May 10, 2023

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Representative:	Hiroyasu Naito, President
Stock Code:	5947
Listings:	Tokyo Stock Exchange, Prime Market Nagoya Stock Exchange, Premier Market
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FOR IMMEDIATE RELEASE

Notice Regarding Opinions of the Corporation’s Board of Directors on the Shareholder Proposals

We, Rinnai Corporation (hereinafter, “Rinnai” or the “Corporation”) received a document from LONGCHAMP SICAV (hereinafter, “Proposing Shareholder”), a shareholder of Rinnai Corporation, seeking to make shareholder proposals (hereinafter, “Shareholder Proposals”) at the 73rd Ordinary General Meeting of Shareholders scheduled for June 29, 2023 (hereinafter, “General Meeting of Shareholders”), and we have been reviewing the contents of those proposals. As a result, we hereby announce that its meeting held today, the Board of Directors has resolved to oppose the Shareholder Proposals.

Details

I. Description of and Reasons for Shareholder Proposal

1. Proposed Agenda
(1) Implementation of Share Buyback
(2) Amendments to the Articles of Incorporation Concerning Handling Shares Held by Directors
(3) Amendments to the Articles of Incorporation Concerning the Composition of Outside Directors

2. Outline of and Reasons for Proposal
The details of the Shareholder Proposals are described in the attached “Details of the Shareholder Proposal.”

This attachment contains the relevant portions of the Shareholder Proposal submitted by the Proposing Shareholder in the original text.

II. Opinions of the Board of Directors on the Shareholder Proposals

Shareholder Proposal 1. "(1) Implementation of Share Buyback"

(1) Opinion of the Board of Directors
The Board of Directors opposes this Shareholder Proposal.

(2) Reasons for opposition
We have formulated a medium-term business plan, New ERA 2025 (hereinafter, "Plan"), which covers the period from fiscal 2022 to 2026 (April 1, 2021–March 31, 2026). Under the plan, we are making steady progress toward "Advancement in addressing social challenges" through "Expansion of business scale," and "Revolution of corporate structure."

During the five-year period of the Plan, we plan to make investments totaling ¥205 billion, which is much more than we invested in the previous five years. As necessary investments to achieve the financial targets of the plan, we have made steady investments to build the Kasugai Logistics Center and expand local production capacity in the United States and China. We also view the period covered by the Plan as an important period of change in our business environment. Therefore, we have positioned it as a key period for ensuring our business survival and competitiveness from a long-term perspective by investing funds to become carbon neutral, address digital transformation (DX), and respond to changes in consumer lifestyles. In April 2023, for example, we acquired land and a building in Minami Aoyama, Tokyo to strengthen our consumer contact points. As a result, cumulative capital investments have reached ¥49.2 billion in the first two years of the Plan (ended March 2023), and we plan to make capital investments of a further ¥50 billion in the current fiscal year (ending March 2024). We will continue aggressively making necessary investments with a view to improving corporate value over the medium and long terms.

We also consider shareholder return to be an important management issue. When we drafted the Plan, we set a shareholder return policy that calls for at least ¥60 billion in total return (dividends and share buybacks) over the five-year period of the Plan and a five-year average total return ratio of 40% or higher. Under this policy, we paid annual dividends of ¥140.00 per share in the fiscal year ended March 2022, up ¥15.00 year on year, and ¥160.00 per share in the year ended March 2023, up ¥20.00. We also conducted share buybacks worth ¥17.4 billion in the year ended March 2022 and ¥10.0 billion in the year ended March 2023. As a result, cumulative shareholder returns for the first two years of the Plan (April 2021–March 2023) amounted to ¥42.2 billion, and the total return ratio reached 84.7%, far exceeding the target under the shareholder return policy stated in the Plan.

On May 10, 2023, we announced its new capital policy. Under the new policy, we added ROE as a performance indicator. We aim to achieve an ROE target of 8% for fiscal 2026 (ending March 2026) and target further improvements during the period of the next medium-term business plan. In addition, we decided to raise the dividend payout ratio in stages (to 40% level in fiscal 2026), in order to further strengthen shareholder return. Our basic policy for improving ROE is to target "sustainable medium- to long-term profit growth." Under this policy, we will achieve by strengthening our earning power to deliver steady profit growth and gradually raising the dividend payout ratio, while enhancing efficiency through flexible share buybacks, targeting ROE of 8% in fiscal 2026. Based on this new capital policy, the Board of Directors decided on May 10, 2023, to conduct a share buyback of ¥10 billion (maximum) and cancel the shares bought back.

With respect to cash requirements, our approach is to increase shareholder returns while maintaining a financial base that enables us to fulfill our responsibility to handle daily necessities while providing the funding flexibility to ensure that we do not miss opportunities for M&As and capital alliances, and placing top priority on investments in future growth and making strategic expenditures.

