

# TOTO Ltd



TSE: 5332 | Industrials – Advanced Ceramics &amp; Sanitary Ware | April 2026

Recommendation <b>BUY</b>	Price Target <b>¥7,303</b>	Current Price <b>¥5,732</b>	Upside <b>+27%</b>
Market Cap <b>¥940bn</b>	EV/EBITDA (LTM) <b>¥10.3x</b>	52-Week Range <b>¥3,335-6,290</b>	Shares Outstanding <b>164.4m</b>

We initiate coverage of **TOTO Ltd (TSE: 5332)** with a **BUY** recommendation and a 12-month price target of **¥7,303**, implying **27% upside** from the current share price of ¥5,732. Our target is derived from a combination of absolute and relative valuation. We apply a **sum-of-the-parts DCF** to value TOTO's Advanced Ceramics and Housing Equipment segments independently, capturing the divergent growth and margin profiles that a consolidated valuation overlooks. Despite TOTO's 5Y 61% underperformance versus the TOPIX (Bloomberg), we believe TOTO's discount reflects the **market's misclassification of TOTO as a pure sanitary ware company** rather than any deterioration in underlying business quality. We believe this mispricing will be corrected by the following three catalysts:

- **Hidden Semiconductor Asset.** The market prices TOTO at 10.3x consolidated EV/EBITDA — in line with HE peer LIXIL (8.9x) — yet the **AC segment generates ~40% of operating profit at a 40.6% margin**. The failure to disaggregate this business is the single most important source of the valuation gap.
- **The 3D NAND Cryogenic Etch Cycle.** TOTO is **the sole qualified ESC supplier** for Lam Research's cryogenic dielectric etch process. With ~two-thirds of global NAND production still sub-200 layer, the structural upgrade cycle is in its early stages.
- **Value Enhancement Plan.** In February 2026, activist investor Palliser Capital published a Value Enhancement Plan arguing TOTO trades at a ¥554bn discount to intrinsic value, proposing: **(1) improved AC disclosure, (2) ROIC-driven capital reallocation, (3) capital structure optimisation**. Even partial execution would be materially value-accretive.

## 1. Company Background

Founded in 1917, TOTO employs 34,673 people across 46 domestic sites and operations in 17 countries. Listed on the Tokyo, Nagoya, and Fukuoka Stock Exchanges. Over more than a century, TOTO has evolved from a ceramic flush toilet manufacturer into a **dual-business conglomerate operating two structurally distinct businesses under a single listing**:

### Global Housing Equipment (HE) Business

- **Manufactures and sells** sanitary ware, WASHLET spray seats, faucets, bathrooms, and modular kitchens across Japan and internationally
- **Unrivalled domestic market position** built over a century; remodelling sector is the primary revenue base
- Cumulative global WASHLET shipments surpassed **70 million units** as of November 2025

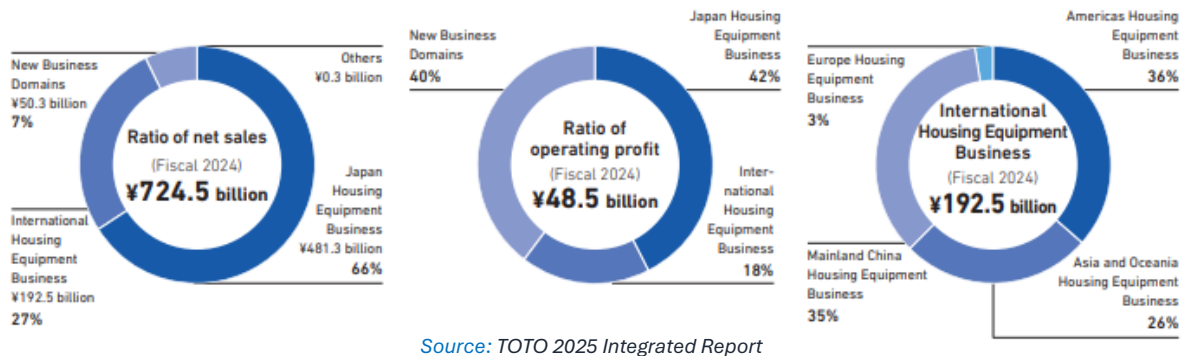
### Advanced Ceramics (AC) Business

- Mass-producing electrostatic chucks (ESCs) since 1988 — TOTO's **most profitable operation**
- **Generates 40% of consolidated operating profit from just 7% of revenue** — a 5.7x profit-contribution leverage ratio the market has failed to price
- ESCs are precision ceramic consumables used in **semiconductor wafer fabrication equipment**

**In this light, TOTO is not a sanitary ware company that happens to make ceramics. It is a semiconductor materials business that happens to own Japan's leading bathroom franchise.**



Fig 1.1: TOTO Revenue, Operating Profit, and Sales Breakdown by Segment - FY24



Source: TOTO 2025 Integrated Report

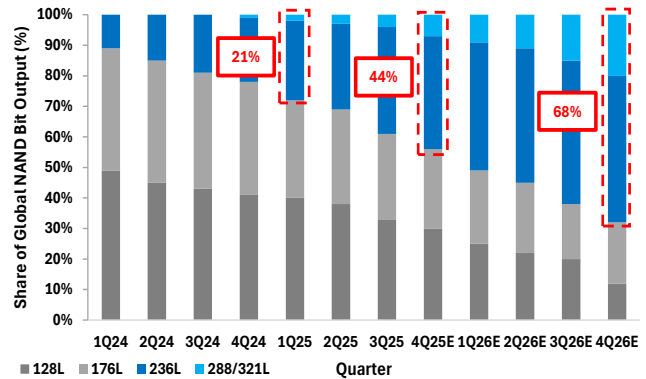
## 2. Inside the AC Segment: ESCs and the 3D NAND Cycle

