Strategic Capital

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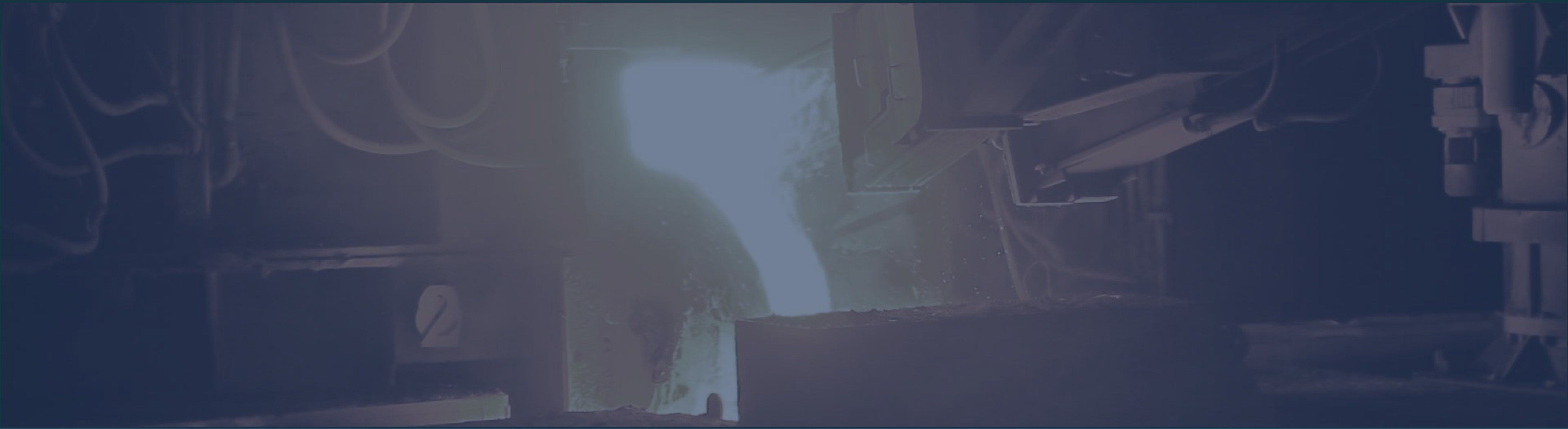


Proposal for Osaka Steel Co., Ltd (5449) to strengthen shareholder value

Disclaimer

Last updated May 1, 2025

Executive Summary

Strategic Capital, Inc.'s (SC) goal is to unlock enterprise and shareholder value through dialogue with the company management team and the exercise of shareholder rights.

SC and the funds managed by our company are shareholders of Osaka Steel Co., Ltd. ("Osaka Steel or the Company"). In order to increase shareholder value, we have submitted the following proposals to Osaka Steel by exercising our right to make a shareholder proposal

i. Set the shareholder return policy to 8% DOE

ii. Establish a Shareholder Value Enhancement and Privatization Review Committee

iii. Make the majority of Directors outside Directors

Background of proposal

Both the Company and its parent, Nippon Steel Corp. ("Nippon Steel"), are both publicly listed and exist as a **parent-child listing**. The Company has **contributed to Nippon Steels profits by providing deposits and loans (hereinafter referred to as "CMS") and used as an *amakudari** destination for Nippon Steel executives**, and it is clear that a **conflict-of-interest risk exists between the controlling shareholder and ordinary shareholders**.

SC believes that it is in the **best interest of the minority shareholders of the Company for Nippon Steel to make the Company a wholly-owned subsidiary or privatize through an absorption-type merger**, but the Company and Nippon Steel are adamant about maintaining the listing without regard for the interests of minority shareholders.

For more than 15 years, PBR has never exceeded 1x PBR, the dissolution value. If the Company is adamant that it should remain listed, then it should **take steps to increase PBR above 1x soon as possible and at the same time establish a governance system to protect the interest of minority shareholders**. To achieve this, we are making the following shareholder proposals.

* amakudari – (天下り,literally "descent from heaven"), similar to the revolving door metaphor, is the institutionalized practice where Japanese senior bureaucrats, executives descend to high-profile positions in the private and public sectors

Details of the proposals

Prolonged stock price slump and need for management reform → Set the shareholder return policy to 8% DOE *(FSP 1)*

The stock price has not exceeded 1x PBR since 2008 and as of March 31, 2025, was extremely undervalued at only 0.72x.

On January 31, 2025, the Company announced its medium-term management plan regarding the "Action to Implement Management that is Conscious of Cost of Capital and Stock Price". However, on the day of the announcement, the stock price fell -13.7%, the biggest drop since 2001 and it is clear that the plan was not well received by investors.

The main reason for the sluggish stock price is that ROE is significantly lower than the cost of capital and the MTBP is not expected to resolve this. Therefore, in order to improve ROE by reducing the excessive shareholders' equity, and reducing the cost of capital by strengthening investor confidence in Osaka Steel, we propose that the Company adopt a shareholder return policy of 8% DOE.

Details cont'd

Obsession with maintaining listing and neglecting interest of minority shareholders→ Establish a Shareholder Value Enhancement and Privatization Review Committee *(FSP 2)*

The Company has a low ratio of tradable shares and there is a possibility that it will breach the delisting criteria of the TSE Standard Market. We believe it is in the best interest of the minority shareholder for Nippon Steel to privatize Osaka Steel and have requested an opportunity for a three-way dialogue to discuss between SC, the Company and Nippon Steel.

