

## **Argyle Street Management Limited**

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28 May, 2018

Mr. Nobuaki Kurumatani  
Chairman and CEO  
Toshiba Corporation  
1-1, Shibaura 1-chome, Minato-ku,  
Tokyo 105-8001,  
Japan

Dear Mr. Kurumatani,

We refer to our letters to the board and yourself dated 12 March, 10 April and 18 May 2018.

Firstly, we would once again like to congratulate the board and yourself on receiving the anti-trust approvals from the Chinese regulators and having all conditions satisfied for closing of the Toshiba Memory Corporation ("TMC") transaction with the Bain consortium.

While we are disappointed that Toshiba did not negotiate for a better valuation with the Bain consortium and continue to feel that TMC was sold below fair value, we believe that completion of the transaction will be a necessary step for Toshiba to finally close the chapter on its most recent troubles and embark fully on the restructuring and revitalization of the remaining businesses in the company.

We would like to express our thanks and appreciation to the board and management team for the efforts in steering the company out of troubled waters and look forward to details of the Toshiba Next Plan. We believe that you now have a real opportunity to show investors that this is indeed a new chapter for Toshiba and that management is committed to value maximization which might not be the most convenient or easiest option for the managers.

As we have highlighted in our previous letter to you, we believe that a critical area for Toshiba going forward is to pursue a disciplined, pro-active approach towards capital allocation, given the especially high cost of equity capital Toshiba currently faces due to its depressed share price, history of questionable decisions and missteps in this area. We believe that the board and management should signal its commitment to capital allocation ahead of the upcoming AGM. We believe that this will be critically important for shareholders' decisions whether or not to be supportive of you and your current vision for Toshiba. Although the Toshiba Next Plan is not to be released until the end of this year, a swift return of capital is absolutely critical since it is evident that Toshiba has excessive cash and this is in line with what management had promised investors during the capital raise last year. Indeed, we are highly distressed at recent media interviews where you have indicated that you are considering significant M&A opportunities. As you are well aware, it was arguably poor capital allocation through disastrous M&A transactions which was the root cause of Toshiba's most recent troubles. It is critical for you to show your alignment and execute your

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turnaround before any consideration of serious M&A (especially when there is an incredibly high return investment opportunity afforded through your own shares).

We reiterate what we believe are the key steps you should take to send such a signal:

i. **Set a JPY1.1 trillion share buy-back program ahead of the upcoming AGM and implement this as soon as possible.**

Given that the board has the authority to implement such share buy-back plans without shareholder approval, this should be implemented as soon as possible ahead of the AGM. Announcing this ahead of the AGM is important as it provides important information for shareholders to consider prior to voting while showing your keen understanding of the best use of incremental capital.

We strongly believe the share buy-back program is the logical next step to undertake and is consistent with what management has communicated to shareholders. The equity issuance in December 2017 was intended for the purpose of temporarily increasing net worth at March-end 2018 to deal with the contingency that the TMC sale was not completed by then. As the sale of TMC even at a distressed value was to deal with negative net worth, you were correct in your concerns about the contingency but this prudence has led to a clear case of excess capital that is clearly no longer required. Moreover, due to your successful efforts in further strengthening Toshiba's balance sheet over the past year, the share buyback can now be for an even larger amount than the equity raised to reiterate your commitments and further send a signal to the market that you are serious about your commitment to value maximization.

As you are undoubtedly aware, the JPY1.1 trillion share buy-back number represents the net cash amount after the TMC transaction, based on the company's own forecast. Even after such a share buyback, the company will still have a robust cash balance and high shareholder equity ratio above the level prior to the most recent problems regarding Westinghouse. Moreover, following the sale of TMC, Toshiba's remaining businesses are significantly less risky and so this capital amount is even more ample. Although we have heard your desire to return to an investment grade rating, we believe that improving profitability as a result of a broad restructuring plan will be the most important factor in achieving a higher rating which we are very hopeful of through your Toshiba Next Plan. We also believe that there are numerous other assets which you have already indicated could be considerations for disposal that would also further raise your cash balances.

ii. **Implement a transparent and appropriate capital allocation policy**

We believe that it is critical with the share buyback program for the board to state that it will implement an appropriate capital allocation policy, and shareholders will be duly informed of the company's capital allocation decisions and the rationale behind them on a timely basis. As we have noted, a perceived lack of appreciation of an appropriate cost of capital is arguably the root cause of many of Toshiba's problems historically. A transparent policy of distributing 100% of free cash flow after

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appropriate capital expenditures and an objective criteria for targeting a sufficiently high return on invested capital (ROIC) should be implemented to ensure that the management team signals it is aware of the cost of equity capital.

### **iii. Reiterate the board's commitment towards the restructuring of existing business units and avoiding premature M&A activity**

We believe strongly that the board should make clear to investors that Toshiba will not embark on any significant M&A transactions until the restructuring of the existing business is fully completed and is generating the returns targeted by management. Management had previously guided that the "rebuilt Toshiba" comprising the current business segments less TMC and Westinghouse, would generate an operating income of around JPY210bn. While we note you are still working on the Toshiba Next Plan, we would like to urge the board to focus all efforts on achieving this outcome before engaging in other M&A distractions.

Toshiba's track record in M&A, such as the Westinghouse acquisition and the acquisition of IBM's POS business by Toshiba TEC, has arguably been highly value destructive for shareholders and has brought the company to the brink of collapse. Given this track record, we do not believe that any plan to retain cash on the balance sheet for future M&A opportunities will be well received by shareholders until trust has been restored. In fact, we are extremely concerned about media reports and communications with shareholders alluding to M&A plans by Toshiba's management team.

As you would know well, M&A deals draw management time and focus away from important day-to-day operations and from the difficult task of executing the restructuring of the current businesses, which we strongly believe should be your core focus, as also mentioned by you. We strongly encourage you to provide the market with greater detail regarding a commitment to not conduct M&A in the near future until you have revitalized Toshiba and restored trust.

We believe that announcing the above points ahead of the AGM would demonstrate that management is serious about disciplined capital allocation going forward and is committed towards the successful restructuring of existing businesses. We believe that this would also provide the reason that shareholders need to be fully supportive of management's election at the AGM. On the other hand, failure to clarify these points would mean that shareholders may feel the need to act against the management to fulfill their own fiduciary duties, especially if it is perceived that management will not be prudent and disciplined with capital allocation decisions.

As we have expressed previously, we are deeply appreciative and grateful to you for having taken up the challenge of guiding Toshiba out of troubled waters. Our objective, as always, is for Toshiba to be positioned strongly for the future for the benefit of all stakeholders. We believe you have a historic opportunity to make Toshiba a company truly focused on value maximization, a company managed consistently with the principles outlined in the Corporate Governance Code, and a shining example of a bold, successful turnaround.

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Kindly note that we do not intend to discuss or receive any confidential or inside information concerning Toshiba or any other company during our dialogue with you. We would greatly appreciate our dialogue being based on solely on publicly available information.

Please contact me at \_\_\_\_\_ or via email at \_\_\_\_\_ any time at your convenience. We look forward to further discussions with you.

Best regards



Kin Chan  
**Argyle Street Management Limited**