Fig 2.1: SWOT Analysis

STRENGTHS	WEAKNESSES
<ul style="list-style-type: none"> <li>• Dominant ESC market</li> <li>• High-margin AC segment</li> <li>• Century-old ceramic R&amp;D</li> <li>• WASHLET brand</li> <li>• Strong balance sheet</li> </ul>	<ul style="list-style-type: none"> <li>• Conglomerate discount</li> <li>• Low HE profitability</li> <li>• China losses</li> <li>• Capital inefficiency</li> <li>• Customer concentration risk</li> </ul>
OPPORTUNITIES	THREATS
<ul style="list-style-type: none"> <li>• 3D NAND upgrade supercycle</li> <li>• Activist-driven re-rating</li> <li>• International HE expansion</li> <li>• Japan remodelling tailwind</li> <li>• Capital return upside</li> </ul>	<ul style="list-style-type: none"> <li>• Semiconductor capex volatility</li> <li>• Japan demographic decline</li> <li>• FX &amp; tariff exposure</li> <li>• Intensifying HE competition</li> <li>• Supply chain &amp; ESG risk</li> </ul>

Source: Analyst Analysis

Fig 2.2: Global NAND Bit Output by Layer Count (Q1 2024–Q4 2026E)



Source: Omdia, cited in Palliser Capital Value Enhancement Plan

### The Technology

- NAND flash memory is the key storage technology in smartphones, laptops, and data centres; modern devices stack **200+ layers** vertically
- Producing each chip requires etching channels ~100x deeper than wide, at this geometry, conventional etching fails
- **Cryogenic dielectric etching** is the enabling solution and Lam Research is the dominant global supplier of cryogenic etch tools
- At the core of each Lam tool sits an **electrostatic chuck (ESC)**, a precision ceramic component maintaining wafer temperature uniformity to within 2°C
- TOTO is the **dominant ESC supplier to Lam Research**, formalised through a Supplier Excellence Award in both 2023 and 2024

### Why ESCs Are Structurally Attractive

- **Consumable with ~1-year replacement cycle**, ~80% of AC revenue is replacement demand, largely insulated from semiconductor capex cycles (Palliser Capital, February 2026)
- **Sole qualified ESC supplier** to Lam Research — a position protected by an estimated 5-year qualification barrier

### Two Structural Growth Drivers

- **3D NAND upgrade cycle accelerating**: 200L+ production was 21% of global NAND bit output in Q4 2024, rising to 44% by Q4 2025 and projected to reach **68% by Q4 2026** (Omdia, cited in Palliser Capital, February 2026)



- **Multi-tier stacking:** transition to 300–400-layer requires **2–3x more cryogenic etch tools per wafer**; Lam Research has guided for a 3x installed base expansion over 3–5 years (Lam Research Investor Day, February 2025)
- Every additional tool requires an ESC. This installed base expansion **directly translates into a structurally larger replacement revenue opportunity** for TOTO

**Palliser Dependency**

Several key figures in this section originate from Palliser Capital, which hold a **significant long position in TOTO and a financial interest in the thesis being correct**. Where possible, we have independently verified Palliser's claims, including segment ROA and operating profit breakdowns using TOTO's company filings. The NAND layer count data is sourced from Omdia, an independent industry research agency, cited via Palliser. **If Palliser's AC growth estimates prove optimistic, our DCF bear case captures this downside, as described in Section 10.**

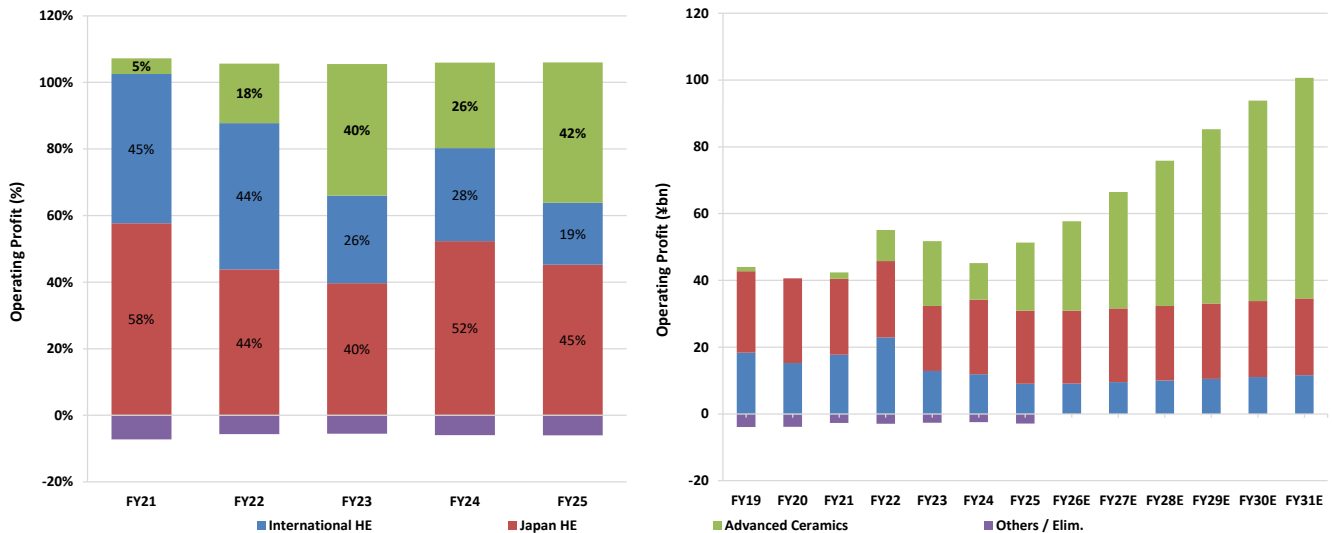
**Lam Concentration**

The AC thesis rests on a **single customer relationship**. TOTO's competitors have attempted to enter the cryogenic ESC market but **none have succeeded** (Palliser Capital, February 2026, citing company filings and proprietary research). ESC qualification for cryogenic etch applications requires multi-year material science validation, tool-level integration testing, and fab-level reliability qualification — **a process estimated at 5+ years**. The cost of requalification to Lam Research would, in our assessment, far exceed any ESC procurement saving, making mid-cycle supplier displacement highly unlikely. This qualification barrier is the **structural basis for the 3.0% terminal growth rate** applied in our SOTP DCF.

