Investor Day 2023 Enhancing Corporate Value Q&A

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Speaker：	**Representative Director, President and Chief Executive Officer**	**Kenichi Hori**

Q1: Appropriate Leverage

Regarding your thinking on the appropriate capital structure as shown on page 3 of the presentation, the actual net debt to equity ratio as of the end of September 2023, for instance, is 0.48x. I understand that a weaker yen has the impact of increasing shareholder equity. However, even if we were to recalculate using an exchange rate of 132-133 yen to the dollar as of the end of March, it would still be in the neighborhood of 0.5x.
Of course, you want to have a buffer in case of unforeseen circumstances, but how should we interpret *optimal leverage* as part of an *optimal capital structure*?
I think this also ties into how we should think about *stronger shareholder returns*, mentioned on the same slide. What is your thinking on the *optimal leverage* at this point in time?

Hori: We are highly sensitive to the operating environment and constantly mindful of the totality of conditions observed around the world and what degree of variation we are up against.
Today's operating environment has a high range of variation, making it difficult to predict the future. As such, we believe it is necessary to maintain a certain amount of funds in reserve to ensure security while at the same time striving for sound management of the balance sheet, so that we maintain the ability to respond to unforeseen circumstances.
We operate according to capital allocation principles based on these assumptions. Specifically, we acquire cash through annual earnings and also generate cash inflow through portfolio reconfiguration. As I mentioned earlier, the latter refers primarily to asset sales through portfolio reconfiguration. While considering such allocable cash and ensuring safety, we hope to balance investing in excellent projects and enhancing shareholder returns.
We prioritize projects in familiar areas of business, and that can relatively quickly contribute to earnings to certain extent. In doing so, we gradually expand our portfolio

while taking into account the confidence we have in our own viewpoint and the quality in terms of both cash-generating potential of the projects and the assets themselves.
Specifically, when we determine that we have sufficient control and adequate risk levers or when the deal itself is a high-quality one, we can be flexible in our approach towards leverage to expand our base of work.
With respect to shareholder returns, we have set a target to proceed with a certain percentage of Core Operating Cash Flow (COCF) in the three-year Medium-term Management Plan (MTMP). We aim to steadily achieve this target, and within such options, we anticipate that leverage will settle within an acceptable range with a certain level of flexibility.

<u>Q2: Cash Flow Allocation</u>

I would like to ask about cash flow allocation. Earlier, you talked about cash flow allocation and explained that leverage would be utilized if suitable opportunities arise. However, cash flow allocation for trading companies, including Mitsui, today is basically managed with the aim of keeping free cash flow positive after shareholder returns. This approach ensures that net debt does not increase and equity continues to accumulate, leading to a decline in ROE.
You also mentioned earlier that you would consider leveraging if you find a good deal, but I think a deal requiring leverage on your scale would be quite a significant investment.
Unless such a deal comes up, I think ROE is likely to decline as a general rule. Are you beginning to consider changing the approach of keeping the free cash flow positive after shareholder returns? Could you talk about your policy?

Hori: As part of our overall operational discipline to adapt to the current operating environment, we want free cash flow after subtracting shareholder returns to be positive.
I think this baseline is essential for the MTMP. At the same time, however, in an operating environment where opportunities are increasing, there is naturally a possibility that we may encounter relatively large-scale acquisition opportunities and other deals.
There have already been cases where we've had opportunities but chose not to proceed. Deals only exist in the presence of a counterparty. Opportunities arise, and they could come from within the pipeline. When coming across such large-scale deals, I believe we should consider our tolerance for borrowing flexibly while maintaining an overall balance. We need to assess the quality of the asset and how confident we are that future profits can be secured.

While communicating our ability to maintain such flexibility through discussions with you all, I also believe that we should protect the neutrality of cash flow over the three-year period.
As for return to shareholders, we hope to consider them along with the efficiency and improvement of capital. It would be a slightly longer time frame, for this MTMP and beyond, but we are very conscious of this.
We will carefully monitor the balance between our investments and our goal of improving profitability, ensuring there won't be a structural limit to ROE and taking action as necessary. We will periodically keep you informed regarding this.
We believe it's important to have a certain basis for the major framework within the MTMP.

Q3: Scale of Portfolio Reconfiguration

Earlier, you explained the possibility of more business portfolio reconfiguration in the future. I believe the investment cash inflow of over 500 billion yen from asset sales in the fiscal year ending March 31, 2024, is quite large. Please provide an idea of the scale we can expect going forward.
I think now is a good time to sell because of the weak yen, but if the environment changes, such as an appreciating yen, are there prospects for maintaining a plan of that scale? Do you have any thoughts on the environment or the scale?

Hori: Deals only exist in the presence of a counterparty and are also something to be understood within the strategies of each business division and the context of changing environments. As such, it is quite difficult to predict macro-level figures.
However, I am feeling the increase in the degree of business portfolio reconfiguration mentioned earlier. For example, investment cash inflows, which up until now had been estimated at just over 200 billion yen per year, are estimated to be 500 billion yen this year. I believe the perception that the scale is increasing is probably correct.
In some cases, we have an idea of the functions we can add as a company, and in cases we feel that we have achieved the limit we may divest. In other cases, we may have a very good investment in which a potential buyer could add even more value than we could, and so we could sell it for a much higher multiple than when we entered the deal.
That is a favorable scenario where cash inflows increase, and we hope to grow the scale with combinations of deals like that.
Given that such asset reconfiguration has become a part of our earnings model, our management policy is to handle this flexibly, carefully building up such cases one by one. That's the overall context.

I would like to add that there is also considerable expansion of cluster building with suitable partners in our investments across the globe. For example, in Asia, we are working with the CT Corp group in Indonesia, Metro Pacific Investments Corporation in the Philippines, where we recently announced the completion of a tender offer, and the Penske group, a long-standing mobility company in North America. Through collaborations with these partners, we have created a considerable number of new business bases.

Another example is the gas distribution business in Brazil. Previously, our partner was Petrobras, but now, in the value chain of biomass fuel production from sugarcane, we are partnering with Cosan S.A. (Cosan Group), one of the world's leading producers. I believe there are numerous potential opportunities that emerge from such a partnering strategy. While firmly focusing on this type of work, there's also a pipeline on the investment side that includes promising projects. As such, we hope to proceed with an expansive model that combines proactive cash outflows with appropriate cash inflows, some of which will be converted into business earnings.

As these activities are generally on the rise, I hope it gives you the image of the scale of cash inflows being raised slightly.

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