FY2019 1st Half Business Results

Investors Meeting

ITOCHU Corporation
November 7, 2018

I am One with Infinite Missions

Opening Remarks

Yoshihisa Suzuki
President & COO

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Net profit attributable to ITOCHU: ¥258 billion, a record high for the second consecutive year. Increased by ¥15.5 billion year-on-year, thanks to a steady growth mainly in non-resource sector.

Further strengthened earnings base which is not affected by commodity price, through “Earn, Cut, Prevent” principle.
Profits and losses of group companies: Renewed the 1st half result record high for the third consecutive year.
Share of group companies reporting profits: Improved to 86%, a 5% improvement on year-on-year basis.

Operating cash flows and Core operating cash flows: Record high, while strengthened the cash generation ability.

Recognized a revaluation gain related to the investment in FamilyMart UNY Holdings and an impairment loss related to the investment in CITIC Limited in this 1st half.

FY2019 Net profit forecast: As announced on Oct 1st, forecast was revised upward to ¥500 billion, a ¥50 billion increase. We will become the second company among general trading companies to reach ¥500 billion.

Based on the dialogue with stakeholders after the announcement of the mid-term plan in May and close examination of future profitability and cash flows, we set the mid-to-long term policy of “gradually increase dividend payout ratio” & “execute share buybacks approx. 100million shares”.

As for “reinvented business”, we need to quickly upgrade our business model that will become outdated. We are promoting the new business model which meets customer needs, while encouraging every employee to understand the need for transformation.

FY2019 1st Half
Business Results Summary

Tsuyoshi Hachimura
Senior Managing Executive Officer, CFO

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Prior to this investors meeting, we held net conference on Nov 2nd, explained about 1st half business result, revision of the net profit forecast, and extraordinary gains and losses. We released the presentation materials and audio archive on our web page.

Today, I will explain the key points of 1st half business result and revision of the net profit forecast; furthermore, a revaluation gain related to the investment in FamilyMart UNY Holdings and an impairment loss related to the investment in CITIC.

FY2019 1st Half

Business Results Summary

ITOCHU Corporation

November 2, 2018

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Summary of Net profit attributable to ITOCHU

ITOCHU

(Unit : billion yen)

- **"Net profit attributable to ITOCHU" increased by ¥15.5 bil., compared with the same period of the previous fiscal year to ¥258.0 bil., which renewed the highest record for the second consecutive year as a 1st half result**. Due to the strong earnings in the Energy, Construction, Realty & Logistics and Forest Products & General Merchandise sectors, "Net profit attributable to ITOCHU" increased compared with the same period of the previous fiscal year in all operating segments, except for the Machinery sector. **Profits of the Non-Resource sector increased by ¥3.8 bil., compared with the same period of the previous fiscal year to ¥211.2 bil., and has been renewing the highest record for a 1st half result since FY2012**. **"Net profit attributable to ITOCHU" progressed 52% steadily toward the FY2019 Revised Forecast of ¥500.0 bil.**
- **"Net profit attributable to ITOCHU after deducting extraordinary gains and losses"** (¥14.0 bil. (profit) in this 1st half, ¥42.0 bil. (profit) in the same period of the previous fiscal year) **increased by approximately ¥43.0 bil., compared with the same period of the previous fiscal year to approximately ¥244.0 bil. and renewed the highest record for the third consecutive year as a 1st half result.**
- **"Profits/Losses of group companies"** was **¥241.7 bil., which renewed the highest record for the third consecutive year as a 1st half result.**
- **"Core operating cash flows"**, after deducting changes in working capital from "Cash flows from operating activities", was a **net cash-inflow of ¥210.0 bil., which renewed the highest record for the third consecutive year as a 1st half result**.

