COMPANY RESEARCH AND ANALYSIS REPORT

ITOCHU ENEX CO., LTD.

8133

Tokyo Stock Exchange First Section

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Index

Summary

Smooth progress reinforcing foundations for advancement to the next stage; headed for all-time high net profit for a fourth straight year in FY3/19

ITOCHU ENEX CO., LTD. <8133> (hereafter, also “the Company”) is an energy trade company that is playing a pivotal role in the energy field for ITOCHU Corp. <8001>. It has a broad business scope, though it mainly sells petroleum products and liquefied petroleum (LP) gas to users ranging from industrial businesses to final consumers. It also entered the electricity business thanks to deregulation and is currently aiming for stable, continuous growth in three main areas of petroleum, gas, and electricity.

1. Posted higher sales and profits (YoY) in FY3/18, including all-time high net profit for a third straight year

The Company posted higher sales and profits (YoY) in FY3/18 with ¥1,156,344mn in sales (+12.4%) and ¥11,025mn in net profit attributable to the Company’s shareholders (+6.0%). These results exceeded forecasts. Sales improved on increases in crude-oil prices and electricity sales volume. In earnings, net profit strengthened as gains in the Life Energy & Logistics Division through Car-Station (CS; in-house name for gas stations) reforms and the Home-Life Division led by higher sales volume and reorganization of the LP gas business more than offset declines in the Power & Utility Division and Industrial Energy & Logistics Division.

2. Two-year medium-term business plan “Moving 2018” progressing steadily
Strengthening both revenue and organizational bases

The Company is implementing its two-year medium-term business plan, “Moving 2018” covering FY3/18 and FY3/19. The plan positions itself as “two years to lay the management base for the next stage of the Company's development” with emphasis on 1) reforming the revenue base and 2) revamping the organizational base. For the former, the Company reorganized the LP gas business with Osaka Gas Co., Ltd. <9532>, withdrew from money-losing CS locations, launched operation of the Sendai Power Station, and expanded the power balancing group in FY3/18. For the latter, it is partially reorganizing business segments from April 2018 to integrate petroleum, gas, and electricity businesses respectively. It is also spinning off the mobility (automotive) business and accelerating decision-making. The Company made qualitative improvements too, including personnel investments and working style reforms.

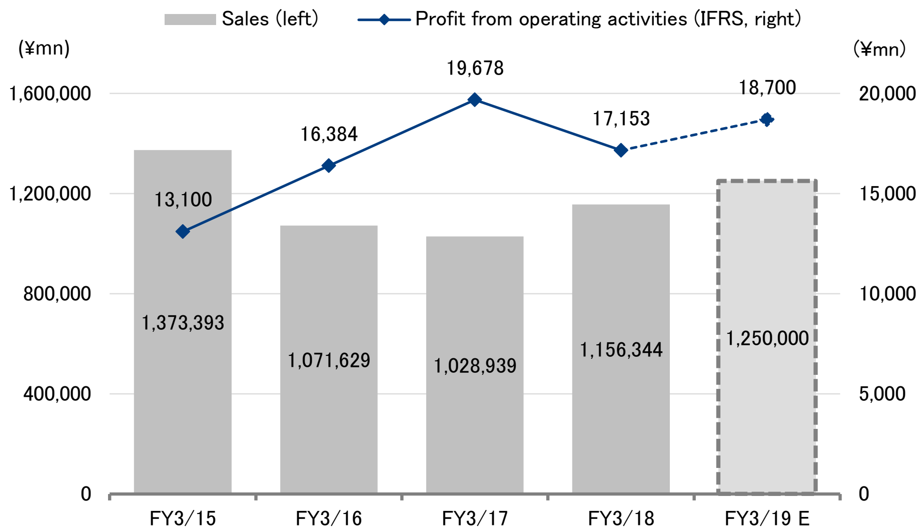
3. Focus on content of growth investments and progress, rather than income results in FY3/19

In FY3/19, the Company intends to continue reinforcing the revenue base and organizational base, as it did in the previous fiscal year. It has already raised targets for profit from operating activities and net profit attributable to the Company’s shareholders from the initial medium-term plan and there are few areas of concern. Hence, key points, in our view, are progress in bolstering foundations and implementation of measures that directly connect to future growth. We think these points are likely to determine whether the Company aims for ¥20bn in net profit immediately in the next medium-term business plan beginning in FY3/20 or allows for some time to consolidate recent gains. The Company lifted its investment budget in the Moving 2018 medium-term plan from ¥45bn to ¥56.6bn and plans to invest ¥32.2bn in FY3/19. Attention should be given to this content and related assessments during FY3/19.

Key Points

- Realizing steady progress with two major themes in the medium-term business plan of 1) reforming the revenue base and 2) revamping the organizational base
- Raised the two-year investment budget in Moving 2018 to ¥56.6bn
- Increased the dividend payout ratio (used as a guideline in setting dividends) to 40%; paid a ¥40 dividend (+¥8 YoY) in FY3/18

Results trends



Source: Prepared by FISCO from the Company's financial results

Results trends

Posted all-time high profits on price stabilization and business restructuring reforms

The Company reported FY3/18 results of ¥1,156,344mn in sales (up 12.4% YoY), ¥17,153mn in profit from operating activities (down 12.8%), ¥19,169mn in profit before tax (down 0.9%), and ¥11,025mn in net profit attributable to the Company's shareholders (up 6.0%).

While profit from operating activities and profit before tax fell YoY, business reorganization impact played a large role, as explained below. Net profit attributable to the Company's shareholders without the impact of reorganization, meanwhile, increased and reached an all-time high for a third straight year. Sales and various profits exceeded period-start forecasts.

Review of FY3/18 results

(¥mn)

	1H results	2H results	Full-year results	1H results	2H forecast	Full-year forecast	Full-year results	YoY	vs. forecast
Sales	466,313	562,626	1,028,939	507,990	648,354	1,150,000	1,156,344	12.4%	0.6%
Revenue	309,516	385,544	695,060	352,395	392,372	-	744,767	7.2%	-
Gross profit	43,742	49,862	93,604	44,193	44,629	-	88,822	-5.1%	-
SG&A expenses	36,210	38,487	74,697	35,385	35,546	-	70,931	-5.0%	-
Profit from operating activities	7,755	11,923	19,678	9,421	7,732	16,500	17,153	-12.8%	4.0%
Profit before tax	7,242	12,102	19,344	8,282	10,887	17,800	19,169	-0.9%	7.7%
Net profit attributable to the company's shareholders	3,707	6,698	10,405	3,969	7,056	10,400	11,025	6.0%	6.0%

Source: Prepared by FISCO from the Company's financial results

Sales were up 12.4% YoY due to healthy product prices that reflected higher crude oil prices and expanded sales volumes for the full range of products handled by the Company. In sales volume, other than a 7.2% drop in gasoline on weaker demand and cutbacks in CS volume, the Company recorded gains in all major products, including a 36.2% increase in electricity sales volume.

