Our Financial Strategy

Striving to achieve the targets in the final year of our Medium-Term Management Plan with the recovery of our powerful growth capabilities

Takeshi Matsui
Representative Director and Executive Vice-President

Major downturn in profits caused by increased costs of LNG procurement due to the impact of Freeport LNG's plant shutdown and other factors

In FY2023.3, the second year of the Medium-Term Management Plan (FY2022.3-FY2024.3), the business environment was extremely harsh due to the impact of the Freeport LNG's liquefaction facility shutdown, the increasing instability of the energy supply-demand balance, and soaring prices, among other things. On the other hand, soaring energy prices have meant increased profits from upstream businesses overseas in the International Energy segment, while we also steadily grew our earnings in the Life & Business Solutions (LBS) segment. These profit increases have resulted in a partial recovery in the depression of consolidated profits, and I see this as evidence that our portfolio management has functioned well to a certain extent.

In the Group's business results for FY2023.3, net sales were 2.275 trillion yen, up 683.9 billion yen from the last year due to the higher unit selling prices of gas and LNG in the Domestic Energy Business and the selling price boom in the US and Australian upstream businesses in the International Energy Business.

Ordinary profit was 75.6 billion yen, down 37.8 billion yen from the last year, due mainly to losses related to Freeport LNG's plant shutdown. Profit attributable to owners of the parent was 57.1 billion yen, down 73.3 billion yen from the last year for the same reason as the ordinary profit decline. The decrease in profit attributable to owners of the parent was more significant than the ordinary profit decline due to the absence of the recording of deferred tax assets and income taxes–deferred (gain), as we had in the previous fiscal year.

Anticipation of increased profits in FY2024.3 with the operation resumption at the Freeport LNG plant and Improvement of time-lag effect

In FY2024.3, the final year of the Medium-Term Management Plan, net sales are expected to decrease from the FY2023.3 level due to lower LNG prices reducing gas unit selling prices in the Domestic Energy Business. However, ordinary profit and profit attributable to owners of the parent are expected to increase from the FY2023.3 level with the resumption of operations at the Freeport LNG plant and the improvement of the time-lag impact. We anticipate an ROIC of 5.4%, which exceeds the target of around 5% in the Medium-Term Management Plan.

More in-depth ROIC-focused management that responds promptly to changes in the business environment

The Daigas Group's business units and corporate headquarter divisions work closely together to maintain and improve ROIC to exceed capital costs (WACC). We aim to enhance our agility as a corporate group where each business unit makes decisions autonomously in divesting assets, making investments to improve ROIC, and implementing initiatives to boost asset efficiency. To that end, we intend to make the business units mindful of the ROIC tree to detect early signs of changes in performance based on visualized significant KPIs.

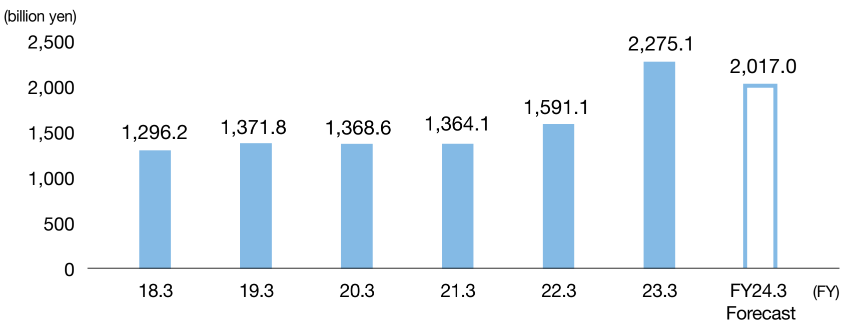
In FY2023.3, our second year using ROIC, we evaluated each business unit against the first-year ROIC results to establish an ROIC-focused management culture across the Group. In addition, we took various measures to raise NOPAT, sold cross-shareholdings, and proceeded with steps to securitize Group-owned real estate. Each business unit has been granted the authority for short-term business operations to speed up its business development processes. Meanwhile, the corporate headquarter divisions have begun work on the regular review of medium-term business plans and resource allocation. The plans will be reviewed in light of changes in the business environment since the current Medium-Term Management Plan was formulated, such as the accelerating decarbonization trend, soaring energy prices, and changes in market competition. Through these endeavors, we aim to improve our Group's response speed to changes and enhance our business portfolio's robustness.

