

# Itochu Enex Co., Ltd.

**8133**

Tokyo Stock Exchange First Section

12-Oct.-2017

FISCO Ltd. Analyst

**Hiroyuki Asakawa**



FISCO Ltd.

<http://www.fisco.co.jp>

## ■ Index

■ <b>Summary</b> .....	<b>01</b>
1. Posted all-time high results in 1Q FY3/18, exhibited healthy progress.....	01
2. Carrying out measures from the “Moving 2018” two-year medium-term business plan that lay the groundwork for growth in the future .....	01
3. Rising expectations to beat FY3/18 forecast, though the cautious stance of remaining at period-start targets for the time being is reasonable .....	01
■ <b>Results trends</b> .....	<b>02</b>
1. Review of 1Q FY3/18 results.....	02
2. Home-Life Division.....	04
3. Power & Utility Division .....	06
4. Life Energy & Logistics Division .....	08
5. Industrial Energy & Logistics Division.....	10
■ <b>Progress with the medium-term business plan</b> .....	<b>11</b>
1. Overview of the new medium-term business plan Moving 2018.....	11
2. Major progress in 1Q FY3/18.....	14
■ <b>Business outlook</b> .....	<b>17</b>
■ <b>Shareholder returns</b> .....	<b>18</b>
■ <b>Information security</b> .....	<b>19</b>

## ■ Summary

### Reported very upbeat results in 1Q FY3/18, making healthy progress toward FY3/18 targets and with measures from the medium-term business plan

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 the ITOCHU Corp. <8001> group. It has a broad business scope, though mainly sells petroleum products and liquefied petroleum (LP; propane) gas to users ranging from industrial businesses to final consumers. Its presence is also growing in electricity sales in recent years.

#### 1. Posted all-time high results in 1Q FY3/18, exhibited healthy progress

Itochu Enex reported sharply higher profit on higher sales in 1Q FY3/18, with ¥245,395mn in sales (+10.5% YoY) and ¥4,664mn in profit from operating activities (+100.4%). Key trends were significant improvement in income from the Life Energy & Logistics Division (former Car-Life Division) on success with longtime efforts to enhance management efficiency amid overall stability in fuel oil prices and healthy profit advances in the Power & Utility Division and Home-Life Division. Itochu Enex posted all-time highs as 1Q in gross profit and following profit items.

#### 2. Carrying out measures from the “Moving 2018” two-year medium-term business plan that lay the groundwork for growth in the future

In the “Moving 2018: Connecting to the future” two-year medium-term business plan covering FY3/18-19, Itochu Enex positions the two years as laying the groundwork for future growth. Activities thus far have confirmed steady implementation of growth measures and investments (some are planned), including the announcement of business integration with Osaka Gas Co., Ltd. <9532> in LP gas sales, which is one of Itochu Enex’s core areas, ramp-up of agent sales and launch of a new thermal-fired power plant in the electricity business, and operation of facilities for GINZA SIX in the heat supply business.

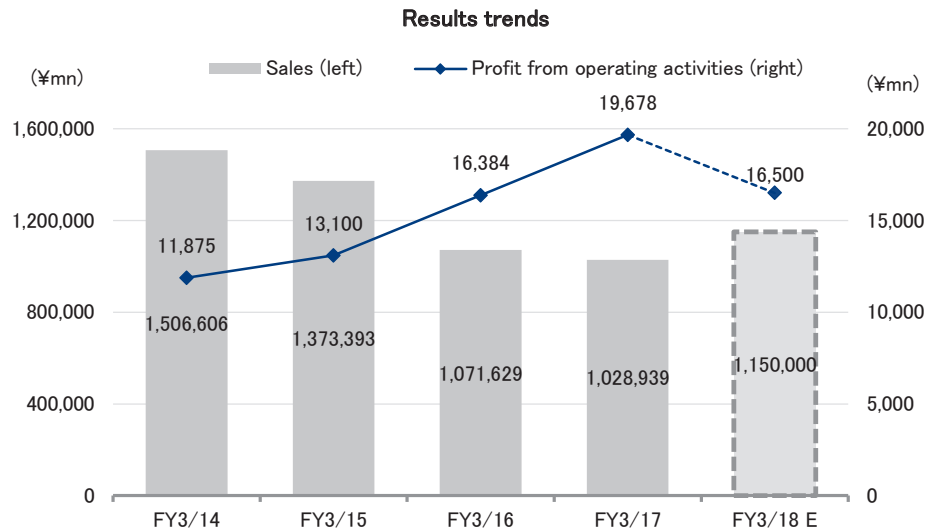
#### 3. Rising expectations to beat FY3/18 forecast, though the cautious stance of remaining at period-start targets for the time being is reasonable

Itochu Enex is sustaining period-start FY3/18 forecast of ¥1,150,000mn in sales (+11.8% YoY) and ¥16,500mn in profit from operating activities (-16.2%). While some observers might expect upside in FY3/18 results after 1Q, we recommend a cautious approach because 1Q has the smallest quarterly weight of the year for Itochu Enex and 1Q advantages might disappear if earnings weaken from 2Q. We agree with a cautious stance for the time being on the basis that precision in the full-year outlook should improve considerably at the 2Q announcement.

#### Key Points

- Laying the groundwork in FY3/18-19 for next-generation growth; rebuilding the income base and revamping the organizational framework
- Making healthy progress in building a growth foundation in each business segment, such as business integration for LP gas sales and entry into agent sales for electricity
- Maintained period-start FY3/18 forecast but a cautious stance despite a rise in upside expectations is reasonable

## Summary



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

## Results trends

### Posted all-time high earnings in 1Q FY3/18

#### 1. Review of 1Q FY3/18 results

The Company reported 1Q FY3/18 results with ¥245,395mn in sales (up 10.5% YoY), ¥172,458mn in revenue (up 15.9%), ¥4,664mn in profit from operating activities (up 100.4%), ¥4,591mn in profit before tax (up 97.6%), and ¥2,523mn in net profit attributable to the Company's shareholders (up 134.3%). The Company achieved considerable profit growth on sales increase, and gross profit and the profit items following it were all-time highs for 1Q.

While it is not possible to offer comparison with 1Q targets because Itochu Enex only discloses a full-year forecast, progress rates in 1Q were at 21.3% in sales and 28.3% in profit from operating activities. The latter rate is more than twice the previous fiscal year. We think the 1Q FY3/18 results were very robust considering the seasonality of Itochu Enex's income (its results are skewed toward 2H).

