Q&A at Investor Meeting

Financial Results for the Year March 2020

Presentation Date: Tuesday, May 12, 2020 15:30 to 16:30

Presenters: Takehiko Kakiuchi: President and Chief Executive Officer
Kazuyuki Masu: Executive Vice President, Chief Financial Officer
Yuzo Nouchi: General Manager, Corporate Accounting Department
Tatsuhiko Terada: General Manager, Investor Relations Department

Questions and Answers

Q. What do you think will drive profit growth from now, even though the outlook for the economy after the COVID-19 pandemic subsides is unclear? What is your management approach in the current business environment? We also think it'll get much tougher to accelerate asset disposal under current conditions, and appreciate it if you'd show us the direction and/or policy such as cost reductions and/or contrarian investments to take advantage of reduced asset prices.

A.

- As you pointed out, it is difficult to forecast economic conditions after the COVID-19 epidemic subsides, thus we will consider a range of countermeasures based on various scenarios. We see this as a time for restraining investment, so will strictly maintain financial discipline to look for opportunities.
- In terms of growth strategy, our Group-wide policy since before the pandemic, has been to advance systemization through digital transformation (DX) to improve efficiency and effectively utilize data. Based on this policy, the business groups are already advancing individual projects, and we will continue to diligently move forward with efforts in this area.

Q. The investment leverage ratio, one of the indicators used to consider share buybacks, was 56% at the end of fiscal 2019, exceeding MC's target range of 40-50%. It seems like additional share buybacks are unlikely during the period of Midterm Corporate Strategy 2021. What are your current thoughts on share

buybacks?

A.

- First, please understand that we do not make decisions about share buybacks based solely on the investment leverage ratio. While we only just completed the buybacks announced last year in April, they demonstrated the efficacy of buybacks as a means of bolstering the share price, thus we will make decisions going forward and don't think our judgement should necessarily be restrained solely by the leverage ratio.
- The investment leverage ratio is currently high because of major investments in fiscal 2019, such as the acquisition of Eneco. We aim to return the ratio to the target range over six years, or possibly as little as three years. As such, we are now at the most leveraged stage we can go. We plan to return the investment leverage ratio into the target range as profit accumulates going forward.
- Despite declining performance as a result of the worsening business environment, we are maintaining our commitment to progressive dividends. In addition, earnings per share is up due to the decrease in the total number of shares achieved through share buybacks. To make sure that shareholders feel the full benefit of this, we are holding total dividends amount unchanged to increase the per-share dividend. We appreciate if you kindly understand that our policy is to continue to proactively provide shareholder returns in this way, mainly through dividends.

Q. Upon the 2008 financial crisis, MC announced to restrain investments and has prioritized financial soundness. Given the uncertainty of fiscal 2020 forecasts, what are your current capital allocation priorities?

A.

- The debt equity ratio (DER) is currently below 1, though it was around 2 at the time of the crisis. Trading companies tend to have higher DER, and business operating companies tend to have lower DER. As I recall, our DER was high due to increasing investments before the 2008 financial crisis, thus we had to lower it. Thanks to those efforts, our financial position today is not like it was then.

- Since adopting our current management structure in fiscal 2016, we have consistently maintained a basic policy of ensuring positive free cash flows, excluding working capital fluctuations, after the payment of dividends. In short, we have avoided allowing interest-bearing liabilities to increase. In fiscal 2019, we executed major investments, which increased outflows, but this was all built into our plans beforehand. Going forward, we will continue to maintain financial discipline based on the above strategy.

Q. Does that mean that you will maintain positive free cash flows (excluding the impact of working capital) after dividends by restricting investments even if financial results deteriorate in fiscal 2020?

A.

- In anticipation of large-scale investments like the acquisition of Eneco, we had been steadily securing the necessary funds since the period of the previous midterm corporate strategy, and returned the excess funds to shareholders by means of share buybacks. As such, it is not that we are being forced to restrain investments for the next two years because of the major investments we have made; rather, we always planned to limit investments before and after executing major investments and to allocate assets in an orderly manner. Going forward, we will maintain our management policy based on certain standards of financial discipline, as before.

Q. Given the impairment losses recorded on MC's investment in Mitsubishi Motors Corporation (MMC), what is the purpose of holding this investment, and what is your strategy for it going forward? Where does MMC's relationship to Renault and Nissan stand?

A.

- MMC and MC are advancing a strategy together to promote certain vehicle models and focusing management resources on Southeast Asia, where we have the strength. We will continue to support MMC in these new endeavors.
- As for the relationship among MMC, Renault and Nissan, we are not in the position to provide comments.

Q. When the external environment worsens, it seems that reductions in profit are rather large not only in market-related segments, but also business-related segments, and this may be due in part to cost structure. Any specific cost cutting measures undertaken?

A.

- The cost reduction measures appropriate for a given business depend on the content of that business, and our response in businesses that are performing well will be different from that in businesses where demand is weak. Accordingly, we will not apply uniform measures across the Group. Rather, we will implement measures tailored to the business of each investee, such as cutting costs to improve productivity and reducing production to minimize losses.