Growth through investment in new businesses where we can leverage our strengths

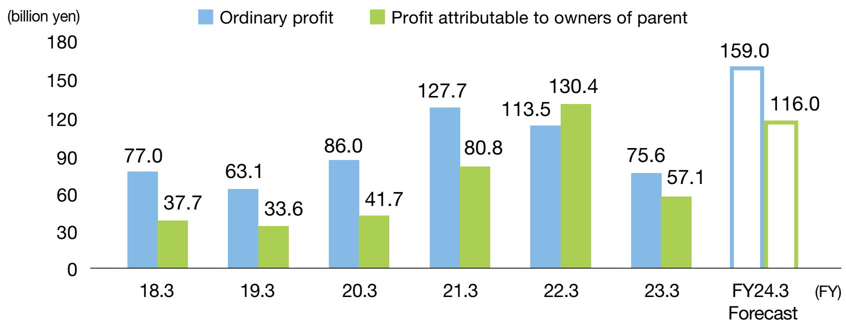
In FY2023.3, as we had envisaged a significant profit downturn since Freeport LNG's plant shutdown, we pursued investments for business growth having paid more consideration than usual to the impact on financial soundness. We invested 172.2 billion yen (86% of the target) in projects to develop power sources, such as the Himeji Natural Gas Power Plant and renewables, upstream business in North America, and real estate development projects.

The Daigas Group plans to execute steady investments in the cumulative amount of approximately 500 billion yen for the period up to March 2024 under the Medium-Term Management Plan. These investments aim for business growth in key areas, including decarbonization-related fields such as renewable energy (about 120 billion yen), International Energy Business, and Life and Business Solutions (LBS) Business. In our investment for business growth, we focus on ROIC as a target in our

■ Net sales



■ Ordinary profit and profit attributable to owners of parent



renewable energy development projects in Japan, where we invest with strategic partners to minimize our investment amounts while maximizing our power offtake in excess of our stakes in the projects. In our investments for quality improvement, we are increasing investments in digital transformation and resilience enhancement. We aim to bring free cash flow into the black in FY2024.3 due to the expansion of operating cash flow from the outcomes of our activities to date. For the sound and sustained growth of the Daigas Group, we will work to maximize ROIC from medium- to long-term perspectives while expanding profits.

Daigas Group's investment risk management

In our investments, we aim to maintain a good balance between risk and return, not taking high risks to seek excessively high returns and avoiding unnecessary risk control. We manage investment risk by ensuring the following four points.

The first is the investment project's consistency with our strategy. Besides evaluating project profitability, we assess the potential for synergies with the Group's other businesses and enhancement of business execution capabilities.

The second is the evaluation of the inherent risks of the investment project. We make decisions on investment through strict evaluations and deliberations of target projects at the Investment Evaluation Committee based on our group-wide investment standards, taking into account the evaluation results made by the Investment Risk Management Office, our internal organizations for financial and legal affairs, as well as external consultants when necessary.

The third is the maintenance of a good balance with financial soundness. We quantitatively assess potential losses for each risk in investment and balance risk and return across the entire Group to make it possible to sustainably conduct investments for business growth while maintaining a certain level of financial soundness in the face of the risks.

The fourth is post-investment follow-ups. We conduct annual follow-ups on investment projects based on our investment monitoring standards, in which we evaluate whether the project satisfies the original purpose of our investment, whether it is keeping up with the changes in the business environment, and whether it faces any issues in terms of progress and profitability. Depending on the evaluation results, we take necessary actions such as improving project profitability and considering divestiture or withdrawal.

Utilizing transition finance

Since FY2023.3, the Daigas Group has continued to procure funds through transition finance to use the funds for initiatives that align with the company's long-term transition strategies to reduce greenhouse gas emissions. In FY2024.3, we have been increasing funding from corporate bond investors and financial institutions by deepening their understanding of our carbon neutral strategy through our briefings on the Energy Transition 2030 announced in March 2023. Our transition loan is the first case in the gas industry.*1 Utilizing transition finance with loans as well as corporate bonds will provide an excellent opportunity to have the Group's transition strategy assessed by more financial institutions. In focusing our efforts on businesses related to carbon emissions reduction and decarbonization, we see transition finance as an effective means of procuring funds and hope to make active use of it going forward.