## Results trends

## Review of 1Q FY3/18 results

(¥mn)

	FY3/17			FY3/18			
	1Q results	Progress rate	Full year	1Q results	YoY	Progress rate vs. forecast	Full year (E)
Sales	222,091	21.6%	1,028,939	245,395	10.5%	21.3%	1,150,000
Revenue	148,808	21.4%	695,060	172,458	15.9%	-	-
Gross profit	20,492	21.9%	93,604	21,998	7.3%	-	-
SG&A expenses	18,161	24.3%	74,697	17,738	-2.3%	-	-
Profit from operating activities	2,328	11.8%	19,678	4,664	100.4%	28.3%	16,500
Profit before tax	2,324	12.0%	19,344	4,591	97.6%	25.8%	17,800
Net profit attributable to the Company's shareholders	1,077	10.4%	10,405	2,523	134.3%	24.3%	10,400

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

In 1Q, business conditions remained generally upbeat for Itochu Enex with continuation of economic growth in Japan as seen in corporate earnings and employment conditions as well as stable crude oil pricing (Dubai monthly average) at around \$50 per barrel. While Itochu Enex had been carrying out reforms for some time aimed at attaining ¥10bn in net profit attributable to the Company's shareholders, these reforms finally paid off in FY3/17. We believe the upbeat 1Q FY3/18 results can be explained as a combination of profitability resilience cultivated through this process and upbeat business conditions.

Itochu Enex started the Moving 2018 two-year medium-term business plan with FY3/18 as the first fiscal year and is pursuing restructuring of the income base and revamping of the organizational foundation. It positions the two years (FY3/18-19) as a period of laying the groundwork for future growth. Conservative earnings targets stand out in this medium-term plan. While it would be difficult to give a favorable assessment if upbeat results occurred due to delaying in such efforts (investments), Itochu Enex took steady actions in 1Q FY3/18. Some specific examples are expansion of heat supply business and an arrangement to integrate the LP gas sales business with Osaka Gas.

Itochu Enex achieved double-digit earnings growth (YoY) in three segments (besides the Industrial Energy & Logistics Division) out of its four business segments. In particular, the Life Energy & Logistics Division generated an extra ¥2,012mn in profit from operating activities (YoY) and contributed about 90% of the ¥2,336mn overall profit increase. The Power & Utility Division delivered a ¥614mn YoY profit increase and provided an addition of over 25% to the total gain.

## Results trends

Segment details are described below.

## Breakdown of results by business segment

		(¥mn)		
		1Q FY3/17 results	FY3/18	
			1Q results	YoY
Revenue	Home-Life Division	19,014	21,704	14.1%
	Power & Utility Division	11,481	15,309	33.3%
	Life Energy & Logistics Division	105,982	119,081	12.4%
	Industrial Energy & Logistics Division	13,309	18,336	37.8%
	Revenue before adjustment	149,786	174,430	16.5%
	Adjustment	-978	-1,972	-
	<b>Total revenue</b>	<b>148,808</b>	<b>172,458</b>	<b>15.9%</b>
Profit from operating activities	Home-Life Division	646	785	21.6%
	Power & Utility Division	1,301	1,915	47.2%
	Life Energy & Logistics Division	-271	1,741	-
	Industrial Energy & Logistics Division	394	-56	-
	Profit from operating activities before adjustment	2,070	4,385	111.8%
	Adjustment	258	279	8.1%
<b>Total profit from operating activities</b>	<b>2,328</b>	<b>4,664</b>	<b>100.4%</b>	
Net profit attributable to the Company's shareholders	Home-Life Division	361	406	12.4%
	Power & Utility Division	652	931	42.7%
	Life Energy & Logistics Division	-376	1,013	-
	Industrial Energy & Logistics Division	306	-12	-
	Net profit attributable to the Company's shareholders before adjustment	943	2,338	147.9%
	Adjustment	134	185	38.1%
<b>Net profit attributable to the Company's shareholders</b>	<b>1,077</b>	<b>2,523</b>	<b>134.3%</b>	

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

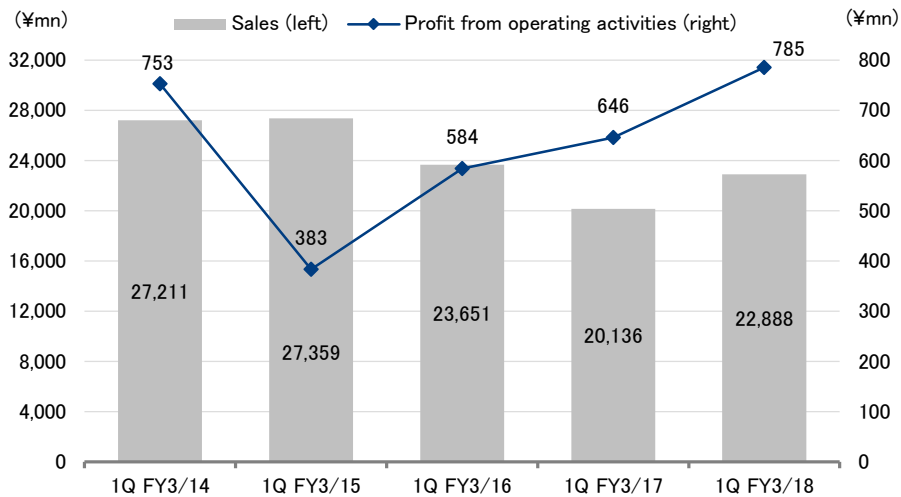
## LP gas sales volume rose YoY and supported a profit increase Electricity sales and equipment sales made healthy progress too

### 2. Home-Life Division

The Home-Life Division booked higher sales and profits in 1Q FY3/18 with ¥21,704mn in revenue (+14.1% YoY) and ¥785mn in profit from operating activities (+21.6%). While LP gas margin narrowed because of decline in the price at period-end (vs. the period-start level), electricity and equipment sales businesses and other areas were upbeat and boosted segment profit.

