Questions & Answers at IR Meeting on Financial Results for FY2023 and New Medium-Term Management Plan Briefing Session

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<Questioner 1>

I would like to ask you about your current thoughts on what you want to accomplish as President and what kind of company you want to make Sumitomo Corporation, and what you want to appeal most to the stock market, which may overlap with your presentation of the medium-term management plan.

<Ueno>

In term of our previous medium-term management plan, SHIFT 2023, we strengthened downside resilience through structural reforms. As the culmination of such initiatives, we completed loss recognition for the major struggling projects at the end of FY2023. With the new medium-term management plan, we aim to meet expectations by climbing the steps of dynamic growth without any worries.

Regarding the future vision for Sumitomo Corporation, both quantitatively and qualitatively, if we leverage the capabilities we have cultivated so far, it is possible to catch up to the top three peers and grow to achieve profits on the scale of one trillion yen. As the first step, we have established this new medium-term management plan. Moreover, we revised the Management Council structure by reducing the number of council members and changing the decision-making method from unanimous consent to majority vote. Autonomous management by nine business groups, reorganized according to strategic priorities, will enable agile decision-making, creating an organization that can swiftly implement growth strategies. The 44 SBUs are also strategically grounded organizations, each led by business line experts, creating a structure capable of executing core strategies effectively.

<Questioner 1>

Regarding dynamic profit growth, given the past fluctuations in profits, how will you achieve 150 billion yen in profit growth by FY2026? Please break down the 50 billion yen from restructuring and the 100 billion yen from growth businesses with strengths and competitive advantages.

<Morooka>

Of the 100 billion yen from growth businesses, approximately 50 billion yen will come from organic growth and the remaining 50 billion yen from inorganic growth. Since the beginning of SHIFT 2023, we have been managing the portfolio using a four-quadrant approach. Most of the businesses listed under "growth businesses with strengths and competitive advantages" on Slide P.11 are categorized as “Steady business growth,” which will be expanded and grown through further investments. Now 18 out of 44 SBUs are categorized as “Steady business growth”, but others also have ambitious plans. When combining all SBU plans, both profit growth and invested capital projections toward FY2026 are even more ambitious than the figures presented. The numbers presented in the medium-term management plan are the adjusted figures from the combined SBU plans, following discussions at the management level. We refrain from providing specific details on the breakdown.

Additionally, regarding the 50 billion yen from restructuring, we have expanded the scope from what was previously classified as "Divestment" to include not only divestment and asset replacement but also turnaround achievements. We will carefully monitor policies related to businesses classified under “Restructuring.”

<Ueno>

The centerpiece of this medium-term management plan is to further strengthen our business, which is our existing strength. The top priority of this medium-term management plan is to further strengthen our accumulated strengths and competitive advantages, and to generate more than JPY100 billion in profits from such businesses.

<Questioner 1>

As a framework to ensure dynamic profit growth, could you please provide details about any changes regarding incentives for employees or personnel reallocation within the four-quadrant approach?

<Ueno>

As a mechanism to ensure growth, I would like to reiterate that we reorganized our structure based on strategies and revised our Management Council structure, while empowering each group by delegating authority to each Group CEO for autonomous management. This is one of the key features of this mid-term management plan.

We will also empower people by enhancing talent management. For instance, we introduced new hiring policy through the Will recruitment to unlock the potential of younger employees, abolish seniority-based systems, identify required capabilities, and develop management personnel. By strengthening global talent management, we aim to lead organizational growth.

<Questioner 2>

The two-year profit growth is planned at a rapid pace, from 530 billion yen in FY2024 to 650 billion yen in FY2026. Are you also planning to achieve a similarly ambitious target for FY 2025, or are you anticipating significant growth in FY 2026? Also, regarding the return from investments, does this refer to profits from investments only in the term of the new medium-term business plan, or return from investments made in SHIFT 2023?