	FY2018 1st Half Result	FY2019 1st Half Result	Increase/ (Decrease)	FY2019 Forecast: Previous Forecast (Disclosed on May, 2)	FY2019 Forecast: Revised Forecast	FY2019 Forecast: Progress
Net profit attributable to ITOCHU	**242.5**	**∗ 258.0**	**+ 15.5**	450.0	**∗ 500.0**	**52%**
Gross trading profit	579.0	∗ 619.6	+ 40.7	1,593.0	∗ 1,600.0	39%
Selling, general and administrative expenses	(429.6)	(452.6)	(23.0)			
Gains on investments	37.3	192.2	+ 154.9			
Equity in earnings of associates and joint ventures	109.3	(9.7)	(119.0)	214.0	82.0	−
Income tax expense	(57.2)	(80.1)	(22.9)			

(Reference)

	FY2018 1st Half Result	FY2019 1st Half Result	Increase/ (Decrease)
Extraordinary gains and losses	42.0	14.0	(28.0)
Net profit attributable to ITOCHU after deducting extraordinary gains and losses	approx. 201.0	∗ approx. 244.0	approx. + 43.0
Profits/Losses of group companies	226.8	∗ 241.7	+ 14.9
Share (%) of group companies reporting profits	81.3%	∗ 85.6%	Increased 4.3pt

Dividend Information (Per Share)	Previous Forecast (Disclosed on May, 2)	Revised Forecast
Annual (Planned)	74.0 yen (minimum)	83.0 yen (minimum)
Interim	37.0 yen	37.0 yen

∗ : Record High

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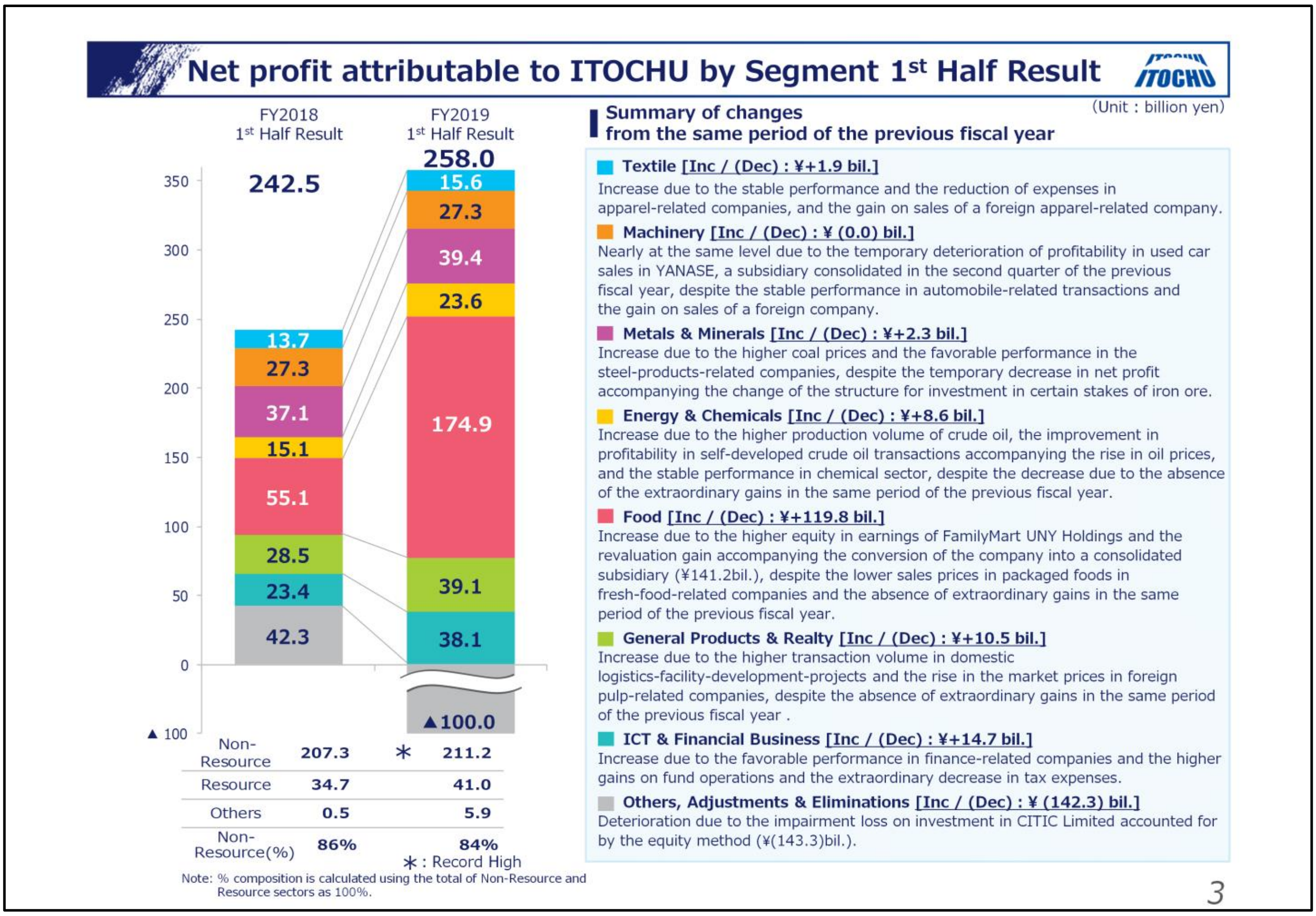
Net profit attributable to ITOCHU: ¥258 billion, which is the historical high.