Results trends

1Q results trends in the Home-Life Division



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

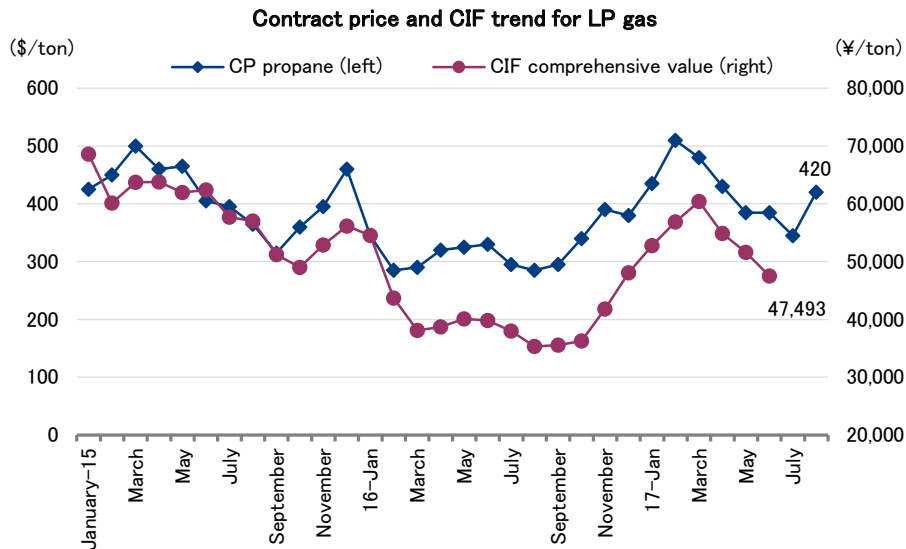
The Home-Life Division's core business is selling LP gas (propane gas). Itochu Enex procures LP gas from Japan Gas Energy Corporation (it owns a 20% stake in this company) and sells LP gas to about 350,000 households through direct-sales subsidiaries. It also sells LP gas on a wholesale basis to about 1,900 distributors (LP gas sales outlets) and covers about 1.08mn households nationwide on a combined basis. Another important target market is automotive gas. Itochu Enex sells LP gas used in taxis that consume this fuel. Automotive gas sales account for about 15-20% of the Company's overall LP sales, and this is an important market.

The LP gas business had higher customer numbers than a year earlier in 1Q FY3/18, thanks to the rise in direct sales customers during FY3/17, and this boosted sales volume (YoY) as well. For pricing, meanwhile, the average contract price (CP; import price denominated in US dollars) during the period was \$400 per ton, exceeding the previous year's \$325, but the average price dropped from \$450 at end-March (period-start) to \$385 at end-June (period-end) in 1Q.

The contract price, which is notified by top exporter Saudi Arabia, is the global benchmark price for LP gas. While the contract price corresponds to raw material costs for Japan's LP gas operators, including Itochu Enex, the raw materials cost adjustment program absorbs fluctuations and supports a certain amount of spread. This is the most important characteristic of the income structure in the LP gas business. While the average price and sales volume influence revenue in the LP gas business, profit largely depends on sales volume because spread is supported at a certain level.

Profit increased in 1Q owing to the rise in sales volume as mentioned above. However, operators (such as Itochu Enex) have LP gas inventories and this means that price change from period-start to period-end affects earnings. Decline in the average price at period-end (compared to period-start) in 1Q, as mentioned above, created a negative inventory impact (putting downward pressure on profit) and reduced the profit increase margin.

Results trends



Source: Compiled by FISCO from trade statistics of the Ministry of Finance

In the electricity business, power handled by the Power & Utility Division is sold to LP gas customer households. Itochu Enex conducts package discount sales of LP gas, the main product in the Home-Life Division, and electricity as its sales strategy, and this activity is a major strength. It added about 4,000 household customers during 1Q, putting total number at 36,000 households at the end of 1Q. The plan targets 70,000 households as total volume at the end of FY3/18 for a net increase of 36,000 households over the year. This works out to more than 9,000 households per quarter. While the 1Q result is lower than this level, we do not see reason for concern because 1Q has the smallest quarterly weight for Itochu Enex. We think the 1Q shortfall can be sufficiently covered by the other three quarters.

Overseas businesses in the Home-Life Division are industrial gas sales in Indonesia (through local-entity PT. ITC ENEX INDONESIA) and LP gas sales in the Philippines (it owns a stake and participates in operation of Isla Petroleum & Gas Corporation). These businesses are both steadily growing their customer bases and are targeting continuation of expansion paths.

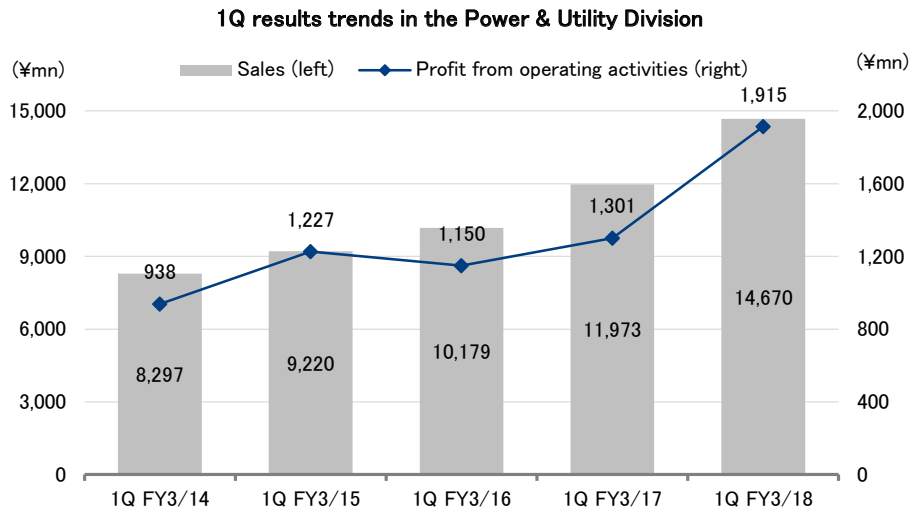
## Step increases in retail and wholesale electricity sales volumes drove sharply higher sales and earnings

### 3. Power & Utility Division

The Power & Utility Division reported sharply higher sales and profits in 1Q FY3/18 at ¥15,309mn in revenue (+33.3% YoY) and ¥1,915mn in profit from operating activities (+47.2%). Retail electricity sales volume to household and corporate customers grew steadily, and wholesale electricity sales increased as well. Heat supply business expanded supply destinations too. This segment significantly raised its overall income.



Results trends



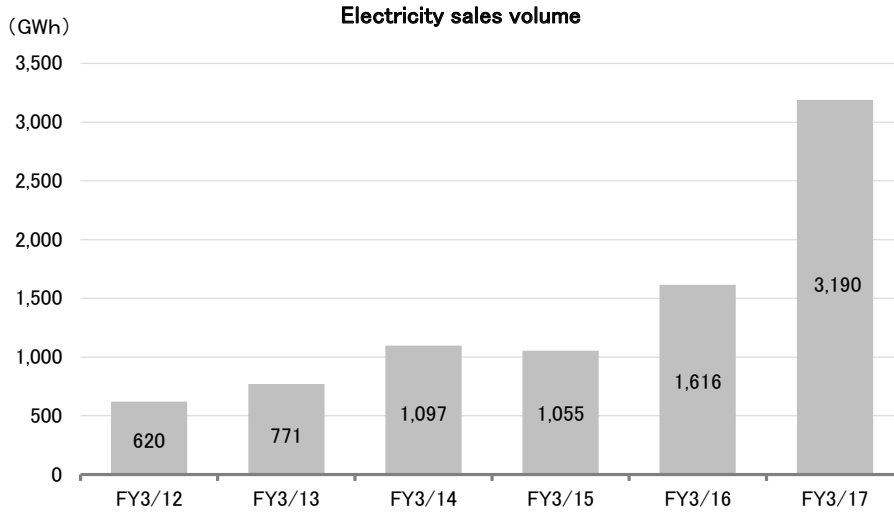
Source: Prepared by FISCO from the Company's financial results

In the power generation business, total power output was lower than in the previous year due to the sale of some wind power facilities in FY3/17 and scheduled maintenance impact. Net profit, however, exceeded the previous year with a boost from one-time profit (insurance payment income) in 1Q.

