

## Independent Directors' Dialogue



## Expectations and Challenges in the Strategic Pursuit of Carbon Neutrality and Well-Being

**Q** How do you view the basic strategies laid out in Obayashi Group Medium-Term Business Plan 2022? And what is your opinion of the Group's sustainability-related initiatives, the strengths required to achieve those initiatives, and the challenges ahead?

**Izumiya** First, I believe that the Obayashi Group needs to make it clearer that construction is at the core of its business. As a company, it is important to increase the profitability and sustainability of the Group's core business. Another vital element is portfolio management. In other words, deciding in which areas to invest limited capital. I believe businesses should consider venture capital as a way to hedge the risk of investing in an uncertain future. On the other hand, I feel that the Group is making steady progress on its sustainability-related initiatives. Social demands are intensifying, however, and the Obayashi Group has to clearly indicate the path it intends to follow to achieve specific numerical targets in a way that links the Group's efforts to resolve social challenges and ensure the sustainability of its business. In such an environment, the Group needs to aspire to improving corporate value

through the comprehensive pursuit of financial value and non-financial value.

**Kobayashi** Obayashi Corporation has focused on ensuring full internal awareness of the 2022 medium-term plan through briefings conducted at main offices and branches nationwide and other means. The aim was to encourage each and every employee to consider the plan's goals as their own. I am looking forward to seeing operational reforms emerge spontaneously from the frontlines in FY2023 as a result of such efforts. It is also vital to expand production capacity in order to strengthen the Company's business foundation, and I believe the technology-focused Obayashi Corporation will be able to secure a competitive advantage by pursuing DX as an engine for technological advancement. At the same time, there is an urgent need to develop and strengthen the human resources required to fuel that engine. I really hope the Company will be able to achieve its performance indicator targets by pursuing these initiatives. Meanwhile, the Obayashi Group's approach to sustainability issues remains consistent, smooth, and clear. For instance, its LOOP50\* concept is more than just a theoretical concept; it is fueling concrete initiatives at each step of the circular use cycle. Forests can lose their ability to retain water if maintained poorly by people, and that can cause major



disasters. However, Japan now faces the serious problem of a decline in its forestry industry—which traditionally carries out such maintenance—due to falling demand for domestic timber and a shortage of workers. To address these issues, Obayashi Corporation is promoting wooden structure and interior projects that use large amounts of forest resources and invigorate the forestry industry. Indeed, Port Plus®, Japan's first fully wooden, fire-resistant high-rise structure is attracting considerable attention. I also admire the Company's consistency in all its efforts, be it strengthening the supply chain in order to promote the circular use of forest resources or exploring the potential for using wood from thinning and wood scraps as energy resources in biomass power generation.

\* Obayashi Corporation's future concept of a city in the highlands and mountainous areas that uses and recycles the rich forest resources in the most effective ways, as well as provide both sustainability and an attractive lifestyle

**Orii** I also feel that the 2022 medium-term plan was carefully conveyed and instilled throughout the Company. For that reason, I view very seriously the fact that consolidated operating income fell below the minimum level stated in the medium-term plan in FY2022, and is expected to do the same in FY2023. It is true that at times, Obayashi has been directly impacted by soaring prices in the wake of unstable social conditions and rising personnel costs, but my understanding is that strengthening the business foundation and accelerating Company-wide transformation is exactly what the Company needs to do to overcome this situation. But I hope the Obayashi Group will not try to strengthen its business foundation first and then tackle transformation. Instead, it should accelerate the implementation of change unfettered by convention, based on a strong awareness that change itself actually strengthens business foundations.

The pursuit of sustainability lies at the core of the Obayashi Philosophy as well as the Obayashi Group's vision and medium-term plan, and the Group is proud to play its part in the building of social infrastructure. In addition to the low-carbon concrete that it pioneered, the Group has been leveraging its advanced technological capabilities for various projects, such as the creation of wooden structures and interiors, WELCS Place®, and the production of green hydrogen. The ability to marry principles and technology is one of the Obayashi Group's major strengths, and I would like to see the whole Group

striving to achieve growth by positioning carbon neutrality and well-being as the sources of value creation and inter-business synergies in each segment.