Progress toward Annual Forecast: 52% is on a track steadily toward the highest record for the third consecutive year to ¥500 billion.

Net profit attributable to ITOCHU after deducting extraordinary gains and losses or core profit: Approximately ¥244 billion.

Core operating cash flows: ¥210 billion.



All of the operating segments, except machinery, increased year-on-year basis.

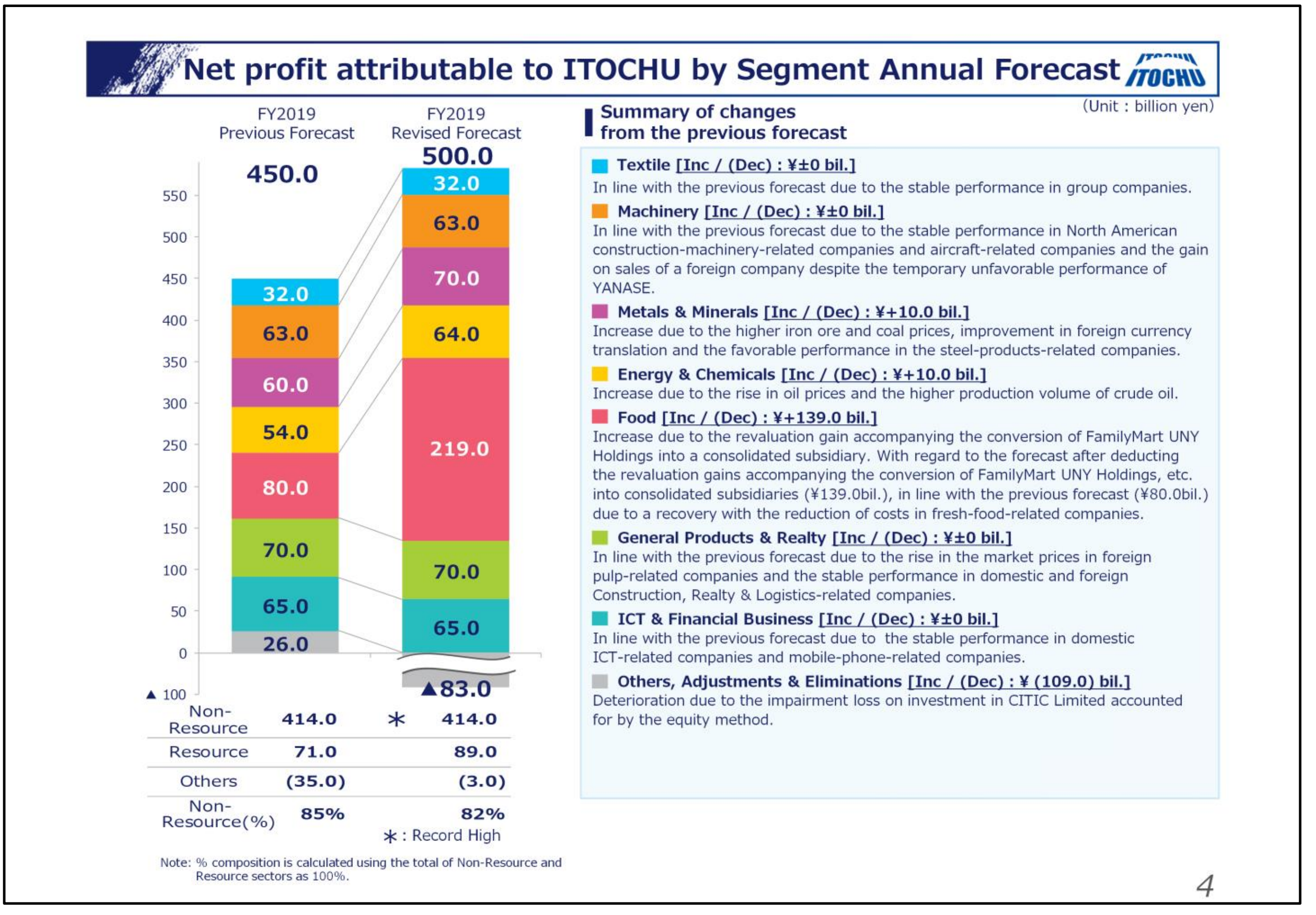
General Products & Realty: Performed well thanks to the higher transaction volume in domestic logistics-facility-development-projects and the rise in the market prices in foreign pulp-related companies.
ICT & Financial Business: Performed well thanks to the favorable performance in finance-related companies.
Energy: Performed well.