However, the Company insists on maintaining its listing and on January 31, 2025, announced it would buy back some shares held by Nippon Steel and cancel the shares (on April 8, subsequently announced a postponement in cancelling the shares). It would also duplicate its listing on the Fukuoka Stock Exchange which has less stringent criteria for maintaining listing.

As a result, the stock price plummeted greatly impairing shareholder value. Maintaining the listing is from a desire to prioritize the interests of the group, and there is concern that decisions that completely disregard minority shareholders interests will continue. As such, we propose establishing a committee composed of outside directors to consider measures to improve shareholder value including privatization independent of the Board.

Effectively a revolving door for Nippon Steel→ Make the majority of Directors outside Directors *(FSP 3)*

As of March 2024, the five full time directors of the Company's eight-member board came from Nippon Steel effectively making it a revolving door.

The directors have contributed to Nippon Steel's funding through the CMS and other means and continued to undermine the Company's own shareholder value. It is clear there is a conflict of interest between the controlling and general shareholders, so we propose that the majority be outside directors to strengthen governance.

What's New

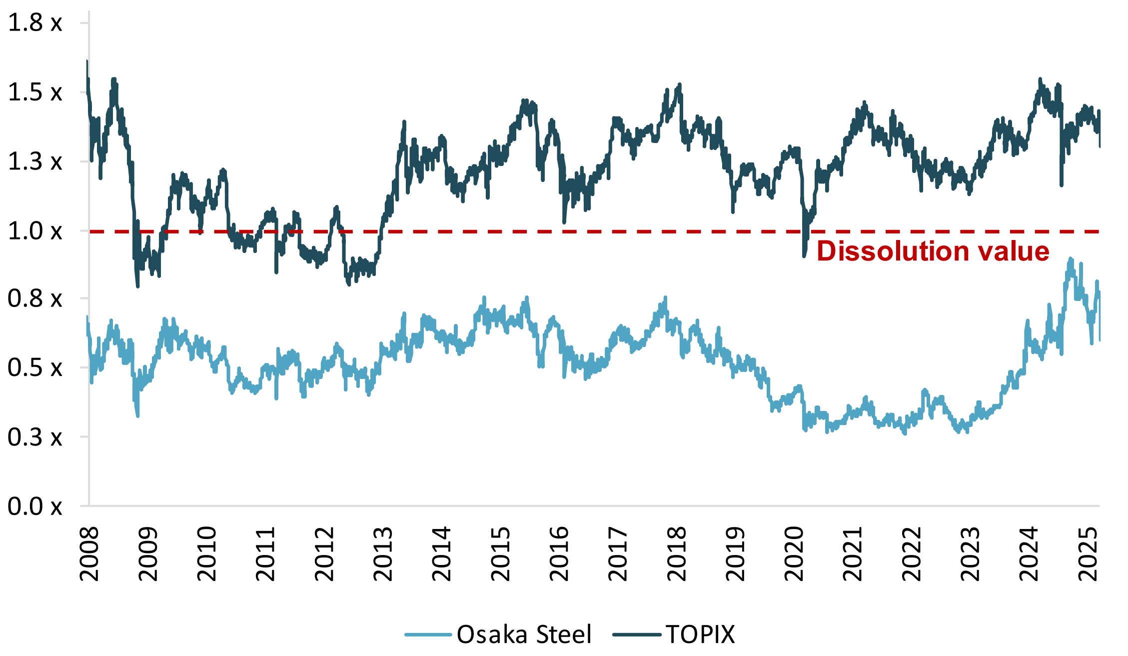
04.17.2025

Submitted Formal Shareholder Proposal to the Company

Market capitalization that can’t exceed 1x PBR

Since 2008, Osaka Steel’s stock valuation has **stagnated below 1x PBR**. As of March 31, 2025 the **PBR is 0.72x, substantially lower than the TOPIX at 1.35x** The stock price valuation clearly shows that the Company’s management policy has been damaging the interests of its shareholders and a fundamental change in management and capital policy is necessary to increase shareholder value.

