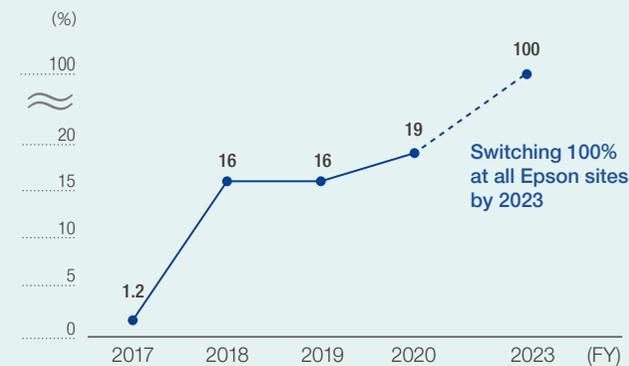
GHG Emissions (Scopes 1 & 2)³



GHG Emission (Scope 3: Categories 1 & 11)



Rate of Renewable Electricity Use (on an Electricity Basis)



³ CO₂ conversion factor of greenhouse gas emissions

• Electric power: In Japan, we use the adjusted emissions factors for the load serving entities (i.e., utilities) from which our sites purchase electricity, pursuant to Load Serving Entity Emission Factors announced by the Ministry of Environment and the Ministry of Economy, Trade and Industry. Overseas, we use the country emission factors listed in IEA (International Energy Agency) or from the load serving entities from which our sites purchase electricity. • Fuel: The factors announced by the IPCC in 2006 were used for both domestic and overseas data.

• GHGs other than CO₂: Equivalent values were calculated based on 100-year GWP values in the Fifth Assessment Report of the IPCC.