### 3. Operational Performance

TOTO delivered consolidated net sales of ¥724.5bn and operating profit of ¥48.5bn in FY2025, implying a consolidated operating margin of 6.7%. Segment-level performance tells a more instructive story.

**Fig 3.1: Historical and Projected Operating Profit by Segment (FY2021–FY2031E)**



Source: TOTO Consolidated Financial Results (FY2021–FY2025); Analyst Estimates (FY2026E–FY2031E)

**Global HE Segment**

- FY2025 revenue ¥673.9bn; operating profit ¥30.9bn; **operating margin 4.6%**
- **L5Y revenue CAGR of 3.9%** vs. LIXIL's -2.3% — outperforming despite similar macro headwinds
- Japan HE dominant at ¥481.3bn revenue, underpinned by **resilient remodelling demand**
- International HE revenue ¥192.5bn; segment operating loss of ¥3.6bn driven by **Mainland China impairment**
- Americas showing momentum: sales +7% YoY to \$373m (Q3 FY2026), although **margins pressured by tariff headwinds and growth investment**
- **Mixed international outlook:** structural North America opportunity vs. China difficulties unlikely to resolve near-term



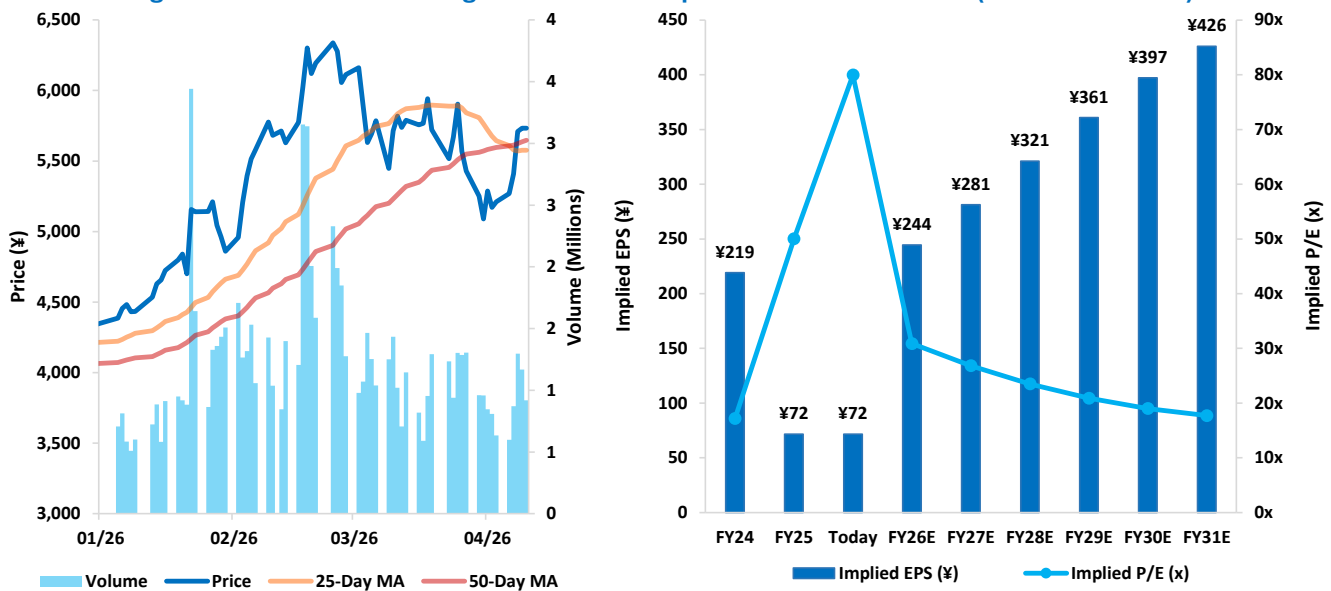
### Advanced Ceramics Segment

- FY2025 revenue ¥50.3bn, **+38% YoY**; operating profit ¥20.4bn; **operating margin 40.6%** (4x NGK Insulators' 10%)
- Q3 FY2026 YTD revenue ¥47.0bn (+37% YoY); operating margin **43%**, up from 42% prior year
- **Cryogenic etch adoption accelerating** — FY2026 on track for another year of strong double-digit growth
- Palliser Capital estimates **30%+ CAGR over next two years**, driven by NAND upgrade cycle and ~80% replacement revenue base (Palliser Capital, February 2026)

Looking forward, our SOTP DCF model projects consolidated revenues of approximately **¥934bn by FY2030E**, with AC segment revenues expanding to ¥165.1bn on a 30%+ CAGR through FY2027E before moderating. Consolidated operating margins are forecast to expand from 6.7% in FY2025 toward **10.8% by FY2030E** as the higher-margin AC segment grows as a proportion of the profit mix.

## 4. Financial Performance & Market Pricing

Fig 4.1: Share Price & Trading Volume YTD / Implied EPS & Forward P/E (FY2024–FY2031E)



Source: S&P Capital IQ; TOTO Integrated Report 2025; Analyst Estimates (FY2026E–FY2031E)

### Share Price & Re-rating

- Share price ¥5,800 at Palliser publication (Feb 2026); since re-rated to ¥5,732 (market cap of approx. ¥940bn) as **market begins pricing AC segment value**
- Current price still implies **27% discount to our ¥7,303 price target**
- **Risk:** recent appreciation may mean **catalyst value is partially priced in**

### Earnings Quality

- FY2025 EPS collapsed to ¥71.73 from ¥219.30 — **driven by one-off China impairment, not operating deterioration**
- Trailing P/E therefore **misleading** at current prices; overstates true earnings multiple
- Our FY2026E normalised EPS of ¥244.5 implies a forward P/E of 23.4x — **elevated but consistent with a business shifting toward a 40%+ margin segment**