Sales volume of core products

Fuel oil sales volume		FY3/17	FY3/18	% change
Gasoline	(thousand kl)	3,587	3,328	-7.2%
Kerosene	(thousand kl)	1,448	1,590	9.8%
Diesel	(thousand kl)	3,271	3,401	4.0%
Heavy oil	(thousand kl)	2,642	2,791	5.7%
Total	(thousand kl)	10,949	11,110	1.5%

Other sales volume		FY3/17	FY3/18	% change
Asphalt	(thousand kt)	354	376	6.4%
LP gas	(thousand kt)	597	619	3.7%
Electricity	GWh	3,255	4,432	36.2%
Steam	(thousand kt)	624	675	8.2%
Heat	TJ	1,258	1,303	3.6%

Source: Prepared by FISCO from the Company's results briefing materials

In earnings, profit from operating activities dropped 12.8% (¥2,525mn) YoY. While the Life Energy & Logistics Division delivered a ¥2,245mn increase, declines in the other three divisions undercut overall profit. Home-Life Division profit weakened primarily because of removal of income from LP gas business in Kanto, Kansai, and Chubu areas from consolidated scope accompanying the reorganization of LP gas business with Osaka Gas from 2H and inclusion under equity-method investment income instead. At the level of net profit attributable to the Company's shareholders, increases in the Life Energy & Logistics Division and Home-Life Division more than offset declines in the other two divisions and supported an overall gain.

We think attention should be given to final profit (net profit attributable to the Company's shareholders) as a more accurate indicator of the Company's profitability in light of the business structure reforms made in FY3/18.

Breakdown of FY3/18 results by business segment

(¥mn)

	FY3/17 full year	FY3/18		
		Full year	YoY change (%)	YoY
Home-Life Division	90,768	104,941	15.6%	14,173
Power & Utility Division	65,654	78,560	19.7%	12,906
Life Energy & Logistics Division	725,481	799,001	10.1%	73,520
Industrial Energy & Logistics Division	147,036	173,842	18.2%	26,806
Sales before adjustment	1,028,939	1,156,344	12.4%	127,405
Adjustment	-	-	-	-
Sales	1,028,939	1,156,344	12.4%	127,405
Home-Life Division	4,831	3,278	-32.1%	-1,553
Power & Utility Division	6,640	4,626	-30.3%	-2,014
Life Energy & Logistics Division	5,766	8,011	38.9%	2,245
Industrial Energy & Logistics Division	2,327	1,804	-22.5%	-523
Profit from operating activities before adjustment	19,564	17,719	-9.4%	-1,845
Adjustment	114	-566	-	-680
Profit from operating activities	19,678	17,153	-12.8%	-2,525
Home-Life Division	2,823	3,958	40.2%	1,135
Power & Utility Division	3,407	2,210	-35.1%	-1,197
Life Energy & Logistics Division	2,571	4,070	58.3%	1,499
Industrial Energy & Logistics Division	1,649	1,253	-24.0%	-396
Profit before taxes and adjustments	10,450	11,491	10.0%	1,041
Adjustment	-45	-466	-	-421
Net profit attributable to the Company's shareholders	10,405	11,025	6.00%	620

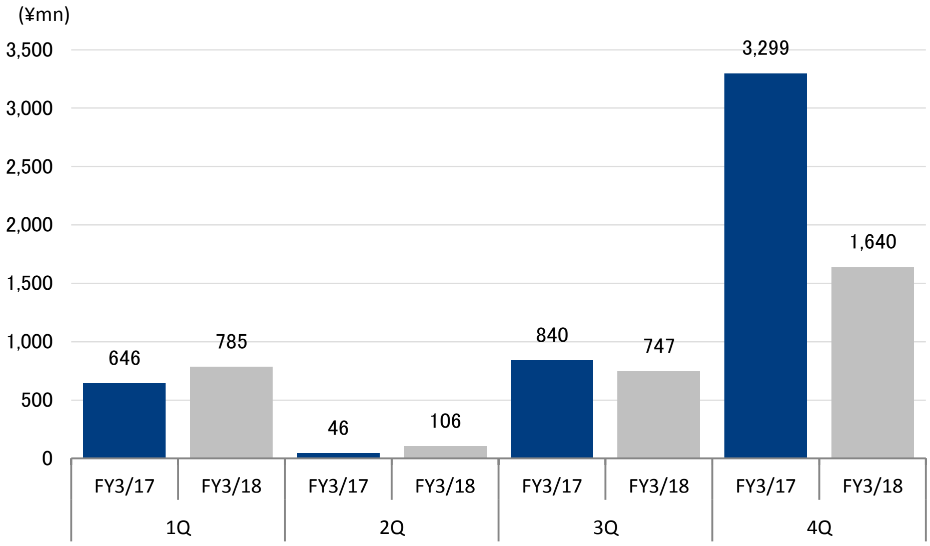
Source: Prepared by FISCO from the Company's financial results

Results trends by business segment

Carried out a major reorganization with Osaka Gas in LP gas business, secured an increase in final profit

1. Home-Life Division

Profit from operating activities in the Home-Life Division



Source: Prepared by FISCO from the Company's financial results and interviews

Sales and profits both increased in the Home Life Division. Sales were ¥104,941mn (+15.6%), and revenue was ¥93,592mn (+8.2% YoY), while profit from operating activities was ¥3,278mn (+32.1%) and net profit attributable to the Company's shareholders was ¥3,958mn (+40.2%) in FY3/18.

The biggest event in the Home-Life Division in FY3/18 was the reorganization of the LP gas business with Osaka Gas. In the three regions of Kanto, Kansai and Chubu, the two companies set up ENEARC Co., Ltd. as a 50-50 joint venture, and transferred both companies' LP gas sales companies to ENEARC on October 1, 2017. In other regions, ENEARC acquired all of the shares of the Osaka Gas Group's three LP gas sales companies (in Hokkaido and two prefectures in Shikoku), bringing these companies under the umbrella of the ENEARC group.

As a result of this reorganization of business, the revenue and profit of the LP gas business in the three regions of Kanto, Kansai, and Chubu were removed from consolidated scope and transferred to ENEARC, and incorporated into the equity in gains/losses of affiliates on ENEARC's income statement. Meanwhile, following the conversion of LP gas sales companies in Hokkaido and two prefectures in Shikoku into ENEARC's subsidiaries, ENEARC's number of direct-sales LP gas customer households increased from around 344,000 just before the reorganization (end of September 2017) to around 546,000 at the end of March 2018.

In the course of this business reorganization, one-time losses and gains other than ordinary profit from operating activities were also recorded. Roughly speaking, losses were incurred in advance in 1H FY3/18, appearing in the form of equity in losses of affiliates on ITOCHU ENEX's income statement. In 3Q, meanwhile, the Company booked business reorganization profits to cover its loss of control in the three sales companies (Kanto, Kansai, and Chubu). It thus rebounded from YoY decline in profit from operating activities to a 40.2% (¥1,135mn) rise in net profit attributable to the Company's shareholders. Income impact, including other SG&A expenses, corporate tax, and other items, worked out to ¥1,101mn.

