

Summary of Q&A session of ESG meeting for institutional investors and analysts

Time and date: 15:30 to 16:50, Thursday, October 15, 2020

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Q: You touched on Sumitomo Dainippon Pharma in your governance explanation. What is your take on parent-subsiary dual listings amid an acceleration of moves against such dual listings? Please give us your overarching view on parent-subsiary dual listings including, listed subsidiaries and affiliated companies other than Sumitomo Dainippon Pharma.

A: Dissolving the parent-subsiary dual listing with Sumitomo Dainippon Pharma surely remains as an option, but, from a realistic standpoint, it is not a high priority given the current capital structure of our Company. Rather, it is important for us to consider how we can make the most of the autonomy of our listed subsidiaries and affiliated companies, or how to ensure the respect for the minority shareholders' rights under effective governance. As long as this autonomy and the minority shareholders' rights are given, making it a wholly owned subsidiary or listing it does not matter so much. More important is how to generate synergies, since they are among our group companies as affiliated companies, including Sumitomo Dainippon Pharma. Talking about the business of drug discovery of Sumitomo Dainippon Pharma, its synergy with Sumitomo Chemical is rather limited. However, pharmaceutical companies including Sumitomo Dainippon Pharm, intend to broaden their business area to health care, such as preventive and prognostic diagnosis. In that respect, I expect the creation of more inter-business synergies, such as technology and market synergies Sumitomo Chemical.

We also have Koei Chemical, Taoka Chemical, and Tanaka Chemical as subsidiaries listed in Japan. I intend to ramp up our efforts to create more synergy from a business perspective and respect minority shareholders from an institutional perspective.

Q: I view that Sumika Sustainable Solutions (Triple S) are a very real environmental contribution of the chemical industry. You set forth as a science-based target a 30% reduction of GHG emissions by fiscal 2030, and a 57% reduction by fiscal 2050. Yet, I think it is better if you set up your goals by explaining how Triple S products can reduce GHG. In my view, Triple S is more important than your Science Based Targets initiative. What do you think of my view?

A: I totally agree with your view. We recognize that fruit of our work is in how our products or technology can be made useful in the society. Therefore, we have long been engaged in environmentally friendly products. The level of our contribution to reduce GHG by way of Triple S has been calculated as you mentioned. We view that the level of our contribution to reduce GHG is pegged to the sales target we set. As the ideas of life cycle assessment and carbon foot print are gaining traction, I believe that there comes a time when the public will understand your view and our perception. Meanwhile, we have discussed and set forth our Science Based Targets at management meetings by taking account of requests from society and our responsibilities as a company. The GHG emission levels in science-based targets must be calculated under the rules of scope 1, 2, and 3 emissions reductions. Thus, this is a calculation, separate from the level of contribution to reduce GHG emissions in Triple S.

Q: I think it is ok to set goals for Science Based Targets by pegging them to the contribution level with Triple S. What is your take on this?

A: One of our challenges is how to present the ratio of our contribution to society relative to the CO₂ we consumed or generated. So, I agree with your view and I would like to continue to address it. Yet, there are some areas that cannot be calculated, such as a heat-resistant separators, one of Triple S items. It helps reduce CO₂ emission of electric vehicles but is not the sole component of electric vehicles. So, it is hard to figure out the extent of CO₂ reduction attributable to heat-resistant separators. We are thus forced to set up goals in terms of the absolute value of our contributions to society, on the one hand, and emissions reductions as an individual company, on the other, as separate perspectives. Incidentally, Science Based Target rules do not recognize our level of contribution.

Q: It is not optimal as a whole unless your true contribution is clearly indicated. I expect that your company will deliver some kind of message as a leader in the industry.

A: Understood.