PBR

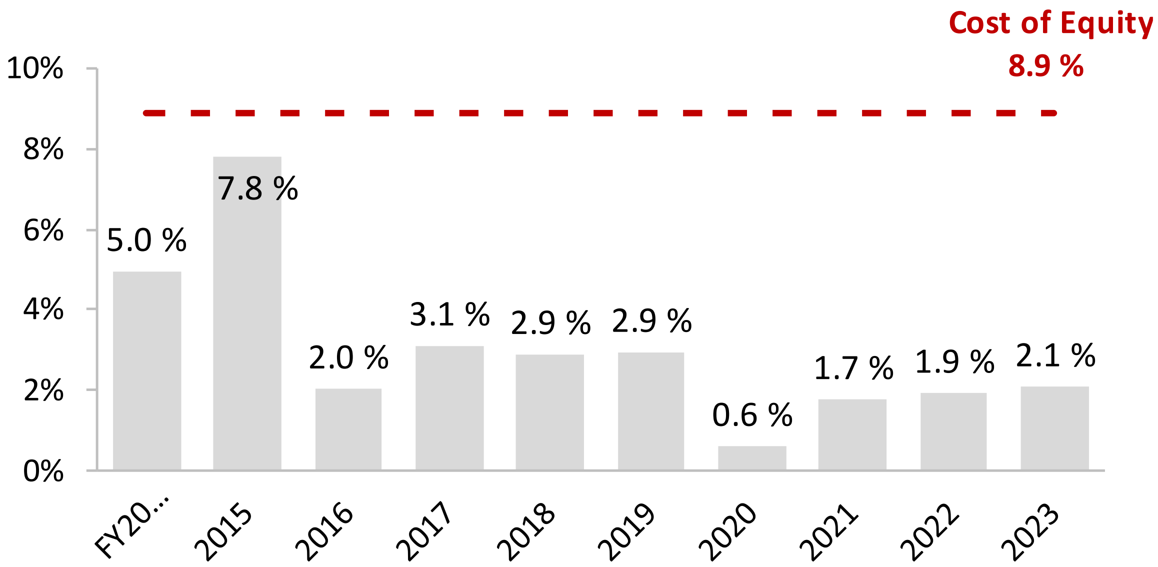


Data Source: QUICK Workstation （Astra Manager）

Capital efficiency below cost of capital

The main reason why the PBR has lagged below 1x is the ROE is less than **Cost of Equity (COE), which we estimate to be around 8.9%,** (as of March 31,2025, Bloomberg and Quick put the cost of equity at around 8.1% and 9.8% respectively) and ROE continues to remain below the level. **The ROE target in the MTBP is only 5% over three years so even if this target is achieved the PBR will remain below 1x.**

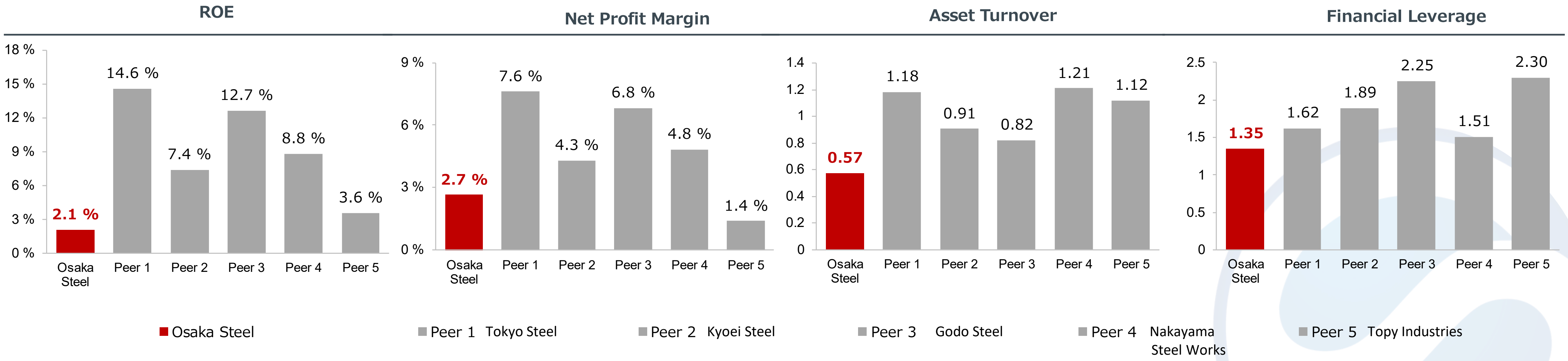
ROE and Cost of Equity



Data Source: QUICK Workstation（Astra Manager）

Capital efficiency far below peers due to CMS and other factors

Comparing ROE components (DuPont analysis) with industry peers, **Osaka Steel is among the lowest in all categories**. In addition to low profit margins, **asset turnover and financial leverage remain low compared to peers**. In order to improve ROE, in addition to improving the profit margin, the Company needs to **aim for an asset-light balance sheet and use interest-bearing debt**.



Data Source: QUICK Workstation （Astra Manager）

Disappointing mid-term business plan

When the MTBP was announced on January 31, 2025, the share price fell by 13.7%, the biggest drop since 2001. This can partially be attributed to lower expectations of an end to the parent-child listing as a result of a simultaneous announcement of a share buyback from Nippon Steel but the very least, it was clear that the MTBP was not well received.

The TSE pointed out the misalignment with investor and corporate management perspectives when looking at responses to the request for "Action to Implement Management that is Conscious of Cost of Capital and Stock Price". **Despite releasing an MTBP nearly 2 years after the request, it is missing the point of the request**.

Misalignment with Investors' perspectives

- There are some cases where the level of target setting seems inappropriate, for example, where ROE targets are set too low. Perhaps such companies consider those low targets to be sufficient because they exceed their internally estimated low cost of capital, but investors cannot assess them because they does not disclose their cost of capital. (Overseas investors)
- **Timeframes for target setting for some companies are problematic.** For example, a company set a target of 8% ROE for a fiscal year that is considerably ahead of schedule; it is thought that the company may not believe that it can achieve this goal. (Overseas investors)
- While there have been positive developments, such as the increased use of ROIC and the analysis of earnings by business segment, companies are only adopting strategies to improve the profitability of unprofitable businesses. **We hope that companies will take the next step by fundamentally reviewing their business portfolios, including withdrawing from unprofitable businesses.** (Overseas investors)
- **Many companies are unable to terminate existing businesses.** When profitability is below the cost of capital, the decision not to exit is not a good sign. **Some companies do not review their business portfolios to generate future earnings and end up only offering short-term shareholder returns.** (Consulting firm)
- A growing number of companies have announced that they will increase shareholder returns, but **some companies appear to be doing this as a short-term measure to boost their share price without first properly considering how to optimize their balance sheet and capital allocation policy.** (Domestic institutional investors, overseas investors, etc.)
- Although many companies have stated that **they are reducing their cross-shareholdings**, many companies do **not disclose their plans for allocating the cash obtained from sales, such as investing in growth and increasing shareholder returns. Therefore, this has not been a positive factor.** It is desirable that there is a growing trend to **disclose medium- and long-term capital allocation policies, including funds obtained by unwinding cross-shareholdings.** (Domestic institutional investors)
- This is a problem for **companies that only cite past medium-term management plans and make superficial disclosures** that they will "continue to improve PBR by implementing the measures outlined in the medium-term management plan." (Overseas investor)