Impact of the reorganization of the LP gas business on profit and loss

Item	Impact (¥mn)
SG&A expenses (increase)	-302
Equity in gains (losses) of affiliates	-848
Gain on business reorganization and others	2,326
Income tax expenses	-75
Total impact on profit and loss	1,101

Source: Prepared by FISCO from the Company's financial results

Conditions were generally upbeat in the LP gas business. Sales volume rose 3.7% YoY, as mentioned earlier. In pricing, the contract price (CP) that heavily affects LP gas business income climbed throughout the fiscal year and helped in lifting the LP gas selling price. CP adjustment at the fiscal period-end, however, ultimately left the FY3/18 price at $480/ton, unchanged from a year earlier. This means that profit impact for the Company's LP gas inventories was very minor.

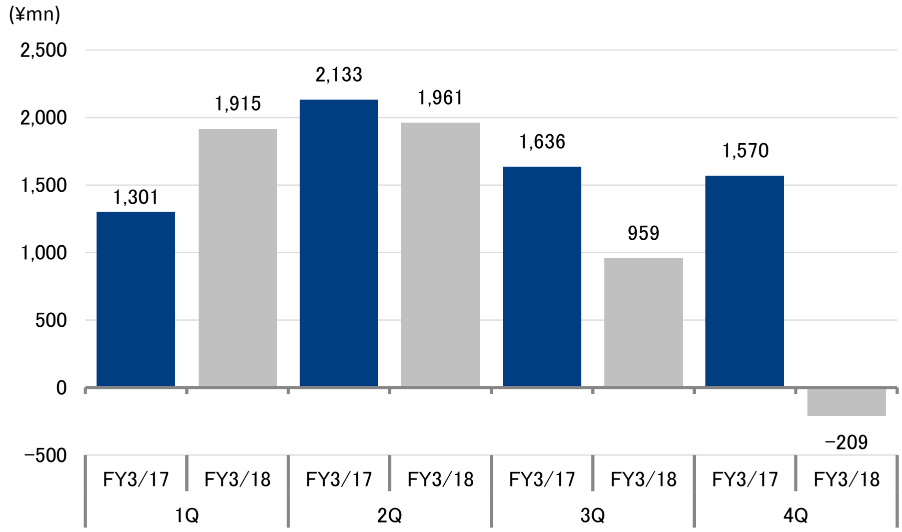
In the Home-Life Division, the Company is promoting bundled sales of LP gas and electricity as a sales company for the Power & Utility Division. It added 12,000 contracts in FY3/18 and had 54,000 contracts at period-end. The Division's electricity sales business realized a profit during FY3/18 and aims to steadily increase customer volume.

In overseas activity, the industrial gas sales business in Indonesia raised customer volume, mainly for Japanese companies and LP gas sales business in the Philippines expanded income with support from healthy consumption in the country.

Healthy gains in power and heat sales volumes; profit lower on backlash from non-recurrence of equipment sales profit in the previous fiscal year but steadily improving on a real basis

2. Power & Utility Division

Profit/loss from operating activities in the Power & Utility Division



Source: Prepared by FISCO from the Company's financial results and interviews

The Power & Utility Division posted lower profits on higher sales in FY3/18. Sales were ¥78,560mn (+19.7% YoY), and revenue increased 18.6% to ¥74,541mn, while profit from operating activities decreased 30.3% to ¥4,626mn and net profit attributable to the Company's shareholders was ¥2,210mn (-35.1%).

We believe power business profit slipped on higher sales versus the previous fiscal year. The Company began operation of the Sendai Power Station, a new thermal power plant, in October 2017 in power generation. On the sales front, it reinforced capabilities through expansion of balancing group (BG) members (Bay Communications Inc., Miyazaki Cable TV Network) and establishment of ENEX LIFE SERVICE Co., Ltd., which oversees retail power sales through agents. These efforts contributed to a hefty 36.2% YoY rise in electricity sales volume to 4,432GWh. We believe power business sales increased YoY thanks to the increase in electricity sales volume.

In earnings, meanwhile, despite the profit boost from higher sales volume, the business confronted setbacks from 1) increased costs due to sustained high coal prices (power generation), 2) a price upswing in the wholesale power market related to harsh winter conditions (sales), 3) tougher competition in the retail market particularly for high-voltage, large-volume customers (sales), and 4) backlash decline from non-recurrence of profit from selling wind power facilities (power generation). We think power business profit ultimately weakened on inability to fully overcome removal of facility sales profits (item 4) with improvements.

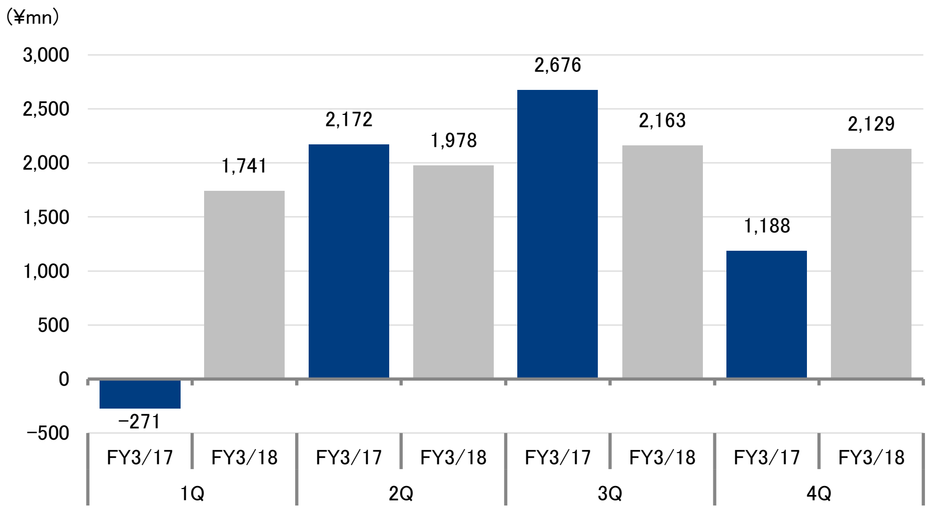
We believe heat supply business sales increased YoY in FY3/18 thanks to the launch of GINZA SIX, a major retail facility, in April 2017 at the start of the fiscal year and beginning of heat supply to this facility. In earnings, however, higher depreciation costs from capacity-increasing investments for GINZA SIX and renewals of other facilities pushed profit lower (YoY).