As for Core Profit, all of the operating segments earned nearly their record high.

Following 2 companies underperformed during the 1st half of this fiscal year.

YANASE: 1st half result was ¥(0.4) billion, and annual forecast was revised downward to ¥2.6 billion from ¥4.7 billion .
During the 1st half, due to adjusting the excess inventory to an optimal level, there was a decrease in sales of new vehicles and decline in profitability of second-hand vehicles. The inventory almost reached to an optimal level at the end of September, therefore we believe YANASE will recover in the 2nd half.

DOLE: Although the 1st half net profit decreased year-on-year, due to the sluggish price in the worldwide packaged food business, the annual forecast of ¥10.5 billion remains unchanged.



Annual Forecast: Announced upward revision to ¥500 billion on Oct 1st. We forecast the record high profit for the 3 consecutive year.

[Breakdown of upward revision of ¥50 billion]

Metals & Minerals: ¥+10 billion.
Energy & Chemicals: ¥+10 billion.
Others, Adjustments & Eliminations: Withdraw initial buffer for unexpected losses of ¥(30) billion, which we decided unnecessary anymore.

We both have bullish and bearish segments. After the upward revision, Metals & Minerals company still has some slack.
Machinery company aims historical high of ¥63 billion; however, the level is challenging due to revised forecast of YANASE.

When each segments reach the annual forecast, they will achieve the factually record high profit.

Cash Flows

ITOCHU

(Unit : billion yen)

- **Operating Cash Flows and Free Cash Flows:**
  "Cash flows from operating activities" was a **net cash-inflow of ¥167.5 bil.,** resulting from the stable performance in operating revenues in the Food, Metals & Minerals, Energy and ICT sectors. **"Free cash flows"** resulted in a **net cash-inflow of ¥220.8 bil.,** due to the increase in cash resulting from the conversion of FamilyMart UNY Holdings into a consolidated subsidiary, despite the acquisition of fixed assets in the Metals & Minerals, Food and Energy sectors.
- **Core Free Cash Flows:**
  "Core operating cash flows", after deducting changes in working capital from "Cash flows from operating activities", was a **net cash-inflow of ¥210.0 bil., which renewed the highest record for the third consecutive year as a 1st half result**. **"Core free cash flows"** resulted in a **net cash-outflow of ¥(15.0) bil.,** due to the acquisition of fixed assets in the Metals & Minerals, Food and Energy sectors and the additional investments in FamilyMart UNY Holdings.
  The revised FY2019 Image of Core Free Cash Flows is ¥140.0 bil. + α.

