

Q&A at Investor Meeting
Financial Results for the Year Ended March 2021

Presentation Date: Friday, May 7, 2021 16:45 to 17:45

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Questions and Answers

Q. In terms of the 380 billion yen guidance for FY2021, how do you view your current true strength, especially with the ordinary income for the 4th quarter (3 months) exceeding 120 billion yen? There seems to be a difference with your peers in the full-year outlook, but is this due to the headwinds in the environment surrounding businesses such as metallurgical coal? Does it also include the impact from the unprofitable businesses that you are currently working on?

A.

- The figure for the 4th quarter (3 months), excluding one-off items, is approximately 120 billion yen. However, there were factors such as the pricing of metallurgical coal normalizing and being higher than what it is today due to price arbitrage in the market, as well as the concentration of profit in the period, due to the seasonality in Eneco's business, etc. When excluding these one-off factors, we believe the true strength of the 4th quarter (3 months) should be slightly below 100 billion yen.
- The 380 billion yen in the full-year guidance includes the effect of the difficult business environment, caused by the sluggish metallurgical coal market due to Australia/China relations.
- We have already begun working on the restructuring of the loss-making and low-profitability businesses. In terms of the entities for which the process has been completed, there will be no losses going forward, but there will be losses related to the restructuring in both FY2020 and FY2021, depending on when the process was started. As for FY2021, the losses from restructuring will be offset by the reduction of losses from the business itself, and there will not be a significant impact on our earnings.
- In terms of further improvement in earnings from the 380 billion yen, MDP generated only around 10 billion yen of earnings in FY2020, compared to more than 100 billion yen in FY2019, and more than 200 billion yen in FY2018. We therefore believe that if the metallurgical coal prices come back, earnings will recover to past levels.

Q. When considering the operating cashflow was 625.2 billion yen in FY2020, despite the tough business environment, you should be able to continue your policy of progressive dividends, even after the current Medium-term Management Plan period. What are your thoughts on dividend policy for FY2022 onwards?

A.

- There is no change to our policy of progressive dividends until FY2021 which is the last year of the current Medium-term Management Plan. We cannot comment today on the next Medium-term Management Plan period in FY2022 onwards, but considering the current status of our cashflow, we should be able to continue paying out the current level of dividends of around 200 billion yen per annum, at least from a financial perspective.

Q. In terms of your shareholder return for FY2021, can we assume there to be an increase in dividends, based on the assumption that you will outperform your guidance? The investment leverage ratio of 54% as of the end of FY2020 was slightly above your comfort level. Would you consider share buybacks as one of the options for capital allocation?

A.

- The dividend payout ratio temporarily exceeded 100% in FY2020, but it will be 52% based on the FY2021 guidance. We will decide on dividend payouts flexibly, depending on the profit level at the time, and taking into consideration factors such as the average dividend payout ratio of the top 100 players in the market being around 40%, etc.
- There is no change to our policy of looking at factors such as the investment leverage ratio when considering share buybacks, and we will flexibly buy back shares if the leverage goes below the level we are comfortable with. Leverage can also be expected to improve depending on our earnings, and we will continue to contemplate share buybacks while monitoring our leverage.

Q. In relation to the capital allocation for FY2021, are there any plans for investments or asset disposals? Which areas/domains are you planning to make new investments in?

A.

- We consider investments based on the 3-year Medium-term Management Plan period. Due to investments such as the Eneco acquisition, and our investment in HERE, etc. taking place early on in the period, the investment leverage ratio is currently above the level we are comfortable with, and we therefore need to control new investments to a certain extent. However, we have no intention whatsoever of limiting the gross amount of our investments, and we seek to maintain financial discipline by controlling net investments, by using proceeds from disposals as part of the asset replacement strategy. Therefore, when making new investments, we will also conduct asset replacements, and control our investments to generate a positive cycle.
- In relation to DX, it is the midstream that will be rationalized, and we therefore expect opportunities for investments in the upstream and downstream areas. We need to work on energy-related businesses as transition in the mid-to-long term. As we have footholds in businesses such as LNG and Power Solutions, we plan to make continuous investments in various areas, thereby changing the nature and quality of the current infrastructure.

Q. As for the metallurgical coal market, pricing recovered in the 4th quarter (3 months), but is falling again recently. We believe your pricing assumptions for metallurgical coal in the FY2021 guidance are relatively conservative, but how do you view the current market conditions?

A.

- The current price is below USD110/ton, which is not rational, and we do not expect this to continue. China is importing from countries other than Australia at extremely high prices and, although it may take some time, there will be price arbitrage, and market prices will recover to a certain extent.
- Aside from pricing, currency also has an impact. Although MDP's revenues are in U.S. dollars, its costs are Australian dollar-denominated, and the weaker U.S. dollar and stronger Australian dollar due to price hikes in natural resources other than metallurgical coal are leading to an increase in MDP's costs. Therefore, currency is also one of the variables causing the profit recovery to be sluggish.

Q. What kind of portfolio do you have in mind for “Reduce”, which is part of your EX strategy?

A.

- If ammonia is to be used as the world shifts to a hydrogen society, LNG production facilities could be used to produce ammonia. By combining this with CCU/S to be conducted locally, we are currently thinking of moving towards a decarbonized society, and we believe this to be an area that we can begin working on most promptly as well as realistically.

Q. Please explain the timeframe for achieving quantitative results from your initiatives on “Key Issues for the future”. Are you expecting contributions in the FY2021 guidance, or should we expect it in FY2022 onwards?

A.