Q. To what extent is the fall in oil prices factored into impairment losses of approximately ¥10.0 billion in the Canadian Shale Gas business? Also, is there any risk of impairment in the LNG business, including assets measured at FVOCI?

A.

- Our shale gas assets in Canada are gas fields, but they also produce condensate, and the income from these liquid products continues to support revenues. This business owns many wells. We recorded impairment on 60 wells to account for worsened profitability due to the recent drop in the price of WTI and/or stoppage of extraction.
- There are a number of projects measured at FVOCI in the LNG business, but the market value of assets measured at FVOCI is re-evaluated at fair value every year, and any difference from the carrying amount is recorded under OCI and reflected in equity, so the need to book impairment does not arise.
- Regarding LNG projects not measured at FVOCI, there is currently no change to our medium- to long-term forecast.

Q. LNG spot prices and prices linked to the price of oil are declining, reflecting the plummet in oil prices. Do you expect this to be only temporary? Or are you thinking that there will be no need to record impairment even if current

conditions continue for longer?

A.

- We cannot currently make any judgement about how long prices will remain low.
- While fiscal 2019 results were impacted by falling LNG spot prices, most of our revenues are based on long-term contracts, and only production in excess of our plants' designed capacity is sold at spot prices. As such, although profit from spot sales is down due to reduced spot prices, that does not necessarily mean that the business will record a net loss.

Q. I understand that you are partnering with NTT to create new systems across a wide range of industries through DX, aiming to eventually generate sales in the hundreds of billions of yen. Could you give us more details about the timetable and scale of profit?

A.

- We have begun initiatives in a number of fields, but the furthest along is DX in food logistics, where we are reducing logistics center inventories by linking data from retailers and wholesalers. NTT is helping on the tech side. Ultimately, we aim to roll out the platforms we are building to other companies in the same industries to further improve the efficiency of entire industries.
- We have long operated businesses that connect manufacturers with end users in all kinds of industries. Accordingly, at present, our basic approach is to begin by utilizing DX to enhance industrial efficiency in these businesses.
- We do not expect these initiatives to generate profits in the tens of billions of yen right away, but we have already formed a Group-wide task force that is working with related companies to implement specific projects, and we expect some of these to reach commercialization within fiscal 2020.

Q. How is the COVID-19 pandemic currently affecting your key businesses?

A.

- The Group operates a wide range of businesses and includes 1,700 companies; the impacts of COVID-19 run the gamut. We cannot accurately maintain a comprehensive picture of the rapidly evolving conditions across all our businesses, so it is impossible to make any rational forecast. As such, it is currently difficult to say what impact COVID-19 is having.

- However, I can tell you about the impact on the mining business, as an example. In the Australian Metallurgical Coal business, all our mines have continued to operate. In the Copper business, in Peru, operations at the Antamina mine have been suspended, and at the Quellaveco mine, where production has not yet begun, we have decided not to resume full-scale construction for another three months or so, focusing instead on maintaining the site and preparing to recommence work. In Chile, all three of our mines remain in operation.
- As this illustrates, even within a single business, the impact of COVID-19 can be completely different from one project to the next, so we cannot currently forecast results.

Q. You said that your basic policy of maintaining positive free cash flows after dividends is unchanged. In light of the changes in the business environment due to COVID-19, do you expect to make any changes to, for example, the targets or speed of management asset allocation?

A.

- Our basic policy will not be changed whatsoever. The business environment is much harsher than before the COVID-19 pandemic, and given the decrease in underlying operating cash flows compared with our initial assumptions, we will have to consider ways to tighten our purse strings.
- In the first place, since we formulated Midterm Corporate Strategy 2021, we have never intended to use all our underlying operating cash flows. Indeed, these cash flows were not expected to be sufficient to fund all the investment projects we were planning. To raise the necessary cash through asset replacement, we have sold approximately ¥2.0 trillion in assets over the past four years. This basic policy remains unchanged going forward.

Q. With the worsening business environment, I'm sure it is difficult to know what the results of MC's business management initiatives will be, but given what

you do know about these results, are there any initiatives you might accelerate or change?

A.

- Our policy of advancing Group-wide DX is unchanged. By building platforms in each industry and through digitization we will create mechanisms for generating profit at the industry-wide level, encompassing MC as well as our Group companies and overseas partners.
- In addition, the acquisition of Eneco has provided us with a foothold in renewable energy, an important field in terms of addressing environmental problems. Building on this, we will gradually shift toward initiatives in renewable energy.
- We will continue to hold fast to this policy going forward.

Q. How much profit do you expect in fiscal 2020, looking just at the three business groups where the impact of COVID-19 is expected to be limited (Consumer Industry, Food Industry, and Petroleum & Chemicals)?

A.

- Even if we were to add up the profit of those three business groups, the result would be meaningless, so I cannot answer your question at present.