## 5. Capital Structure

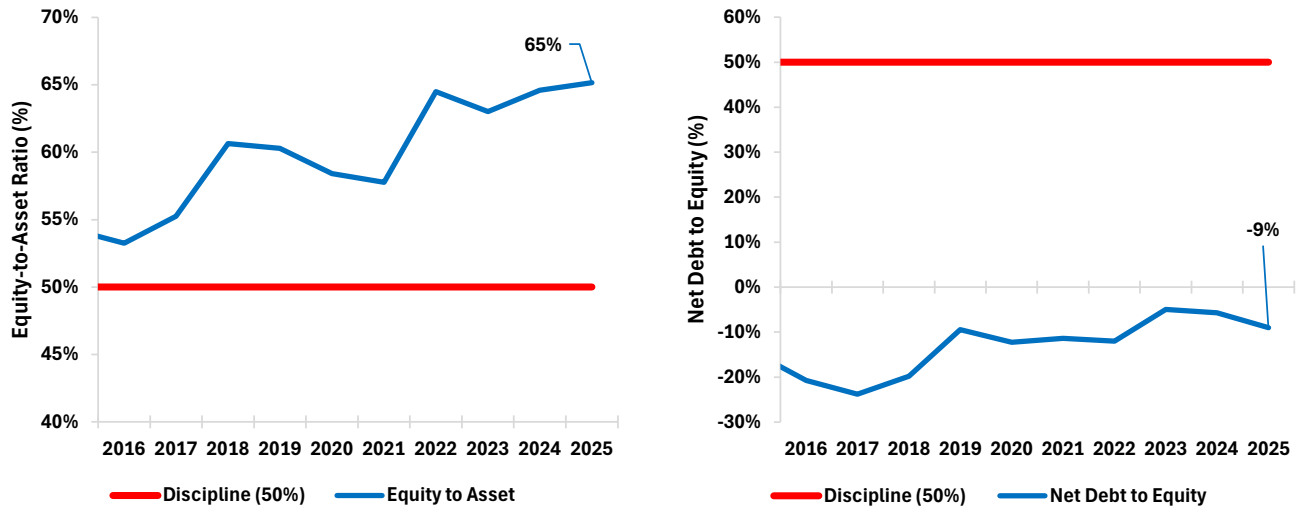
### Balance Sheet Overview

- Equity-to-asset ratio 65.1%; net debt/equity -9%; OCF ¥71.4bn — **conservatively financed, self-funding**



- Balance sheet strength provides **downside protection** in a semiconductor downturn

**Fig 5.1: Historical Capital Structure vs. Financial Discipline Rules (FY2016–FY2025)**



Source: Bloomberg, Palliser Enhancement Value Plan

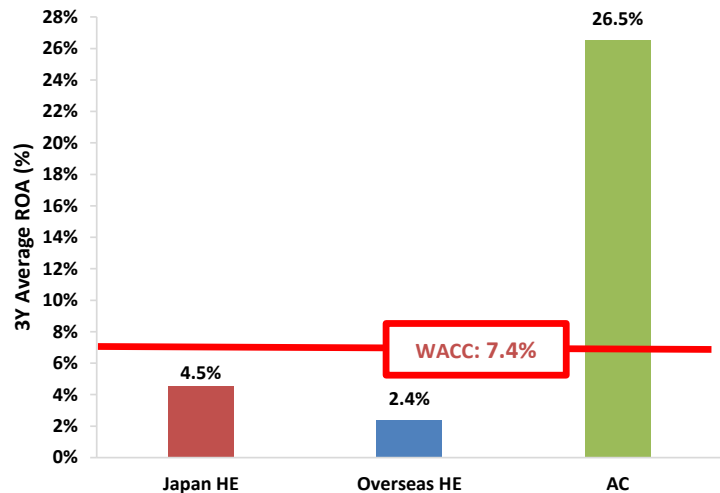
### Conservatism as Value Destruction

Palliser Capital (February 2026) identifies three specific capital misallocations:

- Equity ratio of 64% **exceeds TOTO's own 50% financial discipline rule**
- **¥76bn in non-synergistic cross-shareholdings** maintained for relational rather than economic purposes
- Of ¥175bn FY2025 investment budget, only ¥29bn (19%) directed to AC — the **highest-returning segment at 26.5% ROA vs. 7.4% WACC**.
- Japan HE received 21% of capex despite a 3Y average ROA of 4.5% — **destroying economic value**

**Fig 5.2: Strategic Investment Allocation & 3Y Average Segment ROA vs. WACC**

Strategic Investments (Capital Investments) Breakdown



Source: TOTO Integrated Report 2025; Analyst Estimates (WACC)

## 6. Absolute Valuation

### Methodology

We construct a **sum-of-the-parts DCF (SOTP DCF)**, valuing each of TOTO's three segments independently. This approach is warranted by the **significant dispersion in growth, margin, and reinvestment profiles** across segments — applying a blended DCF would obscure the 5.7x profit-contribution leverage ratio of the AC segment relative to its



revenue share. The model projects FCF for each segment over a **six-year forecast period (FY2026E–FY2031E)**, derived from segment-level operating profit, adjusted for taxes, D&A, capex, and changes in NWC. A single consolidated **WACC of 7.41%** is applied across all three segments, constructed using:

- JGB 10-year risk-free rate: 2.374%
- Japan equity risk premium: 7.025%
- Levered beta: 0.789 (5-year monthly vs. TOPIX)

### Key Assumptions — Advanced Ceramics

The AC segment assumptions translate directly from the investment thesis:

- **Revenue growth 33% in FY2026E**, decelerating to 10% by FY2030E — reflecting the 3D NAND upgrade cycle in the near term and installed base normalisation thereafter
- **Operating margin held at 40%** — consistent with FY2024 reported figure; incremental volume growth not expected to require proportionate fixed cost addition
- **Terminal growth rate of 3.0%** — reflecting long-run semiconductor consumable demand and TOTO's near-monopoly qualification position