We acknowledge that conducting a large share buyback as suggested in the Shareholder Proposal will improve ROE. However, this alone will not result in medium- to long-term improvements in corporate value and may distort our financial base and constrain investment activities aimed at sustainable growth. We believe maintaining a good balance between steady profit growth—by further strengthening our earning power—and shareholder return is important to enhance corporate value. Accordingly, rather than conducting a share buyback at the time or in the amount stipulated in the Shareholder Proposal, we believe it is appropriate, under our Plan and capital policy, to conduct share buybacks in the manner that takes into account overall conditions surrounding the Corporation, including business performance, business investments, financial position, and share price.

Therefore, the Board of Directors opposes this Shareholder Proposal.

Shareholder Proposal 2. "(2) Amendments to the Articles of Incorporation Concerning Handling Shares Held by Directors"

(1) Opinion of the Board of Directors
The Board of Directors opposes this Shareholder Proposal.

(2) Reasons for opposition
We have established a policy on determining compensation for directors under the basic principle of fostering steady improvements in medium- to long-term corporate value while ensuring sufficient transparency and objectivity for the Corporation to fulfill its obligations to shareholders and other stakeholders.

Compensation for directors (excluding outside directors) consists of basic compensation, which is fixed, and performance-linked compensation, with the ratio of fixed to performance-linked compensation set at around 70:30. Our aim here is to properly motivate directors to improve corporate value and achieve targeted goals. Performance-linked compensation consists of an annual bonus (intended to encourage the achievement of solid performance targets for each fiscal year) and restricted shares (intended to steadily increase corporate value and share common interests with shareholders through medium- to long-term share ownership). The ratio of annual bonus to restricted shares is set at around 20:10. We have introduced a similar system for executive officers, who we regard as a pool of candidates for future internal directors, so that they, along with directors, can work to continuously enhance corporate value.

In addition, we established the Compensation Advisory Committee, the majority of whose members are independent outside directors. The Board of Directors determines compensation and other policies after deliberation by the Compensation Advisory Committee, thereby ensuring objectivity and transparency in compensation. In the decision-making process, we also verify the appropriateness of compensation by continuously reviewing compensation levels and composition ratios through objective comparisons with other corporate groups of similar size to the Rinnai Group. On the other hand, compensation for outside directors is limited to fixed basic compensation only, with the aim of encouraging such directors to properly fulfill their duty to supervise and give advice to management from a position independent of executive management.

As of March 31, 2023, the Chairman and President of the Corporation already held approximately 7.36 million and 1.53 million shares, respectively, of the Corporation's stock (after the stock split). Therefore, they have a similar viewpoint as shareholders with respect to seeking medium- to long-term improvement in corporate value.

As stated above, Board of Directors has decided that the current compensation ratio, which is determined by the Board of Directors after deliberation by the Compensation Advisory Committee, ensures objectivity and transparency. With respect to compensation ratios, the Board also believes the Corporation has proper mechanisms in place to ensure that its management team and its shareholders possess shared values. On the other hand, the Shareholder Proposal requests establishment of stock ownership guidelines without specifying the specifics of such guidelines, and thus lacks substance. Under the current compensation system for directors, we have determined that there is no need to stipulate in the Articles of Incorporation the establishment of guidelines that specifically provide only for stock compensation.

Therefore, the Board of Directors opposes this Shareholder Proposal.

Shareholder Proposal 3. "(3) Amendment to the Articles of Incorporation Concerning the Composition of Outside Directors"

(1) Opinion of the Board of Directors of the Company
<u>The Board of Directors opposes this Shareholder Proposal.</u>

(2) Reasons for opposition
The Corporation established the Nominating Advisory Committee, the majority of whose members are independent outside directors, as an advisory body to the Board of Directors for the purpose of further ensuring objectivity and transparency in the selection of directors. Selection of candidates for the Board of Directors is decided by the Board of Directors after deliberation by the Nominating Advisory Committee, and the same decision-making process is used for director candidates to be presented at this General Meeting of Shareholders.

The Nominating Advisory Committee discusses the composition of the Board of Directors, making sure to include members with skills that benefit the oversight function to ensure sustainable enhancement of corporate value. These include members with skills in corporate management, global management, human resources strategy, governance/legal matters, and sustainability/ESG. The Board of Directors, constituted according to this approach, has always engaged in constructive discussions aimed at implementing the Corporation's management philosophy and sustainably enhancing its corporate value. The Board also emphasizes a balance between investments in R&D and human resources and capital expenditures, as well as returning profits to shareholders.

In addition, the composition of the Board of Directors proposed by the Corporation at this General Meeting of Shareholders has a total of nine directors, of whom four are independent outside directors, with the aim of strengthening the Board's supervisory function and management policy formulation function.