Electricity sales consist of retail and wholesale areas. For retail, Itochu Enex sells electricity through a balancing group (BG) that it leads. BG members are its LP gas sales subsidiaries and two external companies (Tottori Citizen Electricity Co., Ltd. and Todok Electricity Co., Ltd.). These entities leverage strong sales bases in their respective regions in selling electricity to ordinary households and small businesses. Itochu Enex is also steadily increasing sales by reinforcing collaboration with other segments and companies outside of the BG scheme too (details provided below).

Wholesale sales also strengthened in 1Q. While Itochu Enex had been mainly putting effort into expansion of retail sales over the past few years, we think wholesale sales climbed because of improved wholesale profitability after the crude oil price moved out of the very low level it had reached at one point. We think the upcoming launch of operations at the Sendai thermal-fired power plant, which is 50% owned by Itochu Enex, in October played a role in expansion of total electricity sales volume (retail and wholesale) as well.

Results trends



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

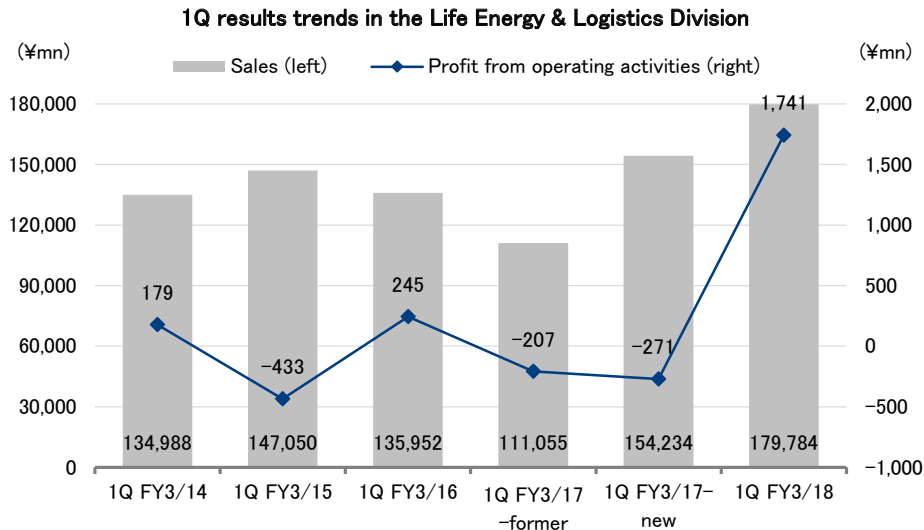
In the heat supply business, while the average temperature in 1Q was lower than a year ago and this reduced demand, heat demand surpassed the previous year and sales expanded YoY thanks to the start of heat supply to GINZA SIX. Earnings fell, however, because of booking disposal costs related to equipment upgrades and other factors.

## Income improved significantly on price stability benefits Steady progress in Car-Life Station income enhancement and business model change

### 4. Life Energy & Logistics Division

The Life Energy & Logistics Division reported ¥119,081mn in revenue (+12.4% YoY) and ¥1,741mn in profit from operating activities (vs. a ¥271mn loss in the previous year) in 1Q FY3/18, posting higher sales and rebounding to an operating profit. Earnings recovered sharply with an increase of more than ¥2bn YoY thanks to price stability and a boost from closures of unprofitable Car-Life Stations (CS; Itochu Enex's in-house term for gas stations).

Results trends



Note: Life Energy & Logistics Division results from "1Q FY3/17-new" and Car-Life Division results before then  
 Source: Prepared by FISCO from the Company's financial results

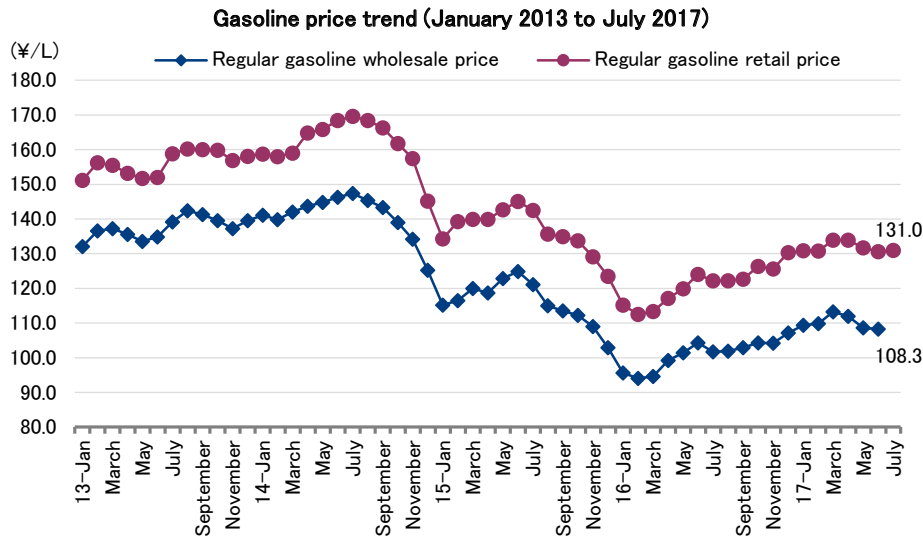
Itochu Enex revamped its organization as part of measures advocated in the new medium-term plan and launched the Life Energy & Logistics Division from FY3/18. It transferred industrial fuels (fuel oil, etc.), fleet (diesel truck fuel, etc.), and AdBlue (truck fuel additive) businesses from the Energy Innovation Division to the Car-Life Division.

JXTG Holdings, Inc. <5020> emerged in the oil industry on April 1, 2017. With this reorganization of oil suppliers, supply-demand gap in gasoline and other fuel oils disappeared and prices generally stabilized, including removal of extremely cheap retail prices for gasoline, in 1Q. In volume, meanwhile, the long-term trend of decline in fuel oil demand continued, but Itochu Enex's gasoline sales volume held firm in a flat range (YoY) and diesel truck fuel sales climbed. We attribute these outcomes to recovery in domestic economic activity and increased truck delivery demand.

