

# Adoption of Environmental, Social, and Governance (ESG) Initiatives as the NYK Group's Next Growth Strategy While Moving to a New Stage through Total Innovation

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## Keep the Logistics Lifeline Open

There is no doubt that many people take the maritime shipping and logistics industries for granted in much the same way as water and air. However, as infections by COVID-19 spread rapidly throughout the world, some regions are struggling with ongoing increases in cases even now. This situation has brought home to many the great social responsibility borne by the maritime shipping and logistics industries, which usually operate unnoticed, expressed by the NYK Group's mission statement, "Bringing value to life." Take air cargo services for example. With passenger services reduced or suspended, the transport of medical supplies, such as pharmaceuticals, masks, and surgical gowns, has now fallen to Group company Nippon Cargo Airlines Co., Ltd. (NCA). As cities go into lockdown one after another around the world, human movement has been severely restricted. Personnel needed to operate transportation services have

been assigned, and we transport freight to its destinations, despite the risk of infection. I am sure you will have seen many news reports of shortages of masks and medical supplies, mainly in Japan. Without the efforts of NCA, Japan may well be in an even worse situation. The same goes for container ships that transport living essentials, dry bulkers that convey foods such as soy and wheat, and tankers that deliver energy resources. The NYK Group operates over 750 vessels worldwide, staffed by nearly 20,000 crew members, which continue to carry the cargoes essential for society. It is our duty to keep the logistics lifelines open, upon which society depends, while making people's daily lives safer and more secure. In light of this, I would like to once again encourage all employees of the NYK Group to take pride in their work and carry out this great mission and responsibility faithfully.

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## Hikawa Maru Evoking a Sense of a "Safety-" and "Innovation-Oriented" History

In writing this president's message, I visited Hikawa Maru, which is moored at Yamashita Park in Yokohama. I have made the trip many times before. Built in 1930, Hikawa Maru was operated as a passenger ship on NYK's Seattle service, carrying not only cargoes but also transporting many people as well. It even served as a hospital ship during World War II. Hikawa Maru was designed to withstand harsh winds and waves, drawing lessons from the sinking of the Titanic in the Northern Atlantic. It was designed with 10 watertight

compartments that could be sealed with waterproof sliding doors in the event of inundation. The vessel was state of the art, brimming with technologies that were considered innovative at the time. The extremely high level of safety is evident even to observers today. Looking at Hikawa Maru with its many innovative technologies designed to ensure absolute safety, I had a strong sense of the NYK Group's "Innovation-Oriented" corporate culture and its determination to be a leader of the times.



## Hitoshi Nagasawa

President, Representative Director,  
President and Chief Executive Officer

### Career at NYK

After joining the Company in 1980, Hitoshi Nagasawa became the general manager of LNG Group in 2004, a corporate officer in 2007, and a managing corporate officer in 2009. He has been in charge of the Energy Division since becoming a director in 2011 and has chaired a committee overseeing the strategies of bulk shipping since being appointed as an executive vice-president corporate officer in 2018. Mr. Nagasawa was involved in the Company's acquisition of upstream interests in the LNG business and development of the offshore business.

The NYK Group uses its diverse human resources drawn from many countries worldwide as a strength, bringing them together in an open corporate culture based on respect for people. Here, a process of repeated “chemical reactions” among people has sparked innovation that has enabled the Group to continue operating in the core maritime shipping and logistics industries. If we can continue to be consciously innovative as a group and parlay this into real action, then we should be able to survive for another 150 or 200 years. Conversely, I am keenly aware of the danger that, if we lose this

virtue, we might be eliminated from the market. Amid a rapidly changing society in an era of rising uncertainty that clouds the future, rather than merely toying with change, we must act as a united group and fully confront the many issues that appear before us while aiming to be a sustainable business through Total Innovation.

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## Utilizing ESG Initiatives to Become the Preferred Choice of Customers

ESG is the foundation for the NYK Group’s aspiration to become a sustainable business entity. The logistics industry, and not only ships, uses a large amount of fossil fuels, which certainly has an impact on the environment. This puts the industry at a disadvantage in terms of responding to climate change and preserving the environment, and we need to understand that the industry is under constant pressure to improve. I believe that, to carry out its social mission, the Group must not only keep the logistics lifeline open but also lead the way in responding to environmental issues. In my opinion, this will become one of our growth strategies going forward. Rather than simply falling into line with other companies and following the mainstream, I am convinced that our way forward is to become a front runner, driven by various innovations. It is with this in mind that we started the NYK Digital Academy, an in-house training program for skills development, in 2019, inspired by the importance of human resource development for sparking innovation for new value creation.

