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Shikoku Electric Power Company, Incorporated

Main Questions and Answers at FY2025 2Q Company Briefing

Q. I would like to commend the new Medium-Term Management Plan 2030 for being both substantial in content and ambitious. During the small meeting at the time of it was disclosed, some attendees pointed out that there was no outlook for cash flow allocation. However, in today's briefing, I felt that disclosure had moved forward as the President stated that "low-carbon and decarbonization investments, which constitute the majority of strategic business investments, are projected to be just under 200.0 billion yen. Although investment in maintenance and renewal has remained at less than 70.0 billion yen per year for the past several years, we expect it to increase in the future due to inflation and other factors."

The new Medium-Term Management Plan 2030 is particularly commendable for clearly outlining a path toward solid growth in the core power generation and electricity sales segment. However, achieving the segment's ordinary profit target of 30.0 billion yen will require growing by approx. 10.0 billion yen from the current level of just over 20.0 billion yen. For Shikoku Electric Power, which already has the nuclear power plant operating normally, I imagine it won't be easy to increase your real profits. How do you plan to achieve this? I believe the key to profit growth lies in competitiveness within the supply chain. Is it correct to assume that the policy is to leverage your supply capabilities to achieve profit growth primarily through wholesale electricity sales?

A. Regarding wholesale electricity sales, while we have been able to maintain stable nuclear power plant operating rates, in recent years, factors such as the impact of interconnected line work stoppages have meant that we have not been able to fully utilize our supply capacity. One of our strengths is our substantial coal-fired generation capacity. With the growing share of solar power and increased market fragmentation caused by interconnected line constraints, we've been using this capacity more frequently for balancing purposes. Once interconnected line conditions normalize, we plan to leverage it as a stable base supply for wholesale electricity sales. We anticipate that Green Transformation Emission Trading Scheme (GX-ETS) will eventually impose certain regulations. However, as this remains some time away, we will first leverage coal-fired power to drive profit growth during the new Medium-Term Management Plan 2030 period.

Regarding retail electricity sales, while demand growth within the Shikoku region over the next five years is not currently foreseeable, we aim to generate revenue by continuing to strengthen sales both within and outside Shikoku to capture demand, while simultaneously working to optimize pricing.

Q. I understand that the targets of 2.5% DOE and 8% ROE are set as goals to be achieved continuously throughout the five-year Medium-Term Management Plan period. Is that correct? Given that premise, it appears that FY2025's ROE, excluding one-off factors, may not reach 8%. However, to achieve over 8% from the early stages of the Medium-Term Management Plan period, it seems appropriate to consider not only profit growth but also the flexible use of share buybacks.

A. ROE is around 9% based on the forecast for FY2025, but we recognize that it will be around 8% if one-off factors are excluded from the forecast. Maintaining this level going forward is the target of the new Medium-Term Management Plan 2030. Considering that this must be achieved alongside our goal of further accumulating shareholders' equity going forward, it will not be easy. Nevertheless, we have positioned it as a target to be consistently achieved throughout the Medium-Term Management Plan period, while maintaining a strong awareness of the level of capital efficiency that is expected of us. To achieve our goals, we will first focus on our core electric power business while expanding and challenging new areas to grow our profits, the numerator. We will maintain a minimum shareholders' equity ratio of 25% or higher and strategically combine dividends with share buybacks. This approach will allow us to control the pace of shareholders equity accumulation while aiming to consistently achieve an 8% ROE.

Q. In your company's case, share liquidity is not particularly high. Could this pose a constraint when conducting share buybacks?

A. We recognize the liquidity is an issue and are considering improvement measures to boost it. On the other hand, we have set a goal to strategically implement share buybacks, but in a sense, we believe that we need to implement share buybacks strategically and systematically, and we will carefully consider the size and duration of buyback programs so that we can implement them appropriately even when liquidity is not so high.

Q. Please tell us your understanding of the competitive environment in the retail electricity market. Looking at the 1H results, it appears that the unit sales price has shifted slightly downward. What are your thoughts on this? Also, please tell me about the potential for future rate revisions.

A. The competitive environment is gradually becoming more challenging as nuclear restarts progress across Japan. Furthermore, as solar power generation increases, the market price for electricity is also declining, making competition even tougher in that regard. We plan to implement differentiated pricing for each category since the competitive environment differs by customer category.