We think improvement in the gasoline supply-demand balance had a similar positive effect in industrial fuel, fleet (diesel truck fuel), and other areas because the pricing mechanism, demand drivers, and other income change factors are fundamentally the same. Transfers of these businesses from the former Energy Innovation Division hence contributed as an earnings lift in 1Q.

Itochu Enex continues to shutter Car-Life Stations that are unprofitable, and period-end station numbers dropped by a net seven sites to 1,881 in 1Q. While planned closures of money-losing sites will continue, the CS business expenses are clearly declining as a result of progress in closures from past years. This aspect aided the significant rebound in 1Q profit.

Results trends



Source: Prepared by FISCO from Agency for Natural Resources and Energy data

Mutual customer introductions utilizing a newly deployed POS system and shared point card program are still taking place as initiatives to enhance top-line growth in the CS-related businesses (broadly includes car-related businesses). Itochu Enex also ramped up the Carlife Stadium service brand in FY3/17 for car-related business and began Carlife Stadium car rental services as the first initiative in April 2017.

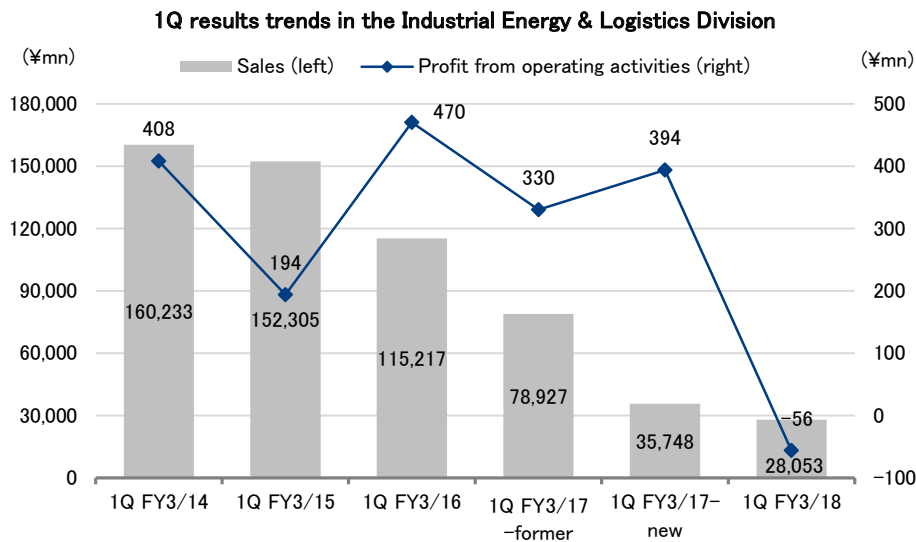
Nissan Osaka Sales Co., Ltd., which handles automobile sales business, significantly increased sales volume in 1Q as a rebound from the sales setback in 1Q FY3/17 due to the impact of fuel economy data falsification at Mitsubishi Motors Corporation <7211>. Both sales and profit improved over the previous year.

## Profit declined on lower trading of oil products due to stabilization of supply and demand

### 5. Industrial Energy & Logistics Division

The Industrial Energy & Logistics Division incurred an operating loss despite stronger sales, with ¥18,336mn in revenue (+37.8% YoY) and a ¥56mn loss from operating activities (vs. a ¥394mn profit a year earlier) in 1Q FY3/18.

Results trends



Note: Industrial Energy & Logistics Division results from "1Q FY3/17-new" and Energy Innovation Division results before then  
 Source: Prepared by FISCO from the Company's financial results

The Industrial Energy & Logistics Division business mainly consists of asphalt sales, marine fuel sales (domestic and overseas), oil product trading, and terminals. It also covers other new businesses.

The division booked a loss from operating activities in 1Q because of decline in the asphalt income base in a weak demand phase and pressure from lower oil product trading. Oil product trading business handles surplus contracts that occur due to the supply-demand gap. Its supply-demand adjustment and removal of price gap expands income at Itochu Enex and also meets the societal need of balanced adjustment for the overall industry. As noted above, business opportunities for oil product trading were extremely limited in 1Q because of the absence of supply-demand gap. Losses in oil product trading also affected earnings for the overall division.

## Progress with the medium-term business plan

### Laying the groundwork for next-generation growth in FY3/18-19 Rebuilding the income base and revamping the organizational framework

#### 1. Overview of the new medium-term business plan Moving 2018

##### (1) Overview

The Company announced its new two-year (FY3/18 and FY3/19) medium-term business plan, Moving 2018: Connecting to the future. The concept behind the new plan is two years to lay the management foundations for the next stage of the Company's development as expressed by the subtitle of the plan, "Connecting to the future."

We encourage readers to review our complete legal statement on "Disclaimer" page.

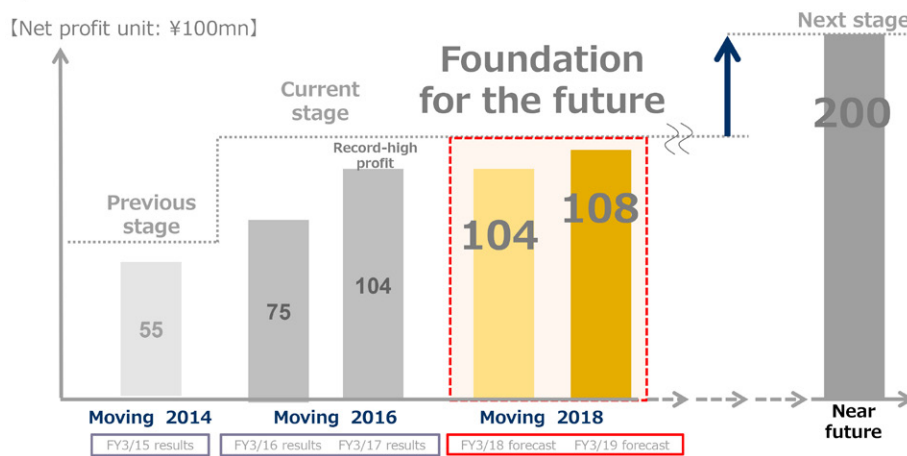
Progress with the medium-term business plan

Itochu Enex implemented measures from the “Moving 2016 – Sowing seeds for tomorrow” two-year medium-term business plan in the two years through FY3/17. One of the main successes was lifting net profit attributable to the Company’s shareholders above ¥10bn in FY3/17. With this threshold met, Itochu Enex set a goal of ¥20bn in net profit attributable to the Company’s shareholders as the next stage. However, it does not expect to immediately realize this goal and presented Moving 2018: Connecting to the future as a two-year phase of solidifying the foundation to support realization of ¥20bn.