Q: On page 31, Mr. Ueda explained the scenario analysis that showed the quantitative financial impact. Looking at this quantitative analysis, however, I cannot help but notice that the negative side of the carbon cost stands out more. Do you intend to disclose the positive side of your contribution with this kind of scenario analysis? Or, in that case, what kind of problems are there? I think these are extremely important points for the materials industry. I am interested in hearing your take on this as your company is ahead of other companies in ESG efforts.

A: There is a negative impact on the emissions level as an individual company. But, for example, if we license out the technology we developed, and this turned out to reduce CO2 as compared with the existing technology, this can be recognized in the future as a positive factor to reduce CO2 emissions. The aforementioned chemical recycling and carbon circulation aim to expand our contribution to our surroundings and society. These should be considered positive impacts. I believe that the calculation and rationale to make the public understand are necessary. As you mention, this kind of visualization of our contribution is very important to our company and industry, and we would like to work more on this going forward.

Q: Please do so. For instance, the efforts mentioned on page 36 alone can reduce CO2 by 900 thousand tons/year. If this is achieved by 2040, as in the previous scenario analysis, 10 billion yen will be saved. Please consider including more positive effects.

A: Understood.

Q: As for the commercialization timeline for chemical recycling and CO2 recycling, you mentioned that the projects in collaboration with Sekisui Chemical were to go into operation in 2022 and start commercial operation in 2025. What about the joint research with Muroran Institute of Technology and the research with Shimane University? If you already have a timeline and scale in mind, please share them with us.

A: As for collaboration with Sekisui Chemical, semi-commercial operation is due to start in 2022, and recycling of polyethylene, in 2025. As for the projects with Muroran Institute of Technology and Shimane University, it remains to be seen which comes first in commercial operation. Shimane University has generated good laboratory data but the key to early commercialization depends on whether such data can be reproduced at a large scale. Both projects are proceeding at the same speed but there are still obstacles to overcome. After commercialization of the initiative with Sekisui Chemical in 2025, the project with Shimane University may follow, if everything goes smoothly. The project with Muroran Institute of Technology is still small in scale, but the olefin yield from waste plastics is 70%, which is very good. The problem is the scale, which needs to be expanded. Thus, the order of commercialization after Sekisui Chemical would be Muroran Institute of Technology.

Q: So is my understanding correct that there is no goal for the scale at this moment?

A: We cannot have a specific image for the project with Muroran Institute of Technology. But for the projects with Sekisui Chemical and Shimane University, we have a rough idea on the scale of commercialization, assuming from output based on the size of incinerators. However, incinerators and waste are under the jurisdiction of each local community. So there are problems as to whether a large scale collection of waste is actually possible or whether a distribution across prefectural borders is possible. There may be facilities of various scales, located around the country.

Q: As part of your efforts to reduce CO2 emissions, you have said you will be converting to fuels such as LNG going forward , but when you take measures such as raising product prices, for example, I think it will be difficult for users to understand unless you clearly explain it, including the investment costs for fuel conversion. What are your thoughts? In meetings such as CLOMA, I notice that your messages focusing on benefits to users are more conspicuous than those focusing on ingredients or materials. I think this may be one reason you have not sufficiently conveyed the severity of your upstream burdens to users. Could you elaborate more on how you will shape your messaging about this in the future?

A: I agree with your view that we must get users to understand the investment costs of fuel conversion. In Chiba Works, however, the decision to convert fuels was made on the premise that the cost would not increase due to the investment in converting from petroleum coke to LNG. This is not an investment with high investment efficiency, but we were of the mindset that if the energy cost were to increase and the competitiveness of Chiba Works were to decline after the investment, we would not switch fuel sources. The reason that we decided to make the investment despite the low investment efficiency is that we have a system in place where carbon pricing (10,000 yen per ton) can be incorporated economically in our investment decisions. As the IRR of this decision is extremely high under such rules, the decision was made on the basis that the investment efficiency was quite high from a societal perspective, with the restriction that it not undermine financial competitiveness.