Cash Flows

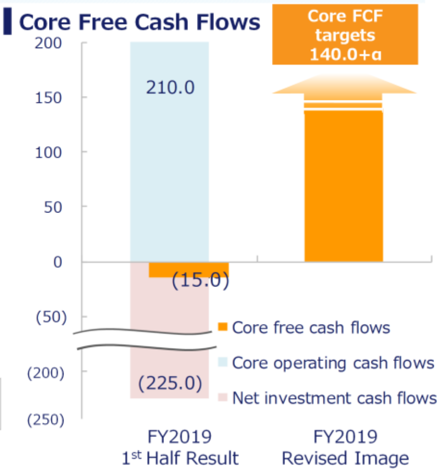
Cash Flows	FY2018 1st Half Result	FY2019 1st Half Result
Cash flows from operating activities	155.0	＊ 167.5
Cash flows from investing activities	(74.8)	53.3
Free cash flows	*80.2*	＊ *220.8*
Cash flows from financing activities	(186.4)	(48.9)

Core Free Cash Flows

Core Free Cash Flows	FY2018 1st Half Result	FY2019 1st Half Result	FY2019 Previous Image (Disclosed on May, 2)	FY2019 Revised Image
Core operating cash flows(Note1)	210.0	＊ 210.0	approx. 500.0	Over 500.0
Net investment cash flows(Note2)	(105.0)	(225.0)		
Core free cash flows	105.0	(15.0)	Over 120.0	140.0+α

＊: Record High

Core Free Cash Flows



Note 1: "Operating Cash Flows" minus "changes in working capital"
Note 2: Payments and collections for substantive investment and capital expenditure
"Investment Cash Flows" plus "Equity transactions with non-controlling interests" minus "changes in loan receivables", etc.

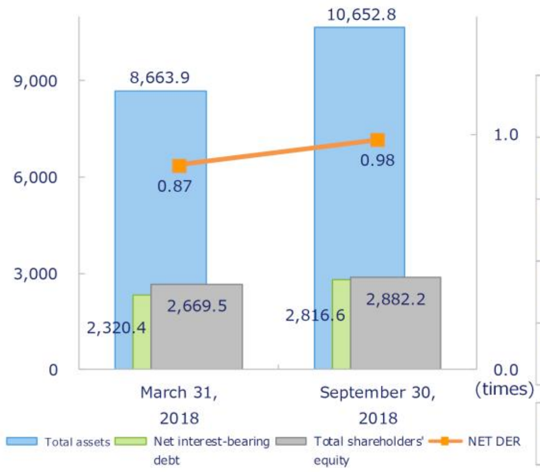
<u>Operating cash flows</u>: ¥167.5 billion. Performed well, along with the net profit.
<u>Core operating cash flows</u>: ¥210 billion.
Both of above renewed the record high.

Based on the upward revision of net profit, we revised the image of core free cash flows and core operating cash flows of FY2019 to a more bullish expression .

Financial Position

(Unit : billion yen)

- **Total assets:**
  Increased by ¥1,988.9 bil., compared with March 31, 2018 to **¥10,652.8 bil.**, due to the conversion of FamilyMart UNY Holdings and a finance-related company into consolidated subsidiaries, the acquisition of a Latin American automobile-related subsidiary, and the effect of the depreciation of the yen.
- **Net interest-bearing debt:**
  Increased by ¥496.2 bil., compared with March 31, 2018 to **¥2,816.6 bil.**, due to the conversion of FamilyMart UNY Holdings and a finance-related company into consolidated subsidiaries, and the effect of the depreciation of the yen.
- **Total shareholders' equity:**
  Increased by ¥212.7 bil., compared with March 31, 2018 to **¥2,882.2 bil.**, due to Net profit attributable to ITOCHU during this fiscal year, despite the decrease due to dividend payments.
- **Ratio of shareholders' equity to total assets and NET DER:**
  Ratio of shareholders' equity to total assets decreased by 3.8 points compared with March 31, 2018 to **27.1%**.
  NET DER (Net debt-to-shareholders' equity ratio) slightly increased compared with March 31, 2018 to **0.98 times**.



	March 31, 2018	September 30, 2018	Increase/ (Decrease)	FY2019 Previous Forecast (Disclosed on May, 2)	FY2019 Revised Forecast
Total assets	8,663.9	＊ 10,652.8	+ 1,988.9	10,600.0	10,300.0
Net interest-bearing debt	2,320.4	2,816.6	+ 496.2	2,450.0	2,550.0
Total shareholders' equity	2,669.5	＊ 2,882.2	+ 212.7	3,000.0	＊ 3,000.0
Ratio of shareholders' equity to total assets	30.8%	27.1%	Decreased 3.8pt	28.3%	29.1%
NET DER (times)	0.87	0.98	Increased 0.1pt	0.82	＊ 0.85
ROE	15.8%	–	–	15.9%	17.6%

＊: Record High (NET DER : Record Low)

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Due to the conversion of FamilyMart UNY Holdings into consolidated subsidiary, the size of consolidated balance sheet was expanded.