<Ueno>

Rather than setting annual profit targets for each of the three years of the new medium-term management plan, we have planned a net profit of 650 billion yen as the growth goal over the entire three-year period. In terms of profit growth compared to FY23, we anticipate a 50 billion yen increase in existing business restructure and a 100 billion yen increase in growth businesses with strengths and competitive advantages. The restructuring of existing businesses includes the nearly complete loss recognition of major struggling businesses, as well as expected results from business turnarounds. For example, Fyffes' banana business achieved record profits in FY2023, and the performance of the TBC, U.S. tire distribution business, has also been recovering. Additionally, we will no longer recognize equity losses from the Nickel mining & refining business in Madagascar ("Ambatovy"), which will positively impact in comparison with previous years. The 100-billion-yen growth target for businesses with strengths and competitive advantages includes returns from new investments, as well as profit realization from investments executed during SHIFT 2023, such as the acquisition of assets from a U.S. construction equipment rental company and domestic real estate projects.

<Takayama>

Please refer to Appendix page 14 of the Annual Results for FY2023 for the timing when some of the investments and loans made under SHIFT 2023 will begin to contribute to profit.

<Questioner 2>

What are the main factors contributing to the increases and decreases in Profit for the Year (Attributable to Owners of the Parent) from the FY2023 full-year results to the FY2024 full-year forecast of 530 billion yen?

<Morooka>

For an overall picture of the main factors behind the increase or decrease, please see page 8 of the FY2023 earnings announcements. Excluding one-off profits and losses, we anticipate a decline in earnings in resource businesses in FY2024 due to falling coal prices. However, significant growth is expected in non-resource businesses, leading to a profit plan of 510 billion yen. On the other hand, Corporate and Eliminations is expected to see a decrease in profit, which is due to the revisions to

the internal interest allocation to business groups starting from FY2024. Due to this policy change, the non-resource businesses will see a positive impact of approximately 25 billion yen, and the resource businesses will benefit by around 10 billion yen. Therefore, the net change will reflect these adjustments. Additionally, the FY2024 full-year forecast is based on an exchange rate assumption of USD 1 = JPY 140, resulting in an approximately 10-billion-yen negative impact compared to the previous fiscal year.
Taking these factors into consideration, the increase/decrease in performance by new business group, excluding one-off profits and losses, is shown on page 9. Groups expected to show significant growth include Steel, Transportation & Construction Systems, Diverse Urban Development, and Chemical Solutions. Particularly in Steel, and Chemical Solutions, we foresee a market recovery and have plans to increase profits by implementing various initiatives. For Transportation & Construction Systems, growth will mainly focus on construction machinery and leasing businesses.

<Questioner 3>
The 100 billion yen in growth businesses with strengths and competitive advantages includes the effects of investments made during period of SHIFT 2023, the previous medium-term management plan. Is it correct to understand that in the new medium-term management plan, about 80% of the planned 1.8 trillion-yen investment will be allocated to such businesses? Additionally, which segments are expected to contribute to FY2026 target of 650 billion yen?

<Ueno>
It's accurate to understand that about 80% of the 1.8 trillion yen will be invested towards the 100 billion yen in growth businesses, but not all investments will necessarily generate returns by FY2026. Our strategy is to allocate around 80% of these investments to projects that can yield returns in a shorter timeframe, while the remaining 20% will be directed to developmental areas with longer-term profitability.
The growth businesses with strengths and competitive advantages involve investing in fields where we possess experience to capitalize on our strengths. Specific investment targets will be evaluated on a case-by-case basis.

<Questioner 3>
Regarding cash flow allocation, the material indicates a cash inflow of 2.8 trillion yen and a cash outflow of 2.5 trillion yen. I'd like to understand the thoughts behind the 0.3 trillion-yen gap. After 50-billion-yen share repurchase is finalized, achieving the profit plan of 650 billion yen without adjusting the capital would also enable an ROE of over 12%. From this standpoint, will the 0.3 trillion yen be allocated for investment or for shareholder returns? Additionally, what is the intention behind setting the total payout ratio at 40% “or more"?

<Ueno>

If investment opportunities that can lead to growth arise, we will consider investing more than the planned 1.8 trillion yen. Moreover, as the total payout ratio is set at 40% or more, it's also possible to return over 0.7 trillion yen to shareholders. We aim to balance growth investments with shareholder returns.