Source: Status Update and Future TSE Initiatives (Provisional) Regarding "Action to Implement Management that is Conscious of Cost of Capital and Stock Price" 08/19/2024

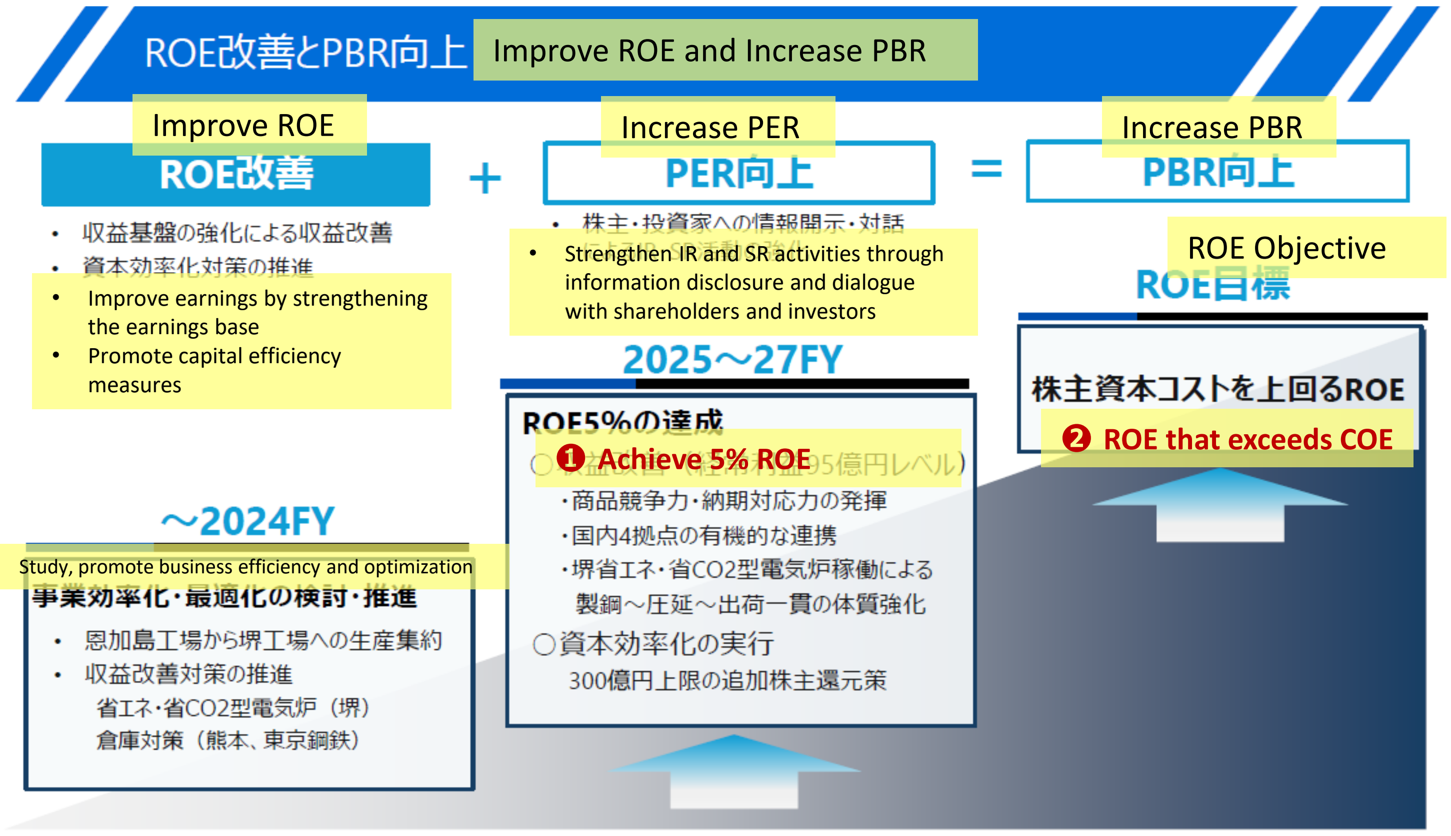
Disappointing mid-term business plan cont'd

Specifically, the **ROE target for the final year of the MTBP is only 5%**, which is significantly below the 8% minimum required of a listed company, not to mention the cost of capital so even if the target was achieved it would be difficult to achieve 1x PBR.

In addition, although they state it will **aim to achieve an ROE that exceeds cost of equity in the future, there is no time frame or specific measures**. SC believes that it will be **impossible to achieve an ROE that exceeds the cost of equity under the current policy**.