Notable advances in FY3/18 were beginning operation of the Sendai Power Station in power generation, expansion of balancing group members and establishment of agent sales functions in power sales mentioned above, as well as formation of Reliance Energy Okinawa Co., Ltd. in heat supply. The latter is a joint venture among ITOCHU ENEX Group, Okinawa Electric Power Company, Incorporated <9511>, and Osaka Gas. Group subsidiary TTS (Tokyo Toshi Service) owns 33.4% (Okinawa Electric has a majority position with its 51.6% stake). Reliance Energy Okinawa operates an energy service provider (ESP business that covers the entire scope from energy equipment design to operation and proposes ideal solutions for energy utilization. While profit fell sharply YoY in FY3/18, we think the Company is making steady progress in its growth strategy for this segment on a real basis.

Steadily promoting structural reforms, such as retreat from unprofitable CS, and posted significantly higher profits amid improved business conditions

3. Life Energy & Logistics Division

Profit/loss from operating activities in the Life Energy & Logistics Division



Source: Prepared by FISCO from the Company's financial results and interviews

The Life Energy & Logistics Division finished FY3/18 with higher sales and significant growth in profits. Sales were ¥799,001mn (+10.1% YoY), and revenue rose 1.8% YoY to ¥488,399mn, profit from operating activities rose 38.9% to ¥8,011mn, and net profit attributable to the Company's shareholders was ¥4,070mn (+58.3%).

In sales, gasoline sales volume dropped 7.2% YoY, but diesel oil and kerosene volumes increased. Sales prices were healthy thanks to higher crude-oil prices and optimization of supply-demand balance for the industry through wholesale reorganization. These trends facilitated stronger sales (YoY). Decline in gasoline sales volume reflected structurally weaker demand due to inroads by hybrid cars and electric vehicles (EVs) and fewer CS (Car-Stations; internal name for gas stations), just as in previous years.

In earnings, meanwhile, profit from operating activities rose sharply with a gain of almost 40% YoY on structural improvement from closing unprofitable CS and other actions, a higher margin related to healthy gasoline retail prices, and increased profit from stronger diesel oil sales.

The Company eliminated 76 unprofitable CS (net decline) during the period and had 1,812 CS at the end of FY3/18. In CS operations, it deployed new POS facilities and moved forward with its decision to implement a system of shared points. It completed rebranding of the rental car business, a CS-related activity, from "Itsumo Rental Car" to "Car Life Stadium Rental Car."

Sales volume fell significantly in the dealer business run by Nissan Osaka Sales Co., Ltd. in 3Q because of the improper final-vehicle inspections incident in September 2017 and backlash from the previous year's new vehicle effect. However, sales volume still rose for the full year with help from the release of new models of popular vehicles in 4Q. Earnings faced decline in sales prices and higher costs accompanying store renovations. Nissan Osaka Sales therefore ended up with weaker profits on an increase in sales.

Business performance trends of Nissan Osaka Sales

FY3/18 results		
	Results (¥bn)	YoY change (¥bn)
Sales	1,053	42
Profit from operating activities	21	-3
Net profit*	6	-1

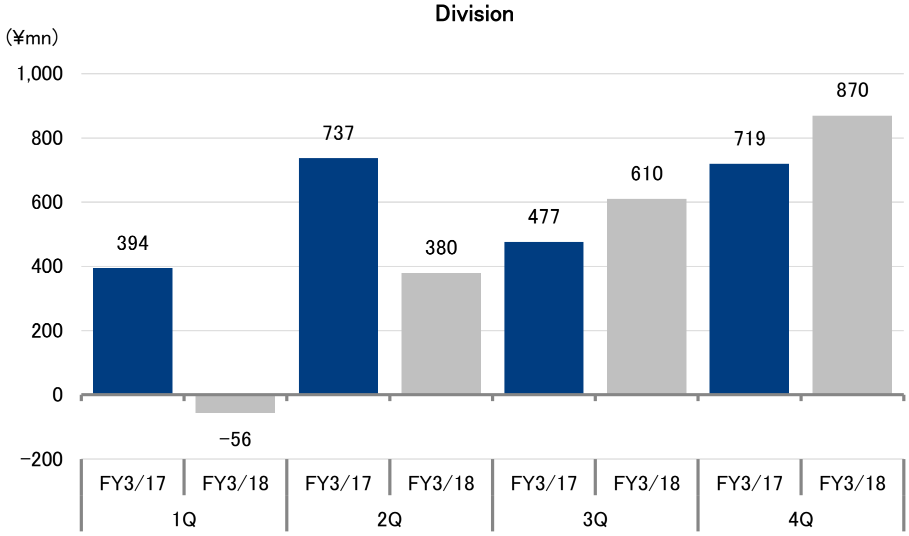
Vehicle sales volume		
	Results (thousands of units)	YoY change (thousands of units)
New cars	29	2
Pre-owned cars	25	1

* Net profit represents the share of net profit attributable to ITOCHU ENEX
Source: Prepared by FISCO from the Company's results briefing materials

Generally upbeat business conditions, profit decreased YoY with decline in petroleum product trade

4. Industrial Energy & Logistics Division

Profit/loss from operating activities in the Industrial Energy & Logistics Division



Source: Prepared by FISCO from the Company's financial results and interviews

The Industrial Energy & Logistics Division posted a decrease in profits, despite an increase in revenue, in FY3/18. Sales were ¥173,842mn (+18.2%), and revenue rose 33.3% YoY to ¥88,235mn, while profit from operating activities decreased 22.5% to ¥1,804mn, and net profit attributable to the Company's shareholders was ¥1,253mn (-24.0%).

Sales climbed YoY because of a boost in product prices from higher crude-oil prices and higher sales volumes for asphalt and other major products. Profit, however, declined on fewer transaction opportunities in the petroleum product trading business. Petroleum product trades take place in order to erase the market supply-demand gap. With elimination of the supply-demand gap in Japan's petroleum products market through wholesaler reorganization, prices held stable and trading opportunities sharply declined.

The Industrial Energy & Logistics Division mainly has four businesses – the above-mentioned petroleum product trading, asphalt business, ship fuel sales business, and terminal business. Asphalt business sales volume was healthy with a 6.4% YoY increase. While the ship fuel sales business struggled due to changes in the domestic market environment, the Company built a new supply ship in Oita Port and thereby established operations with eight ships nationwide.

In new business areas, the Company continued to pursue coal ash recycling and commercialization of the slop and recycled oil business. It jointly invested in Kano FA Co., Ltd. for the fly (coal) ash recycling business and has ramped up operations.

Progress in the medium-term business plan and future initiatives

Aims to stably generate ¥10bn in final profit and solidify the foundation to proceed to the next stage during the two-year medium-term business plan

1. Overview of the medium-term business plan and its quantitative targets

The Company is implementing its two-year medium-term business plan, "Moving 2018" covering FY3/18 and FY3/19. The concept behind the new plan is defined as "two years to lay the management base for the next stage of the Company's development." With this concept, the Company is pursuing 1) reforming the revenue base and 2) revamping the organizational base.

