Question & Answer at IR Meeting on Financial Results for FY2022 Q2

[Date]	**November 7, 2022**	
[Presenters]	**Masayuki Hyodo**	**Representative Director, President and Chief Executive Officer**
	Reiji Morooka	**Representative Director, Senior Managing Executive Officer, Chief Financial Officer**
	Hirokazu Higashino	**Representative Director, Managing Executive Officer, Chief Strategy Officer**
	Yoshiyasu Fuse	**General Manager, Accounting Controlling Dept.**
	Yoshinori Takayama	**Corporate Officer, General Manager, Investor Relations Dept.**

< Questionnaire 1 >
In order to achieve ROE target 12% to 15% regardless of the external environment, as shareholders' equity has grown to nearly JPY4 trillion, a profit of JPY480 billion to JPY600 billion level needs to be generated. Considering deteriorating economic outlook and the slow progress on new investments, what measures and steps are needed to achieve the target range of ROE?

< Hyodo >
Though it is difficult to predict how far the overall market will fall in recession in the future, we continue to promote the three shifts in the current medium-term management plan to strengthen our profitability. Then our 62 SBUs, we think, would reliably generate ROIC above WACC, and we can build a corporate structure capable of achieving ROE of 12% or more. Regarding the progress on new investments, we are simultaneously executing investments that will contribute to earnings over the medium term. In order to maintain a reliable dividend policy in line with the enhancement of shareholders' equity, we will continue to steadily implement individual measures under current medium-term management plan.

< Questionnaire 1 >
Please tell us how to distribute the JPY70 billion of retained earnings which is the portion over JPY480 billion of net profit, equivalent to DOE of 4.5%, as annual profit forecast is revised to JPY550 billion.

< Morooka>
As per the initial shareholder return policy, the minimum line of the dividend payout ratio to be 30% or more. However, there are multiple option for shareholder returns, such as share buybacks, additional dividends, or a mix of these two. We will determine the method and the amount against the excess portion by taking into consideration return ratio, which is not necessarily the 30%, the economic environment, future growth investments, and our financial position at that time.

< Hyodo >
At this moment, we have not yet made formal decision on further shareholder returns against excess portion however, I would like to flexibly make it in a substantial manner. We will continue to consider the method and amount and announce the details once it is decided.

< Questionnaire 2 >
Regarding the allocation of cash inflows that exceed the initial forecast, could you tell us the balance among investment, debt repayment, and shareholder return?

< Morooka >
The current cash flow plan which presented this time does not assume the upward revision of the annual forecast and shareholder returns. Since one of our important goals is to recover financial soundness, we would like to ensure aggregate free cash flow post dividend is positive as a bottom line under the current medium-term management plan. Regarding shareholder returns, the decision will have to be made from multiple perspective including our business conditions however, it will be made based on the shareholder return policy we have presented. As for investments and loans, we have not made much progress so far, but various projects are being discussed internally. Our policy is to actively make those investment with due consideration based on our new investment discipline. We will plan a new three-year rolling plan towards the end of the fiscal year. At that time, we will be able to share our plans including profit outlook which assures future growth.

< Questionnaire 2 >
The market is concerned about potential decline in the profit and dividend in the next fiscal year. Do you have any plans to allocate excess funds to avoid or mitigate dividend decrease for the stability of the future shareholder returns?

< Morooka >
That will be one of the options we will consider, taking into consideration the profit outlook and investment plan for the next fiscal year and beyond.

< Questionnaire 3 >
Regarding real estate business, if the economy slows down going forward due to rising interest rates, is there a possibility that your real estate business will incur a large loss, as we understand there are certain exposure in overseas markets?
Besides, what is the weight of overseas real estate in your real estate portfolio of over JPY980 billion?

< Morooka >
At this time, we do not expect to incur any significant losses. The likelihood of such losses in the portfolio as a whole is also small.

< Takayama >
The current ratio of overseas assets is about 13% to 14% in total asset basis. Our strategy is to increase the ratio to around 20% in the future while keeping an eye on the growth potential of regions not only the U.S. but including Asia. Interest rates are rising , and the business environment is not necessarily positive. We will proceed with our plans while assessing the business situation.

< Questionnaire 3 >
Regarding the outlook for the Transportation and Construction Systems business, as this business is expected to slow down in H2 of the year, could you tell us more details such as areas where growth will slow, areas where it will improve?

< Morooka >
As for automotive manufacturing business, we believe that our customers' automobile production volume will gradually recover, and raw material prices seems to be coming to a halt and gradually recover. We have also been working on structural reforms, including cost reduction efforts, therefore, we expect a certain improvement in H2 of the year. On the other hand, we expect shipping market will be softening, and seasonal

factors, inventory supply shortages, rising labor cost in the construction & mining system business in North America is also downside factor. In the aircraft leasing business, while revenues from Russian market cannot be expected, the demand is increasing due to increase in people traveling. Further, we have newly acquired an aircraft leasing company, which we believe will contribute to increase revenues in the future.

