Investor Briefing on FYE 2022 Business Results and FYE 2023 Management Plan: Q&A Summary

This document is an English translation of a statement written originally in Japanese. The Japanese original should be considered as the primary version.

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Respondents: Keita Ishii, President & Chief Operating Officer
Tsuyoshi Hachimura, Chief Financial Officer
Hiroyuki Naka, Chief Strategy Officer, and Chief Digital & Information Officer
Kazuaki Yamaguchi, General Manager of General Accounting Control Division

1. **Economic Environment and P/L Related**

Q: What impact will inflation have on the consumer-related sector, including the food business? Also, with the lockdowns being enforced due to China's zero COVID policy, what kind of impact will that have on China-related businesses?

A: Even while on the verge of an economic downturn, ITOCHU has leveraged its strengths and enhanced its economic resilience through hands-on micro-management. To enable each business to take initiative, we aim to thoroughly implement the "earn, cut, prevent" principles in each business to enhance their core profit capability and build an even more robust earnings base. Although inflation is partially impacting our consumer-related sector, the key point is whether it is possible or not to pass on costs to product prices in a timely and appropriate manner in each business. Regarding manufacturing-related Group companies, such as those in the food business, while there are some cases where it is currently not easy to pass on costs, downstream businesses that directly interact with consumers are steadily working to pass on the costs. Trade that leverages general trading company functions, including in energy and chemicals, will need to work to pass on costs and secure margins while carefully monitoring the inflation situation. In addition, the North American construction materials business has worked to sufficiently assess demand amid a turbulent market and enhance profit margins by raising prices in advance. As a result, FYE 2022 consolidated net profit was high at around ¥20.0 billion, but it will be difficult to enhance profit margins as markets calm down. Regarding cost hikes in tandem with inflation, we will need to think about ways to address that from a market-oriented perspective. Since April, three major convenience stores have raised product prices, and consumers seem willing to forgive a certain level of price increases. In some areas of the consumer-related sector besides convenience stores, there are currently businesses that are not making much headway on passing on costs, but they will need to provide new added value from the customer perspective, sell attractive products, and secure profits.
Regarding the current situation in China, the GDP growth rate between January and March 2022 was 4.8%. Although it did not meet the government's annual target of 5.5%, it was higher than the 4.0% between October and December 2021 and the 4.3% market consensus, showing it is on an improvement trajectory. COVID-19 cases peaked in China in early April, and lockdowns were implemented in 45 cities that account for around 40% of China's GDP. Although we cannot fully relax, case numbers fell significantly from the end of April into May, and lockdowns are being lifted. Amid this situation, consolidated net profit related to China in FYE 2022 was around ¥260.0 billion, accounting for around 30% of total consolidated net profit. Excluding profits of CITIC and IMEA iron ore trade to China, this was around ¥50.0 billion, approximately 6% of the total. As for the impacts of lockdowns on CITIC, we have determined that the downward pressure risks are limited due to the following three points. The first point is that, under the Chinese government's policy on strengthening state-owned companies, we think that CITIC can receive benefits from the government's support and economic measures. The second point is that CITIC outlined a five-year plan from FY 2021 to 2025 to double consolidated net profit to HKD100.0 billion and is making steady progress toward that goal, achieving a very high level of consolidated net profit in

FY 2021 with HKD70.2 billion, up 24% year on year. CITIC has a high success rate for its plans to date. It formulated a high growth rate plan in FY 2022 to achieve its five-year plan. However, ITOCHU's FYE 2023 plan still takes a conservative approach and incorporates various risk factors. The third point is that CITIC's January to March FY 2022 results, which ITOCHU will record in the first quarter of FYE 2023, showed good progress, with the mainstay CITIC Bank increasing profit by 10% from the same period of the previous fiscal year. For the above reasons, we think the downward pressure concerns are limited. On the other hand, iron ore trade with China is currently being affected by the lockdowns. Since economic stability and expansion represent the largest issue for the Xi Jinping government as he aims for a third term in office, it is expected that infrastructure and capital investment will further increase going forward. We therefore do not think that demand for iron ore in China will fall by much. Lastly, regarding consolidated net profit related to China excluding CITIC and IMEA iron ore trade, under the FYE 2023 plan, we accounted for such impacts as restrictions on corporate activities due to protracted lockdowns and resulting economic recession, and conservatively plan for a 20% decrease in profit, or around ¥40.0 billion. We anticipate the Chinese government's financial and monetary measures through lower corporate taxes, and we do not assume other major impacts that would lower results under our conservative plan.