For the second point that our messaging with regard to materials at CLOMA and other meetings is lacking, I think the reason it appears that our efforts have been lacking is that our technologies are not in a place where we can explain things properly. Meanwhile, downstream industries are active in expressing their desires, such as a need for carbon-free materials, or environmentally friendly materials. This creates a gap between the actual technology and their expectations reality, thereby making it seem that our efforts are insufficient. We are conducting three projects simultaneously, and our competitors are also working on many projects, so when a technology is fully developed, or when we have a clear image of the path to commercialization, I feel that our ability to speak about it also increases, and we gain a certain momentum.

Q: Unless you start messaging from the current stage about subjects such as the target timing for commercialization, it will not be possible to deliver returns immediately to society, your company or investors when the technology is actually launched. I know it is going to be a ways down the line, but we expect you to start explaining it in advance to address this point.

A: Understood.

Q: In dialogues with investors, while some voiced their appreciation for your ESG efforts and your philosophy of “benefiting society at large, not just your own interests” (*Jiri Rita*), many others expressed the view that you would be better balanced if your focused more on the part about “your own interests.” Especially in governance, some say that the efficiency of your return on investment has been going down recently, so I would like to ask how discussions by directors, including outside directors, as well as feedback from analysts and investors obtained through your engagement with them, are being reflected in your efforts.

A: In the IR department, we receive a wide range of advice, recommendations and even criticism, including through meetings such as this, and we operate under the rule that the contents of such feedback will be discussed at periodic meetings of Board of Directors. To touch on the point about pursuing our own interests, we are analyzing why our efforts to benefit society have not also benefited our own interests, and we are taking measures to address this issue based on that analysis. Because this process takes time, however, we would like to continue to steadily take measures, and we hope achieve a balance between benefiting society and benefiting our own interests by around 2024.

Q: Do you have any cases where the voices of investors are put to actual use in the management?

A: I cannot answer with the examples of individual cases but discussions with investors and analysts inspire management in many ways, which I believe is leading to good management decisions. As we have received several brilliant ideas today, I would like to incorporate them into our management.

Q: Isn't it possible for you to be more proactive in expressing the qualitative definition of the chemical industry? Or if you have already been engaged in such effort, please tell us. Because ESG investment targets all industries, the fact that the chemical industry is regarded as a sector that produces CO2 through sectors such as petrochemicals has become a bottleneck to investment. Even though the chemical industry contributes enormously as a provider of materials infrastructure, people tend to focus only on surface issues, so I think that perhaps the entire industry association should focus on messaging around the degree of contribution of the chemical industry, even if only in a qualitative way. I feel that your company and several others ought to take the lead in this effort. Can I expect that such move can be expected, or please give us your view on this.

A: You are right about this, not only for the chemical industry in Japan but from the global perspective. There is an organization called the International Council of Chemical Associations (ICCA), which is engaged in various activities backed by a considerable amount of budget to promote understanding of chemistry and proper recognition of its contributions. In Japan, the Japan Petrochemical Industry Association and Japan Plastics Industry Federation (JPIF) are also undertaking efforts to communicate the value of chemistry, such as holding chemistry classes in elementary schools and junior high schools. The image of plastics, however, has been deteriorating these days. Every few years, the JPIF conducts a survey of thousands of people about the image of plastics to make observations against baseline data. According to this year's results, while the positive view of plastics as something "familiar and useful" remained at a high level, the view of plastics as "safe and friendly to the environment" and "an effective use of resources" has significantly deteriorated in the evaluations of consumers this time. Serious discussion has been going on within the industry as to how to take measures to improve this image. Yet, it is also true that the industry has not done enough to communicate its stance and its contributions to society. We are continuing to make efforts to address this.

Q: Since we take plastics for granted, it might be a bit extreme but it would be a good idea to focus messaging on what we would do in a world without plastics, and on whether there are any problems with other materials as substitutes. Opinion advertising like this is common in other industries, so I would like your company to communicate to the public how the chemical industry contributes to the world.

A: Understood.

(END)

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