< Questionnaire 4>
As you presented various risk factors, could you also let us know if there are any businesses or regions that are showing signs of slowdown?

< Morooka >
As for the upstream mineral resources business, market price has already weakened except for some commodity. For the midstream and downstream businesses, including gas, we were able to generate trading profits in H1 of the fiscal year because the market was very volatile, but we expect these businesses to remain calm in H2. With regard to the infrastructure business, the domestic electricity retail business expects further loss in H2 due to increased sourcing price in soaring electricity market in Japan. Sales of TBC, retail and wholesale of tires business in the US, have already begun to be affected by inflation because the business is for US consumers. TBC is working to offset the impact of inflation through further cost reductions and other measures.

< Questionnaire 5>
I think the tubular products business was one in which you were able to achieve high profits due to the implementation of rationalization for value up. Will you allocate the management resources to grow the business or maintain on your current path of streamlining and focusing on efficiency? With energy supply and demand expected to remain tight, is there a possibility that this business will become a further earnings driver in the future? What are your thoughts on these points?

< Morooka >
To speak only about our tubular products business in North America, there has not been any internal discussion about expanding our scale. We focus on sharpening our function maintaining lean operations. Against this backdrop of very favorable market conditions, we have been aiming to reduce inventory risk, or not holding risk, and pursuing a business model that is resilient to downside risks in the event of a market reversal.
Not limited to North America but our business is being operated globally. As we explained in presentation with the example of Sekal, who provides solutions contributing autonomation of drilling, we are advancing our business model and creating new business opportunities together with customers.

< Takayama >
I would like to follow up a bit on restructuring of tubular products business. The distributor business has been integrated and consolidated. Functions that were previously separated are now more consolidated and enhanced. Even in difficult market situation, we’ve provided our customers and suppliers with a variety of functions and many solutions. The direction of this business is to further deepen this value-added service.

< Hyodo >
In tubular products business, we have very close and trusting relationships with customers, working to turn our customers' important needs into ideas and discuss with them to add new services. We consider this network of customers to be an important intangible asset, working hard to leverage this asset to strengthen our profitability and expand our business areas. With two themes of enhancement of sustainability management and DX, we plan to implement a transition to a new format for our tubular products business in near future.

< Questionnaire 5>
Could you tell us your management plan how to keep certain level of profit, while shifting your focus from fossil fuels related business to renewable energy?

< Hyodo >
We do not see this as an either-or question of carbon or renewable energy. We need to reduce the amount of CO2 that stays in the air utilizing the value that LNG produces, while still providing the energy needed for the economy, and a system must be created toward this end. The development of renewable energy and its combination with various technologies to reduce CO2 emissions presents us with unlimited investment opportunities, and we will carry out our investments based on the formation of specific projects. Japanese government suggested to promote the Asian Zero Emission Community initiative as a pillar of its foreign policy. We would like to cooperate with the government in concrete ways, considering the role Japan should play in the execution of various new projects for CO2 reduction in that region in future. We believe that asset replacements will be necessary for this purpose, and we will work on a scheme to fill the gap in the viability of funds on the part of creditors while coming up with new ideas. We would also like to discuss such initiatives one by one in concrete terms as we believe this is an area where integrated trading companies can play an active role.

< Questionnaire 6>
You mentioned the business in Ethiopia. Regarding Media and Digital business unit, my impression is that it is difficult to see growth potential for this segment as a whole. What is your opinion on this point?

< Morooka >
In addition to the Ethiopian business which will be monetized in several years, we have DX center and CVC functions to pursue various growth opportunities for the future. We are not at a stage where we can talk about this yet, but I hope to be able to explain growth potential of this segment as one of our strengths.

< Questionnaire 6 >
Regarding steel sheets business, it seems to be a more bullish comparing to Q1 meeting. What is the background and your outlook for the steel sheets business?

< Fuse >
The utilization rate of our steel service center which is main driver of steel sheets business, during Q1 of 2022, the utilization rate was about 65% to 75%, and in Q2, it was about 70% to 80%, showing a slight recovery. We expect the utilization rate to remain almost the same from October onward. It has recovered a bit in China, and the utilization rates in Asia and the US have been steady. As for the overall business performance, while we were able to secure large profits in Q1, especially in the US, there was a slight decline from July onward. We expect this situation to continue during the current fiscal year.

< Questionnaire 7 >
We understood the uncertainty of external environment and current management situation. With only half of the medium-term management plan remaining, what is the point you most want to emphasize to the capital market?

< Hyodo >
What I believe is important in business is to produce numerical results. Accordingly, we have been analyzing Sumitomo Corporation's overall portfolio, identifying problem areas, and withdrawing from unprofitable businesses and we are still in the middle of formulating and implementing specific improvement measures in each business model where it is necessary. We must work through these to completion, while at the same

time actively pursuing new business and profit-earning opportunities. It is important for us to promote our business by both improving existing businesses and pursuing new businesses. We are implementing measures to this end and are confident that results will follow. While going back to basics that the entire group is committed to cash flow management, we will expand capital investment in profitable business even if it requires additional borrowing. Such a balanced approach will be extremely important to shift in Sumitomo Corporation's overall portfolio, which in turn will strengthen our earning power.
Currently, we have a bird's eye view of the entire portfolio broken down into 62 SBUs. There are still many areas that can be improved, but we have already decided on a policy for those improvements, so all we have to do is to put it into action. By doing so, we will be able to ensure that ROE is constantly above 12%. We hope you will have high hopes for us to achieve this.