We have also integrated ESG perspectives into our management strategies. I am constantly communicating to the directors and executive officers involved in decision-making that I want them to include ESG perspectives in their judgments as well as the conventional financial perspectives when considering investments. We now have some actual cases of investments being made through comprehensive judgments emphasizing ESG perspectives that will produce a competitive advantage over the medium to long term in addition to financial viability. To give an example, there is a project for dry bulkers fueled by liquefied natural gas (LNG). The dry bulk business is under immense pressure from excess capacity supply, making it difficult to achieve high profits. There was some

disagreement within management over whether we should build the more expensive LNG-fueled ships, but we decided to make the investment after giving weight to the future potential of dry bulkers that are kinder to the earth’s environment. We might have put off investment and watched global trends carefully; however, this led us to fall behind in the field of LNG-fueled dry bulkers, leaving us at a disadvantage in terms of preserving the environment. Building up a track record is also a very important factor in differentiating ourselves in the maritime shipping industry.

In sales activities, we emphasize that the Group should compete not only on price but also by confidently offering high-quality modes of transportation that are highly conscious of the environment and safety. For example, being able to transport a finished vehicle while reducing CO<sub>2</sub> emissions by 20%, compared with doing so via a conventionally fueled vessel, also seems like a tangible benefit to the customer.

When meeting with members of top management of other companies, I find that ESG comes up as a topic of interest extremely frequently. These days, our customers are also anxious to partner with companies taking a firm approach to ESG initiatives and the Sustainable Development Goals (SDGs). The NYK Group can become the preferred choice of many customers as a company that is taking serious, concrete action on social problems, by making use of innovative technologies and providing modes of transportation that are highly environmentally conscious. We plan to increasingly approach customers with the idea that partnering with the Group will enable them to engage in cutting-edge, sustainable business operations.



## Moving toward a Deep Understanding of ESG and Creating the NYK Group ESG Story

I believe that the true value of a company should be measured not by how long it has been in operation, but rather by how tirelessly it has strived to continue to fulfill its social responsibility across eras. Companies that present a sincere stance naturally attract empathy and support. I feel that the ESG issues in which people around the world are engaging need to be at the foundation of all of our growth strategies going forward. Moreover, ESG is by no means some kind of window-dressing; rather, it is an essential factor for ensuring the NYK Group's sustainability—a growth strategy and a differentiation strategy. This must be accepted by all Group employees. In April 2020, we established the Framework for promoting ESG management, under which I will personally head the Group's internal and external efforts to place ESG at the center of management. We are also focused on creating the NYK Group ESG Story, which presents its ESG initiatives. This initiative is intended to share the direction that we should be heading in, as well as to enable the entire Group to engage with a common awareness (see page 17 for details).

It is also important to disclose information inside and outside the Group to show how serious our ongoing efforts are. In addition to quantitatively measuring our progress, we need to provide a careful explanation of our specific route forward. Setting quantitative targets should enable us to further align the vectors of each business site. Currently, the Group is disclosing various qualitative and quantitative ESG data, such as management's environmental target of reducing CO<sub>2</sub> emissions by 30% in fiscal 2030 and by 50% in fiscal 2050, compared with fiscal 2015 levels. Beyond properly disclosing our progress on these targets each year, the 2021 edition of the NYK Group ESG Story will describe the measures for raising our level of achievement and the emergent issues presented in the 2020 edition. We will continue to present our annual improvement measures via subsequent editions of our ESG Story. In this way, I want to enable our stakeholders to evaluate the Group's serious and continued efforts.

## Heading toward a Sustainable Business Structure for Growth Strategies Based on ESG Initiatives

Under our medium-term management plan, we have presented four key initiatives, including ESG, in line with the theme of "Digitalization and Green." This framework has not changed significantly; however, from now on, rather than placing ESG on the same level as other key initiatives, we will treat it as a compass that shows management's long-term direction while drawing up medium-term business strategies looking at a three- to five-year period to increase the NYK Group's corporate value. Right now, we are undertaking structural reforms of the dry bulk business, which has a substantial downside risk to earnings from high-cost charters. Once these reforms reach a certain stage, we will be able to formulate a long-term strategy for the next leap forward. ESG initiatives will be the starting point when we begin devising this strategy. Among the themes of "Digitalization and Green" in the medium-term management plan, I see Digitalization as an important tool for accelerating our initiatives on the environment. For example, we are currently working with four laboratories, including Monohakobi Technology Institute Co., Ltd., on a project using big data and AI to analyze optimal operations and weather phenomena. If we can use the fruits of this project to improve fuel consumption, we will be able to reduce our CO<sub>2</sub> emissions. Digitalization is also applicable for promoting workstyle reforms and responding to risks that have emerged in the past few years around information management and logistics system security. Furthermore, we expect to be able to create new value by combining the various data that we

