◆ Cosmo Energy Holdings (Stock code: 5021)
The 7th Consolidated Medium-Term Management Plan
- Explanatory Meeting for Analysts and Investors - Summary of Q&A

- This material contains descriptions regarding future prospects. Notes are provided at the end of this material. -

1. Date and time : Thursday, March 23, 2023, 17:30 to 18:30 (JST)
2. Attendees : 95 persons
3. Main questions and answers :

Q1: What is your view on market conditions and ROE targets?
ROE target of the 7th Consolidated Medium-Term Management Plan (hereinafter "the 7th MTMP") is to generate a stable ROE of 10% or more, but profit level is likely to be affected by market conditions. Can we tell us about the concept behind the ROE target, whether the target is to be achieved even if affected by market conditions, or ROE of 10% or more can be achieved if the petroleum refining margin and petrochemicals spread, which are the assumptions for ordinary profit excluding impact of inventory valuation of ¥165.0 billion are achieved?

A1: While market fluctuations certainly affect our financial performance, we recognize that the domestic market has been stable since FY2017. The overseas market swings have been large, but the impact on us has not been significant. Therefore, we believe that we will be able to achieve our targets if we can firmly enjoy the stable domestic market environment by maintaining high uptime of refineries and implementing the measures set out in the 7th MTMP.

Q2: I believe that the major shareholder has raised the issue of spinning off renewable energy business, together with the level of net worth, when the 7th MTMP was published.
What are your views on this?

A2: The renewable energy business is one of the Group's key growth strategies.
Until now, all electricity generated by renewable energy projects has been purchased at a fixed price through the FIT, but the transition to FIP will require the electricity generated to be sold efficiently while complying with obligation of simultaneous planned quantity and time. Currently, Cosmo Eco Power does not have supply-demand adjustment or sales functions, so it will need to acquire these functions on its own if spinning off has executed.
On the other hand, the Group already has a function for electricity retailing. In addition, the Group already has a function for supply-demand adjustment, although the validation of electricity storage business will start in FY2023. The assumption is that by combining these functions, the green electricity business can be expanded.

For offshore wind power generation, there is not a huge amount of investment. We are assuming that 20-30% of the total project investment will be funded by equity and the rest by project finance. Even equity is not considered to be a major capital risk as it assumes a form of investment handled by several companies.
In addition, Cosmo Eco Power has active human resource exchanges within the Group, and we do not believe that it is in the best interests of maximizing the enterprise value to separate it through a spin-off.

Q3: With regard to spin-off, human resources and know-how are more important than capital constraints, and since both are within the Group, does this mean that the Company has concluded to make use of them?
A3: If there is a huge capital expenditure, spin-off would be worth considering, but we do not anticipate any major capital expenditure at this time.

Q4: Operating profit target for bolster green electricity supply chain is ¥40.0 billion in 2030.
As of FY2022, operating profit of the renewable energy business was ¥3.0 billion, and we would like to ask how you plan to jump up this figure.
We would also like to ask which of renewable energy generation, supply-demand adjustment/storage and green electricity sales will be the main source of revenue.
A4: Of the ¥40.0 billion in ordinary profit in 2030, the value of electricity generated is expected to be about ¥15.0 billion, supply-demand adjustment/storage about ¥5.0 billion, and green electricity sales about ¥10.0 billion.
Although the value of green electricity is not well recognized at present, we believe that it will grow, given the recent auctions of non-fossil power at the maximum price, the increase in the number of RE100 member companies, and the fact that electricity retailers will be obligated to have a 44% non-fossil quota by 2030.
For the remaining approx. ¥10.0 billion, the Company hopes to earn in the mobility field, such as by expanding EV leasing, which is included in green electricity sales.

Q5: Regarding your net worth target of ¥600.0 billion or more, how did you calculate the necessary figures when it was calculated on a risk basis?
In addition, regarding your shareholder return policy, you state that additional returns will be made when the financial health target is achieved. Is it correct to understand that additional returns will be done when both the net D/E ratio and the amount of net worth have been achieved?
A5: A total of approx. 130 similar domestic and overseas companies were selected for each segment, and ROA fluctuation data for the past 20 years was used to calculate how much risk was covered by the net worth. From the result, we calculated a coefficient and multiplied it by our assets to derive the necessary figures for each segment, which totaled more than ¥600.0

billion.

Although we refrain from disclosing specific examples, we used as objective a method as possible, with the assistance of an outside organization, to calculate the necessary net worth from a risk perspective. We have heard that trading companies and financial institutions use similar methods for the financial health approach.

With regard to the shareholder returns policy, we will make additional returns to shareholders when both the net D/E ratio and the amount of net worth are achieved.

Q6: I think you have presented an excellent policy on shareholder returns.
What are your thoughts on the policy?

A6: Basically, we have expressed our intention to increase enterprise value by balancing shareholder returns, financial health, and capital efficiency, while improving each elements. Of the three elements, we have recognized that shareholder returns is a commitment to the stock market. After thorough discussion at the Board of Directors meeting, we decided on a dividend of at least ¥200 per share and a total shareholder return ratio of 60%, a level that is one step higher than other companies in the industry. We determined that the lower limit on the dividend was sufficient based on the earnings outlook.