❶ 5% target is too low
❷ No timeline or concrete measures (not possible under current policy)

Problems with the MTBP



Source Osaka Steel's "Action to Implement Management that is Conscious of Cost of Capital and Stock Price"' (Japanese only) 1/31/2025,

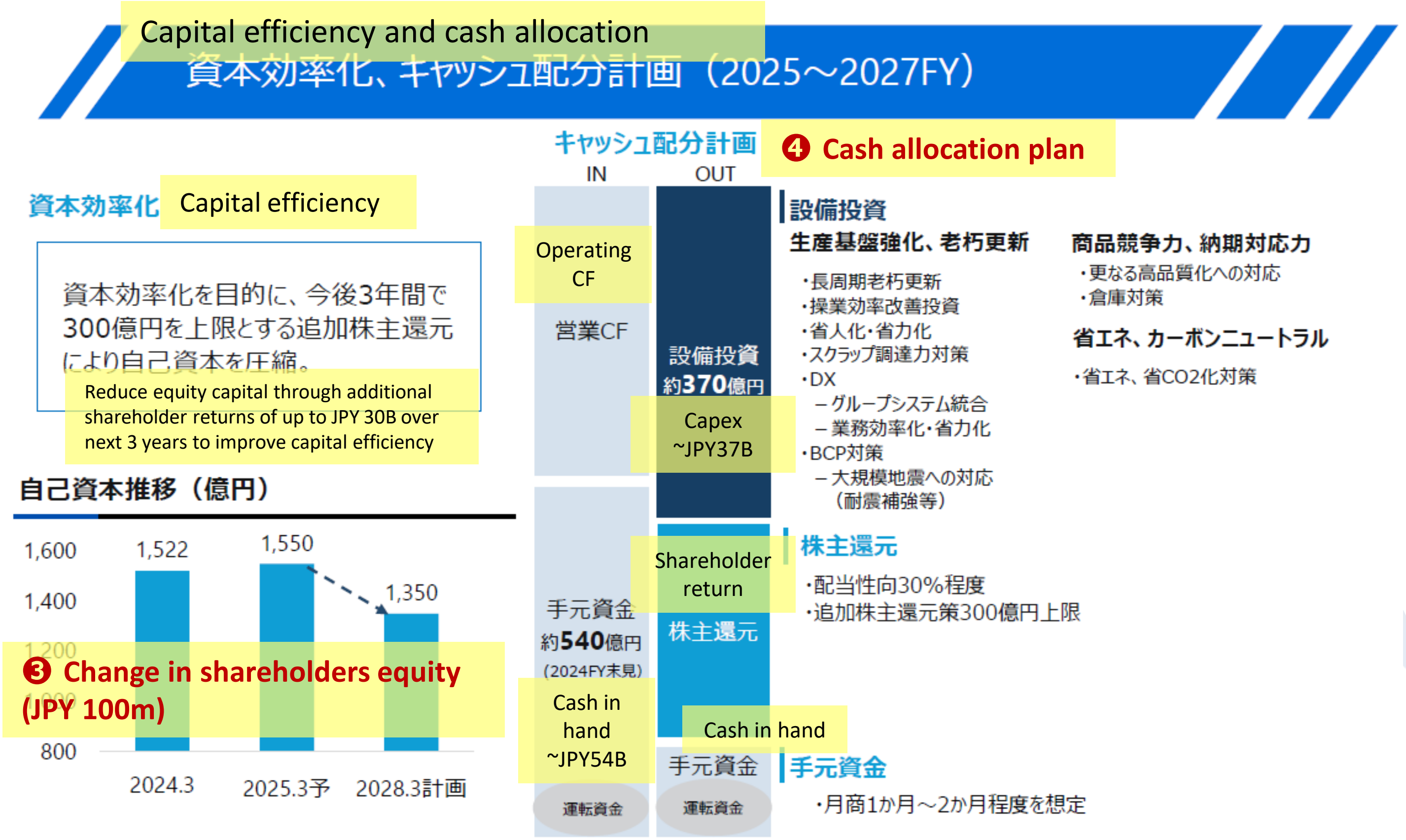
Disappointing mid-term business plan cont'd

Also, no consideration has been given to increasing financial leverage. Since **the shareholder equity ratio is currently at an excessive at approx. 76%, it is expected to remain above 70% even after the stock buyback from Nippon Steel** and **under the current policy it is expected to expand again after the completion of the MTBP**.

In addition, the **cash allocation plan calls for all capital expenditures and shareholder returns to be funded entirely by cash on hand and operating CF**, with **no consideration given to the use of interest-bearing debt**.