< Questionnaire 8 >
As for Sekal, it is said that 80% of the rigs in operation in Norway are using this service. Please tell us about the current situation and prospects for area expansion, scale and profit image.

< Hyodo >
Even we say Norway as one of the countries, Norway is one of the difficult drilling areas in the North Sea and has one of the highest concentrations of rigs in the world. And I think there is tremendous value in being trusted and used by 80% of the rigs there. In the global oil and gas sector, it is difficult to develop new resources and energy without drilling in these difficult locations. I personally believe that it can be one of the two wheels of the tubular products business, and I hope that it will develop into such a business, although we cannot tell profit target. Also, regarding the tubular products business, we are collaborating with a variety of customers around the world. Each customer and each type of rig has very different requirements. We have distributors on the front lines who are well versed in these differences, and we are simultaneously expanding into different business models. I will explain this in more detail when the time comes.

< Questionnaire 8 >
The business performance has been extremely strong in trade in mineral resources and chemicals business. What do you think is the external environmental effect and what is the normal level of your earning strength?

< **Morooka >**
The trading gains in the mid- to downstream business was a very unique situation and we do not expect it to continue indefinitely. Therefore, we estimate that the trading gains will be about JPY40 billion decrease from H1 to H2 of the year having the different premises. It is very difficult to determine the level of underlying profitability. Profit levels were reinforced by particularly high commodity prices of mineral resources and energy. We expect a decrease of about JPY70 billion in profit from the mineral resources and energy business alone. If we assume that this portion of profit is due special factors, I think we can say that about JPY70 billion of the JPY550 billion profit could be due to external environmental effects. Adjusting a JPY20 billion buffer, H2 forecast is JPY220 billion. Taking into account the profit timing imbalance in real estate business and large deficit in domestic electricity retail business, we think that the profit level will be slightly higher than JPY220 billion without special factor. Therefore, if the current conditions continue, it would suggest a profit level of more than JPY440 billion plus alpha as annual base. Thus, it can be said that we are capable of securing profit in the upper JPY400 billion range, even if special factors are excluded. It is also in line with that 12% ROE on JPY4 trillion in shareholders' equity means that we need to generate JPY480 billion in profit. Honestly, I think that our targets are somewhat conservative, but our forecast for H2 of the year does not include the external environmental effects.

< Questionnaire 9 >
I would like to ask you about the outlook for the domestic electricity retail business for the next fiscal year. The major electric power companies in Japan have announced increases in metered or regulated rates at the same time as the announcement of financial results. Are these price hikes by Japan's major electric power companies positive for your electric power business as an alternative power company? On the other hand, however, raw fuel prices will still rise from H2 of this fiscal year, and I believe they will remain at a high level in the next fiscal year. In that context, in the current external environment, is it difficult to turn a profit only by your own efforts? Please tell us about your thoughts on these points.

< Fuse >
As you have pointed out, the business is currently affected by rising fuel prices, and furthermore, there is a risk of a tight energy supply and demand situation in the winter. Therefore, we have developed our forecast for H2 of the year, taking into consideration the concern that the loss will be worse in H2 of the year than in H1. We are currently in the process of renewing our purchasing and sales contracts and are negotiating with suppliers regarding the relative procurement of power sources and electricity sales prices for the next fiscal year and beyond. Currently, we are working toward the goal of turning the business profitable in the next fiscal year and beyond.

< Hyodo >
The three-year medium-term management plan is not the end of the story. The plan is a rolling one, and we will continue to solidify the foundation while making new investments and ensure that every step we take in this medium-term period will lead to long-term growth. The keywords for our target businesses toward this end are sustainability and DX.
While the prospects for a recovery in the Media and Digital business unit and strengthening of its earnings power are unclear, we are making upfront investments in Ethiopia's telecommunications business and steadily building earning power for the future. While keeping our basic approach in mind, we are expanding our investment funds to businesses where we can draw a clear business model. By doing so, we believe we can provide appropriate shareholder returns commensurate with the enhancement of shareholders' equity. Our commitment is to realize this in word and deed.
Accordingly, we will ensure the achievement of the goals in the current medium-term management plan. Furthermore, we will make group-wide efforts to strengthen the management foundation that will lead to future growth. So please look forward to Sumitomo Corporation in the years ahead.
We have received feedback that it is difficult to understand what makes Sumitomo Corporation attractive. Our strength is that we are firmly rooted in industry circles, as evidenced by our recent business performance. And although limited, we have established solid earnings pillars in the areas of consumers and distribution, businesses that are unique to Sumitomo Corporation. We will continue to expand these businesses as we move forward. We look forward to your continued support.

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