All of the five candidates for the Board of Directors (excluding independent outside directors) are familiar with the Corporation's business and have diverse skills, with knowledge and experience in technology (development/production/environmental), business plans/marketing, finance/accounting/capital policy, and human resources strategy, respectively. We also plan to propose the appointment of four independent outside directors, including one female, at this General Meeting of Shareholders, ensuring that outside directors are independent as well as diverse. Specifically, Mr. Hideyuki Shiraki, a new candidate for director, has special expertise in business plans/marketing, and Mr. Kazuto Inoue has solid management experience in the field of technology (development/production/environmental). Meanwhile, Mr. Tadashi Ogura, a new candidate for independent outside director, has special expertise in corporate management and governance/legal matters, and Ms. Yoko Dochi has deep insights especially in the fields of finance/accounting/capital policy and sustainability/ESG. We believe that having these candidates participate in management will further strengthen the functions of our Board of Directors.

As described above, the Board of Directors, consisting of directors proposed by the Corporation, maintains a sufficient degree of independence. We believe that the composition of the Board is optimal and diverse with respect to supervising the execution of management to achieve the targets of the Plan and thus sustainably enhance our corporate value. This will benefit all shareholders.

On the other hand, the provision in the Articles of Incorporation stipulated in the Shareholder Proposal may limit the selection range of director candidates and hinder our ability to consider and form an optimal Board of Directors at some point in the future.

Therefore, the Board of Directors opposes this Shareholder Proposal.

Reference: Skills Matrix of Director Candidates Proposed by the Corporation

【Areas particularly expected of the relevant directors】

Name *Newly appointed	Current Title	Expertise and Knowledge for Corporate Management								
		Corporate management	Global management	Technology (development/ production/ environmental)	Business plans/Marketing	Finance/ Accounting/ Capital policy	Human resources strategy	Governance/ Legal matters	Sustainability/ ESG	IT/DX
Kenji Hayashi	Representative Director Chairman	●	●	—	—	●	●	●	—	—
Hiroyasu Naito	Representative Director President and Executive Officer	●	●	●	—	●	—	—	●	—
Tsunenori Narita	Representative Director Executive Vice President	●	—	●	●	—	●	—	—	—
Hideyuki Shiraki *	Senior Managing Executive Officer General Manager of Marketing & Sales Headquarters	—	—	—	●	—	●	—	—	●
Kazuto Inoue *	Senior Managing Executive Officer General Manager of Production Engineering Headquarter	—	●	●	—	—	—	—	—	●
Nobuyuki Matsui	Outside Director	—	—	●	—	—	●	●	—	●
Takashi Kamio	Outside Director	●	●	—	●	—	—	●	—	—
Tadashi Ogura *	—	●	—	●	—	—	●	●	—	—
Yoko Dochi *	—	—	●	—	—	●	—	—	●	—

Note: The above table does not represent all of the candidates' knowledge and experience.

(Attachment: “Details of the Shareholder Proposal”)
*The relevant portion of the Shareholder Proposal Document submitted by the Proposing Shareholder is provided here in its original text.

I. Proposed Agenda
1. Implementation of Share Buyback
2. Amendments to the Articles of Incorporation concerning Handling Shares Held by Directors
3. Amendments to the Articles of Incorporation concerning the Composition of Outside Directors

II. Outline of Proposal and Reasons for Proposal
1. Implementation of Share Buyback
(1) Outline of Proposal
1. Share Buyback: The Company shall, in accordance with Article 156, Paragraph 1 of the Companies Act, acquire its own common shares through the delivery of monies, with a limit on total number of shares of 15,000,000 and a total acquisition price of ¥50,000,000,000 within one year from the conclusion of the AGM.
2. Other Retained Earnings: The Company shall withdraw ¥50,000,000,000 from general reserve and transfer the same amount to retained earnings brought forward.

(2) Reasons for Proposal
In recent years, the Company has steadily implemented measures such as expanding into overseas markets, increasing the ratio of high value-added products, and reducing costs. As a result, the Company’s sales doubled and operating income tripled in the past 20 years, and its ROIC (“Return on Invested Capital”), which is considered a measure of business competence, dramatically improved. Additionally, the Company was quick to recognize changes in the external environment and launched a hybrid water heater which uses both gas and electricity in 2010, a market that is expected to grow in earnest in the future. Also, the Company has already developed the world's first hydrogen water heater last year, which is expected to be needed by society in the future.

On the other hand, despite the company's remarkable growth, PBR (“Price to Book Ratio”), an indicator of the capital market's evaluation of companies, was 1.3 times in 2006, when the current top management took over, and remained at the same level as of March 31, 2023. Also, compared to competitors in the water heater industry in the United States and Europe, the Company’s PBR is far lower (i.e., undervalued). The main reason is that ROE (“Return on Equity”), which is highly correlated with PBR, has been stagnant as capital efficiency has declined due to the continuous accumulation of underutilized financial assets. In fact, the Company's average ROE over the last five years is 7.1%, excluding the fiscal year ended March 2021, when there was a stay-at-home demand due to the Covid pandemic.