receive from our existing businesses with ESG concepts. On the other hand, under the Green aspect of the medium-term management plan, we are working to commercialize green businesses based on the theme of renewable energy. This involves organically linking our sales and engineering divisions and making use of the global network we have developed over many years to collaborate with leading partners in Japan and overseas. Among these collaborations, we have made steady progress in offshore wind power, with proactive support from the Japanese government following the enactment of a new law to promote offshore wind power in 2019. With regard to fuels for shipping, we will also step up our research and development efforts in such areas as hydrogen and ammonia. Decarbonization cannot be achieved by the NYK Group alone. However, by cooperating with various stakeholders to make progress toward the same target, we can contribute to achieving it as early as possible.

To report on our progress regarding the medium-term management plan, against our fiscal 2022 target for consolidated recurring profit of between ¥70.0 billion and ¥100.0 billion, in fiscal 2019 we recorded recurring profit of ¥44.4 billion after factoring in a recurring loss of ¥15.5 billion in the Air Cargo Transportation segment. Excluding this loss, recurring profit was almost ¥60.0 billion, within reach of our aforementioned fiscal 2022 target. However, the impact of COVID-19 is significant, and amid major uncertainties, we are



projecting recurring profit of ¥20.0 billion in fiscal 2020. For the last 10 years, our shareholders' equity has been negatively impacted, so our first priority is to establish a sustainable capital structure. If we can generate recurring profit of between ¥70.0 billion to ¥100.0

billion, then our net profit will be around the ¥50.0 billion level. After paying stable dividends in accordance with profits, our duty at this time is to quickly return shareholders' equity to an appropriate level and then look to draw up larger strategies.

## Transforming Highly Volatile Businesses into Businesses Realizing Stable Earnings

The NYK Group has steadily built up business with stable freight rates based on medium- to long-term contracts. On the other hand, we are working on structural reforms for businesses operating in highly volatile market conditions, such as the dry bulk business, the container shipping business, and the air cargo transportation business, and these efforts are gradually beginning to produce results. In the container shipping business, we established Ocean Network Express Pte. Ltd. (ONE) with other Japanese shipping companies, and saw it begin operations in fiscal 2018. While losses for ONE were unavoidable in fiscal 2018, its first year of operations, the company suddenly turned a profit. Given the significant impact of the spread of COVID-19 on global supply chains, ONE's earnings forecast for fiscal 2020 is still undetermined. However, the alliance with other shipping companies that gave rise to ONE has stabilized the freight rate market more than previously, while achieving a profitable structure in just one year, a truly remarkable feat.

In the dry bulk business, where a mismatch between freight on the income side and vessel charter periods on the expense side is driving market volatility risk, we are working to increase market

resilience by eliminating this mismatch through a process of encouraging early returns of high-cost chartered vessels. Dry bulk is said to account for around half of global seaborne trade, which is estimated at 12.0 billion tons annually. Most of these dry bulk cargoes are under short-term contracts. Some are of the opinion that we should deal only in long-term contracts. However, since long-term contracts make up only a part of dry bulk cargoes, I do not share this view. By allocating short-term chartered vessels to short-term contracts, we can avoid market risk while utilizing our strengths, such as our operational expertise and ability to combine cargoes that reduce our percentage of ballast voyages. These measures will allow us to compete on short-term contracts, and we are already seeing results. We are only part way along in shifting to this track, but once this reform is complete, we can expect the dry bulk business to begin generating stable profits in the same way as our car carrier and energy businesses. The direction of our initiatives is correct, and we are already making progress. It is for this reason that I believe we must move now to generate powerful momentum on the theme of ESG as our next step.

## Further Enhancement of Corporate Governance

Since Japan declared a state of emergency over COVID-19 in April, I have worked with all chief executive officers—almost every day, including weekends and national holidays—to ascertain and share the status of our business sites. When emergencies occur, it is important at the minimum to have a system for gathering information quickly, and I was able to confirm that the NYK Group has established a strong corporate governance system.