In Moving 2018, the Company initially set second (final) year goals of ¥18.5bn in profit from operating activities, ¥10.8bn in net profit attributable to shareholders, and at least 9.0% ROE in FY3/19. It also called for ¥45bn in growth investments over the plan's two years. In these points, the Company places particularly strong emphasis on having net profit attributable to the Company's shareholders take hold in the ¥10bn range. While it wants to advance to the next stage of the ¥20bn range over the longer term, this is unlikely to happen all at once, and the Company thus positions Moving 2018 as the period for securing the corporate wherewithal to stably book ¥10bn.

As explained earlier, profits beat period-start forecasts in all items in FY3/18 from profit from operating activities. In light of these results, the Company changed its FY3/19 outlook from the medium-term plan's initial stance with upward revisions from ¥18.5bn to ¥18.7bn in profit from operating activities and ¥10.8bn to ¥11.3bn in net profit attributable to the Company's shareholders.

Additionally, the Company raised its ROE goal from 9.1% to 9.5% and dividend payout ratio in shareholder return from "at least 30%" to "at least 40%" and increased the investment budget as explained later.

Quantitative targets in "Moving 2018"

	Moving 2018			
	FY3/18		FY3/19 initial forecast	FY3/19 revised forecast
	Forecast	Results		
Profit from operating activities	¥16.5bn	¥17.2bn	¥18.5bn	¥18.7bn
Net profit*	¥10.4bn	¥11.0bn	¥10.8bn	¥11.3bn
ROE	9.3%	9.8%	9.1%	9.5%
Dividend payout ratio	Over 30%	Over 40%	Over 30%	Over 40%
Cash flows from operating activities	¥22.0bn	¥24.2bn	¥24.0bn	-
Investment plan (single year)	¥19.7bn	¥24.4bn	¥25.3bn	¥32.2bn
Investment plan (two-year total)	¥45.0bn (over two years)		¥56.6bn	

* "Net profit" refers to net profit attributable to the Company's shareholders.
Source: Prepared by FISCO from the Company's results briefing materials

Making steady progress in reforming the revenue base and revamping the organizational base

2. FY3/18 results

(1) Progress in reforming the revenue base

Reforming the revenue base involves 1) asset optimization, 2) improvement in profitability, and 3) development of the customer base.

Exiting unprofitable CS locations is a concrete example of asset optimization. The Company had a net decline of 76 sites in FY3/18 as explained above, and its volume has dropped by 370 sites from 2,182 sites at the end of FY3/13, the recent peak. It implemented a merger of Home-Life Tohoku and Tohoku Tank Shokai from the standpoint of "utilizing local strengths." While it sold some power generation facilities as part of asset optimization in FY3/17, the Company did not take such actions in FY3/18.

The Company's launch of operations at Sendai Power Station, a new-type thermal power plant, as planned in October 2017 contributed to better profitability in the power business. This initiative also helped in optimizing assets when viewed together with the sale of wind power facilities in FY3/17. In the LP gas business, the Company acquired LP gas retail operations in Hokkaido, Kochi, and Ehime from the Osaka Gas Group as part of reorganization with Osaka Gas. These additions significantly raised LP gas direct-sale customer volume from 344,000 sites just before the purchase (at end-September 2017) to 546,000 sites (at end-March 2018).

To develop the customer base, besides its expansion of LP gas direct-sale customer volume as mentioned above, the Company also strengthened its position in the Power & Utility Division. Specifically, it added Bay Communications and Miyazaki Cable TV Network to the balancing group that handles retail electricity sales, established ENEX LIFE SERVICE, and built a retail electricity platform based on an agent model. Furthermore, it entered the energy service provider business through formation of Reliance Energy Okinawa.

Progress in rebuilding the revenue base

Reforming revenue base		FY3/18 achievement
Asset optimization	Accelerate asset replacement in pursuit of profitability and growth potential	Asset optimization • Exiting unprofitable CS locations (79 sites in FY3/18 and a total of 164 sites over two years) • Integration of HL Tohoku and Tohoku Tank Shokai Increase earnings potential • Launch of Sendai Power Station Operations • Acquired three retail companies from Nissho Petroleum Gas Corporation (one in Hokkaido and two in Shikoku) • Established Kano FA (fly (coal) ash recycling business) Customer base reform • Reorganizing the HL business (establishment of ENEARC Co., Ltd.) (lifted customer volume from 345,000 customers to 546,000 customers) • Expansion of the electricity balancing group (Bay Communications, Miyazaki CATV) • Formation of Reliance Energy Okinawa (promotion of ESP business) • Investment in Euglena Co., Ltd.
Increase earnings potential	Raising income efficiency with the spending ratio as an indicator (79.9% spending ratio in FY3/17)	
Customer base development	Horizontal pursuit of power business and expansion of the customer base with emphasis on retail prospects	

Source: The Company's results briefing materials

(2) Progress in revamping the organizational base

The Company is engaged in various initiatives to revamp the organizational base. In addition to establishing a group management base, the Company is also cultivating personnel and promoting working style reforms.

The most significant point of progress in establishing a group management base is ITOCHU ENEX's reorganization on April 1, 2018. According to the Company, the reorganization is being undertaken for the purpose of "business development using the group's own network in each region and speeding up decision-making processes in the power and mobility businesses in response to the shift to electrical energy."

Specifically, it integrated the Life Energy & Logistics Division and Industrial Energy & Logistics Division to form the Life & Industrial Energy Division, upgraded and renamed the Automobile Business Office as the Mobility Life Department, and transferred the business of Nissan Osaka Sales in the Life Energy & Logistics Division to the Mobility Life Department.

These organizational changes aim to 1) make strategic approaches to the customer base in regional areas, 2) further strengthen the electricity pipeline, and 3) pursue business with new content (mainly automotive).

In people, it started an overseas training program as part of enhancing its personnel education program. In working style reforms, it adopted the ENEX EARLY BIRD slogan, opened an ENEX Nursery (daycare) and introduced casual Fridays.

Progress in reforming organizational base

Reforming organizational base		FY3/18 achievement
Strengthening organizational capacity	Development of a group management base	Developing the organizational base • Revision of investment standards • Launch of a digital task force • Headquarters move resolution (moving to the Kasumigaseki Building) Personnel investments and working style reforms • Opening the ENEX Nursery (daycare) (work environment reform) • Introduction of casual days • Began an overseas training program (overseas personnel cultivation)
Autonomous human resource development	Cultivation of independent human resources with a clear mission	
ENEX EARLY BIRD	Promotion of a working style that realizes high performance in a short period	

Source: The Company's results briefing materials

Raising the two-year investment budget in Moving 2018 to ¥56.6bn, steady advances with investments in business structural reforms, power source development, and other areas

3. Investment plan and progress

The Company initially planned to invest ¥45bn in the two years covered by the Moving 2018 plan. It used ¥24.4bn in FY3/18, the first fiscal year, versus a starting target of ¥19.2bn, making very healthy progress. Given this result, it raised the two-year investment budget to ¥56.6bn and is aiming to invest ¥32.2bn in FY3/19.