*1 As researched by the Daigas Group based on publicly available information

Transition finance conducted

Transition finance	Month of issue	Amount	Use of funds
1st Transition Bonds	June 2022	10.0 billion yen	Inami Wind Power Plant, Noheji Mutsu Bay Wind Farm, Yokohama Town Wind Power Plant, Daigas Oita Mirai Solar Power Plant, projects that contribute to fuel conversion at customer facilities to natural gas
2nd Transition Bonds	September 2022	27.0 billion yen	Kuwaharajou Mega Solar (No. 4), the Extra-high-voltage Power Plant in Isohara-cho, Kitaibaraki City, Ibaraki Prefecture, Himeji Natural Gas Power Plant
Transition loan	January 2023	35.0 billion yen	Himeji Natural Gas Power Plant
3rd - 5th Transition Bonds	June 2023	35.0 billion yen	Himeji Natural Gas Power Plant

Shareholder returns according to profit growth

As our shareholder return policy, we intend to provide stable dividends while maintaining a consolidated dividend payout ratio of 30% or higher, excluding short-term profit fluctuation factors. We also consider increasing dividends when we achieve profit growth. In FY2023.3, despite projections of a downturn in profit, we issued dividends of 60 yen per share, an increase of 2.5 yen, as initially planned, in view of the achieved growth and estimated future profits. We also aim for a further increase of 5 yen to 65 yen per share in FY2024.3.

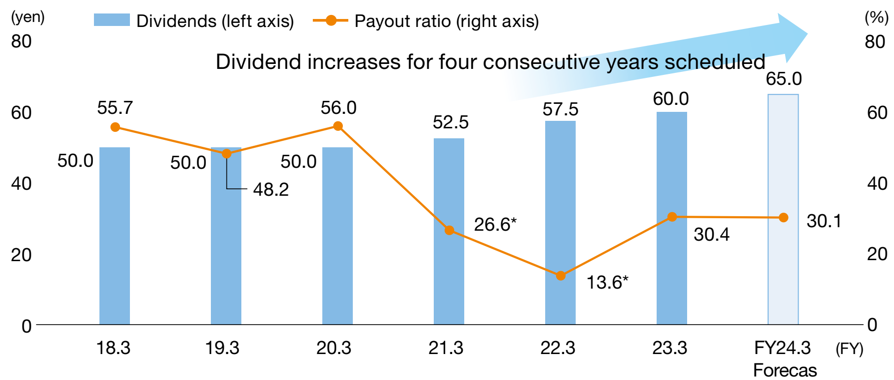
Going forward, we will implement an optimal shareholder-return policy formulated based on a comprehensive evaluation of projected free cash flow, progress in investments for business growth, business performance, and financial situation, taking into account factors such as the accelerating decarbonization trend and intensifying competition driven by non-energy players' entry into the gas and power markets.

Enhancement of corporate value through dialogue with capital markets

We consider dialogue with capital markets to be highly important. Through such exchange, we obtain the capital markets' understanding and appropriate evaluation of the Group's strategies. For example, with the above transition finance, we gained the market's support by carefully explaining our management plan, which resulted in the increased number of our corporate bonds purchased by investors, including those with a strong interest in climate change issues. In addition, investors' frank opinions have helped us learn the capital markets' views on the Group's circumstances, which gave us different perspectives in deliberating management strategies. Recent investor relations activities have served as opportunities for us to renew our recognition of the importance of addressing ESG-related issues, including climate change, human capital, and governance, as we received many questions about our ESG strategies besides opinions about optimal capital composition, free cash flow, and shareholder returns. Through constructive dialogue with capital markets, we aim to enhance our corporate value from the financial front so that we will remain worthy of long-term support from our stakeholders, including investors and shareholders.

■ Dividend amounts and payout ratios

Note: For the payout ratio, time-lag profit/loss, including those in the power business since FY2021.3, only has been adjusted as a factor in short-term profit fluctuation.



*The payout ratio fell below 30% in FY2021.3 and FY2022.3 due to short-term causes of profit fluctuation besides the time-lag profit/loss.