❸ limited reduction in shareholder equity ratio, increase after end of MTBP
❹ Assumes cash + operating CF will be used to cover all cashout, use of interest-bearing debt not being considered

Problems with the MTBP

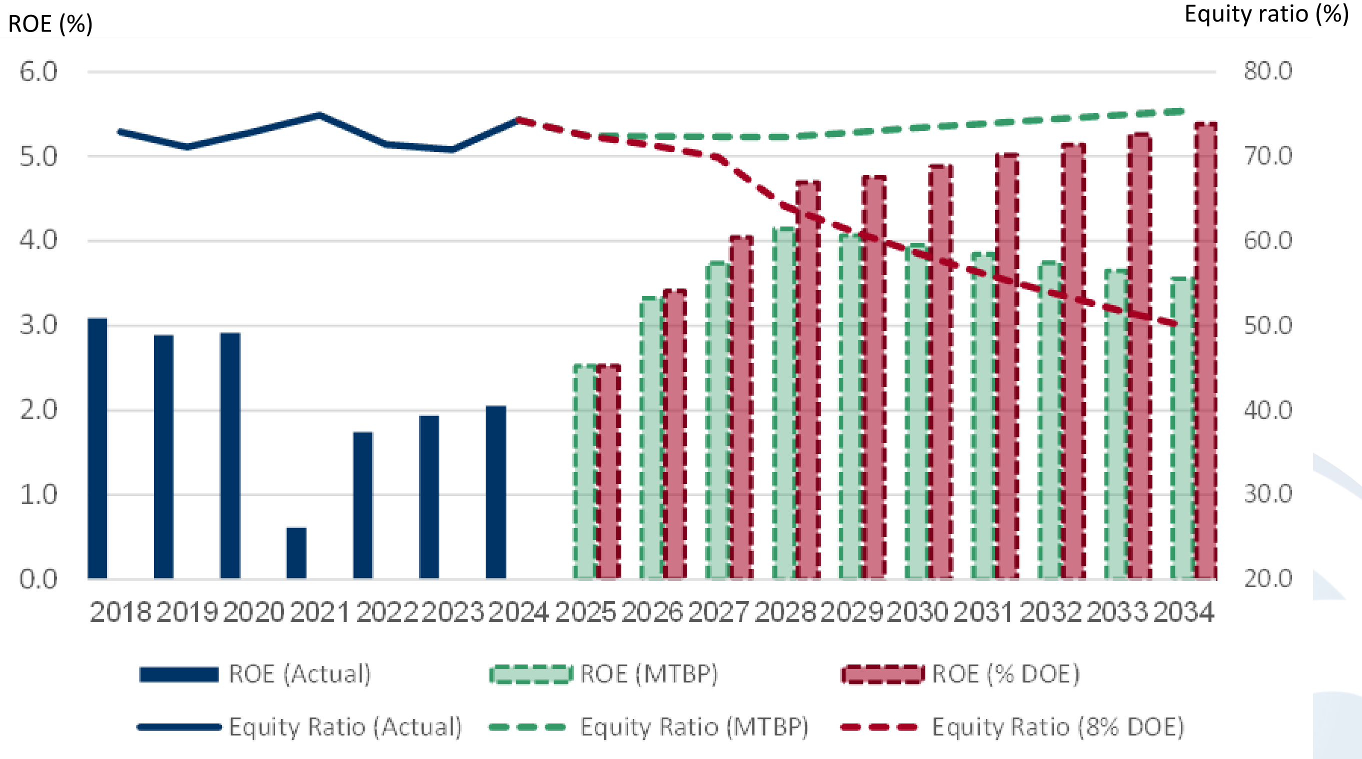


Source Osaka Steel's "Action to Implement Management that is Conscious of Cost of Capital and Stock Price"' (Japanese only) 1/31/2025,

Effect of 8% DOE (1): Reduce shareholder equity ratio and improve ROE

Therefore, SC **proposes an 8% DOE as a shareholder return policy**. This would allow for a gradual reduction of shareholders' equity and an improvement in ROE. It is estimated that it will take about 10 years for the capital adequacy ratio to be reduced to about 50%. The use of interest-bearing debt is also desirable.

Simulation of shareholders equity ratio and ROE (image)



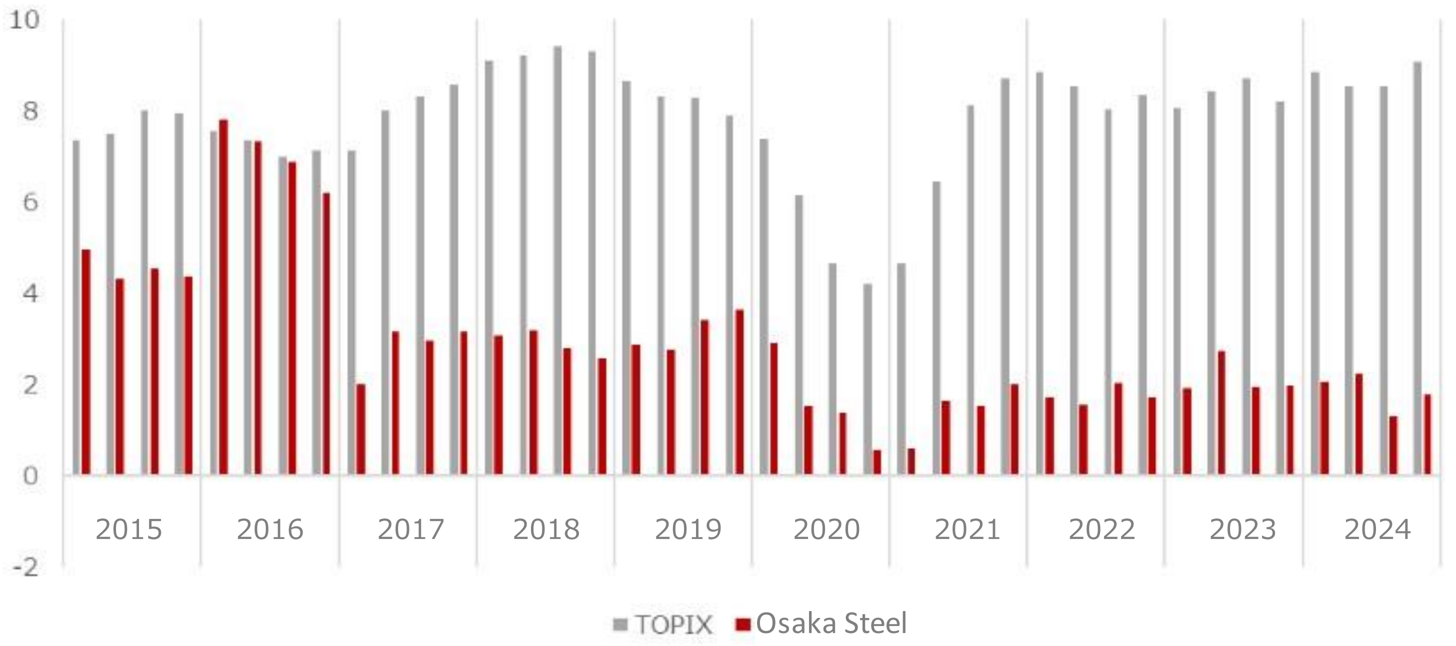
Source: Scenario based on assumption that performance and capex will reflect the MTBP until FY2027 and performance will be flat, capex JPY8B from FY2028 onwards. Shareholder returns assumed to be a JPY22B share buyback in FY2024, 30% dividend PO ratio or JPY8B over 3 years from FY2025 to 2027. the “8% DOE” introduces an 8% DOE. All other assumptions remain the same