<Questioner 3>

Assuming a 5% ROI on 80% of the 1.8 trillion-yen investment (i.e., 1.4 trillion yen), the profit contribution would be 70 billion yen. Is it correct to understand that the remaining difference of 30 billion yen would come from the profit contribution of investments made during the SHIFT 2023 period?

<Ueno>

Your understanding of the approach is accurate, but ROI assumptions and timing of profit contributions vary with each project.

<Questioner 4>

I recall that, like this time, the previous medium-term plan, SHIFT 2023, also aimed to turn things around after revisiting the impairment losses. How does the new medium-term management plan differ from SHIFT 2023? What impact will the four projects, which recorded one-off losses in FY2023, have on future P&L and B/S? Additionally, is there a risk of further impairments in the period of the new medium-term management plan, and does the 650-billion-yen target include a buffer?

<Ueno>

The largest struggling business in SHIFT 2023 was the Ambatovy project. In FY2020, production was temporarily halted due to COVID-19, and maintenance was undertaken to repair and improve facility process. Production resumed around mid-2021, so when SHIFT 2023 began, the business was progressing steadily, and no further impairments were anticipated. However, due to the subsequent decline in nickel prices and facility process issues, we ended up fully impairing the project. Since the carrying value of the investment in the project is now zero except some minor shareholder loan receivable, we will not recognize any further equity losses, meaning that the P&L impact will be zero for us.

Regarding the telecommunications business in Myanmar, political turmoil in Myanmar and resulting delays in recovering USD-denominated lease receivables, which were unforeseen when SHIFT 2023 started, led to provisioning. However, efforts to recover those receivables will continue.

We do not anticipate further losses from the four projects. While future business conditions may affect other businesses, there are no significant concerns at present. The 650-billion-yen target does not include a buffer.

<Questioner 4>
Of the 44 SBUs, 18 are classified as “Steady business growth”, but what is the breakdown by quadrant? What is the mission given to the “Value-up” and the “Restructuring,” and what kind of management resource allocation and direction are you considering?

<Ueno>
While we refrain from providing a detailed breakdown, most of the invested capital will be directed toward "Steady business growth" quadrant. "Value-up" businesses are expected to grow profits without requiring additional capital investment. They could potentially transition into "Steady business growth", and if that happens, they will also receive capital investments.

<Questioner 5>
I've had the impression that investments haven't been particularly successful, and I thought there were issues with the structure of the Management Council. Could you explain what problems existed with the previous structure and what benefits you expect from the changes made this time?

<Ueno>
There are two reasons why we changed the structure of the Management Council. First, to increase agility, and second, to separate the Management Council that discusses the entire company's portfolio from the business group CEOs. This ensures that the Management Council can focus on portfolio transformation from company-wide perspective. Business group CEOs are given decision-making authority, and issues within their purview are discussed in their group management meetings to ensure optimal outcomes at the group level. Meanwhile, the company-wide Management Council focuses on discussions related to the entire company's portfolio, aiming for optimal outcomes on a broader scale.
We've already conducted Management Council meetings under the new structure, and I feel that the benefits of quick decision-making and separating group-level optimization from overall optimization are effectively functioning.
Regarding investment success, we aim to eliminate investment failures by placing invested capital in areas of strength, namely businesses with a proven track-record.

<Questioner 5>
Regarding the Ambatovy project, it is mentioned that all options will be considered, but is it realistically possible to exit this business? Should we be concerned about potential disadvantages in financing after the exit? If the project continues to run at a loss, the capital investment may need to be further increased. What is your current understanding of the situation?

<Ueno>

Our immediate priority is to get the business back on track. Currently, monthly nickel production is just over 2,000 tons, and we're focusing on repairing and replacing equipment to restore the plant to normal operations as soon as possible.