As a first step in improving governance, we will promote improvements in the decision-making process. The Board of Directors makes decisions on matters above a certain level. The forum for decision-making has been changed from the previous Committee of Corporate Officers, which had 28 corporate officers, to a newly established Management Meeting of nine members comprising the president, chairman, and chief executives. Thanks to the reduced

membership of the Management Meeting and the sharing of all internal information among its members, discussions are extremely active and intense, while the transparency of the decision-making process feels markedly improved. The title of corporate officer has been changed to executive officer, as the officers who are not on the Management Meeting are intended to focus on business execution (see page 66 for details).

Management Meeting members are always expected to express their agreement or disagreement with management proposals, including their reasons, and I make the final decision in my role as president. All statements are recorded in the minutes. The accumulation of these minutes should serve as a textbook for future management teams. By continuing with this system, we should further improve the decision-making process. In addition, it is naturally transmitted to our employees that the management team is thoroughly discussing matters, which has a good influence on employees' attitude and approach to work. We will completely eliminate opacity and show everyone inside and outside the Company a more transparent, more serious decision-making process. I believe this is very important for increasing the NYK Group's corporate value in

both times of emergency and ordinary times.

Furthermore, from a perspective of supervising business execution, the opinions and guidance of our outside directors will become more important. At Board of Directors' meetings, outside directors require the execution side to give explanations on how they envisage and manage risks, and how they will respond in the event that they materialize. For example, with regard to climate change risk, we received a question about how we are analyzing this risk and the future business model of the Energy Division amid uncertainty over the handling of fossil fuels. We have had many very candid opinions stating that our recognition of the issue is poor, and that we ought to obtain opinions from third-party experts. It is true to say that we overlooked several points, and we have therefore completely taken on board the opinions we received. Moreover, in light of past incidents of inadequate business operations, we have received guidance to the effect that compliance ought to be managed in not only sales divisions but also across the Company by corporate divisions. Such guidance has made a significant contribution to improving the NYK Group's governance.

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## The NYK Group's Latent Strengths and Total Innovation

Prior to my appointment as president in 2019, I was in charge of the Energy Division for many years. During that time, I created an environment where my team worked cheerfully and energetically while sticking to results in order to contribute to the NYK Group's earnings. As president, I still stick to results, but one thing that has fundamentally changed is how I now think constantly about all of the Group's stakeholders, including shareholders, instead of concentrating on just its employees. As I have become more conscious of a wider range of stakeholders, my sense of responsibility has also grown considerably.

As part of this, I would like all employees to see the Group as a great stage upon which to express themselves to the best of their ability. If we can make such a group, it will surely be full of energy, happiness, and enthusiasm, giving rise to a sense of achievement. The entire Group will certainly head in a good direction. The NYK Group has a strongly established culture in which we naturally support each other in times of trouble, without trying to hold one

another back. I would like us to treasure this wonderful culture that has been left to us by our predecessors. The sight of Group employees working cheerfully and with motivation is the best moment in my day. At the same time, we are also making revisions to the personnel system, as I suspect that we are not drawing out the full potential of the Group's employees. I would like the management team and our employees to take on their challenges seriously at all times. If we discuss matters seriously as we work, I believe we will get the right results every time. Following the spread of COVID-19, we introduced a telecommuting system and, even though we are faced with a situation that makes relieving crew members difficult, our fleet of over 750 vessels continued their voyages without causing any great turmoil. Cargo airlines also operated at full capacity, and even when emergencies occurred, we took safety countermeasures, managed employee health, and showed ourselves once again to be an amazing corporate group with a strong chain of command, including at Group companies around the world. On the other hand, as working

from home unexpectedly took root due to the spread of COVID-19, the workstyles of mainly our onshore personnel have changed considerably. Now, we will address the issues of how to incorporate this new workstyle as a Company system and how we can foster a corporate culture of active communication.

Assuming that vaccines and treatments will be developed at some stage in the near term, we are envisaging a scenario in which we gradually return to relative normality between winter 2020 and 2021. However, considering the possibility of second and third waves of infection, we cannot be naively optimistic. We may be obliged to revise the figures of both our earnings forecast and our medium-term management plan financial targets due to the impact of COVID-19. Nevertheless, the direction of the strategies presented in the medium-term management plan and the direction that I personally wish to take are absolutely aligned, and we will proceed based on our current policies. Just to reiterate, ESG is an issue that we should

address as a member of society, as well as an approach that we should thoroughly promote as a growth strategy to be explored by the NYK Group. Even when emergencies occur, you can count on the Group's latent strengths, as it continues to transport the cargoes that society needs, and on its Total Innovation inspired by ESG. We would like to ask for your continued support going forward.



**Hitoshi Nagasawa**

President, Representative Director,  
President and Chief Executive Officer

