Investors Meeting for Reinvention of Business: 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.

Date: June 27, 2019 (Thu.) 13:30 to 15:00
Speaker: Shunsuke Noda, Chief Digital & Information Officer
Respondents: Tsuyoshi Hachimura, Chief Financial Officer; Kiyoshi Sekikawa, General Manager, Business Innovation Department
MC: Suguru Amano, General Manager, Investor Relations Department

1. Path to Profitability

Q: Could you give us an idea of the scale of profit expected in reinvented businesses, as well as the fields in which ITOCHU will invest and the timescale for achieving profitability?

A: In the year since we set the target for next-generation investments, we have invested in a range of fields based on a broad perspective. Only investing in start-ups is not profitable; while such companies sometimes end up having an IPO, we do not make initial investments with that in mind, so the question becomes when to invest more to turn them into a business investment. The valuation of next-generation start-ups can rise suddenly, so we seek to decide whether to invest more when we find clear potential for profitability or collaboration, but before their valuation jumps. Generally, we have to make these decisions in two to three years. We send dedicated staff to the companies where we make investments to thoroughly analyze a model for business collaboration during the first year, then decide our next move from there.

Q: Synergy is key. As an investor in a company, the whole Group can benefit from its services, while having the entire Group to do business with helps each business develop. Besides dispatching employees, what measures are you taking to foster synergy and increase the internal rate of return (IRR)?

A: In the past, our approach to start-up investing has been to narrow down a large pool of potential investees to focus on the most promising. We often did not send staff when making minor investments. Now, however, we are proactively sending the very employees who proposed the investment to represent ITOCHU from the time the investment is made in order to thoroughly explore opportunities for synergy. These are often employees who have been with ITOCHU for 10 to 15 years, and, having built up a toolbox of experience, are eager to take on a new business. Honed by the experience of working on a new business in a different corporate culture, they then return to ITOCHU, helping us find the next opportunity. Increasing IRR depends on creating synergy, and we are beginning to see opportunities for even greater synergy creation than we initially expected.

2. Investment Selection

Q: As I understand it, the main thrust of ITOCHU's next-generation investments is to expand its investments in start-ups Company-wide and make them into business investments. In the past, there have been times when start-up investments went poorly. As you expand such investments across ITOCHU, what kind of project selection criteria will you use to increase the success rate?

A: Our start-up investments in the information technology field have been early- to mid-stage investments in a large number of projects, some of which have turned out to be better than others. As we expand start-up investments across the Company, we are focusing investments on the later middle stages to the near late stages, with an emphasis on synergistic promise. Because of this, while our start-up investments in the information technology field have been in the ¥100–500 million range, many of the next-generation investments are around ¥1 billion. Accurately assessing the potential for profitability and collaboration is crucial.

Q: Why is it necessary to invest in companies rather than just purchase their services? For example, what is the benefit of investing in the satellite company Spire, when purchasing its services seems adequate to meet ITOCHU's needs?

A: It varies by project, but, for example, while ITOCHU has only sales agent rights for Spire and has not made any investment at the moment, we are seeking an opportunity to invest in Spire, because doing so would provide ITOCHU important rights relating to the business. We do sometimes decide that investment is unnecessary and opt solely for business collaboration, instead. However, there is always the risk that companies providing important services will go under, so it is important to monitor their management. Even minor investments can secure us the right to observe board of directors meetings and periodically meet with top management. We therefore view getting involved through investment as significant to securing good communication.

Q: I imagine ITOCHU's employees come up with many interesting and challenging proposals; what portion of these result in investments?

A: Yes, a great number of new project proposals have come up. We decide which to implement based on whether they fit into our strategic fields. This is not to say that we never take on projects in new areas, but we are currently considering the extent to which we should do so. Businesses in fields adjacent to our existing business areas can receive significant support from those related areas, but projects in completely new areas do not have that benefit. Going forward, we will examine whether we need to alter our existing approach to investment.

3. <u>FamilyMart</u>

Q: ITOCHU has announced FamiPay and the use of apps as measures to reinvent FamilyMart, and these seem likely to quickly reach profitability. How will the reinvention of FamilyMart's business contribute to the ITOCHU Group as whole?

A: FamilyMart is a listed company, so we cannot say anything more than what FamilyMart has announced. We are working with FamilyMart to examine initiatives in peripheral areas, such as digital advertising and fintech, as well as the strategic use of POCKET CARD going forward. Merely enabling the use of multiple point programs and electronic payments does not allow FamilyMart to retain customer data, so we aim to use FamiPay to collect our own customer data that can be used by the Group in the future. Linking data and optimizing supply chains across the ITOCHU Group requires the involvement of operating companies, so ITOCHU and operating companies will collaborate to advance such efforts. Regarding realizing profitability in new projects, for example, we have drafted estimates of expected profits from new advertising and other businesses, cost savings from value chain optimization, and quantitative effects from productivity improvements, but we are still in the early stages of verifying these.

4. <u>Other</u>

Q: You said that investments in next-generation businesses totaled about ¥30.0 billion in the previous fiscal and will be about ¥30.0 billion in the current year, as well. Do you plan to increase this amount next year or beyond?

A: As we explained at the financial results presentation, for the current fiscal year, in addition to the ¥30.0 billion to be invested under the CDO & CIO, we have earmarked ¥70.0 billion to be invested by the Division Companies, for a total of ¥100.0 billion. After investing in start-ups, the Division Companies may tap the ¥70.0 billion allotment to make them into business investments.

Q: Another trading company recently announced its entry into the medical field in China. What are ITOCHU's investment plans in this area?

A: Our healthcare investments are separate from the next-generation investments, but we are investing in dialysis-related businesses, which we aim to expand into medical facilities in China. We have also invested in a healthcare-related fund put together by CITIC Capital, and we are examining ways to develop medical-related businesses in China based on our resulting indirect involvement in the operations of multiple medical facilities.