All options that we will consider mean a wide range of possibilities. While the carrying value of the investment in the project is now zero except some minor shareholder loan receivable, it is extremely difficult to exit from this project. We must assess the impact on various stakeholders, including senior lenders, and recognize our social responsibilities in Madagascar due to the jobs created there. Additionally, economic security considerations related to securing nickel need to be factored into the decision. Despite the complexities involved, we're at a stage where we must contemplate this, so we have expressed it more explicitly.

<Questioner 6>

What is the outlook for the telecommunications business in Ethiopia?

<Ueno>

Although plans for facility expansion have faced delays due to political instability in Ethiopia, we see this as a long-term project that will support the country and handle its mobile telecommunications business. We are working to realign the business with the original plan in consultation with partner companies such as Vodafone and a Kenyan company.

As the Ethiopian business is not an acquisition, there is no goodwill related to this project, and as it is still in the development stage, there is no possibility of impairment at this time.

<Questioner 6>

Since Executive Officer Nakazawa joined from a foreign company as Head of HR, what HR initiatives have been implemented over the past year, and what have been the results? Additionally, what needs to be done in the future?

<Ueno>

Her mindset, shaped by her experience at foreign companies, is evident in many areas, contributing to the overall reforms of our HR system. Example of such reforms that were implemented incorporating her insights include the introduction of Will recruitment, changing the format of the onboarding ceremony, revising the role of corporate officers, and Capabilities identification due to the removal of the seniority system. This has introduced mechanisms to increase internal mobility. This is expected to be a driving force for future growth. A mechanism to enhance internal talent mobility was also introduced. These initiatives will likely drive future growth. Moreover, while challenges remain in the development of management personnel, she has established a system to nurture talent through new methods.

<Questioner 7>

You've mentioned that the level of interest-bearing debt is relatively high. With the new medium-term management plan prioritizing positive free cash flow post shareholder returns, is it correct to understand this as a message emphasizing careful management of financial soundness?

If you were to increase shareholder returns or investments in the future, could credit ratings potentially become a hurdle?

<Morooka>

We continue to believe that restoring our credit rating to an A grade is highly important. While S&P upgraded our rating last year, Moody's did not. We would like to improve our rating as soon as possible, as it represents our company's credibility and is also a source of competitiveness. To achieve this, we will maintain financial discipline by ensuring positive free cash flow post shareholder returns, while flexibly allocating cash for shareholder returns and investments in the most optimal manner. As long as we maintain a positive free cash flow post shareholder return in this manner, our financial structure will not be adversely affected. While it will not be included in free cash flow post shareholder returns, working capital will still be managed carefully. Even with the current financial structure, improving resilience should lead to improved credit ratings, and maintaining and enhancing the level of cash flow will be crucial.

<Questioner 7>

Does the 1.8 trillion-yen investment include increasing equity stakes in existing business companies where your current share is around 50%?

<Morooka>

Increasing stakes in existing business companies is understood to have a high likelihood of success since we are familiar with those businesses. However, we should not invest solely for the purpose of acquiring a greater share of profits. We will carefully consider whether such investments align with our strategy and if they can generate returns exceeding the investment amount. We will refrain from providing specific details about the composition of the 1.8 trillion-yen investment.

<Questioner 8>

What exactly does “No. 1 in each field” mean? For instance, in the agriculture business, does it involve becoming No. 1 in Brazil and expanding to other regions? Or in the steel business, does it mean growing as No. 1 in sales to CCU? If there are any specific examples, please share them.

<Ueno>

In SHIFT 2023, we implemented structural reforms and strengthened our resilience against downturns. In the new medium-term management plan, the term "No. 1" is being used to set a mindset for rapidly advancing toward growth.
Since the definition of No. 1 varies across business lines, we are intentionally not providing a specific definition. Instead, each business line should analyze what it means to aim for No. 1 in their respective areas and translate it into strategies, considering a range of factors like growth potential, profitability, capital efficiency, and customer satisfaction. The mindset of thinking about what strategies to develop in order to reach No. 1 is essential, and that itself will form the growth strategy.
However, striving to achieve competitive advantages in business is a key part of becoming No. 1, and there are multiple ways to achieve those advantages.

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