Q: You mentioned that switching to a new supply chain would be a good opportunity for entering new businesses, but what specifically did you have in mind?

A: For example, if the shift away from Russia continues, including import bans on Russian oil, it will be necessary to find alternative sources from one of the few other oil-producing countries in the world, and we assume that will effect changes in the oil and gas supply chain. Because we need the cooperation of oil-producing countries that would have sympathy with western European nations, it will be very difficult to build an oil and gas supply chain in the short term. But when this switch in supply chain occurs, it could be an amazing opportunity in resource-related businesses. Ammonia fertilizers, which have natural gas as a raw material, could also be forced to change supply routes if it becomes difficult to import the gas from Russia. Furthermore, there could also be business opportunities that include technologies for manufacturing fertilizers that are not dependent on fossil fuels, do not emit carbon, or are biologically sourced. In addition, production of the petroleum products of jet fuel and gasoline is increasing in the United States and Middle East, and they will likely need to change their suppliers. Going forward, because we assume that the business environment in the basic industry sector and non-resource sector will gradually change in a similar way, we will continue seeking out good opportunities to enter new businesses through our global network as a general trading company.

Q: What were the factors behind the decrease in core profit from 3Q to 4Q of FYE 2022 and, looking at performance, how did the momentum change?

A: Core profit was around ¥171.5 billion in 3Q and around ¥140.0 billion in 4Q of FYE 2022, a decrease of around ¥31.5 billion. Because it partially reflects seasonal and other extraordinary factors, we expect a recovery in 1Q of FYE 2023. The Machinery Company's ¥6.3 billion decrease in core profit (from ¥20.4 billion to ¥14.1 billion) reflected the impact from an increase in temporary expenses, including higher bonus provisions at Group companies in line with strong business performance, and its profit is expected to normalize in 1Q of FYE 2023. The Food Company's ¥2.5 billion decrease in core profit (from ¥13.2 billion to ¥10.7 billion) was mainly due to seasonal factors, as profit decreased following 3Q, which typically sees especially high demand. In addition, Dole saw a worsening of expenses in line with higher distribution costs in 4Q, but we expect an improvement from FYE 2023. The General Products & Realty Company's ¥7.2 billion (from ¥20.5 billion to ¥13.3 billion) reflected a normalizing of the soaring profit margins in North American construction materials businesses in line with soaring procurement prices and a lull in demand for construction in winter. We expect these seasonal extraordinary factors to fall away and see a recovery in 1Q of FYE 2023.

Q: Core profit in the resource sector for the FYE 2023 Plan is around ¥190.0 billion, down ¥9.0 billion year on year, but what assumptions have you made on resource prices?

A: We have not disclosed the resource price assumptions for metal resources, but the core profit for metal resources is expected to include a major decrease in iron ore profit. On the other hand, profit is expected to increase in coal, albeit modestly, as ITOCHU has small exposure. In addition, regarding energy resource sectors, although we expect oil prices to increase, we expect the amount to decrease, and the total will decrease by ¥9.0 billion.

Note: After holding this briefing, the Group company Tokyo Century Corporation announced it will record impairment losses in FYE 2023 for its exposure related to leased equipment (around USD380 million) within its total exposure to Russia as of March 31, 2022 (around USD600 million). Regarding the profit after tax impact of ITOCHU's portion (around negative ¥8.5 billion) related to this impairment loss recording, we have already accounted for it in the FYE 2023 plan.

2. **Cash Allocation (Shareholder Returns and Growth Strategy)**

Q: Can you tell us about the cash allocation policy?

A: Under the current business environment, the value of investment candidates within the non-resource sector may be lower than assumed, so it will be important to proactively select candidate projects while calmly assessing their value. Considering growth going forward, it would be limiting to only brush up existing investments so we think it will be important to proactively promote new investment, and we will not subordinate investment in terms of cash allocation. ITOCHU established stringent investment criteria, and regarding overseas investments, the hurdle rate is rising due to a weaker yen and inflation, but if they clear the investment criteria and have future potential, we will invest in them. We do not assume there will be extremely large investments at a ¥600.0 billion level, such as CITIC in FYE 2016 and FamilyMart in FYE 2021, but we are discussing several investments on the scale of ¥100.0 billion. In addition, we think that we can move forward on these investments without exerting leverage. ITOCHU aims for a credit rating level that will not cause concern for fund procurement even amid a harsh business environment. In this light, shareholder equity is currently ¥4.2 trillion, and the ratio of shareholders equity to total assets is over 30%. NET DER is 0.5 times, which is much lower than the 0.7 to 0.8 times we assume, and at a comfortable level for rating agencies. In FYE 2022, core free cash flows after deducting shareholder returns accumulated. There were investments that were shifted from FYE 2022 to FYE 2023, and there are investment pipelines being considered by each sales department. We need to control the balance between shareholder returns and growth investments while managing these factors. Quantitative disclosures regarding this will be challenging, but it is up to management whether this balance can be achieved. We will achieve positive core free cash flows after deducting shareholder returns while constantly thinking about increasing satisfaction for shareholder returns based on the monitoring of the share price. We will continue conducting shareholder returns that are not inferior to our peers.