Effect of 8% DOE (2): Raise the stock price floor and reduce volatility

With an extremely low average ROE of 1.9% over the past five years, a dividend based on net income is completely unappealing. In contrast, with a **8% DOE, the dividend is based on net asset balance, so even a company with extremely low capital efficiency, the stock price can be expected to rise**.

Also, given business performance can be influenced by market conditions, dividends based on net income can have low visibility. **With DOE, dividends would be more stable as they would not be influenced by performance in a single year, which in turn would reduce cost of capital and stabilize the stock price.**

Quarterly ROE Forecast (%)



Source: Bloomberg

Misalignment with Investors: perspectives on parent-child listings

The TSE has noted a misalignment between investors and companies regarding parent-subsidiary listings. For the CMS, **investors are concerned with large surplus funds being deposited with the parent at a level below cost of capital, resulting in lower ROE and PBR**. Osaka Steel has continued its CMS for years on a scale that accounts for more than half of its market cap. Although a portion is expected to be used for the share buyback from Nippon Steel, the **CMS has greatly deteriorated capital efficiency and it should all be eliminated immediately and used for business investment and shareholder returns.**

Investor Comments

- ✓ Most listed subsidiaries explained their reasons for participating in the group's cash management system only by saying that the interest rate is more favorable than bank interest rates.
- ✓ **Essentially, there are significant issues with the listed subsidiaries' capital efficiency and their balance sheets.** In fact, many of them have deposited large sums of excess funds relative to their market capitalization at their parent companies at low interest rates below the cost of capital. **This results in low ROEs and PBRs.**

Source: The Investor's Perspective on Such Matters as Parent-Subsidiary Listings, TSE, 2/4/2025

TSE Comments

- ⇒ Listed subsidiaries need to reexamine **their reasons for participating in group cash management in terms of capital efficiency and medium- to long-term improvements in their corporate value**, as well as in light of TSE's request to take "Action to Implement Management that Is Conscious of Cost of Capital and Stock Price."
- ⇒ Listed subsidiaries should also consider **how to allocate the excess funds currently on deposit for investments in growth that exceed the cost of capital and returns to shareholders over the medium to long term.**
- ⇒ Listed subsidiaries are also expected to disclose **the actual state** of the group's cash management system **(details on interest rates and other arrangements).**

Current state of Osaka Steel

- Has held CMSs that account for more than half of our market capitalization for many years
- Has explained that cash on hand is at an appropriate level, and that CMS is favorable compared to external investment (e.g., bank interest rates). However, on January 31, 2025, they announced a major change in policy and would use its cash reserves to buy back shares from Nippon Steel

Misalignment with Investors: perspectives on parent-child listings cont'd

In addition, **investors have voiced doubts regarding the effectiveness of governance, as they do not know the content of discussions at the Board and special committees**. While Osaka Steel's management has contributed to the interests of its parent through the CMS and as a revolving door for executives, it has continued to undermine the interests of minority shareholders, and a particularly high level of transparency is required.

SC has requested to inspect and copy the minutes of the Board meeting to confirm whether Osaka Steel is making decisions that take into consideration the interests of minority shareholders, **but the Company continues to refuse to do so**.

Investor Comments	TSE Comments
✓ Although listed subsidiaries are making progress in appointing independent directors and establishing special committees, they **do not disclose what is actually discussed by their boards of directors or their special committees, so the effectiveness of their meetings is questionable**.	⇒ It is useful to **disclose what is actually discussed at the board of directors meetings and the special committee meetings** (e.g., the agendas) regarding the following issues because they are likely to cause problems in terms of conflicts of interest.