Investment results and plan

(¥bn)

Division	FY3/18		FY3/19	
	Investment amount	Main points	Investment amount	Main points
Home-Life	72	Acquired shares of LP gas sales companies in Hokkaido and 2 prefectures in Shikoku	40	Purchase of business rights, M&A, and facility renewals
Power & Utility	127	Ramped up capacity for heat supply to GINZA SIX and upgraded existing facilities, and power source development	214	Power source development, TTS facility renewal
Life Energy & Logistics	25	Renovated the dealerships of Nissan Osaka Sales	-	
Industrial Energy & Logistics	14	Built a new marine fuel supply ship	-	
Life & Industrial Energy Division	-		35	Asphalt tank and CS system renewals
Mobility Life Department	-		25	Nissan Osaka facility renewal
Others	7	Core system improvements, etc.	9	Core system improvements, etc.
Total	244		322	

Source: Prepared by FISCO from the Company's results briefing materials, interviews, etc.

Looking at FY3/18 results, Home-Life Division investments mainly went toward the purchase of shares in LP gas sales companies in Hokkaido and Shikoku from Nissho Petroleum Gas, a member of the Osaka Gas Group, while Power & Utility Division investments were divided between about half in new heat supply facilities for GINZA SIX and existing facility renewals at TTS and the other half in power source development.

In FY3/19, the Company’s investment plans target business right purchases and M&A deals for ongoing pursuit of reorganization in the Home-Life Division, power source development and heat supply facility renewal in the Power & Utility Division, just as in the previous fiscal year, asphalt tank and CS system renewal in the Life and Industrial Energy Division, and Nissan Osaka facility renewal in the Mobility Life Department.

FY3/19 initiatives

Primarily reinforcement of LP gas business, though also efforts to expand peripheral and overseas businesses

1. Home-Life Division

In the Home-Life Division, the Company intends to primarily reinforce the mainstay LP gas business, but also pursue growth strategies in peripheral business and expand overseas business.

In the LP gas business, while last year's reorganization with Osaka Gas removed LP gas operations in Kanto, Kansai, and Chubu areas from the consolidated scope, the Company significantly increased direct-sales customer volume to 546,000 customers with acquisitions of three companies in Hokkaido, Ehime, and Kochi. It intends to expand the customer base via these operations, including building customer databases and improving precision, making optimal approaches to individual customers based on these data resources, and reviewing ideal products and strengthening bundled sales of electricity, kerosene, and other items. In electricity sales, which ramped up in FY3/18, the Company aims to add 36,000 contracts during FY3/19 and thereby reach 90,000 contracts at the end of the fiscal year.

In peripheral business, the Company wants to expand the general high-pressure gas business (through alliances with other companies, M&A, and other activities), stabilize income in the high-pressure gas container pressure test business, and develop new B-to-B peripheral businesses.

In overseas business, the Company intends to diversify the sales scheme and create demand and expand business via utilization of Japanese knowhow in the industrial gas sales business in Indonesia and LP gas sales business in the Philippines.

Implementing a two-front strategy in B-to-B-to-C and B-to-B businesses

2. Life & Industrial Energy Division

The Life & Industrial Energy Division is generally built around petroleum, albeit with a broad product line-up that extends from gasoline and other items close to the upstream to operations that interact with final consumers. Based on this presence, the Company intends to pursue new opportunities that leverage the unique aspects of its B-to-B-to-C and B-to-B businesses.

The Car-Life (CL) chain business is the core B-to-B-to-C business with a foundation of about 1,800 CS sites. While the Company will continue to exit money-losing CS locations, it wants to pursue strengthening of individual CS profitability through clarification of a new CS image. We think the new CS image envisions CS that generate profits from a variety of services and products, such as car-related business and electricity and do not rely just on gasoline sales. This is something that the Company has been pursuing for some time. To achieve this goal, the Company is deploying new POS and shared point cards and ramping up new marketing that utilizes these capabilities.

B-to-B businesses include asphalt, ship fuel, industrial energy, and terminals. The Company is already involved in these areas with a solid presence, and they are likely to remain as primary operations. Additionally, the Company is accelerating new business initiatives (slop and recycled oil, PCB processing arrangement, and others) following fly (coal) ash recycling.

Seeks to continually expand retail power volume by increasing low-voltage, small customers in retail electricity business

3. Power & Utility Division

In the power business, the Company calls for "strengthening the electricity pipeline of development, procurement, supply/demand, and sales." Power source development covers last year's launch of operations at Sendai Power Station and reviews of new power plants using biomass and other renewable energy in the current medium-term business plan's capital investment scheme. For sales, the Company intends to pursue improvements that factor in changes in the industry environment.

Additions of high-voltage, large-scale customers contributed substantially to the Company's expansion of its power business. However, competition has heated up in this segment due to initiatives by existing power companies (such as TEPCO). Given these conditions, the Company aims to continue increasing retail electricity volume and expanding income through renewed emphasis on low-voltage, small-scale buyers.

The Company has already completed platforms with its own balancing group (BG) and agent sales managed by ENEX LIFE SERVICE and intends to recruit customers by combining its platforms with an approach of "collaboration with other industries." A specific example is Nissan Osaka's "car and electricity collaboration" initiative.

For the heat supply business, the Company started supplying GINZA SIX and conducted large-scale facility renewal investments during FY3/18. It plans to ramp up its ESP business at Reliance Energy Okinawa, which it established at the end of last year, in FY3/19.

Targeting growth with auto-centric, social and infrastructure-centric, and environment-centric businesses

4. Mobility Life Department

Mobility business refers to activities at Nissan Osaka Sales. The Company's slogan in the Mobility Life business for FY3/19 is "creation of content that links the environment, society, and living and fostering an attractive social base in regional areas." The first half of the slogan incorporates the reason for the decision to separate Nissan Osaka as an independent business unit. The Company views "the automobile as a mirror that reflects changes in society" via its concentration of new technologies, fashions, and trends. By having an independent business unit, the Company enhanced its flexibility to convert these opportunities into businesses in a timely manner.

Given this background, the mobility business targets growth with auto-centric, social and infrastructure-centric, and environment-centric businesses. The auto-centric business covers the existing Nissan Osaka business model of growth mainly based on increasing sales volume and development of new auto-related businesses using this customer base.

The social and infrastructure-centric business involves review of new social and infrastructure businesses that cater to customer bases of ENEX LIFE SERVICE and other group entities and promotion of businesses that create new content and contribute to building regional infrastructure (farming IoT, HEMS, and others).

The environment-centric business refers to preparation of a biofuel plant in the US and supply of raw material (waste cooking oil) to Euglena's <2931> biojet fuel verification plant.