The reason why the unit sales price appears to have declined in the 1H results is due to the sales strategy of increasing contracts outside the Shikoku area, where unit sales prices are relatively low, to compensate for the slight downward trend in demand within the Shikoku area. This may appear to lower the overall average unit price, but we intend to set appropriate prices tailored to each competitive environment while ensuring solid profits.

Q. Regarding the 2.5% target for DOE, is the denominator representing shareholders' equity based at the beginning or the end of the period?

A. We assume average shareholders' equity during the period (average of the beginning and end of the period) (actual results over time are shown on page 25 of the company briefing materials).

Q. In formulating the new Medium-Term Management Plan 2030, could you reiterate the background behind your decision to set the DOE target at 2.5%? If DOE is 2.5% and ROE is 8%, the dividend payout ratio would be about 30%. If there is a possibility of raising the dividend payout ratio further at some point, what would be the trigger for that?

A. As shown on page 25 of today's company briefing materials, the projected dividend of 50 yen for this fiscal year translates to DOE of 2.3%. In setting the target for the new Medium-Term Management Plan 2030, we aimed for higher level than these recent results and set the target at around 2.5%. Whether we can raise this even further remains uncertain at this point. However, once we firmly achieve the 2.5% level and are able to generate even greater profits than currently projected, we will consider that step. Note that while this new Medium-Term Management

Plan 2030 was formulated with a five-year target duration, I personally believe it is uncertain whether we can maintain this plan as is throughout the entire five years, given the significant changes in the business environment. Of course, I don't want to make changes in a negative direction and will strive to avoid doing so, but I also believe it's possible to make positive changes midway through the period. At this juncture, we plan to review the plan again around the midpoint of the new Medium-Term Management Plan 2030 period.

Q. Looking at the diagram of the business portfolio for the new Medium-Term Management Plan 2030 shown on page 19 of the company briefing materials, is it correct to assume that significant restructuring or revision of the business portfolio is not particularly anticipated? Or, while nothing specific has been decided yet, is there a growing determination to streamline assets with asset efficiency in mind?

A. The business portfolio diagram is based on the new segmentation of Core business, Expansion areas, and Challenge areas in the new Medium-Term Management Plan 2030, and the existing business domains are applied to each of these segments. We do not intend to make major changes to the main business segments themselves, such as IT/Communication or Construction & Engineering. However, within each business, we will consider asset restructuring with a view toward improving asset efficiency. As an example, regarding the International Business, while the current number of participating projects has expanded to about 15 with an equity stake of approximately 2 million kW, our policy is not to hold investments indefinitely. We aim to enhance asset efficiency by carefully considering portfolio rotation, including the replacement of projects.

Q. For the International Business and Construction & Engineering Business segments, the targets for FY2030, namely, ordinary profit of 13.0 billion yen and a ROIC of 7%, look quite aggressive. Please explain your plan to generate profits.

A. In the International Business, we are currently participating in a total of 15 projects in 10 countries, which are currently generating profits of about 4.0 billion yen. We are often asked whether aiming to double our revenue from 4.0 billion yen to 8.0 billion yen within five years might be overly ambitious. Yet, among the 15 projects, five are still under construction. If these proceed smoothly and begin contributing profits, the returns on our existing investments alone are projected to generate additional profits of several billion yen. In addition, we aim to achieve the target of 8.0 billion yen by 2030 by expanding investments in projects with better capital efficiency.

The Construction & Engineering Business is a sector significantly swayed by market conditions. Over the past few years, we have enjoyed strong orders for renewable energy-related construction projects. However, as this momentum is beginning to run its course, we are focusing our efforts on securing construction contracts in areas such as the Tokyo metropolitan area and the Kansai region as the next growth areas for this business. We aim to achieve our profit and ROIC targets by expanding these markets.

Q. Over the next five years, there are concerns about rising costs, including inflationary impacts. What is your outlook for fee collection?

A. The Transmission & Distribution business is heavily influenced by regulatory frameworks, making these issues difficult to resolve through individual company efforts alone. However, for Power Generation and Electricity Retail, we will first pursue cost reductions through digital transformation, including indirect department costs. Furthermore, regarding costs associated with decarbonization, we intend to engage in thorough discussions with the government to ensure these costs can be added to rates through regulatory mechanisms. We will explore ways to enable a direction where fees are added externally, rather than simply raising them.

Q. Given that 1H ordinary profit was 65.0 billion yen compared to the 53.0 billion yen ordinary profit forecast for FY2025, it appears the 2H is projected to loss-making. Please explain the rationale for this.