“The Ito Review” published in 2014 by the Ministry of Economy, Trade and Industry notes that “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”. In our April 2022 public presentation, we stated that the Company’s current capital policy assumes an excessive level of required cash (ie., a majority of net assets) and is designed to cover all funding needs with shareholders' equity, while there are alternative funding methods with less than 1% funding costs, and that the management needs to revise such a capital policy to run the company with an awareness of the cost of capital.

Considering the nature of the Company's business and its capabilities, we believe that it is quite possible to set a minimum ROE target of 12% and aim for 15% to 20% in the medium to long term. We believe that the Company's commitment to ROE targets, after a fundamental review of its current capital policy, including revisiting the level of required cash, will contribute to enhancing the Company's corporate value. We propose that the Company, as part of the above process, implement a share buyback which can be implemented immediately, as long as its share price remains at a cheap level.

2. Amendments to the Articles of Incorporation concerning Handling Shares Held by Directors

(1) Outline of Proposal

Article 12 of the Company's Articles of Incorporation is hereby amended as follows to provide for the handling of shares held by the Company's directors.

（Underlines indicate amendments.）

Before change	After change
（Share Handling Regulations） Article 12. The handling and handling fees of shares of the Company shall be governed by the Share Handling Regulations established by the board of directors, in addition to laws and regulations or these Articles of Incorporation. <u>2 （Addition）</u>	（Share Handling Regulations） Article 12. The handling and handling fees of shares of the Company shall be governed by the Share Handling Regulations established by the board of directors, in addition to laws and regulations or these Articles of Incorporation. <u>2 The handling of shares held by directors shall be in accordance with the shareholding guidelines established by the board of directors.</u>

(2) Reasons for Proposal

We believe that the greatest weakness of Japanese boards of directors lies in the small number of shares held by each director and the resulting lack of a shareholder perspective. At the Company, with the exception of those from the founding family, the majority of directors' economic benefits are tied to base remuneration and short-term performance, which we believe is insufficiently correlated with medium- to long-term corporate value improvement.

In the United States and Europe, almost all major listed companies have adopted shareholding guidelines that stipulate a certain amount of shares that are considered necessary to share value with shareholders, as well as a requirement for continued shareholding for a certain period of time. After a grace period of several years, in most cases, top management team members are required to hold 3 to 5 times their base compensation in shares, and outside directors are required to hold shares equivalent to their base compensation.

We propose that the board of directors and other managers of the Company not be bound by the norms of the past, but instead aim for a level of ownership that is no less than world class, and demonstrate that commitment through appropriate disclosure. Therefore, we propose that the Company establish stock ownership guidelines.

3. Amendments to the Articles of Incorporation concerning the Composition of Outside Directors

(1) Outline of Proposal

Article 19 of the Company's Articles of Incorporation shall be amended as follows so that the majority of the directors of the Company are outside directors.

（Underlines indicate amendments.）

Before change	After change
（Share Handling Regulations） Article 19. The number of directors of the Company shall be 10 or less. 2 （Addition）	（Share Handling Regulations） Article 19. The number of directors of the Company shall be 10 or less. 2 As long as the company remains a listed company, the majority of the directors of the company shall be outside directors defined according to Article 2, Paragraph 1, Item 15 of the Companies Act.

(2) Reasons for Proposal

While we appreciate the Company's current effort to expand the number of outside directors, we believe that a more independent and diverse board of directors will help the Company, whose founding family has a strong influence, to reduce governance risk over the next 10 to 20 years and increase the company's resilience.

A diverse board means a board that is able to make management decisions based on a wide range of perspectives, such as skills, experience, age, nationality, and gender, while an independent board means a board comprising at least a majority of independent directors. The required elements of "diversity" vary from company to company. However, we believe that a universal and urgent agenda should be for boards to “include women and highly skilled investors and analysts”.

Principle 4.8 of the Corporate Governance Code states, “Independent directors should fulfill their roles and responsibilities with the aim of contributing to sustainable growth of companies and increasing corporate value over the mid-to long-term. Companies listed on the Prime Market should therefore appoint at least one-third of their directors as independent directors (two directors if listed on other markets) that sufficiently have such qualities. Irrespective of the above, if a company listed on the Prime Market believes it needs to appoint the majority of directors (at least one-third of directors if listed on other markets) as independent directors based on a broad consideration of factors such as the industry, company size, business characteristics, organizational structure and circumstances surrounding the company, it should appoint a sufficient number of independent directors”.

The Company is one of Japan’s leading comprehensive makers of heating equipment. We expect the Company to be a role model of corporate governance in the capital market as well.