Business outlook

Aiming for all-time high final profit for a fourth straight year with profit gain in the Power & Utility Division as the main driver

The Company forecasts sales and profits rising, with ¥1,250,000mn in sales (up 8.1% YoY), ¥18,700mn in profit from operating activities (up 9.0%), ¥18,500mn in profit before tax (up 3.5%), and ¥11,300mn in net profit attributable to the Company's shareholders (up 2.5%) in FY3/19.

Overview of the forecast for FY3/19

(¥mn)

	FY3/17 results	FY3/18		FY3/19		
		Results	YoY(%)	Forecast	YoY(%)	Change
Sales	1,028,939	1,156,344	12.4%	1,250,000	8.1%	93,656
Revenue	695,060	744,767	7.2%	-	-	-
Gross profit	93,604	88,822	-5.1%	-	-	-
SG&A expenses	74,697	70,931	-5.0%	-	-	-
Profit from operating activities	19,678	17,153	-12.8%	18,700	9.0%	1,547
Profit before tax	19,344	19,169	-0.9%	18,500	-3.5%	-669
Net profit attributable to the Company's shareholders	10,405	11,025	6.0%	11,300	2.5%	275

Source: Prepared by FISCO from the Company's financial results

Profit before tax is likely to drop YoY because of non-recurrence of business reorganization profit related to reorganization of the Home-Life Division in FY3/18. We think net profit attributable to the Company's shareholders is the most accurate indicator of the Company's profitability due to various structural reforms implemented in recent years. If the Company realizes the period-start target in FY3/19, it would post an increase to an all-time high for a fourth straight year.

The outlook for each business segment is described below.

Forecast by segment

(¥bn)

	FY3/18 full year	FY3/19		
		Full year (forecast)	YoY	Change
Home-Life Division	1,049	1,150	9.6%	101
Life & Industrial Energy Division	8,675	9,444	8.9%	769
Power & Utility Division	786	848	7.9%	62
Mobility Life Department	1,053	989	-6.1%	-64
Sales before adjustment	11,563	12,431	7.5%	868
Adjustment	-	-	-	-
Sales	11,563	12,431	7.5%	868
Home-Life Division	33	37	12.1%	4
Life & Industrial Energy Division	78	78	-0.3%	0
Power & Utility Division	46	64	39.1%	17
Mobility Life Department	20	9	-55.9%	-11
Profit from operating activities before adjustment	177	188	6.2%	11
Adjustment	-5	-1	-	4
Profit from operating activities	172	187	8.7%	15
Home-Life Division	40	30	-25.0%	-10
Life & Industrial Energy Division	51	53	3.8%	2
Power & Utility Division	22	28	27.3%	6
Mobility Life Department	2	1	-69.2%	-1
Profit before tax before adjustment	115	112	-2.6%	-3
Adjustment	-5	1	-	6
Net profit attributable to the Company's shareholders	110	113	2.7%	3

Source: Prepared by FISCO from the Company's results briefing materials

(1) Home-Life Division

Home-Life Division targets are ¥115,000mn in sales (+9.6% YoY), ¥3,700mn in profit from operating activities (+12.1%), and ¥3,000mn in net profit attributable to the Company's shareholders (-25.0%).

While business reorganization conducted in FY3/18 moved income from LP gas operations in Kanto, Kansai, and Chubu areas to equity-method income, the Company projects higher sales and profits on income additions from LP gas sales companies in Hokkaido and Shikoku and increase in electricity customers (it expects to recruit an extra 36,000 contracts in FY3/19 and raise total volume to 90,000 contracts at end-FY3/19). Anticipated decline in net profit attributable to the Company's shareholders stems from removal of a special factor in the previous fiscal year (business reorganization profit). The outlook assumes a flat average contract price (YoY) and does not factor in profit changes from higher sales and inventory impact due to increase in the contract price.

(2) Life & Industrial Energy Division

Life and Industrial Energy Division targets are ¥944,400mn in sales (+8.9%), ¥7,800mn in profit from operating activities (-0.3%), and ¥5,300mn in net profit attributable to the Company's shareholders (+3.8%). The outlook expects flat profit from operating activities on higher sales.

Despite likely continuation of a decline in gasoline sales, the Company projects higher segment sales driven by price increases resulting from a rise in the crude-oil price and expansion of B-to-B business (particularly asphalt). Petroleum product trading is expected to remain at the same level as the previous year. The Company envisions profit on par with the previous year, even considering some risk factors, such as shrinkage of the gasoline margin, led by increased sales and cost savings from closure of money-losing CS locations.

(3) Power & Utility Division

Power & Utility Division targets are ¥84,800mn in sales (+7.9% YoY), ¥6,400mn in profit from operating activities (+39.1%), and ¥2,800mn in net profit attributable to the Company's shareholders (+27.3%). This outlook forecasts higher sales and profits.

The main sales driver is an anticipated rise in electricity volume (roughly 13% increase in retail electricity sales volume from 2,496GWh in FY3/18 to 2,800GWh in FY3/19). Profit, meanwhile, is expected to experience a steep increase primarily on an improved margin from changes in customer mix alongside double-digit growth in retail electricity sales volume. As explained earlier, the Company has changed its sales strategy from auction-based high-voltage, large deals to increasing sales to low-voltage, small customers. Change in product mix is likely to contribute to stronger profit. Additionally, we expect a favorable impact on earnings from exhaustion of investments in large-scale facility renewals in the heat supply business.

(4) Mobility Life Department

Mobility Life Department targets are ¥98,900mn in sales (-6.1% YoY), ¥900mn in profit from operating activities (-55.9%), and ¥100mn in net profit attributable to the Company's shareholders (-69.2%). The outlook expects weaker sales and profits.

The Company anticipates lower sales, despite the prospect of flat sales volume (YoY), because of anticipated decline in sales prices. This stance appears to factor in larger discounts in the absence of model changes for main vehicle models in FY3/19. Main profit setbacks are a narrower margin due to lower sales prices and non-recurrence of store sale profits booked in FY3/18.