Concept and positioning of new medium-term business plan



Focus over next two years: investment in electric power, planting seeds with overseas development. Firming up management foundation for next stage over next two years under the medium-term business plan.



Source: The Company’s medium-term business plan briefing materials

Quantitative targets in the new medium-term business plan are for profit from operating activities of ¥18.5bn, net profit attributable to the Company’s shareholders of ¥10.8bn, and ROE of 9.1% in FY3/19, the final year of the plan. While growth appears to stall in the current medium-term business plan versus FY3/17 results, we see this stance as a message from Itochu Enex of putting a top emphasis on ensuring that net profit attributable to the Company’s shareholders firmly takes hold above ¥10bn through solidification measures.

We focus more on investment plans in the new medium-term business plan than on quantitative targets. The Company plans to make ¥45bn in investments during the two years covered by the plan. On an annualized basis, this is roughly 70% higher than investments made in FY3/17. This is perhaps given that the Company has designated the period covered by the plan as a time to lay the foundations for the next stage. However, we believe it is important to note that operating cash flow over the two-year period is expected to reach ¥46,000mn and that the Company is therefore positioned to make aggressive investments even as it maintains or strengthens its financial position.

Progress with the medium-term business plan

Quantitative targets in the medium-term business plan

	FY3/17	Moving 2018	
		FY3/18	FY3/19
Profit from operating activities	¥19.7bn	¥16.5bn	¥18.5bn
Net profit attributable to the Company's shareholders	¥10.4bn	¥10.4bn	¥10.8bn
ROE	10.0%	9.3%	9.1%
Dividend payout ratio	Over 30%	Over 30%	Over 30%
Cash flows from operating activities	¥17.8bn	¥22.0bn	¥24.0bn
Investment plan	¥13.4bn	¥45bn (over 2 years)	
Average rate	Crude oil price	\$50/bbl	
	CP price	\$400/MT	
	Forex rate	¥108.4/\$	

Source: Prepared by FISCO from the Company's materials

(2) Basic policies in the new medium-term business plan: Rebuilding the income base and revamping the organizational framework

Fundamental policies (items being targeted) in the new medium-term business plan period are rebuilding the income base and revamping the organizational framework.

Basic initiatives of Moving 2018: two connections

Reforming revenue base (Connecting to the future)		Reforming organizational base (Connecting people and functionality within the Group)	
Asset optimization	Accelerate asset reallocation in established businesses to improve profitability and growth, continue to increase investment in electric power (new business), upgrade assets while monitoring rise in asset risk (establish exit policy)	Strengthening organizational	Reform group's management base including communication methods, risk management, and compliance systems in order to form a healthy, open-minded and strong corporate group
Increase earnings potential	Margins narrowing in established businesses owing to shrinking market size, preparing for heating up of competition in electric power business, improve earnings efficiency using ratio of gross profit to costs as an indicator	Human resource development fostering independence	Create ways to share missions between organizations and businesses and foster human resources capable of autonomously identifying and solving problems
Customer base development	Transfer customer base (intangible asset) of established businesses to electric power business and expand customer base through future retail trends	ENEX EARLY BIRD	Transition to a style of work where employees complete tasks in a relatively short amount of time Improve work quality, prevent long working hours, improve health Work together as team of three

**Management base**

Strengthen revenue base and organizational base, connect to the future.

Source: The Company's medium-term business plan briefing materials

Rebuilding the income base involves measures that lead to future growth. Itochu Enex presented optimization of assets as an initiative in the medium-term business plan. This targets replacement of business assets aimed at raising profitability and growth potential in existing areas (oil and gas) and new areas (electric power, etc.). Through its updates to asset composition, Itochu Enex aims to raise asset share of electricity and other new business to over 50% and improve the ratio of fixed assets to profit from operating activities from 6.2% to 7.0%. It is also targeting asset optimization within business segments. One example is the sale of some wind power facilities in the electricity business. Itochu Enex is currently reviewing biomass as a new power source to replace the sold power facilities.

Progress with the medium-term business plan

The Company aims to change its organizational structure from one where each product (oil, gas, electric power, etc.) is managed separately to a healthy, open-minded and strong corporate group organization. This is based on the decision that the organizational system governing the group's management must be reformed in order to improve communication methods, risk management, and compliance systems. One aspect of organizational reform is the strengthening of the skills of each and every employee by fostering human resources capable of autonomously identifying problems, proposing solutions, and solving problems. This will involve demanding higher quality of work from employees. The Company is also simultaneously transforming its approach to work. Under the slogan "Enex Early Bird" the Company aims to transition to a style of work where employees complete tasks in a relatively short amount of time.

## Making healthy progress in initiatives to support a growth in its various segment, including business integration for LP gas sales and entry into electricity agent sales

### 2. Major progress in 1Q FY3/18

Refer above for quantitative targets in the new medium-term business plan. This stance has not changed from the previous view following 1Q FY3/18.

**Segment breakdown of quantitative targets in the new medium-term plan**

		(¥mn)					
		FY3/17		FY3/18		FY3/19	
		Full year	Full year (forecast)	YoY	Full year (forecast)	YoY	
<b>Sales</b>	Home-Life Division	90,768	99,400	9.5%	107,300	7.9%	
	Power & Utility Division	65,654	84,300	28.4%	90,800	7.7%	
	Life Energy & Logistics Division	740,400	763,100	3.1%	771,800	1.1%	
	Industrial Energy & Logistics Division	132,100	211,700	60.3%	194,600	-8.1%	
	Total sales before adjustment	1,028,939	1,158,500	12.6%	1,164,500	0.5%	
	Adjustment	-	-8,500	-	0	-	
	Total sales	1,028,939	1,150,000	11.8%	1,164,500	1.3%	
<b>Profit from operating activities</b>	Home-Life Division	4,831	4,500	-6.9%	5,000	11.1%	
	Power & Utility Division	6,640	4,400	-33.7%	5,500	25.0%	
	Life Energy & Logistics Division	5,800	5,400	-6.9%	5,600	3.7%	
	Industrial Energy & Logistics Division	2,200	2,100	-4.5%	2,400	14.3%	
	Profit from operating activities before adjustment	19,564	16,400	-16.2%	18,500	12.8%	
	Adjustment	114	100	-12.3%	-	-	
	Total profit from operating activities	19,678	16,500	-16.2%	18,500	12.1%	

Source: The Company's financial results and medium-term business plan briefing materials

