IR Day 2024: Part 2 Panel Discussion

[Date]	December 10th, 2024	
[Presenters]	Shingo Ueno	Representative Director, President, and CEO
	Takayuki Sumita	Managing Executive Officer, CSO
	Takashi Mitachi	Outside Director
	Yoshinori Takayama	Corporate Officer, Head of Investor Relations Dept.

<Takayama>

In the first part of IR Day 2024, we presented three examples from our growth businesses, focusing on their competitive advantages and outlining the path for future growth. We also welcomed questions and feedback.

In this second part, we will elevate these discussions to a company-wide perspective, primarily through a panel discussion on transforming our business portfolio.

Under the theme of "No.1 in Each Field" in our Medium-term management plan 2026, our fundamental policy is to enhance our competitive advantages and grow through addressing social challenges. I would like to start by asking Mr. Sumita what he believes are the common sources of our competitive advantage.

<Sumita>

Sumitomo's business philosophy and corporate culture are rooted in integrity and sincerity, forming the foundation of trust with business partners and customers. For instance, the commercial aviation business has evolved step-by-step from trade to after-sales service, leasing, and asset management. Employees share the spirit of "Benefit for self and others, private and public interests are one and the same," which is the source of business sustainability and competitive advantage. Additionally, "enterprising spirit" drives innovative efforts in the digital and new energy sectors. For example, by incorporating subsidiaries like SCSK, we are expanding our digital business and entering the new energy sector through the Energy Innovation Initiative. These business philosophies and corporate culture are deeply ingrained as human capital, representing a significant strength that cannot be easily replicated by other companies, developed over 100 years, or even 400 years in the context of Sumitomo.

<Takayama>

What are your thoughts on this, Mr. Mitachi?

<Mitachi>

As an outside director, I have incorporated three key discussions on competitive advantage into our current medium-term management plan to enhance shareholder value.

First, the strength of individual businesses is crucial, and it is necessary to secure excess profits. We must protect strengths at the SBU and Business Group levels while managing the overall portfolio at the corporate level.

Second, by combining the strengths of SBUs and Groups, we can generate the next phase of growth. This involves skillfully creating a portfolio that outperforms competitors. The current medium-term management plan, which has been thoroughly discussed by the board, clearly emphasizes the "No.1 in Each Field." This focus will make it easier to create a strong portfolio and allocate resources effectively.

Third, and the main topic today, is the need to replace the portfolio. Using tools like ROIC/WACC introduced in the previous medium-term management plan, we can assess cost of capital and establish a common understanding of how to replace the portfolio. The ability to have these discussions was a significant value of the previous medium-term management plan. Now, we need to focus on how to implement these changes as portfolio managers, leveraging our diverse business with various timelines. For example, the industrial park business involves long-term land acquisition, followed by shorter-term services like DX and utilities. Combining these allows us to maximize the balance sheet's strength and achieve sustainable competitive advantage. With these initiatives and the established metrics, we are now in a position to demonstrate our track record and gain market recognition.

<Takayama>

Regarding what Mr. Mitachi just said about using the internal tools and mechanisms established in the previous medium-term management plan to enhance the business portfolio, I would like to go back to the executive side and ask you again, Mr. Sumita. As the Chairman of the Global Innovation & Portfolio Committee (GIPC), an advisory body to the Management Council, could you please elaborate on the discussions held within GIPC regarding our business portfolio transformation?

<Sumita>

Mr. Mitachi, as an outside director, provides the above comments on a monthly basis. The executive team has reaffirmed the importance of portfolio management and established a company-wide framework to implement it. Discussions at the GIPC, the advisory body to the Management Council, have become even more active this fiscal year and the portfolio is being evaluated across three axes: business sectors, time, and regions.

Regarding the time axis, as mentioned in the presentation materials from the Diverse Urban Development Group, as we make various preparations and investments, a mountain of profit is built up in chronological order. This allows us to discuss, from a company-wide perspective, which areas of long-term investment have issues and which can be strengthened or promoted.

In terms of regions, in addition to traditional country risk management, we are discussing which countries offer high returns on investment. For example, while domestic real estate business is profitable, focusing solely on domestic investments does not increase ROIC. Therefore, we are discussing how to achieve high profits in regions where we can manage the risks of overseas investments.

Regarding business sectors, we are advancing portfolio management by allocating management resources to “Steady business growth areas” and “Value creation areas” in the four quadrants, where we can leverage our competitive advantage and where we can aim to become the No.1 in each field.

<Takayama>

In discussions with the market, questions about the desired portfolio in terms of industry axes for the next five to ten years always arise. While these discussions are ongoing internally, I would like to hear Mr. Mitachi's thoughts on the effectiveness of portfolio discussions based on industry axes in the context of an integrated trading company or Sumitomo Corporation.

<Mitachi>

In discussions with the market, questions about the desired portfolio in five or ten years are inevitable. There are two reasons for the existence of industry axes. One is the difference in risk profiles and timelines, making categories like mineral resources easy to understand. The other is that industries are categorized in specific ways by entities like the SEC in the U.S. and the Tokyo Stock Exchange in Japan. However, this approach limits us to doing the same as other companies. For example, it is crucial to earn revenue from businesses that do not fit traditional industry categories, such as categorizing industrial parks with DX support, rather than real estate. To promote this, our internal organization needs to categorize areas of strength uniquely, and the introduction of the nine-Business Group system is the first step. While the market wants to compare us with other companies and general perspectives, demonstrating this connection remains a challenge. To execute our strategy and create value, it is essential to identify the most profitable unique categorizations. We should particularly focus on portfolio management at the SBU and group levels.

<Takayama>

In our current medium-term management plan, we have adopted the theme of "Achieve growth through addressing social challenges." There are three values that the "No.1 in Each Field" will bring: economic value, social value, and environmental value. Could you share your thoughts on the linkage of these three values?

<Sumita>

Under the theme of "No.1 in Each Field," there is a growing enthusiasm within the company for new significant investments. This theme emphasizes "value creation and growth through addressing social challenges," highlighting that addressing social challenges itself is a form of value creation. In the past, we pursued economic value, which subsequently led to social and environmental value. However, our current approach aims to simultaneously pursue economic, social, and environmental value through addressing social challenges directly.

From an investor relations perspective, there might be concerns that focusing on social and environmental value could undermine economic value. However, this is not the case. The market's perspective is evolving, and considering environmental and social value alongside economic value reduces future risks and significantly impacts current evaluations. Striving for the simultaneous achievement of these three values is essential for our sustainable growth and the establishment of our competitive advantage.

<Mitachi>

From a stakeholder's perspective, DX (Digital Transformation) and GX (Green Transformation) are essential initiatives. However, I view them more from a value creation standpoint. Historically, since the Industrial Revolution, both Japan and Japanese integrated trading companies have thrived by converting carbon into significant energy and mobility. This paradigm is now shifting dramatically.

Simply burning carbon is no longer viable. As the nature of energy evolves, integrated trading companies must seek new revenue opportunities not only in energy itself but across all industries that utilize it.

During the Industrial Revolution, harnessing carbon's power enriched people’s lives. Similarly, DX expands human cognitive abilities, transforming how industries and wealth are created. Failing to embrace this change means being left behind. DX and GX are not just revenue opportunities but also imperatives to avoid obsolescence. Especially, in the energy sector, the profitability of hydrogen and ammonia remains uncertain, but it is crucial to strategically invest within our capabilities. The same applies to AI; it is not just about the creators but also about how users can generate value. We must develop strategies that incorporate social and environmental value to avoid missing out on significant opportunities and falling behind.

[END]