- There are almost no investments related to “Reduce” that will take place in FY2021. We are conducting proof-of-concept trials to transport ammonia to Japan, but we are not in the phase of making investments yet. LNG production facilities can be used to make ammonia, and we are currently conducting studies, including on geopolitical aspects of regions such as the Middle East, Asia and North America, in order to turn this concept into a reality.
- We have included some earnings contribution in the FY2021 guidance from renewable energy such as wind and solar power. However, this is part of the process of doubling the ratio of renewable energy towards FY2030, and profit contribution in FY2021 will be limited compared to FY2030.

Q. Your earnings in FY2020, excluding one-off factors, is around 320 billion yen. If the 380 billion yen figure for FY2021 does not include one-off factors, that means there will be profit growth of around 60 billion yen year-on-year. What are the drivers of this improvement?

A.

- In the LNG business, there is a 6 month time-lag before the oil price is applied, and the rise in oil price will take effect from FY2021, leading to profit growth. Moreover, in relation to Mitsubishi Motors (“MMC”), although we will not comment on the details of our outlook until they announce their results, simply not repeating the huge loss in FY2020 will lead to a significant improvement in profit. There are various other factors that have positive/negative effects on our profit, and for example we are expecting a market recovery in the salmon business.

Q. Any progress in the reinforcement of the downstream areas, which you raised as one of the top priorities in the Medium-term Management Plan?

A.

- We manage our business portfolio through a matrix of 12 segments, and have already taken firm steps in the upstream areas. Because our business was founded in the midstream areas, we have footholds in all industries, but have been somewhat weak in the downstream, which is closest to consumers. This was behind our decision to acquire Eneco, which sells electricity mainly generated by renewable energy sources to households in Europe, centered in the Netherlands. We also invested in HERE, the location technology company. As a result, we believe we have improved the balance between the up, mid and downstream of our portfolio, as we initially intended.
- Going forward, the key challenge will be realizing DX digitally connecting the upstream with the downstream, or accumulating data from consumers and using AI to connect that to the upstream. We have already materialized around 60 projects, and are working on improving productivity, rationalizing and reducing losses such as food loss, by connecting data to the upstream or horizontally.
- We plan to monetize these DX businesses by digitalizing the capability to come up with ideas. However, this is only the beginning, and the first step will be to implement these ideas in our Group companies, and then share with companies outside the Group as we generalize those practices. We are currently applying DX within the Group, thereby seeking to grow the profits of each Group company.

Q. The 53 billion yen earnings guidance in FY2021 for the Automotive & Mobility Group seems somewhat conservative, considering the true strength of the Group. What is the outlook on the Thailand and Indonesia businesses, as well as other businesses?

A.

- The Automotive & Mobility Group consists of the MMC business and the Isuzu business. We will not comment on the details of MMC, because they have yet to announce their results, but simply removing the huge loss in FY2020 will lead to a significant profit improvement. Meanwhile, the Isuzu business in Thailand was extremely strong, despite the weak market environment, and we have factored in the possibility of a slowdown in the business, which led to the 53 billion yen guidance for the entire Group in FY2021.

Q. The profit guidance for the Food Industry Group in FY2021 is 41 billion yen, up 1.6 billion yen from FY2020. This seems conservative, when considering the recovery in the salmon market. What assumptions did you use in the FY2021 guidance?

A.

- In FY2020, Cermaq's earnings were weak due to market deterioration, while the meat business did well, thanks to stay-home demand from COVID-19. Meanwhile, in FY2021, we expect profit to grow at Cermaq, due to improvements in the salmon market, but there could be a negative rebound in the stay-home demand for the meat business. Considering these factors, we are expecting only a slight year-on-year recovery for the overall Group.

Q. Why were you not able to achieve the 200 billion yen guidance for FY2020? And based on this experience, did you make any changes in how you set your guidance for FY2021?

A.

- The main reason is the impairment loss for Lawson, which we were not expecting when we announced the 200 billion yen guidance last August. We have taken a cautious approach in setting the FY2021 guidance, and are not assuming a significant rise in natural resource prices, while anticipating a decline in oil and copper prices from the current levels.

Q. When you announced the 3rd quarter results this February, you still had the 200 billion yen outlook. What changed since then, which led to you not achieving the target?

A.

- The Lawson impairment is the main reason. The figure excluding this impairment was roughly in line with the outlook we had in mind when announcing the 3rd quarter results.

Q. You say Lawson has potential, and that you will pursue a new business format. Any details?

A.

- We believe all convenience store chains have potential. Lawson, with around 14,000 stores, has very close access to consumers from a data marketing perspective. This platform could be used by players in other industries, which will generate various business ideas. There are almost no institutions in Japan, other than the top 3 convenience store operators, that have this level of access to consumer data. This is why we believe in Lawson's potential value.
- On the other hand, in terms of food supply, demand is expected to shrink in Japan, with the declining population and the aging society. Therefore, it is necessary to provide services that are completely different from the past, and our challenge is to bring out the potential value of Lawson. We will not go into the details today, but will seriously consider what we can do.

Q. The pricing of some commodities has recovered to pre-COVID-19 levels. How do you view the economy and business environment going forward?

A.

- As for the impact from COVID-19, the U.S. has pretty much recovered, China has already recovered, and it is a matter of time before Europe recovers. However, Asia, especially Japan seems to take more time for recovery.
- Meanwhile, trends such as digitalization using AI, and the energy revolution driven by decarbonization are taking place globally, creating a once in a century opportunity. It is important for us to determine how to adapt to this major change in the environment.