Consolidated income statements

(¥mn)

	FY3/15	FY3/16	FY3/17	FY3/18	FY3/19 forecast
Sales	1,373,393	1,071,629	1,028,939	1,156,344	1,250,000
YoY	-8.8%	-22.0%	-4.0%	12.4%	8.1%
Revenue	936,841	723,645	695,060	744,767	-
YoY	-3.0%	-22.8%	-4.0%	7.2%	-
Gross profit	85,720	89,562	93,604	88,822	-
YoY	19.7%	4.5%	4.5%	-5.1%	-
% of sales	6.2%	8.4%	9.1%		-
SG&A expenses	71,184	73,226	74,697	70,931	-
YoY	23.0%	2.9%	2.0%	-5.0%	-
% of sales	5.2%	6.8%	7.3%	6.1%	-
Loss from tangible assets, intangible assets and goodwill	-1,825	-593	-982	-1,544	-
Other – net	389	641	1,753	806	-
Total other expenses	-72,620	-73,178	-73,926	-71,669	-
Profit from operating activities	13,100	16,384	19,678	17,153	18,700
YoY	10.3%	25.1%	20.1%	-12.8%	9.0%
Profit before tax	12,155	15,004	19,344	19,169	18,500
YoY	-12.2%	23.4%	28.9%	-0.9%	-3.5%
Net profit attributable to the Company's shareholders	5,503	7,469	10,405	11,025	11,300
YoY	-22.7%	35.7%	39.3%	6.0%	2.5%
EPS (¥)	48.71	66.10	92.09	97.63	100.11
Dividend (¥)	22	24	32	40	40
Book-value per share (¥)	862.30	889.70	960.37	1,028.57	

Source: Prepared by FISCO from the Company's financial results

Consolidated balance sheets

(¥mn)

	IFRS				
	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Current assets	188,193	157,708	137,865	178,127	212,769
Cash and cash deposits	14,251	16,184	20,824	22,727	22,573
Trade receivables	140,289	98,449	71,968	94,759	119,541
Inventories	18,655	27,794	25,160	27,155	28,380
Other	14,998	15,281	19,913	33,486	42,275
Non-current assets	132,531	171,351	166,188	166,476	169,852
Investments accounted for by the equity method	5,927	10,551	8,786	11,749	26,145
Other investments	7,349	8,924	8,029	7,461	3,406
Property, plant and equipment	66,988	88,836	88,311	87,588	85,326
Intangible assets	10,280	23,474	24,329	23,638	20,798
Other	41,987	39,566	36,733	36,040	34,177
Total assets	320,724	329,059	304,053	344,603	382,621
Current liabilities	158,336	149,443	111,997	143,751	174,929
Bonds and borrowings	11,499	14,208	5,299	9,318	12,432
Trade payables	125,655	104,564	80,745	101,902	127,445
Other	21,182	30,671	25,953	32,531	35,052
Non-current liabilities	58,268	66,669	74,894	73,375	70,626
Bonds and borrowings	27,099	26,746	32,366	31,702	30,273
Other	31,169	39,923	42,528	41,673	40,353
Equity	94,651	97,432	100,526	108,511	116,104
Common stock	19,878	19,878	19,878	19,878	19,878
Capital surplus	18,737	18,743	18,740	18,740	18,892
Retained earnings	59,884	62,223	66,024	73,300	80,352
Other components of equity	-2,098	-1,661	-2,364	-1,655	-1,145
Treasury stock	-1,750	-1,751	-1,752	-1,752	-1,873
Non-controlling interests	9,469	15,515	16,636	18,966	20,962
Total equity	104,120	112,947	117,162	127,477	137,066
Total liabilities and equity	320,724	329,059	304,053	344,603	382,621

Source: Prepared by FISCO from the Company's financial results

Consolidated cash flow statements

(¥mn)

	IFRS				
	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Cash flows from operating activities	17,530	34,336	30,322	17,831	24,239
Cash flows from investing activities	-12,556	-20,410	-16,673	-14,712	-18,458
Cash flows from financing activities	-8,859	-12,115	-9,059	-1,195	-5,850
Net increase/decrease in cash and cash equivalents	-3,885	1,811	4,590	1,924	-69
Cash and cash equivalents at the beginning of the period	18,062	14,251	16,184	20,824	22,727
Effect of exchange rate changes on cash and cash equivalents	74	122	50	-21	-85
Cash and cash equivalents at the end of the period	14,251	16,184	20,824	22,727	22,573

Source: Prepared by FISCO from the Company's financial results

Shareholder returns

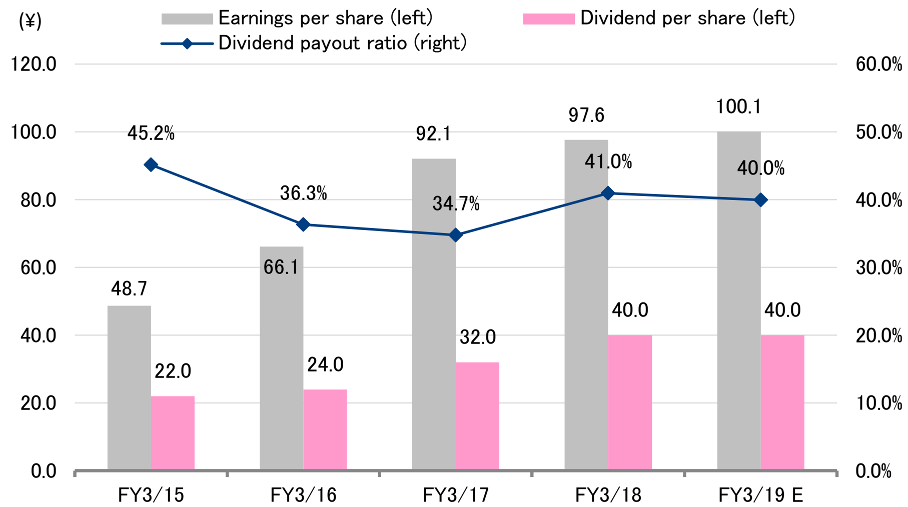
Raised the dividend payout target (used to set the dividend) to 40%, lifted the FY3/18 dividend by ¥8 YoY to ¥40

The Company mainly compensates shareholders through dividends. It raised the dividend by ¥8 YoY to ¥40 in FY3/18 (¥16 interim dividend, ¥24 period-end dividend). It had previously intended to pay ¥32 (¥16 interim, ¥16 period-end), on par with the previous year.

The direct catalyst of the dividend-hike decision was an increase of the dividend payout guideline from 30% to 40% in light of healthy income progress in FY3/18 that put the Company ahead of pace toward realization of quantitative goals in the medium-term business plan. The FY3/18 payout ratio was 41.0%.

The Company expects to pay a ¥40 dividend (¥20 interim, ¥20 period-end), which is unchanged YoY, in FY3/19 using the revised standard. Payout based on projected earnings per share is 40.0%.

Earnings and dividend per share and dividend payout ratio



Source: Prepared by FISCO from the Company's financial results

Information security

Acquired certification based on international standards for information security, in addition to setting strict in-house rules

ITOCHU ENEX has defined its own personal information protection policy for protecting the personal information of customers. The Company has been working to put an organizational framework in place, implement and maintain information security measures and pursue continuous improvements. The Company also fosters awareness among directors, employees, and other relevant personnel, along with actively promoting personal information protection.

In the electricity business, the electricity supply-demand group handles personal information as part of electricity sales. This group obtained ISO/IEC27001/JIS Q 27001 (known as ISMS*) approval, the international standard for information security management systems, in October 2016, thereby ensuring secure information handling.

* ISMS (Information Security Management System) is a comprehensive information security management system that protects information assets from various threats and mitigates risks. It has international and domestic standards (ISO/IEC27001/JIS Q 27001). Satisfying these criteria and acquiring certification is usually referred to as having "acquired ISMS."

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