A. While this tends to occur annually, power companies typically experience a concentration of payments for repair costs and outsourcing fees at the fiscal year-end. For our Company as well, we anticipate a difference of approximately 50.0 billion yen in such expenses between the 1H and 2H in FY2025. Furthermore, while the Ikata Power Station operated at full capacity during 1H, its operating rate will decline in 2H due to scheduled inspections, with this impact expected to amount to approximately 10.0 billion yen. Furthermore, the recent tendency toward drought conditions during winter months is another factor causing uncertainty. Considering the risk of reduced demand due to the mild winter, we believe there is a possibility of posting a loss in 2H. Therefore, we have not revised our earnings forecasts at this stage, but we intend to reassess the situation once the impact of such factors becomes more concrete.

Q. They were briefly mentioned at the President's presentation, but I would like to confirm the cash flow allocation outlook for the new Medium-Term Management Plan 2030. Please provide an outlook on cash outflows corresponding to the five-year target of 550.0 billion yen or more in cash flows from operating activities, including maintenance and renewal investments and strategic business investments, to the extent that you are able to disclose such information.

A. Investment for maintenance and renewal has been around 70.0 billion yen per year for the past few years, but we expect it to exceed 350.0 billion yen, which is simply five times the current level, when taking into account the increase in investment to contend with the aging of power transmission and distribution systems and price hikes. Also, among business strategy investments, investments that contribute to low carbon and decarbonization (thermal power transition and renewable energy investments) are projected at just under 200.0 billion yen. Taking into account investments in the International Business and new businesses, we anticipate that overall strategic business investments will amount to 200.0 billion yen and upward.

Q. When you talk about thermal transition, what specifically is envisioned for these projects?

A. Primarily, this concerns new construction of Unit 5 at Sakaide Thermal Power Station currently under consideration and the related expansion of LNG terminal storage tanks.

Q. Based on the outlook for FY2025, the actual profit level for the Power Generation & Sales segment appears to be around 30.0 billion in ordinary profit. However, the profit target for that segment in the new Medium-Term Management Plan 2030 is set at 30.0 billion yen. Is this a target set as an endeavor to maintain the status quo in the face of downside factors such as fixed costs driven higher by inflation?

A. The outlook for FY2025 includes one-off factors in the Power Generation & Sales business, such as the time lag effect of the fuel cost adjustment system and the impact of amortization of actuarial gains and losses related to retirement benefits. Excluding these, the underlying profit is estimated to be just over 20.0 billion yen. We believe achieving the target will require approximately 1.5 times growth. As I mentioned earlier, to achieve our goals, we will make efforts in both retail and wholesale electricity sales.

Q. The ordinary profit target for the Transmission & Distribution business in the new Medium-Term Management Plan

2030 is set at 7.0 billion yen. I assume this target is based on the rate of return corresponding to the business profitability rate under the current first regulatory period. Is this understanding correct?

A. Regarding the Transmission & Distribution business, amid rising costs for materials and equipment, discussions are currently underway within the national council on how to reflect fluctuations during the regulatory period in rates. On the other hand, the new Medium-Term Management Plan 2030 spans two regulatory periods: the first regulatory period (2023–2027) and the second regulatory period (2028–2032). Since the institutional design for the second regulatory period is difficult to foresee at this stage, the target profit is set based on the business profitability rate for the first regulatory period.

Q. Is it difficult to negotiate with the government that a 1.5% business profitability rate for transmission & distribution is too low, making it impossible for a corporation to operate profitably?

A. As a private-sector business operator, we have consistently appealed to the government regarding issues such as the current business profitability rate being too low and the fact that the system did not anticipate the Transmission & Distribution business becoming unprofitable. We intend to continue working diligently on these matters, collaborating with other electric power companies within the industry.

Q. Similar to other regions, if projects such as the establishment of large-scale data centers were to emerge in Shikoku, I think further growth could be anticipated. I'd like to hear about new developments, such as those related to data centers, and your company's specific initiatives.

A. Regarding data centers, while there are no specific projects we can definitively announce at this time, we have established an internal Data Center Business Development Office We are actively pursuing the attraction of data centers ourselves, collaborating with municipal governments. Alongside our activities to attract investment, we are also considering the development of backbone telecommunications networks. By enhancing the surrounding infrastructure, we aim to create an environment that makes it easier for data center operators to choose our location. Although these initiatives have yet to bear fruit, we will continue to work diligently.