### Key Assumptions — Housing Equipment

- Japan HE: **1.0% revenue growth p.a.; 4.5% operating margin; 1.0% terminal growth** — consistent with mature, remodelling-driven domestic market
- International HE: **5.0% revenue growth p.a.; 4.5% operating margin; 2.0% terminal growth** — reflecting WASHLET adoption in North America and emerging market penetration

Fig. 6.1: SOTP DCF: Advanced Ceramics Segment

	FY26E	FY27E	FY28E	FY29E	FY30E	FY31E	Terminal
<b>Revenue</b>	66,932	87,012	108,765	130,518	150,096	165,105	170,058
Revenue Growth (%)	33.0%	30.0%	25.0%	20.0%	15.0%	10.0%	3.0%
<b>Operating Profit (EBIT)</b>	26,773	34,805	43,506	52,207	60,038	66,042	68,023
Operating Margin (%)	40.0%	40.0%	40.0%	40.0%	40.0%	40.0%	40.0%
<b>Less: Taxes on EBIT</b>	-8,139	-10,581	-13,226	-15,871	-18,252	-20,077	-20,679
Tax Rate (%)	30.4%	30.4%	30.4%	30.4%	30.4%	30.4%	30.4%
<b>NOPAT</b>	<b>18,634</b>	<b>24,224</b>	<b>30,280</b>	<b>36,336</b>	<b>41,787</b>	<b>45,965</b>	<b>47,344</b>
D&A Rate (%)	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	-
Add: D&A	4,016	5,221	6,526	7,831	9,006	9,906	-
Capex Rate (%)	10.0%	10.0%	9.0%	8.0%	8.0%	8.0%	-
Less: Capital Expenditure	-6,693	-8,701	-9,789	-10,441	-12,008	-13,208	-
NWC Rate (%)	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	-
Less: Change in NWC	-1,661	-2,008	-2,175	-2,175	-1,958	-1,501	-
<b>Free Cash Flow to Firm (FCFF)</b>	<b>14,296</b>	<b>18,736</b>	<b>24,842</b>	<b>31,551</b>	<b>36,827</b>	<b>41,162</b>	<b>47,344</b>
Discount Factor	0.9310	0.8668	0.8071	0.7514	0.6996	0.6513	-
<b>Present Value of FCFF</b>	<b>13,310</b>	<b>16,241</b>	<b>20,049</b>	<b>23,707</b>	<b>25,764</b>	<b>26,811</b>	-

Source: Analyst Estimates

### SOTP Summary

The sum of segment enterprise values is **¥1,142.4bn**. After a net equity bridge adjustment of +¥97.9bn (including cross-shareholdings of ¥76bn per Palliser Capital estimates), total equity value is **¥1,240.2bn**, implying a share price of **¥7,544** — representing 31.6% upside to the current share price. The **AC segment accounts for 72.3% of total segment enterprise value**, quantifying the market's failure to price that nearly three-quarters of intrinsic value is attributable to the high-growth semiconductor materials business. Terminal value accounts for 84.3% of total enterprise value — with International HE particularly reliant on long-run assumptions at 94.3% — underscoring the model's sensitivity to terminal growth and discount rate assumptions, as explored in the sensitivity analysis below.



Fig. 6.2: SOTP DCF: Valuation Summary (¥ millions)

	Advanced Ceramics	Japan HE	Intl HE	Total
Sum of PV of Projected FCFF	125,881	47,141	5,985	<b>179,008</b>
Terminal Value (Gordon Growth)	1,074,344	252,283	152,425	<b>1,479,052</b>
PV of Terminal Value	699,765	164,322	99,281	<b>963,369</b>
<b>Segment Enterprise Value</b>	<b>825,647</b>	<b>211,463</b>	<b>105,266</b>	<b>1,142,376</b>
TV as % of Segment EV	84.8%	77.7%	94.3%	84.3%
% of Total Segment EV	72.3%	18.5%	9.2%	

Source: Analyst Estimates

## Sensitivity Analysis

Fig. 6.3: SOTP DCF: Sensitivity Analysis

		WACC				
		6.4%	6.9%	7.4%	7.9%	8.4%
AC Terminal Growth Rate	2.5%	¥8,838	¥7,880	¥7,111	¥6,479	¥5,951
	2.8%	¥9,185	¥8,143	¥7,316	¥6,642	¥6,084
	3.0%	¥9,583	¥8,440	<b>¥7,544</b>	¥6,823	¥6,229
	3.5%	¥10,585	¥9,165	¥8,089	¥7,244	¥6,563
	4.0%	¥12,003	¥10,139	¥8,794	¥7,774	¥6,974

Source: Analyst Estimates

Given the model's sensitivity to terminal assumptions, we conduct a sensitivity analysis varying the **AC terminal growth rate against WACC**. Across the full range, implied share prices span **¥5,951** (bear: 2.5% terminal growth, 8.4% WACC) to **¥12,003** (bull: 3.5% terminal growth, 6.4% WACC). Even under the most conservative scenario, the model continues to indicate **material undervaluation** relative to the current share price. A key limitation of this model is the application of a single WACC to three segments

with meaningfully different risk profiles. To test this, **we apply differing segment WACCs**: 6.5% for Japan HE (reflecting stable, remodelling-anchored domestic cash flows), 9.0% for International HE (reflecting emerging market exposure, China restructuring risk, and US tariff headwinds), and 8.5% for AC (reflecting customer concentration risk and NAND cycle sensitivity). **This yields an implied share price of ¥7,271 approximately 4% below the consolidated base case**. This result underscores the sensitivity of the valuation to the risk premium assigned to the AC segment and **reinforces our thesis: the market is implicitly applying an even greater discount to AC's cash flows than a standalone 8.5% WACC would imply**.