Q: In FYE 2023, dividends per share were set at a minimum of ¥130, an increase of ¥20 from FYE 2022. What is your basic idea for decisions regarding shareholder returns? When the FYE 2022 results for 3Q were announced, there was mention of shareholder returns that consider a total shareholder return ratio of 30%. Is 30% used as a benchmark for shareholder returns?

A: In FYE 2022, based mainly on harsh opinions from the market that ITOCHU's shareholder returns policy is inferior to that of other general trading companies, we announced the specific progressive dividend policy for the medium-term management plan period when we announced the 1st half results for FYE 2022 and the new dividend policy of achieving a dividend payout ratio of 30% by FYE 2024. Furthermore, if there is excess in cash allocation, we mentioned that our direction is to raise the total shareholder return ratio as much as possible through share buybacks and dividend increases. Based on our commitment to continue the progressive dividend policy during the current medium-term management plan, and as a result of considering the FYE 2022 total shareholder return ratio of 27.1% (dividends per share of ¥110 and share buybacks of ¥60.0 billion), the minimum for dividends per share in FYE 2023 is ¥130 and the dividend payout ratio is 27.3%, somewhat higher than the total shareholder return ratio in FYE 2022. In both FYE 2022 and 2023, we mentioned that for the total shareholder return ratio we use share buybacks to fill in the difference between our goal of a 30% dividend payout ratio in FYE 2024 and our current ratio. It does not mean that the benchmark for total shareholder returns is 30%.

Q: With NET DER lower than the level outlined in the medium-term management plan, I am paying attention to the cash allocation policy going forward to enhance corporate value. Although they are not simple business fields because there is a lot of competition and a long time will be needed to achieve profitability, is there a possibility of accelerating SDGs-related businesses, such as Energy Storage Systems (ESS), hydrogen, and ammonia?

A: Due to the uncertainty regarding revenues in the SDG-related businesses, we need to consider them over the medium to long term. Major projects located upstream in the value chain, such as offshore wind power plants and hydrogen, will take time, such as over five years for construction and start of operations. Furthermore, because we assume there will be changes in cost structure and technological advancements during that time, we need to seriously craft our long-term strategy. There is no rush to immediately invest in these businesses, and we are moving forward on this while assessing our best options, such as selecting partners and business models. In addition, for midstream businesses, it will be possible to fail if we readily latch onto one business, so we need to conduct careful assessments, including what kind of subsidies will apply and other government policy trends. For example, ammonia and hydrogen ships and tank transport and storage are businesses that will require significant time in midstream fields with relatively high risk. Therefore, our policy is to engage in these businesses after carefully analyzing and determining the amount, frequency, and capacity needed in Japan. However, in downstream fields, where ITOCHU has its strengths, we are focusing on these fields during the current medium-term management plan because they will not require much investment and the outlook is easier to forecast. This does not mean that it would be good to blindly increase the electric power supply in line with demand, such as simply shifting to nuclear power or increasing wind power. To lower Japan’s dependence on overseas sources and increase its energy self-sufficiency, it is most critical to build a system that can effectively use clean electric power and implement electric power control downstream. Currently, electric power is being wasted in a wide variety of ways, such as transmission loss, but we think we can solve the recent electric power supply bottleneck by stabilizing peaks in demand. We think that solving these social issues and promoting extreme power savings will lead to an increase in Japan’s electric power self-sufficiency.

Q: What is the growth potential for the non-resource sector over the medium to long term?