The decision was based on a balance between financial health and capital efficiency, not necessarily shareholder returns alone.

Q7: Regarding the capital efficiency target, we understand that it is difficult to generate a stable ROE of 10% or more, given the industry environment for petroleum wholesalers.

Looking back on the past, I think it is commendable that you were able to achieve ROE of 10% during the 6th MTMP, although we had expected it to be difficult. I believe this is due to the fact that you were able to improve profitability more than peers in the petroleum wholesale industry.

On the other hand, with regard to the ROE target of 10% or more in the 7th MTMP, from the perspective of expanding enterprise value, couldn't you show a further improvement in capital efficiency? With the ROE target of 12% for 2030, what are your thoughts on the fact that the 7th MTMP target appears to be flat from the 6th MTMP?

A7: In the 7th MTMP, we would like to improve our financial health while maintaining a stable ROE of 10% or more. Since the Oil business is still the main earnings driver during the 7th MTMP, it will not be easy to raise profitability significantly beyond the current level. We have indicated the target as the level we would like to achieve at any cost.

During the 6th MTMP, the Company improved its operation rate through a short position strategy, resulting in a significant increase in profitability. We expect to maintain high profitability during the 7th MTMP.

On the other hand, although untransferred costs are increasing due to yen depreciation, inflation, and other factors, the current profit plan does not incorporate the reflection of untransferred costs in prices. If these costs are reflected in sales prices, as other companies are proceeding with price transfers, an upward swing can be expected.

Q8: Regarding the ROIC target of 6% or more for FY2025 and 8% or more for FY2030, what is the current level of ROIC excluding impact of inventory valuation?
In addition, what is the assumption for the cost of equity during the 7th MTMP?
A8: The current ROIC result is in the upper 6% range. Since the target for FY2025 is 6% or more, ROIC appears to be deteriorating. This is because upfront investments will be made in the offshore wind power generation business, etc. during the 7th MTMP, while the contribution to profits will not be realized until 2030 or later. The cost of equity is assumed to be 7-8% on a CAPM basis.

Q9: The explanation of the concept of necessary net worth was very clear and the material was easy to understand. It would have been better if the necessary net worth for each segment had been explained more quantitatively.
On the other hand, the amount of necessary net worth is an point where there are differences of opinion with major shareholder, and I think it is an area that needs to be explained carefully.
With the net worth outlook for FY2022 of approx. ¥530.0 billion, you mentioned that it is necessary to increase it to ¥600.0 billion while also looking at the risk buffer for each segment. Could you tell me which specific segments need to be built up of net worth?
A9: Previously, we have focused our attention on inventory valuation risk in petroleum refining, but there are more risks in other segments than we had thought. Although it is difficult to present them quantitatively, we have come to the conclusion that it is necessary to build up corresponding net worth, especially in the Oil E&P and Renewable energy segments.

Q10: What is the breakdown of investments in the green electricity supply chain?
Is it correct to understand that the ¥130.0 billion to be invested in the offshore wind power generation project is for equity investment?
Also, is there a possibility that the investment will be reduced if the bid for the offshore wind power generation project is not successful?
A10: The ¥130.0 billion for the offshore wind power generation project is for equity investment only. If the bid is not successful, the investment will be reduced.
In addition, the other breakdown is that approx. ¥240.0 billion will be invested in the onshore wind power generation business, but the actual amount is expected to be about ¥20.0 billion due to the leaseback.
The remaining approx. ¥150.0 billion will be invested in energy storage and development of other renewable energy sources.

Q11: I have the impression that the investment in the energy storage area is higher than expected, is it solidified as a business model?

A11: The approx. ¥150 billion includes investments in power generation projects other than wind power, such as solar and biomass, so investment in energy storage is not large. We plan to conduct a validation of the energy storage business from FY2023, and expect price volatility to increase as green electricity becomes more widespread in the future.

On the other hand, since the cost of storage batteries is high, validation will be conducted, including whether the returns are commensurate with the high cost.

Q12: If the amount of investment is lower than expected, the burden on cash will be reduced and the increase in interest-bearing debt will be controlled. In that case, I believe that net worth will increase against targets as planned, and the net D/E ratio will improve more than planned in some cases. Will additional shareholder returns be implemented if the net worth target is not achieved?

A12: This is a difficult question, but we believe that ¥600.0 billion in net worth is important from the standpoint of financial health under the assumptions of the 7th MTMP. On the other hand, assets should be decreased due to lower-than-expected investment, and the figures will change in tandem with this. We would like to respond to these issues after carefully examining them.

Q13: Regarding the concept of additional shareholder returns, if both net worth and net D/E ratio targets are achieved, in what form will the returns be implemented?

Specifically, will the portion of the net worth in excess of the ¥600.0 billion targets be returned to shareholders, or will this be considered again when the targets are achieved?

A13: Although this is subject to change if the assumptions change significantly, if both net worth and net D/E ratio targets are achieved under the assumptions of the 7th MTMP, the portion exceeding ¥600.0 billion will be subject to additional returns in principle.

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