

Investor Day 2021 Q&A

【Date】 June 8, 2021

【Speakers】 Kenichi Hori Representative Director, President, and CEO

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【Moderator】 Masaya Inamuro General Manager of IR Division

<Q1>

How you will transform your portfolio, from the viewpoint of decarbonization, gathers attention since natural resource and energy business accounts for a large percentage in your current portfolio. What is your vision for the portfolio in 15-20 years and what will be challenges to realize it?

<Hori>

We would like to play an important role in global energy transition. Our energy business has very strong cash generation power. Our LNG portfolio, which will be a leader of energy transition, will continue to be core of our energy business in the medium-term during transition. With LNG as our core, we want to accumulate post-transition business. We believe that weight of LNG in our portfolio is going to lessen in the long-term period and we are going to see more new energy businesses that are going to be large contributor of our profit. We will utilize our knowledge, partnership, network including relationship with oil and gas producing countries, in a clever manner and realize such energy portfolio. In terms of level of profit from energy business in the future, we aim for a higher level than that of current Energy segment. Energy Solution Business Unit, newly established last year, is taking on this challenge.

We also regard business area of Wellness, from prevention to treatment, as our growth engine and expect it to play important role in our portfolio.

In addition, we would like to capture growth of Asian consumer market by leveraging a strong partnership. With our expertise on growing business such as Mobility, Infrastructure, Chemicals, Lifestyle, and Innovation & Corporate Development (including digital expertise from our ICT business), we would like to grow the area of Market Asia as one of earnings pillars. We would like to live up to your expectations by realizing growth of our company with those initiatives.

As for challenges to realize it, we need to introduce new technologies and knowledge.

For example, multiple technologies need to be combined to create a competitive hydrogen business and we would like to coordinate such process. In order to drive data-driven management and create new business models, in business areas such as healthcare, we need to secure digital human resources by utilizing partnership and developing in-house digital human resources. We also need to become more proactive about moving beyond boundaries of existing businesses to enhance our capabilities.

<Q2>

You aim to reduce GHG impact by 2030 to half of what it is in 2020. Please let us know specific measures, including technical measures, to achieve it.

<Hori>

Halving GHG impact by 2030 is an important milestone. We will achieve it through Reduction, Transition, and Opportunity initiatives, and among them, replacement of coal fired power generation assets, one of Reduction initiatives, will be very important and necessary action. We would like to accelerate the timeline of such portfolio restructuring. We are already working on tapping markets and negotiation for individual asset and will disclose it when we realize such transactions. With regards to the portfolio restructuring, we have to ensure economic viability and will pursue transactions that will economically make sense.

We will also utilize technical measures to reduce GHG emissions of each asset. We will try to improve the efficiency of our power plants and consider new technical measures such as ammonia fuel mix.

<Q3>

Please let us know your approach on upstream assets of crude oil in the near future.

<Hori>

We have several competitive crude oil upstream assets, but they could become targets of portfolio restructuring. We have to make sure that those would not be stranded assets. If there are transaction opportunities that would be economically feasible, we have to capture them. We no longer aim for maintaining quantity of reserves.

<Q4>

Please let us reconfirm the meaning of 33% as a target ratio regarding total shareholder returns as a percentage of core operating cash flow which you explained in your opening remarks.

<Hori>

We have provided the guidance of total shareholder returns as a percentage of core operating cash flow in the period of both of previous Medium-term Management Plan (MTMP) and current ongoing MTMP.

When we announced the current MTMP last year, we explained that we would like to improve % of total shareholder returns as compared to approximately 28% on a 3-year average in the previous MTMP and, at this point, around 33% has become the target. Therefore, 33% is the target ratio for three years of the current MTMP. Regarding the shareholder returns for FYE Mar / 2022 and FYE Mar / 2023, we will decide them while having dialogue with market and taking into consideration capital allocation, projects in our pipeline, stock prices and business environments etc.

<Q5>

One of the biggest challenges for you is how to restructure some business domains with low profitability. The Lifestyle segment is one of the examples and my understanding is that its ROA has been less than 1% even if we calculate % based on a base profit without one-time profit or loss. Please explain your strategy including its timeline to improve and optimize the businesses with low profitability.

<Hori>

We continue to focus on our initiatives to improve the business domains having track record of lower return on assets. Though the Lifestyle segment was raised as one example, the recovery from COVID-19 has been seen in healthcare domains and IHH has announced good performance for January through March. In this way, the healthcare business gradually becomes at the stage of reaping the return, or of improving the base of profitability. We can see increased awareness of ROIC including working capital and a return on asset for the areas of food, retail and fashion, which results in comprehensive portfolio review with thorough internal discussions to improve. Especially in food materials, the market prices have been stable or strong, and in the retail business, there are significant changes of consumer trends. If we combine digital marketing with e-commerce, and also connect online with offline, we can have lighter assets with higher ROIC. We are making such an attempt considerably. That's what we have been doing for improving the return on the Lifestyle segment.

<Q6>

Please advise the philosophy of internal profitability indicator including its timeframe and evaluation method for each project, such as CT Corp project and IHH.

