Briefing on Upward Revision of FYE 2023 Forecast and Additional Shareholder Returns: 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: October 4, 2022 (Tue.) 10:30 to 11:10
Respondents: Tsuyoshi Hachimura, Chief Financial Officer

Q: What is the meaning of the "¥800.0 billion profit stage" for consolidated net profit in the slides released? This is different from stably "Aiming to build an earnings base of ¥700.0 billion." Can you explain the general direction of ITOCHU for the next fiscal year?

A: We initially positioned the current medium-term management plan "Brand-new Deal 2023" as a stage where we secure an earnings base of ¥600.0 billion, but the FYE 2022 result was ¥820.3 billion due in part to soaring resource prices and extraordinary gains. When the FYE 2023 plan was released in May 2022, ITOCHU conservatively estimated the Company's performance, at over ¥600.0 billion. At the time of the General Meeting of Shareholders in June, however, we determined that, excluding extraordinary gains, we could still stably target a ¥700.0 billion profit stage based on the growth of core profit in the non-resource sector, and this led us to revise the forecast. Furthermore, the first quarter results released in August showed strong progress, getting us 33% toward the initial FYE 2023 plan of ¥700.0 billion. Excluding extraordinary gains in the non-resource sector, the first quarter strength in core profit largely continued into the second quarter, and there were no significant changes in trends for each segment. Despite the price of iron ore and coking coal hitting a ceiling and the persistently high prices for fuel, namely thermal coal and crude oil, we do not expect a significant change in the ratio between the non-resource sector and the resource sector, and we now believe that we can achieve a profit of ¥800.0 billion for FYE 2023. We will need to pay more careful attention to the business environment in the second half of FYE 2023. Though I cannot get into specifics right now, ITOCHU has built a highly resilient defensive earnings base even when faced with an economic downturn. Based in part on market expectations, regarding FYE 2024 (the final year of the medium-term management plan), we are not lowering our sights to ¥700.0 billion. Instead ITOCHU's management have strong consciousness to achieve ¥800.0 billion and present the Company's sustainable growth to the market.

Q: Regarding the aim of a "¥800.0 billion profit stage" in FYE 2024, which segments are expected to be able to sustain performance at that level?

A: Trends in the second quarter will not change much from the first quarter. Businesses in Japan and overseas both have their strengths, but looking at the Division Companies, we see the following on the rise: the Machinery Company, the General Products & Realty Company, the Metals & Minerals Company, and the Energy & Chemicals Company. In the Metals & Minerals Company, although iron ore prices are falling, thermal coal prices remain high. In addition, steel pipes and other steel products remain strong. In the Machinery Company, due to the semiconductor shortage for automobiles, domestic import dealers and overseas dealers are short on inventory, so sales prices are rising. Furthermore, overseas IPP-related businesses are strong. In the Energy & Chemicals Company, high crude oil prices are causing LNG prices to rise, resulting in strong trade and business profit. In the General Products & Realty Company, we maintained a rather conservative assumption for pulp prices, but they have stayed higher than our expectations. In addition, in the North American construction materials-related business, although housing starts and mortgages declined, performance has continued to hold steady. From the second half of the year onward, the main points of focus will be how much the strong segments can alleviate the effects of a market downturn and how the struggling ICT & Financial Business Company and the Food Company can catch up. In the case of FamilyMart, the key point will be how consumers react going forward if we continue passing on costs to prices. Since our two convenience store competitors have also exhibited strong performance by passing on costs, we are not that worried. Although there have been some positive effects from yen depreciation, there is a high probability that negative effects from soaring prices for imported products and gasoline will increase going forward, so we need to pay attention to these effects from FYE 2024 onward. Nevertheless, regarding FYE 2023, while we have concerns about the economic situation in the second half, we believe we will be fully able to achieve the ¥100.0 billion upward revision. ITOCHU has said that it can display its strengths amid an economic downturn, and the Company intends to continue thoroughly implementing not only the “earn” principle, but also the “cut and prevent” principles in FYE 2024 and beyond. When formulating the forecast for FYE 2024, we will need to fully assess the second half of the current fiscal year, and it could be impacted by the pipeline and progress of future growth investments.

Q: The dividend per share was increased from a minimum of ¥120 to ¥130 under the initial FYE 2023 plan released in May 2022. Now that this is being lifted to a minimum of ¥140, it seems like there may be a change in the Company’s previously cautious stance on shareholder returns that was predicated on the continuation of a progressive dividend policy. Is that correct?

A: We have not changed our aim of balancing the three factors of shareholder returns, growth investments, and control of interest-bearing debt, and there has been no change in our shareholder returns policy. Regarding growth investments, while there are quite a few in the pipeline currently, none have entered the execution stage as of the second quarter, but they could enter that stage from the second half. We will continue discussions of additional returns, aiming to maintain a level of shareholders’ equity that can withstand an uncertain business environment and avoid affecting credit ratings. Furthermore, through dialogue with analysts and investors, both in Japan and overseas, we are fully aware that there are high expectations for additional returns through share buybacks. Accordingly, this ¥35.0 billion round of share buybacks is similar to the active and continuous share buybacks we have executed over the past six consecutive years. In particular, in light of the Company’s target dividend payout ratio of 30% by FYE 2024, the current share buyback is intended to close the gap with the current dividend payout ratio in order to achieve a total payout ratio of 30%. Upward revision of ¥100.0 billion in consolidated net profit we expect, we have decided to allocate 50% to shareholder returns. We are executing additional returns to eliminate any concern that the Company’s stance on shareholder returns is inferior or that the market might find ITOCHU’s shares less attractive amid soaring resource prices.

Q: I understand ITOCHU is striving to steadily increase operating cash flows as seen in the current upward revision, but to enhance corporate value, I would think that it is important to pursue more active methods like growth investments, rather than simply accumulating cash. What is your current approach to cash allocation and balance?

A: ITOCHU practices management that considers balancing three factors: shareholder returns, growth investments, and control of interest-bearing debt. Sometimes we need to adjust these conflicting factors. Since FYE 2016, we have continuously executed investments within the profit earned, always maintaining stringent financial discipline. As such, to maintain positive core free cash flows after deducting shareholder returns each fiscal year, we must amass reserves over multiple years in order to fund large-scale investments, such those in CITIC and privatizing FamilyMart. There are still some investments in the pipeline in FYE 2023, but amid the harsh business environment, we will not let up our financial discipline. By conducting more diligent analyses than ever, we will execute investments that contribute to growth over the medium- to-long term. Core operating cash flows are steadily increasing in tandem with consolidated net profit, and we think in the current environment we can more flexibly conduct growth investments.