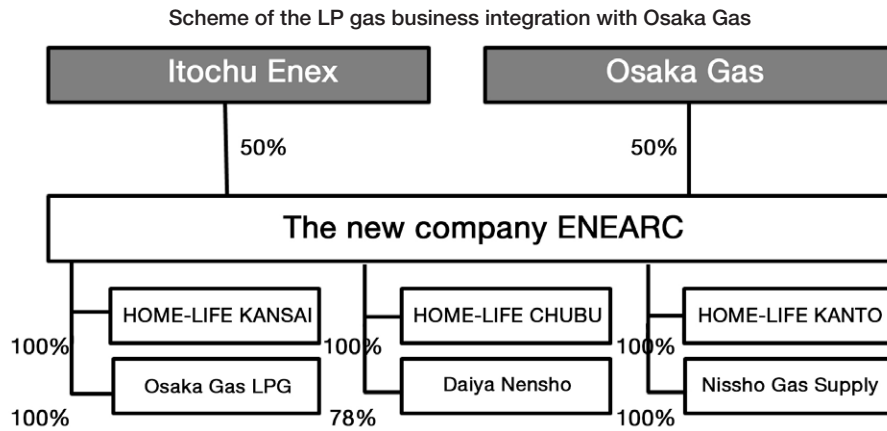
This section reviews progress by business segments in 1Q FY3/18 along with outlooks and key points.

#### (1) Home-Life Division

A major step forward in 1Q was the agreement on integration of LP gas wholesale and retail business with Osaka Gas (release issued on August 3, 2017). The two companies will establish joint venture ENEARC Co., Ltd. with each owning a 50% stake. They plan to transfer shares in their LP gas sales firms with sales territories of Kanto, Chubu, and Kansai to the new entity. Separate business activities respectively will continue in other regions, just as previously. The integration also involves the transfer of shares owned by NISSHO PETROLEUM GAS CORPORATION, a subsidiary of Osaka Gas, in three LP gas sales companies to Itochu Enex. This reorganization comes into effect on October 1, 2017.



Progress with the medium-term business plan



Source: The Company's press release

Earnings from joint venture ENEARC will be booked in investment income through the equity method. The integration will lower sales and profit from operating activities versus previous levels because IFRS accounting standards utilized by Itochu Enex add this income just before pretax profit. We confirmed in our contacts with Itochu Enex that it included impact from the business integration on income in the period-start outlook.

We think the integration offers a nearly best combination for Itochu Enex. The decision takes into account a tough business environment with decline in the number of households and fierce competition with other energy types. We expect strong advantages in surviving the difficult competitive conditions from the ability to harness Osaka Gas' name recognition and brand strength. Itochu Enex has 350,000 LP gas customers for direct sales and is actively offering package discounts for LP gas and electricity, as explained above. The integration adds 180,000 direct sale customers from Osaka Gas. Itochu Enex is likely to sell a variety of related products, including electricity, to these customers. These developments should be closely watched.

**(2) Power & Utility Division**

In power generation, Itochu Enex sold some wind power facilities in FY3/17, but has indicated that it considers bolstering initiatives in the biomass power business. Additionally, it begins operation of a coal thermal-fired power plant at Sendai Power Station, which is jointly owned (50% stakes each) with The Kansai Electric Power Co., Inc., in October 2017. This plant completed facility installations and was conducting test operation in August. It is likely to begin commercial service in October, as planned.

Sales initiatives are occurring on the sales front with the aim of expanding the customer base. Itochu Enex formed a balancing group (BG) to develop customers in electricity retail sales. While BG-led customer recruitment has achieved healthy progress up to now, as explained above, it founded ENEX LIFE SERVICE Co., Ltd. in July 2016 as well.

ENEX LIFE SERVICE is an organization that oversees agent sales in the electricity retail business. The BG requires individual members to register as a power producer and supplier (PPS). Member companies each serve as contract parties in the relationship with customers. Agent contracts, meanwhile, do not require PPS registration and the Company is main contract party. Group firm Nissan Osaka Sales started the collaboration business between cars and electricity for the purpose of selling electricity to automobile customers in 2016, becoming the first sales agent.

Progress with the medium-term business plan

We are closely monitoring activities by ENEX LIFE SERVICE. Our interest is not limited to expectations for electricity sales via an agent format. Itochu Enex positions ENEX LIFE SERVICE as a company that provides support in life-related areas to corporate customers. In other words, it functions as a comprehensive operator of businesses that sell life-related goods with other companies. "Collaboration business between cars and electricity" is an example of combined sales of electricity and other products. We think it is likely to go further by handling communications and products in other areas and thus will be paying attention to trends in new goods and services.

Heat supply is another business in this division and began supplying heat to the GINZA SIX, a large-scale commercial facility that opened in Ginza. Itochu Enex entered this market by acquiring subsidiary Tokyo Toshi Service Co., Ltd. (TTS; it owns a 66.6% stake) from Tokyo Electric Power Company, Incorporated <9501>. The business acquired this deal thanks to its abundant track record and strong competitiveness, including its roots. We think capital investment for heat supply to GINZA SIX amounted to about ¥5bn. This means that Itochu Enex took action on an important piece of the ¥45bn in investment outlays targeted in the two-year medium-term business plan during 1Q.

### (3) Life Energy & Logistics Division

Itochu Enex continues to exit money-losing Car-Life Stations in the CS-related business. This effort promotes optimization of assets, which is taking place on a companywide basis, and also reduces spending and raises profitability in the CS business as seen in 1Q results.

In the CS business, Itochu Enex is deepening its auto-related businesses, such as car rentals and purchases, insurance, and repairs under the Carlife Stadium brand. It hopes to unify under one brand previously dispersed services to bolster profitability and efficiency. The first initiative was the launch of Carlife Stadium car rentals in 1Q.

### (4) Industrial Energy & Logistics Division

The main advance in 1Q was building a new fuel supply ship in the marine fuel sales business. This new ship is being deployed at Hakata Port. Itochu Enex aims to build stable marine fuel distribution operations in Japan with seven ships nationwide.

Possible new and strategic projects include launching a recycling business or participation in a bio-based jet fuel project. We understand the Company has already made progress toward the launch of a recovered oil and fly ash recycling business and is nearly ready to start operations as a profitable business. Regarding participation in a bio-based jet fuel project, the Company partnered with Euglena Co. Ltd. <2931> in a domestic biofuel project which, in June 2017 received a third-party capital infusion and is now working toward starting operation of a proof-of-concept plant in 2019. Further developments on both going forward are awaited.

Progress with the medium-term business plan

## Business outlook

### Maintained period-start FY3/18 forecast but a cautious stance despite a rise in upside expectations is reasonable

The Company forecasts sales rising, but profit declining with ¥1,150,000mn in sales (up 11.8% YoY), ¥16,500mn in profit from operating activities (down 16.2%), ¥17,800mn in profit before tax (down 8.0%), and ¥10,400mn in net profit attributable to the Company's shareholders (down less than 0.1%) in FY3/18. The Company did not change from the period-start estimate.

