

Showa Denko's Wholly-owned Subsidiary Issues Preferred Shares—Equity Content Assessed as “Medium or 50%”

The following is Japan Credit Rating Agency, Ltd. (JCR)'s opinion on issue of preferred shares by HC Holdings K.K., a wholly-owned subsidiary of Showa Denko K.K. (security code: 4004).

HC Holdings K.K. (“HC HD”), a wholly-owned subsidiary of Showa Denko K.K., announced that it would issue preferred shares (paid-in amount: JPY 275 billion). Along with this announcement, Showa Denko K.K. (“Showa Denko”) announced that it would enter into an agreement on subordinated committed syndicated loan (total committed amount: JPY 275 billion) by April 27. The funds to be raised by the issue of preferred shares will be appropriated for a part of tender offer by Showa Denko through HC HD of shares in Hitachi Chemical Company, Ltd. The preferred shares will be acquired by HC HD and be purchased by Showa Denko, and the funds to be raised by the loan will be resources of these acquisition and purchase.

The following are JCR's Assessment of Equity Content of the Preferred Shares and Rationale. JCR will announce the rating and assessment of equity content on the loan after conclusion of loan contract. Please refer to JCR's press release 20-D-0051 dated today for the rating on Showa Denko.

<Assessment of Equity Content of the Preferred Shares and Rationale>

JCR assessed equity content of the preferred shares at "medium" or "50" (against 100 of a stock). The preferred shares will be acquired by HC HD and be purchased by Showa Denko, and the resources of these acquisition and purchase will be the funds to be raised by the loan. It is therefore expected that the preferred shares will be substantially transferred to the loan at the time of the acquisition and purchase. As for the preferred shares and the loans, as key points in assessment of equity content including annual dividend rate and interest rate step-up, exceptions to replacement, terms and conditions for suspension of dividend and interest payments are designed in the same manner, JCR assessed the equity content for both instruments as the one.

JCR takes into account that “there is no obligation to redeem principal or no maturity,” “there is no obligation to pay dividends” and “the ranking of claims at the time of bankruptcy is subordinated” when assessing the equity content of hybrid securities.

Although the preferred shares' maturity is not defined, acquisition by HC HD under certain conditions such as after the lapse of 5 years from the issue date or purchase by Showa Denko is defined. As the annual dividend rate will step up after the lapse of 5 years from the issue date and will be higher by about 100 bps from the initial rate, incentives for the effective redemptions such as acquisition and purchase are high. Showa Denko and HC HD, however, expressed their intentions not to acquire or purchase the preferred shares without issue of replacement securities, etc. (replacement).

This expression defines exemptions that allow Showa Denko, parent company of HC HD, to forgo the replacement if it can achieve certain levels of financial indicators, provided that such indicators defined in the exemptions satisfy the adequate levels. JCR therefore considers it is unlikely that HC HD and Showa Denko will acquire and purchase the preferred shares without replacement when their creditworthiness declines and thus factored this view into the assessment of effective redemption obligations and maturity. This judgment reflects, along with other factors, that JCR, based on hearing from Showa Denko, etc., was able to ascertain the future financial management policy including positions of the preferred shares and loan and that Showa Denko, a wholly-owning parent company of HC HD, has long been winning confidence of investors and creditors by maintaining good relations with them in the financial market.

As for dividends, the fact that there is no clause for mandatory dividend suspension weakens similarity of the preferred shares to common stock. However, the optional dividend suspension clause provides a mechanism whereby the dividend payments can be suspended in a stressful situation. JCR took into consideration the fact that the ranking of claims to the preferred shares is subordinated to the ranking of claims to the senior obligations at the time of bankruptcy as well as these mechanisms for substantial maturity and dividend suspension.

<Outline of Preferred Shares>

Issuer: HC Holdings K.K.

Issue	Amount (bn)	Issue Date	Due Date	Annual Dividend rate
Class A Preferred Shares	JPY 275	Apr. 27, 2020	No Maturity	(Note)

(Note): swap rate + spread till the day before the corresponding day after the lapse of 5 years from the Issue Date. On and after the corresponding day after the lapse of 5 years from the Issue Date, Yen TIBOR + initial spread + 1.0%

Acquisition/ Purchase:	Acquisition on and after the corresponding day after the lapse of 5 years from the Issue Date Purchase by Showa Denko
Replacement:	There has been representation of intention for replacement.
Optional Dividend Suspension:	The issuer may suspend dividend payment at its discretion.
Mandatory Dividend Suspension:	No provisions
Accumulation/Non-Accumulation:	Accumulation
Ranking of Claims:	The preferred shares are subordinated to all debts (excluding the preferred shares and the subordinated debts ranking pari passu with the preferred shares) and rank pari passu with the first preferred stock

<Outline of Subordinated Committed Syndicated Loan (Scheduled)>

Issuer: Showa Denko K.K.

Issue	Amount (bn)	Drawdown Date	Due Date	Interest rate
Subordinated Committed Syndicated Loan	(Note 1)	(Note 2)	Apr. 27, 2055	(Note 3)

(Note 1): Borrowing Limit: JPY 275 billion

(Note 2): Drawdown: from April 27, 2020 to April 27, 2025; 1 drawdown is possible during this period

(Note 3): Yen TIBOR + spread till the day before interest payment date in April 2025

Yen TIBOR + initial spread + 1.0% on and after interest payment date in April 2025

Early Repayment:	Repayment after the lapse of 5 years from the contract day Repayment upon occurrence of Tax Events or Rating Events Repayment by agreements with all lenders and agents
Replacement:	There has been representation of intention for replacement.
Optional Interest Suspension:	The Borrower may suspend interest payment at its discretion.
Mandatory Interest Suspension:	No provisions
Accumulation/Non-Accumulation:	Accumulation
Ranking of Claims:	The loan is subordinated to all debts (excluding the loan and the subordinated debts ranking pari passu with the loan) and ranks pari passu with the first preferred stock

<Reference>

Long-term Issuer Rating: A Outlook: Negative

Japan Credit Rating Agency, Ltd.

Jiji Press Building, 5-15-8 Ginza, Chuo-ku, Tokyo 104-0061, Japan
Tel. +81 3 3544 7013, Fax. +81 3 3544 7026

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