## 7. Relative Valuation

### Peer Group Construction

A relative valuation for TOTO presents an inherent challenge: **no single listed company combines a dominant-share sanitary ware business with a high-margin semiconductor ceramics operation**. The comparable universe therefore spans five peers selected to capture exposure across both of TOTO's principal segments.

**Housing Equipment peers:** LIXIL Group Corporation (TSE: 5938), Geberit AG (SIX: GEBN), Sanwa Holdings (TSE: 5929)

- Share TOTO's exposure to residential/commercial construction cycles, renovation activity, and new housing starts
- **LIXIL is the most direct comparator** — Japanese peer with significant product category and geographic overlap
- **Limitation:** Geberit operates at materially higher margins, reflecting premium European plumbing market positioning

**Advanced Ceramics peers:** NGK Insulators Ltd. (TSE: 5333), Niterra Co., Ltd. (TSE: 5334)

- Both produce electrostatic chucks for semiconductor manufacturing equipment
- **Limitation:** neither is a pure-play ESC business — NGK has significant power insulator and automotive battery exposure; Niterra spans spark plugs and automotive sensors. **Revenue diversification compresses observed EBITDA multiples** relative to what a standalone high-margin ESC business would command



Fig. 7.1 — Relative Valuation: Peer Trading Multiples and Implied Share Prices

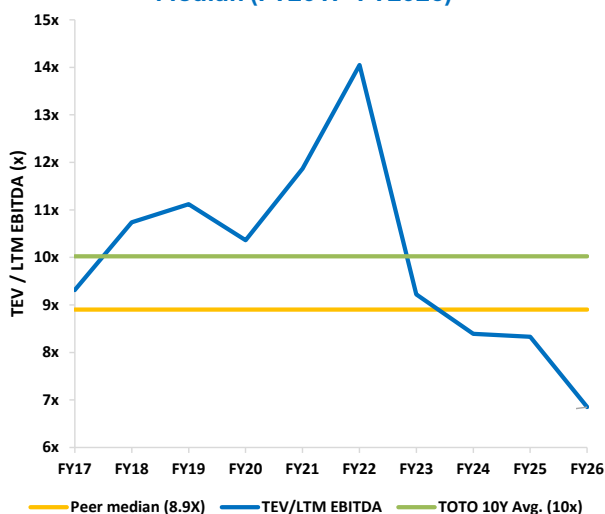
Multiple	TOTO	Peer Multiple			Implied Price		
		Low	Median	High	Low	Median	High
TEV / Revenue (LTM)	1.2x	0.7x	1.9x	6.0x	¥3,645	¥9,134	¥26,897
TEV / EBITDA (LTM)	10.3x	7.4x	8.9x	20.8x	¥4,335	¥5,130	¥11,143
TEV / EBIT (LTM)	17.5x	8.8x	15.0x	31.1x	¥3,203	¥5,017	¥9,780
TEV / Revenue (FY+1E)	1.2x	0.7x	1.8x	5.9x	¥3,517	¥8,407	¥25,673
TEV / EBITDA (FY+1E)	10.5x	7.4x	8.8x	19.8x	¥4,062	¥4,692	¥9,856

Source: S&amp;P Capital IQ; Analyst Estimates

## Multiple Selection

- **Primary: EV/EBITDA** — preferred for capital-intensive businesses where D&A policies differ across the peer set
- **Secondary: EV/Revenue** — retained as a sanity check only; blind to profitability and therefore unable to distinguish TOTO's 40% margin AC business from its low single-digit margin HE segment
- **EV/EBIT** — included for completeness; distorted by varying D&A treatment across peers

Fig. 7.2 — TOTO Historical EV/EBITDA vs. Peer Median (FY2017–FY2026)



Source: S&amp;P Capital IQ

## Results

Peer median LTM EV/EBITDA of 8.9x implies ¥5,130; **forward EV/EBITDA of 8.8x implies ¥4,692**, with the forward figure incorporating our own FY2026E EBITDA estimates from the SOTP DCF model. A blended peer median will naturally sit between HE and AC multiples — **the relative valuation structurally undervalues TOTO absent a SOTP decomposition**, which is why we assign it only a 10% weight in our blended price target (see Section 8)

## Historical Trading Multiples

TOTO's December 2025 EV/EBITDA of 6.85x represents a significant discount to the company's own **10-year average of 10x** and to the peer median of 8.9x. The compression in EV/EBITDA suggests **investor ignorance of segment-level dynamics** rather than any deterioration in underlying business quality.

## 8. Valuation Summary

Fig. 8.2 — Blended Valuation Summary

Method	Weight	Implied Price (Median)
SOTP DCF	90%	¥7,544
Relative Valuation (Med.)	10%	¥5,130
<b>Blended Price Target</b>	—	<b>¥7,303</b>
Current Price	—	¥5,732
<b>Implied Upside</b>	—	<b>27.41%</b>