Total assets: Exceeded ¥10 trillion for the first time. The impact of the conversion of FamilyMart UNY Holdings was approximately ¥1.6 trillion.

Total shareholders' equity: ¥2.9 trillion yen, a record high.

Financial ratios: Dropped due to the growth of total assets amount; however, it will be adjusted to the forecasted level by the end of fiscal year.

ROE: Projected 17.6% for FY2019. We pursue efficiency not scale.

Total assets and Interesting-bearing debt forecast: Total assets will slightly decrease, and net interest-bearing debt will increase slightly, from the previous forecast, due to FamilyMart UNY Holdings' capital policies such as future sale of UNY and the depreciation in yen.

Major Indicators

	FY2018 1st Half Result	FY2019 1st Half Result	FY2019 Previous Forecast (Disclosed on May, 2)	FY2019 Revised Forecast	(Reference) Sensitivities on net profit attributable to ITOCHU for FY2019 2nd half against forecast
Exchange rate (YEN / US$) average	111.25	109.44	105	110	Approx. ¥(1.2) bil. (1 yen appreciation against US$)
Exchange rate (YEN / US$) closing	Mar. 2018 106.24	Sep. 2018 113.57	105	110	-
Interest JPY TIBOR 3M, average	0.057%	0.069%	0.10%	0.10%	Approx. ¥(2.5) bil. (1% increase)
Crude oil (Brent) (US$/BBL)	51.49	75.40	55	70	±¥0.11 bil.
Iron ore (CFR China) (US$/ton)	67*	66*	N.A.**	N.A.**	±¥0.34 bil.
Hard coking coal (FOB Australia) (US$/ton)	190*	189*	N.A.**	N.A.**	±¥0.07 bil.
Thermal coal (FOB Australia) (US$/ton)	87*	111*	N.A.**	N.A.**	

(The above effect varies according to changes in sales volume, foreign exchange rates and production costs.)

* FY2018 1st half and FY2019 1st half prices for iron ore, hard coking coal and thermal coal are prices that ITOCHU regards as general transaction prices based on the market.

** The prices for iron ore, hard coking coal and thermal coal used in the FY2019 forecast are assumed in consideration for general transaction prices based on the market. The figures are not presented since the actual sales prices are decided based on negotiations with each customer, ore type and coal type.

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	Previous forecast	Revised forecast
YEN / US$:	¥105	¥110
Crude oil (Brent):	$55	$70

Iron ore and coal prices are not disclosed; however, we have revised these to the current price levels.

We revised the sensitivities as the 1st half has passed.

Extraordinary Gains and Losses

(Unit : billion yen)

	FY2018 1st Half Result		FY2019 1st Half Result	
Gains(Losses) related to investments	**24.0**	・Gain related to partial sales of a Chinese fresh-food-related company: approx. 18.0 (Food) ・Merger of Takiron and C. I. Kasei: approx. 3.0 (Energy & Chemicals) ・Gain on sales of an asset-management -related company:approx. 2.0 (General Products & Realty)	**149.0**	・The revaluation gain accompanying the conversion of FamilyMart UNY Holdings into a consolidated subsidiary: 141.2 (Food) ・Gain on sales of a foreign textile-related company: approx. 2.5 (Textile) ・Gain on sales of foreign machinery-related company: approx. 1.5 (Machinery) ・The revaluation gain accompanying the conversion of a finance-related companies into a consolidated subsidiary: approx. 1.0 (ICT & Financial Business 2.5, Food (1.5)) ・Gain accompanying the restructure of European-energy-related companies: approx. 1.0 (Energy & Chemicals) ・The impairment loss on Chia Tai Enterprises International Limited: approx. (2.5) (Others, Adjustments & Eliminations)
Equity in earnings (losses) related to associates and joint ventures,	**9.0**	・Gain on investments in related companies in CITIC Limited: approx. 8.0 (Others, Adjustments & Eliminations)	**(141.0)**	・Gain on sales of a foreign GMS company in FamilyMart UNY Holdings: approx. 1.0 (Food) ・The impairment loss on investment in CITIC Limited accounted for by the equity method: (143.3) (Others, Adjustments & Eliminations)
Income tax expense, Others	**9.0**	・Decrease in tax expenses relating to pulp-related companies: approx. 5.5 (General Products & Realty)	**6.0**	・Decrease in tax expenses relating to foreign finance-related companies: approx. 5.0 (ICT & Financial Business) ・Decrease in tax expenses relating to apparel-related companies: approx. 1.5 (Textile)
Total	**42.0**		**14.0**	
Non-Resource	45.5		13.5	
Resource	0.5		0.5	
Others	(4.0)		–	