Source: The Investor's Perspective on Such Matters as Parent-Subsidiary Listings, TSE, 2/4/2025

Current state of Osaka Steel

- SC has requested access to and copies of Board meeting minutes regarding CMS and other related party transactions, efforts to manage the company in a cost of capital conscious manner, etc., but Company continues to refuse.

Misalignment with Investors: perspectives on parent-child listings cont'd

The Company should also take comments of investors and the remarks made by the TSE regarding the dispatch of management seriously. Although all the full-time directors are from Nippon Steel, it is clear **they are not contributing to the enhancement of our corporate value, as evidenced by the fact that the PBR is consistently below 1x**. In addition, for the two proposals made by SC at the 2024 AGM, more than 50% of the minority shareholders were in favor. This suggests a **conflict of interest exists between Nippon Steel and the minority shareholders**.

Investor Comments

- ✓ While an effective governance system, including the appointment of a sufficient number of independent directors, is a given, there are still many cases where part of a listed subsidiary's management team is dispatched from its parent company.
- ✓ Although a parent company is not flatly denied from dispatching executives to its listed subsidiary, the problem is that there are cases where the listed subsidiary cannot explain the reasons for doing so or its function in terms of improving the listed subsidiary's corporate value, such as when executives are dispatched to a company with little or no synergy.

TSE Comments

- ⇒ A listed subsidiary is also expected to consider and explain the reasons for the dispatching of executives from its parent company and whether the executives are appropriate candidates in terms of improving the listed subsidiary's corporate value.
- ⇒ In addition, if a large number of a listed subsidiary's minority shareholders vote against the dispatching of executives from the parent company, the listed subsidiary should proactively analyze the reasons why and have dialogues with its shareholders.

Source: The Investor's Perspective on Such Matters as Parent-Subsidiary Listings, TSE, 2/4/2025

Current state of Osaka Steel

- All of Osaka Steel's full-time directors are from Nippon Steel, but it is clear they have not contributed to increasing corporate value, given that PBR is consistently below 1x.
- More than 50% of minority shareholders (i.e. shareholders other than Nippon Steel), approved of SC's proposal during the 2024 AGM to "establish and disclose a plan to achieve a PBR of at least 1x" and "make the majority of directors outside directors".

Insistence on maintain listing → Establish Shareholder Value Enhancement and Privatization Review Committee

Since shares held by Nippon Steel, SC and treasury exceed 75%, there is a possibility that Osaka steel will breach the delisting criteria of the TSE Standard Market. SC believes it is in the **best interest of minority shareholders for the Company to be privatized by Nippon Steel** and has requested a three-way dialogue to discuss.

However, the Company and Nippon Steel insist on maintaining Osaka Steel's listing and on January 31, 2025, announced that it would do a stock buyback of some shares held by Nippon Steel and cancel those shares as well as apply for listing on the Fukuoka Stock Exchange which has lax standards for maintaining listing.

In response, the Company's stock price plummeted, and shareholder value was greatly impaired. **Maintaining listing is the Group's desire, and so long as it continues to be listed, there is concern that decisions will continue to be made that disregard the interests of minority shareholders**. For this reason, we propose the **establishment of a committee consisting of outside directors, who from a standpoint independent of the Board of Directors, to consider measures to improve shareholder value including privatization**.

Overview

Org.	■ Established under the Board of Directors
Member	■ All Outside Directors ■ Allow for an independently appointed external advisor
Role	■ Hearing shareholder's opinions on measures to increase shareholder value including those related to general business, financial, appropriateness of CMS, corporate governance, and going private from shareholders ■ Consider measures based on information gathered and present to Board ■ Explain the shareholder value enhancement measures presented to the Board including any reference materials provided to the shareholders and other stake holders. ■ In the event of a TOB, consider and decide on the merits as a special committee independent of the acquirer including success and failure, pros and cons.

In addition to Osaka Steel, another Nippon Steel group company, NS Solutions (2327), a TSE Prime-listed company, was also listed on the Fukuoka Stock Exchange (as well as the Nagoya Stock Exchange). Like Osaka Steel, NS Solutions is a listed subsidiary of Nippon Steel, and because of its low tradable shares, it is may have been listed on these exchanges in anticipation that it too could also violate the TSE standards for maintaining a listing.

An *amakudari* destination for Nippon Steel → Make the majority of directors outside directors

As of March 31, 2024, **all five full-time directors** (of the eight total) **came from Nippon Steel, effectively making the Company an *amakudari* destination.**

The Corporate Governance Code stipulates that “Controlling shareholders should respect the common interests of the company and its shareholders and should not treat minority shareholders unfairly, and accordingly, companies with a controlling shareholder are required to develop a governance system to protect the interest of minority shareholder”(notes, General Principle 4) , while the “Practical Guidelines for Group Governance Systems (Group Guidelines)” (Japanese only) that “with respect to the nomination of management of a listed subsidiary, given the existence of risk of conflicts of interest between the controlling shareholder and general shareholder, to select persons who can contribute to the enhancement of corporate value as a listed subsidiary while also taking into account the interest of general shareholders.”

While the Company’s directors have contributed to the management of the parent company’s funds through CMS and other means, they have continued to undermine its own shareholder value. It is **clear there is a risk of conflict of interest between the controlling and general shareholders, and we propose the majority of the Company’s directors be outside directors and that governance be strengthened**. Going forward, it is essential that the Company's outside directors be appointed as independent outside directors who can respect the interests of minority shareholders.

Revisions

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