#### Overview of the forecast for FY3/18

	FY3/17			FY3/18			
	1Q results	1H results	Full year	1Q results	Full year (forecast)	YoY	
						% change	Change
Sales	222,091	466,313	1,028,939	245,395	1,150,000	11.8%	121,061
Revenue	148,808	309,516	695,060	172,458	-	-	-
Gross profit	20,492	43,742	93,604	21,998	-	-	-
SG&A expenses	18,161	36,210	74,697	17,738	-	-	-
Profit from operating activities	2,328	7,755	19,678	4,664	16,500	-16.2%	-3,178
Profit before tax	2,324	7,242	19,344	4,591	17,800	-8.0%	-1,544
Net profit attributable to the Company's shareholders	1,077	3,707	10,405	2,523	10,400	-0.0%	-5

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

As explained above, FY3/18 is a year of laying groundwork to support further growth in the future. Emphasis hence should be placed on whether Itochu Enex steadily conducts investments toward growth, rather than nominal earnings. Thus far, Itochu Enex has integrated the LP gas sales business, entered agent sales for retail electricity, and implemented other notable measures explained earlier in this report. We will be focusing on whether this upbeat momentum continues or not as the most important evaluation point in FY3/18 and FY3/19.

Segment details were already covered above. Key points in the Home-Life Division are progress with LP gas integration from 2H and trends in electricity sales customer numbers. In the Power & Utility Division, we will be focusing on ramp-up at the Sendai Power Station, which is slated to begin operations in October, and ENEX LIFE SERVICE trends. Important points in the Life Energy & Logistics Division are Itochu Enex's own measures and industry supply-demand balance. External conditions played a major role in upbeat results for this division in 1Q. In the Industrial Energy & Logistics Division, we intend to focus on asphalt business arriving at a demand phase and progress in new businesses.

While 1Q results were upbeat, we think it is too early to anticipate upside in the full-year outlook. One reason is that income scale in 1Q has the smallest quarterly weight among the four quarters due to seasonality. Extra income could be readily eroded depending on trends in 3-4Q, the main demand quarters. The other reason is poor weather in the summer months. This might have affected demand for air conditioners and vacation-related gasoline consumption. We believe there is still enough time to make an assessment of FY3/18 results after seeing 2Q.

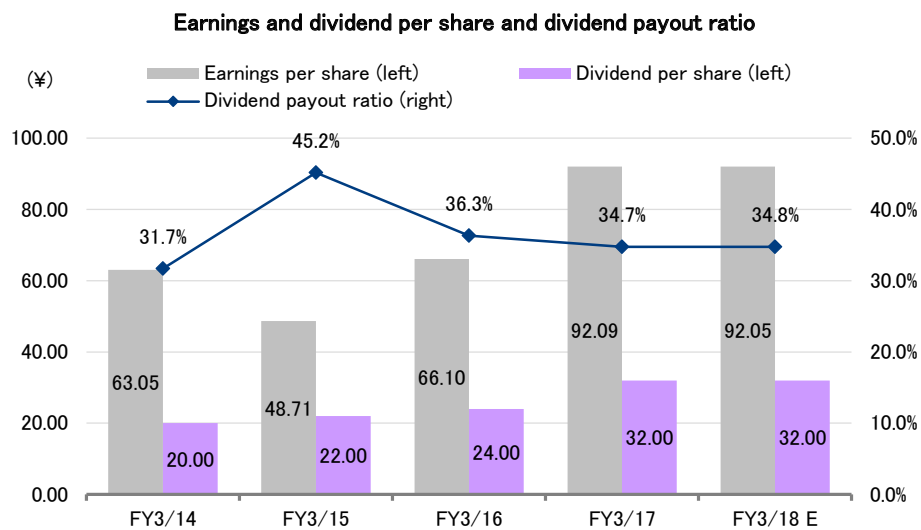
## Shareholder returns

### Projecting a flat dividend YoY at ¥32 in FY3/18

The Company utilizes dividends to compensate shareholders and has a basic policy on shareholder returns of maintaining a dividend payout ratio of 30%.

Itochu Enex raised the annual dividend in FY3/17 by ¥8 YoY to ¥32 (¥13.5 for the interim dividend and ¥18.5 for the period-end dividend) due to the steep increase in EPS to ¥92.09 (+39.3%). This worked out to a dividend payout ratio of 34.8%.

FY3/18 calls for a flat annual dividend of ¥32 (¥16 for the interim dividend and ¥16 for the period-end dividend). Itochu Enex stayed with the period-start estimate at the 1Q announcement. This view reflects a target of ¥92.05 in net profit attributable to the Company's shareholders per share, on par with the previous year. Although 1Q earnings were very upbeat as mentioned above, we think it is still too early to raise expectations of upside in FY3/18. This suggests that dividend outlooks should adhere to the period-start level. We advise against excessive expectations for a dividend increase as the 34.8% budgeted dividend payout ratio exceeds the 30% ratio target. Moreover, even with a modest earnings increase the payout ratio would be unlikely to drop much below 30%.



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

## ■ Information security

Itochu Enex has defined its own personal information protection policy for protecting the personal information of customers. It built an organizational framework, implements and maintains measures, and pursues continuous improvements. It also fosters awareness among directors, employees, and related people and actively promotes 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, buttressing the safeness of 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."



## Disclaimer

FISCO Ltd. (the terms “FISCO”, “we”, mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Exchange, and Nikkei Inc. as to the usage of stock price and index information. The trademark and value of the “JASDAQ INDEX” are the intellectual properties of the Tokyo Stock Exchange, and therefore all rights to them belong to the Tokyo Stock Exchange.

This report is based on information that we believe to be reliable, but we do not confirm or guarantee its accuracy, timeliness, or completeness, or the value of the securities issued by companies cited in this report. Regardless of purpose, investors should decide how to use this report and take full responsibility for such use. We shall not be liable for any result of its use. We provide this report solely for the purpose of information, not to induce investment or any other action.

This report was prepared at the request of its subject company using information provided by the company in interviews, but the entire content of the report, including suppositions and conclusions, is the result of our analysis. The content of this report is based on information that was current at the time the report was produced, but this information and the content of this report are subject to change without prior notice.

All intellectual property rights to this report, including copyrights to its text and data, are held exclusively by FISCO. Any alteration or processing of the report or duplications of the report, without the express written consent of FISCO, is strictly prohibited. Any transmission, reproduction, distribution or transfer of the report or its duplications is also strictly prohibited.

The final selection of investments and determination of appropriate prices for investment transactions are decisions for the recipients of this report.

FISCO Ltd.