Obayashi Corporation is also working to promote the active participation of women by appointing three women to senior leadership positions for the first time this spring. When I interact with female employees at the Obayashi Group, I always feel reassured by their ambition and their determination to drive change, and I hope they will demonstrate that power even more effectively going forward. I would also like to see D&I efforts further strengthened under the direction of the Diversity & Inclusion Promotion Department, which was established in 2021. I believe that the active participation of diverse personnel serves as a major driving force for corporate transformation.

**Kato** The Obayashi Group has built a very strong business foundation in the construction business, but technological advancement and innovation never cease. Optimizing the Obayashi Group's overall business portfolio is extremely important for sustainable growth. However, optimizing the order portfolio in the core construction business is also essential for the Group's sustainable growth. It is important to separate construction projects into various categories according to the scale of the work, the degree of difficulty, and any particular characteristics relating to the client or other aspects of the project, and to consistently pursue the optimal solution. However, these factors can alter depending on the external environment, so I would like to discuss them more deeply.

Creating spaces that promote well-being is one of the Obayashi Group's most important missions, so the most desirable outcome would be to use as much carbon-free energy in these spaces as possible. The Obayashi Group's ability to recognize these challenges as important management issues is a strength in itself. The Group is building a pioneering track record in the construction of mid- to high-rise wooden structures, the renewable energy business, and other fields, and I expect its corporate value to increase as it pursues these initiatives.

**Kuroda** FY2022 was a difficult year for the Obayashi Group on the profitability front in light of sharp rises in the price of raw materials and other products. Equally tough profitability-related challenges continue in FY2023, but



Independent Directors' Dialogue

I feel that this environment has propelled the Group to further strengthen the foundation of its construction business. Specifically, the Group has pursued initiatives to ensure the profitability of each individual project and reduce costs across the entire Group. I hope that these determined efforts will continue, even when inflation subsidies. Meanwhile, in the green energy business, hydrogen production and sale in New Zealand is progressing. Although the scale of the business is still small, it can be expected to both expand the Group's business portfolio and help protect the global environment.

I was selected as a member of the Sustainability Committee, which was newly established in FY2022. In addition to the already identified priority areas of decarbonization, safety and security, the Committee also recognized biodiversity, human rights, and other issues as being key. This enabled me to confirm the comprehensive nature of the Group's sustainability-related initiatives. We also reviewed the KPIs and target values for each issue and recommended the adoption of more effective indicators, which were duly implemented. In today's era, all companies are advocating sustainability initiatives as a matter of course, so the Obayashi Group needs to bear in mind the fact that stakeholders will start questioning the effectiveness of those measures more earnestly going forward.

**Q** How do you assess Obayashi Corporation's current efforts to ensure the board's effectiveness?

**Izumiya** The mission of the Board of Directors is to achieve sustainable business growth and improve medium- to long-term corporate value as entrusted by shareholders. On the governance front, governance involves the defensive guarantee of transparency and fairness and the offensive pursuit of aggressive and bold action. Achieving results through the pursuit of both defensive and offensive governance will increase the effectiveness of the Board of Directors. To achieve these aims requires extensive discussion. In fact, you could say that this act of extensively discussing issues is what the monitoring and supervisory functions of the Board of Directors are all about.

**Kobayashi** With respect to composition of the board, the majority of the independent directors are women, but I believe diversity is ensured not only in terms of gender, but also in terms of the variety of expertise and experience represented. Furthermore, discussions at advisory bodies to the board, such as the Recommendation Committee and the Remuneration Committee, are extremely active. Following major revisions to the remuneration system in FY2021, in FY2022 the committees clarified the criteria for the appointment and dismissal of the president and the selection of successor candidates. Directors are given multiple training opportunities. I find the annual training that I receive together with executive officers on compliance with Japan's Antimonopoly Act to be

particularly detailed and extremely thorough, and I feel that I am still able to grow through my work.

**Orii** If we look at the board's effectiveness evaluation over time, I think that the PDCA cycle of identifying issues, forming countermeasures, and confirming their implementation and effectiveness in the next fiscal year's evaluation is working well. I also feel that everyone who is actually involved in the Board of Directors is invested in making this system function better as time goes on. However, expectations and the responsibility to demonstrate the functioning of the board are growing all the time. I would like to utilize the newly established Directors' Roundtable Meeting and other venues to facilitate in-depth discussions of vital themes in Board of Directors' meetings. With that aim in mind, I would like to increase contact points with construction sites and with employees.