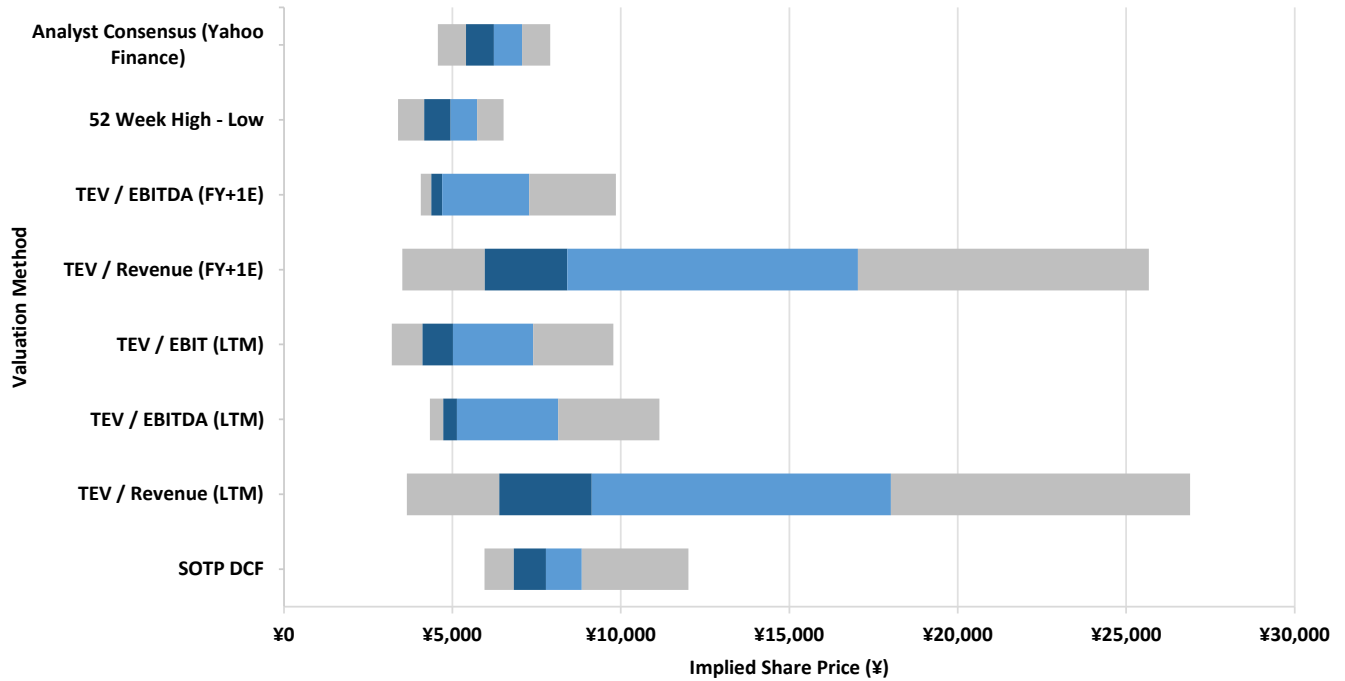
Source: Analyst Estimates

To arrive at our 12-month price target, we apply **a weighted combination of both valuation methods: 90% SOTP DCF / 10% relative valuation**. The dominant 90% weight reflects the structural superiority of the SOTP DCF for a company of TOTO's composition — it is the only framework capable of separately valuing two structurally distinct businesses,



applying differentiated growth and margin assumptions to each. The residual 10% weight acknowledges the inherent limitations of the peer group. The **absence of a true comparator** means implied price ranges carry wider uncertainty than the DCF output. Relative valuation nonetheless serves as a useful cross-check, anchoring the SOTP result against observable market pricing.

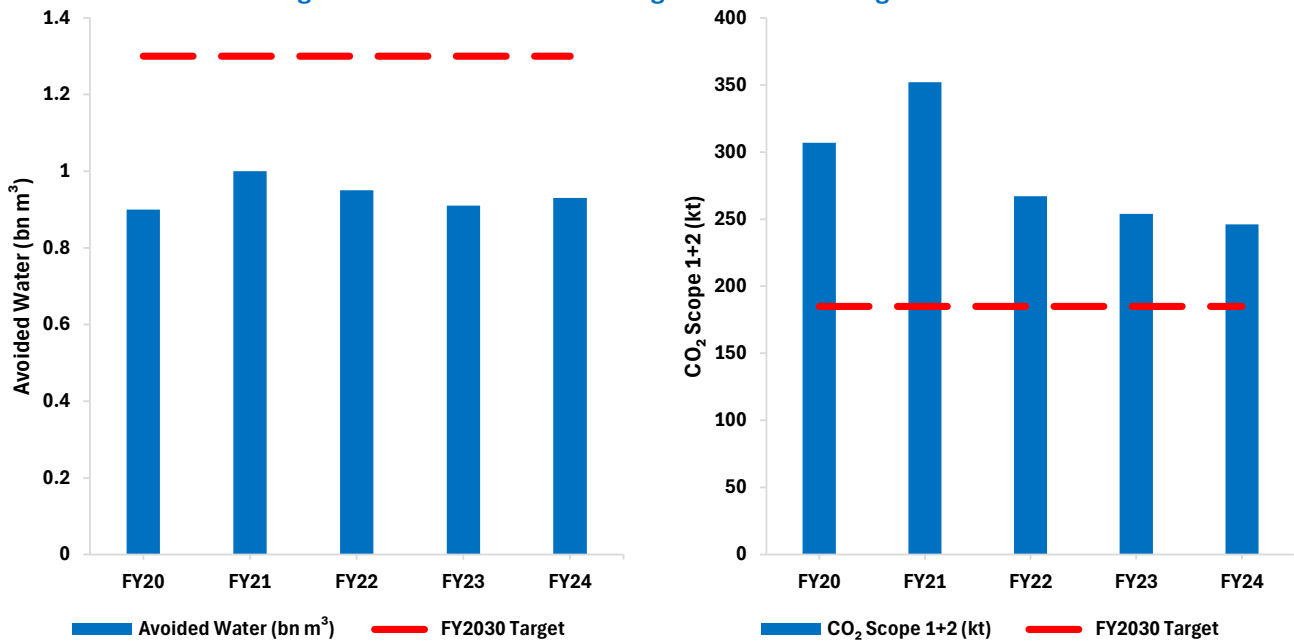
Fig. 8.1 – Valuation Summary: Implied Share Price Range by Methodology (¥)



Source: Analyst Estimates; S&P Capital IQ; Yahoo Finance

## 9. ESG Considerations

Fig. 9.1 - Environmental KPI Progress: Water Savings & Carbon



Source: TOTO Integrated Report 2025



## Environmental

- Avoided water use reached **0.93bn m<sup>3</sup> in FY2024** vs. FY2030 target of 1.3bn m<sup>3</sup> — tracking materially below target
- CO<sub>2</sub> Scope 1+2 emissions: 246,000 tonnes in FY2024; targeting **47.5% reduction vs. FY2021 by 2030**, underpinned by 90% renewable electricity commitment by 2030 and 100% by 2040
- **CDP A-List status** for both climate change and water security for the second consecutive year — held by fewer than 2% of companies assessed globally
- Sustainable products: **78% of total product mix in FY2024** vs. 83% FY2030 target