A: Under the current business environment with high resource prices and market price hikes, it is easy to leverage strengths in the resource sector or heavy basic industries, such as steel and chemicals, and that is driving the performance of every general trading company. Looking at the medium to long term, however, we have high expectations in businesses with many customer contact points, such as our strong non-resource sector, FamilyMart, YANASE, and HOKEN NO MADOGUCHI. For example, FamilyMart has sprinted ahead of the competition to incorporate DX and is working to develop attractive stores and products while partnering with NIPPON ACCESS to make distribution more efficient. This is even happening in manufacturing. For example, HYLIFE and Prima Meat Packers in the food sector are more effectively transforming their businesses based on customer contact points. We will simultaneously develop our existing non-resource sector and proactively promote new investments, such as Hitachi Construction Machinery and Nishimatsu Construction. The construction industry is not expected to grow going forward solely through the existing product-oriented business model. ITOCHU's policy is to create synergy in peripheral businesses by working together with these companies, and that is why ITOCHU invested in them. Our partnership with Nishimatsu Construction does more than just deliver construction materials, aiming to expand their business fields via, for example, the development of low-carbon materials with chemical manufacturers and the development of AI construction site monitoring system with CTC. In addition, the aim of our investment in Hitachi Construction Machinery is to capture the North American construction machinery market. North America is seen as a region that will steadily grow even amid the COVID-19 pandemic. Using the Group company MULTIQUIP, which sells small construction equipment, we will continue expanding downstream business with Hitachi Construction Machinery. From the perspective of ensuring national security, it is possible that some U.S. companies will move basic industry bases located outside the United States back into the United States. We also assume that aging facilities and infrastructure will be repaired and rebuilt. Accordingly, we expect an increase in construction opportunities and construction demand due to a scrap and build approach. If our relationship strengthens, we think we could also jointly undertake other various businesses going forward, such as renewable energy.

Q: What is the progress of the investment in Nishimatsu Construction and Hitachi Construction Machinery?

A: Nishimatsu Construction has been in the construction business for around 140 years and specializes in the construction of distribution warehouses and tunnels. Going forward, we assume that we will see a lot of renovation work for facilities, such as for emergency preparedness and enhancing national resilience, but we will also take on large-scale businesses together that ITOCHU would otherwise find challenging to do alone. We are already working together to develop several hotels and redevelop a distribution site. In addition to supplying materials and receiving dividends from them, we feel that we have steadily begun initiatives that go beyond these undertakings. Also, Hitachi Construction Machinery has steadily started to support sales and distribution, and we have achieved construction machinery exports to North America, with the number of deals exceeding our initial assumptions. We are also moving ahead with sales activities that use the Group company MULTIQUIP's bases. The aim of the investment is to seize the North American market together as business partners, and Hitachi Construction Machinery, Tokyo Century, and ITOCHU are advancing talks about establishing a finance company. Through the finance company, we will maintain customer contact and utilize construction machinery operation data to meet customer needs, such as part sales, repairs, sales of used equipment, and rentals. Although we have not yet gone through with the investment, we are aware that our collaboration with Hitachi Construction Machinery is making steady progress.

Q: For example, regarding the investment in Hitachi Construction Machinery, we can confirm the specific synergy with Tokyo Century and MULTIQUIP through your announcement. But for recent increases in funding for existing investments, what kind of KPIs have you set for generating synergy? What kind of profit boosting effect do you expect from synergy through additional investment?

A: When it comes to investment judgment, ITOCHU requires returns in cash while giving consideration to possible synergy. The appropriateness of synergy cannot be easily justified and is the most contentious point when assessing investments. We, of course, review the rate at which synergy is realized after an investment, but we are more focused on returns for the overall investment exceeding assumptions at the time of investment. For example, CITIC has not yet realized the synergy we assumed it would, but dividends received in FYE 2022 were ¥25.3 billion, so there was no problem with the overall returns. We conduct an annual review to determine whether the overall return on each business investment has reached the exit criteria, which are 1) cumulative losses for last three years; 2) overall returns, including synergy, that are lower than 50% of original plans made at time of investment; and 3) three fiscal years of negative results for added value, which should exceed the cost of capital (cumulative basis). Furthermore, we carefully scrutinize how much return we can really expect from synergy when assessing the investment and conduct a detailed analysis about the level of CAPEX generated every fiscal year. However, if a business investment has not provided returns at the initial assumption level, we will swiftly divest. The effect arising from increases in funding for existing investments can be easily predicted as we are well-versed in individual business content. In terms of individual investments, we are focusing on ensuring overall returns from Dole, our third biggest after FamilyMart and CITIC, get a little bit higher. Meanwhile, YANASE's operating results have thus far been quite steady. We have thus been closely monitoring all the major investees on a company-by-company basis. When considering an investment, we are always aware of the risk of overestimating the synergy portion, and we carefully analyze whether that synergy can really be generated based on the track record. We will support our investment in Hitachi Construction Machinery with all our might because the success of the investment will be determined by how much synergy we can generate, mainly in North America, over the next five years.