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This time, we released the financial results with conservative manner, while considering how to maintain the financial soundness.

We announced the TOB with acknowledging the accounting revaluation gain from the conversion of FamilyMart UNY Holdings into consolidated subsidiary. On the other hand, there were no indications of impairment on CITIC at the end of FY2018 and 1st quarter of FY2019.

Regarding the investment to CITIC, although there are some views to this investment, the performance of CITIC itself is steady. The impairment was conservative treatment to wipe out risk in the future. Some press said that the trade friction between the U.S. and China declined the stock price, but share price of CITIC has no direct impact from the trade friction.

While assumed a massive revaluation gain by the conversion of FamilyMart UNY Holdings into consolidated subsidiary, we discussed the mid-to-long term fair value. The fairness of the TOB price of ¥11,000 was decided based on the market price method, the comparable company method and the DCF method etc.

The stock price was ¥7,000 level at the beginning of this year, ¥8,000 level in Mar, ¥9,000 level before the announcement of TOB, ¥10,000 level after the announcement of TOB on Apr 19th, and just before the TOB term from Jul 17th to Aug 16th, the price was too bullish of ¥12,000 level.

We appreciate the higher stock price and PER compared to comparable companies stem from the positive expectation on the company's future growth; however, TOB price includes control premium in the comparable cases. Therefore fair value should be calculated by removing the premium in general. We also took third party opinion to discuss the fair value. The stock price reached to ¥9,600 after the TOB(early Sep), and then increased again by the effect of capital policy at the end of Sep.

Considering our current favorable performance, we do not rely on extraordinary profit which does not contribute in mid-to-long term, along with paying attention to the goodwill amount. The fair value was decided to the mid-¥9,000 level, and as a result, the revaluation gain was ¥141.2 billion.

CITIC keeps steady performance and we revise the equity pick-up forecast upward to ¥63 billion from the previous forecast of ¥60 billion. It is true that the CITIC's stock price remains low, but we acquire the stock below the Book-value Per Share(BPS). The stock price was HKD 13.8, and BPS was HKD 17.37 when we acquired.

CITIC does not announce quarterly financial results; however, BPS increased to HKD 19.5 at the moment. This is not the investment for capital gain, but BPS increased about 12%. The problem is sluggish stock price performance, their asset value as an investment target is increasing, and their performance is steady. It is true that synergies are slower than originally expected, but we consider the investment horizon should be mid-to-long term.

58% of the stock was held by Chinese government, the liquidity is low, and their 80 to 90% of profit is coming from financial businesses. The financial sector's stocks in Hong Kong market tend to be discounted. The stock price is gradually increasing, but still in the range between HKD 11 and HKD 12.

Under their good performance, our consolidated book value of the investment is increasing since the undistributed surplus is piling up. The bigger the difference in appreciation speed between book value and stock price, the higher the risk of future's impairment.

At the end of FY2018 and 1st quarter of FY2019, we judged that there were no indications of impairment on CITIC, by examined all elements not only stock price, but also possibility of recovery, expected future profitability of CITIC, and future growth of China etc.
On the other hand, we made a review at the end of 1st half of FY2019, as the consolidated book value increases by quarterly equity pick-up. Although we believe the Chinese government takes all action to sustain the economy, the speed of the appreciation in stock price will be projected slow. So we obtained the third party opinions on CITIC, Hong Kong capital market and Chinese economy etc. from think-tank, investment bank and so on. And then discussed with our audit firm, judged it is appropriate to review its value slightly below the purchasing price of HKD 13.8, and as a result, we recognized impairment loss of ¥143.3 billion.