## Social

- Customer satisfaction (after-sales): **95.1 points** — exceeding the FY2030 target of 95 points
- Employee satisfaction (Japan): **77.8 points** vs. 80-point FY2030 target — **lagging**
- Female managers: 21.2% vs. 21.5% FY2026 target — **narrowly lagging**
- Male childcare leave: 72.6% vs. 85% FY2026 target — **materially lagging (-12.4pp)**

## Governance

- Board: 13 directors; 38.5% independent outside directors; 15.4% female — **meets Corporate Governance Code**
- Executive compensation linked to ROE achievement and sustainability index (WILL2030 indicators)
- Principal governance weakness: **elevated cross-shareholdings and capital allocation discipline** — cross-shareholdings insulate management from market discipline; capital flows toward sub-WACC segments; significant idle cash remains on balance sheet
- Palliser Capital's Value Enhancement Plan directly addresses these weaknesses — see Section 10 for the governance-valuation linkage

**Fig. 9.2: TOTO Social KPI Progress: Actual vs. Targets**

KPI	FY24A	FY26 Target	On Track?	Gap to FY26T	FY30 Target
Employee Satisfaction (Japan)	77.80	77.40	✓ On Track	0.4	80
Female Managers (Japan)	21.20	21.50	✗ Lagging	-0.3	—
Customer Satisfaction (After-Sales)	95.10	94.80	✓ On Track	0.3	95
Male Childcare Leave (Japan)	72.60	85.00	✗ Lagging	-12.4	—

Source: TOTO Integrated Report 2025

**The ESG-valuation linkage is central to our scenario analysis: the bear case is reinforced by governance weaknesses, while the bull case depends on their resolution.**

## 10. Risks and Scenario Analysis

### Key Risks

- **Semiconductor capex volatility.** While ~80% of AC revenue is replacement demand, a prolonged NAND oversupply cycle could delay tool deployments and suppress near-term growth
- **Customer concentration.** AC segment is substantially dependent on Lam Research. Any qualification of an alternative ESC supplier, or structural shift in tool architecture, would materially impair AC revenue
- **Palliser execution risk.** If management resists reform — maintaining excess equity capital, retaining cross-shareholdings, and continuing to underinvest in AC — the re-rating catalyst may not materialise
- **Americas tariff exposure.** Americas operating profit declined 23% year-on-year in 9M FY2026, with TOTO explicitly attributing the decline partly to tariff impacts. Further US tariff escalation could potentially stall the WASHLET penetration story that underpins the International HE growth case
- **FX exposure.** Currency movements reduced consolidated operating profit by ¥1.7bn in 9M FY2026. The AC segment's FX sensitivity is notable given its outsized profit contribution — the ¥1.1bn impact in 9M FY2026 indicates material foreign currency exposure, likely USD-denominated given the primary customer relationship



with Lam Research. Annualising the segment's 9M FY2026 revenue (¥62.67bn) and assuming it all is USD-denominated, a 10% yen appreciation would reduce AC revenue by an estimated ¥6.27bn, equivalent to roughly 23% of segment operating profit.

- **China HE structural losses.** Mainland China HE generated an operating loss of ¥3.6bn in FY2025. Further deterioration or additional impairment would drag consolidated profitability

**Fig. 10.1 - Scenario Analysis: Bear, Base, and Bull Case Implied Share Prices (¥)**

	Bear Case	Base Case	Bull Case
<b>Narrative</b>	Prolonged NAND downturn; no Palliser execution	3D NAND upgrade on track; status quo capital allocation	Full Palliser execution; buybacks + cross-shareholding unwind
<b>AC Revenue CAGR (FY26E–28E)*</b>	10%	~30%	35%
<b>AC Operating Margin</b>	35%	40%	42%
<b>HE Operating Margin</b>	3.50%	4.50%	4.50%
<b>Capital Return Adjustment</b>	None	None	+¥76bn unwind + buyback
<b>AC Terminal Growth Rate</b>	1.50%	3.00%	3.50%
<b>Implied Share Price (SOTP DCF)</b>	<b>¥4,144</b>	<b>¥7,544</b>	<b>¥10,209</b>
<b>vs. Current Price (¥5,732)</b>	<b>-28%</b>	<b>32%</b>	<b>78%</b>

\*AC Revenue CAGR calculated as the geometric mean of annual growth rates over FY2026E–FY2028E. Base case implies a three-year CAGR of 29.3%, derived from individual year growth rates of 33%, 30%, and 25% respectively. Bear and Bull figures represent flat annual growth rates over the same period. *Source:* Analyst Estimates

## Scenario Commentary

The scenario table above quantifies the range of outcomes. The bear case (¥4,144) highlights the **asymmetric dependence of our thesis on AC segment execution** — if the NAND cycle stalls and Palliser fails to secure reform, the investment case deteriorates materially. The base case (¥7,544) reflects our SOTP DCF assumptions. The bull case (¥10,209) captures the upside from **full Palliser execution** alongside an **accelerated NAND upgrade cycle**; in this scenario, the unwinding of ¥76bn in cross-shareholdings and funded buybacks directly accrete equity value per share.

## ESG–Valuation Linkage

The scenario range is largely anchored by governance. **Historically activist campaigns have had limited effectiveness in Japan** — cross-shareholding networks, long-tenure management, and a corporate culture that prioritises stakeholder consensus have collectively insulated boards from external pressure. Palliser has **no guarantee of board engagement**, and TOTO management has made **no public commitment** to any proposed reform. If Palliser fails to secure board-level support, or exits the position before reforms are enacted, **the re-rating catalyst could disappear entirely**. Conversely, the bull case is the scenario in which **governance reform catalyses financial value** — Palliser's proposed ROIC hurdle rates and capital return programme directly address the misallocation identified in Section 5. For TOTO, **governance risk and valuation upside are two sides of the same coin**.



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