<Hori>

It depends on the projects because for some projects we need to extend timeframe to implement our strategy, so we are looking at the individual timelines. For instance, in the case of the CT Corp project, for the time being, earnings will be coming from the coupon of convertible bond, but once the bond is converted into equity, it will be a different stage. And at the same time, we seek to generate additional profits from peripheral businesses through collaboration with CT Corp. Therefore, we will take in incremental steps, but un-periodically we would reorganize our portfolio to maximize our profits as we have been recycling our assets such as Columbia Asia Healthcare. In this

sense, we have to look at the longer-term profitability indicators. It is important to build up earnings base where we generate profit as a flow, which can achieve a satisfactory outcome when we take a snapshot. Therefore, we would like to show strong numbers at a given point in time even though many projects are running on different timeframes.

<Q7>

You explained that you will be increasing the ratio of total shareholder returns as a percentage of core operating cash flow up to around 33% in current MTMP. Please advise the background of it. Is it because you are confident that you can generate sufficient returns through various measures such as implementation of ROIC, etc, or is it because you have not allocated enough to shareholder returns in the past?

<Hori>

Looking at the cash flow during MTMP, it is true that our earnings base of cash flow is increasing due to the enhancement of earning power and this is a basis for our strategy.

Another major factor is that, in the energy sector, for example, we have shifted to value over volume strategy which means that we will not seek to maintain reserves but to introduce a more flexible approach, and as a result, cash out for sustaining Capex is now within the lower range of our forecast. The positive impact of portfolio restructuring will also be a factor here. We are discussing our shareholder returns by reviewing the forecasted amount of Management Allocation which considers what I have said so far. We have already disclosed that we will allocate 140 billion yen for share buybacks, 40 billion yen for dividend increases, and 150 billion yen for growth investment. This allocation is based on current situation, but it could be possible that we can find out more high-quality projects in the future, so we will consider this allocation based on all of these factors. We believe it is appropriate to define our cash flow allocation based on a comprehensive consideration of the cash balance, projects in our pipeline, and business environment.

<Q8>

I have a question about the balance of investment of management resources. In the long term, I believe that you will plant seeds for the future in the Strategic Focus areas, while in the near term, you will steadily invest management resources in existing pipeline projects as a growth driver. For example, if a pipeline deal does not proceed on schedule due to unexpected impairment or country risk issues, how will the investment discipline, including deal quality and risk management, be reconsidered and reflected in terms of allocation of management resources? In the future, I think your strategy will be to invest in a wide range of new technologies and energy materials. I would like to know your thoughts on how to balance the allocation of management resources and the balance between investments in some areas, such as natural gas, which will eventually peak out, and investments in other areas, such as ammonia and hydrogen, which will be focused on cutting-edge investments.

<Hori>

Our perception of the operating environment is that there are many variables, the global issues are massive, and there are many major trends occurring that we have never experienced before. We believe that it is very important for corporate management to build up resilience against such things. We believe that we must expand our business by networking globally, focusing on regions where we are relatively strong. The speed of recovery from Covid-19 will vary from region to region and geopolitical movements cannot be easily predicted 10 years in advance, so I think we will have to adopt regionally diversified strategies while networking globally.

In existing businesses, there are also significant developments in initiatives across different operating segments. For example, when Mobility, Energy, and Chemicals business units work together, they can create the next generation of energy-conscious vehicles that are earth-friendly and efficient. This is the kind of idea that comes from talking with various players in the existing businesses every day. In this way, I feel that there are more and more opportunities to create new businesses that are a variation of the existing businesses. I believe that how to combine the existing businesses with new businesses will be very important for the future management of the company.

To give you an example of how to invest in a wide range of new technologies, in the case of hydrogen and ammonia, if we want to produce blue hydrogen, we need to understand the geological structure in the energy-producing countries and think about how to capture carbon and produce hydrogen there. It requires experiences, knowledges and a keen eye for which new technologies can be utilized, and this can be done not by us alone, but by working with existing partners. When we think that we can see something that others cannot, we will start to select technologies. For example, if we try to transport non-hydrogen, we will have to add the technical element of transporting ammonia and combine it with a new rationale based on real operations. We will not blindly challenge new technologies, but will evaluate their feasibility and effectiveness, and proceed based on the criteria of whether we can collaborate with partners who have experience.

<Q9>

You declared your support for TCFD and have provided various qualitative analyses in your Sustainability Report, but I understand that your quantitative analyses are still limited. I hope that, in the near future, you will provide your quantitative analysis that is clear and comprehensive. I would like to know your thoughts on the disclosure of quantitative analysis required by TCFD in coming ESG presentations and IR activities.

<Hori>

We have established the Sustainability Committee that analyzes and proposes to management the action plans that each company should take with regard to the environment in keeping our Earth clean, as well as our own portfolio, including how to measure them. We have also established the Portfolio Management Committee, which reviews our portfolio strategy. These two committees work together to discuss how to achieve our visions while also looking at various quantitative indicators. We are currently analyzing management data while determining how to measure quantitative indicators and how to capture them in a long industrial chain, and we are preparing to present some of these at the ESG Day scheduled in December.

Taking the portfolio restructuring of the power generation business as an example, it is important not only to set targets but also to complete the transaction responsibly. While the economic viability of our businesses is important, it is also important to consider with which partner and how the transaction will take place. I think it is our responsibility to show a combination of long-term goals and actual results. I think it is necessary not only to present targets, but also to show the figures by verifying the actual values and targets.

[END]