**Kato** I feel that the Board of Directors is always working to increase its effectiveness. Discussion on essential challenges toward improving corporate value and achieving sustainable growth for the Obayashi Group is now being pursued in a much more open and in-depth way than ever before. The Directors' Roundtable Meeting has only been in existence for a few months, so I hope that it will become a key venue going forward. The most important thing is that each director maintains his or her own unique perspective and discusses any issue in a sincere and determined manner. I will always discuss what is best from the perspective of the Obayashi Group's stakeholders.



**Kuroda** I have served as an independent director at a number of companies, and I feel that Obayashi Corporation explains things carefully in advance so that more time can be spent on discussions rather than explanations at board meetings. In that respect, the operation of the board is well balanced. I also think the establishment of the Directors' Roundtable Meeting is a unique way of enabling us to fully discuss themes relating to the improvement of medium- to long-term corporate value. The roundtable nature of the gathering enables us to have free and open discussions. However, measures for improving medium- to long-term corporate value should

also be discussed in Board of Directors' meetings, so this point should be considered when setting the agenda for future board meetings.

**Q** How do you view the expectations and challenges that the Obayashi Group is facing?

**Kobayashi** I think one of the issues at Obayashi Corporation is that there are very few women in management positions in core business operations. The proportion of female managers is one of the highest in the industry and there are a number of senior female leaders, but I think there is still some way to go. I have spoken to many female employees, and I feel that the female employees at Obayashi Corporation are not only extremely talented, but are also very passionate about their work. I was impressed to see so many women with strong communication skills, which is considered a vital attribute for a future leader regardless of gender. When it comes to empowering women, it is important not only to help support the balance between work and family life, but also to provide systemic career support tailored to each individual and to increase the number of female leaders appointed internally because I expect that will help revitalize the Company as a whole in the long run.

**Orii** I participated in OBAYASHI VISION SHOWCASE 2022\* held in the fall. I witnessed numerous technological developments designed to support social infrastructure and human and environmental health as well as the extraordinary enthusiasm displayed by all employees involved in the development. This heightened my expectation that the implementation of these advanced initiatives would drive sustainability. If the whole Group unites behind its aspirations and avidly commits both thought and action to creating value that contributes to societal sustainability, then the Obayashi Group will naturally grow toward realization of its long-term vision and enhance its own sustainability.

\* An event held to commemorate the 130th anniversary of the founding of Obayashi Corporation. It showcased Obayashi Group technologies and initiatives in various fields spanning construction and peripheral areas to realms further afield into the future, both in the event venue and online.



**Kuroda** I also participated in OBAYASHI VISION SHOWCASE and felt the strong client interest in wooden structures. I expect this interest will enable Obayashi to build new architectural standards through co-creation with clients, contribute to resolving environmental issues, and establish a competitive advantage at the same time.

**Kato** I expect great things to come from the Group's dedication to increasing social value, their efforts to improve technical capabilities, and their attentive approach to the treatment and training of people. However, I do get the impression that they tend to align themselves with their peers and that something is lacking in their desire to beat competitors, in their determination to pass on even a little of the increase in costs to the client, and in their commitment to profits and the Company share price. Everyone needs to remain acutely aware of what needs to be changed and what needs to stay the same, and to debate those issues.

**Izumiya** Obayashi Corporation's technical prowess and commitment as a contracting company are clear strengths that never disappoint a client's expectations. TOKYO SKYTREE® and ES CON FIELD HOKKAIDO exemplify that. However, with competition intensifying, it would be unwise to ignore the fact that the Company's profitability has declined significantly due to issues such as construction capacity, cost increases, and the insufficient commitment to increasing market share. Obayashi Corporation might need to review its management KPIs to enhance the sustainability of its own business.

Furthermore, the value that the Obayashi Group's core construction business provides lies in the creation of environment-conscious, enriching spaces. That value is created by technology, so the Group must be strong in technology. That's why the Company is expected to improve its technological capabilities by investing in human resources, intellectual property, DX, and other areas, and to establish corporate value creation processes that improve future orders and profitability. There are many challenges that need to be addressed, but I am confident that the Obayashi Group has the power to overcome any difficulties and achieve success.