



**NIPPON STEEL &
SUMITOMO METAL**

**Nippon Steel & Sumitomo Metal Corporation FY2018, 3rd Quarter IR Briefing
(Held on February 6, 2019)
Summary of Q&A**

Note: Based on information available as of the date of the IR Briefing

Representative from NSSMC

Katsuhiro Miyamoto, Representative Director and Executive Vice President

Hidetake Ishihara, Executive Officer and Head of Accounting & Finance Division

Q What are the factors behind the forecast decline of ¥32 billion in business profit in the 4th quarter relative to the 3rd quarter? What is your current underlying profit level, excluding the impact of a drop in production caused by not only natural disasters but also your operational troubles and other factors?

A NSSMC's recording of fixed costs tends to be concentrated in the 2nd and 4th quarters. That is a major reason for the ¥32 billion decline in the profit forecast. Concerning actual factors, a decline in international steel prices has a negative impact while an increase in production volume and cost improvement are positive factors. In total we are not expecting any significant factor to cause a profit decline in the 4th quarter relative to the previous quarter.

Our underlying profit is considered to be around ¥170.0 billion, based on the business profit forecast of ¥172.0 billion for the second half of FY2018 and assuming little temporary profit and loss, including an inventory valuation gain. However, let me emphasize that this amount of ¥170.0 billion includes the impact of a drop in production caused by operational troubles. I wish I could give you our underlying profit capability based on our inherent normalized production level, but I will be able to do so only after the production level actually recovers.

Q Please explain the cause of trouble and measures taken to address the productivity decline at Oita Works' blast furnace. Also, you mentioned a drop in production of 200,000 tons caused by factors other than the blast furnace troubles at Oita and Wakayama. What are their causes? In addition, have you solved the minor internal troubles you mentioned at the 2nd quarter IR briefing?

A Oita Works' blast furnace began to encounter problems around the 2nd quarter but did not suspend tapping of molten pig iron, yet at around 10-20% less productive levels. Its operation has already stabilized and is now back to normal productivity. Given the high capacity of this blast furnace, this trouble has resulted in a drop in production of around 300,000 tons.

While it is difficult to identify specific causes, we understand that a change in the quality of raw materials triggered the operational malfunction. For example, when the pre-treatment facilities for raw materials, such as sintering machines or coke ovens, suspend operations due to repairs and for other reasons, the blast furnaces use sintered ore or coke, which are stored in the yard and may therefore contain more water or be of smaller grains. Use of these materials requires adjustment to the operational conditions of the blast furnace. If it is not well controlled, the furnace operation can deteriorate.

In the case of the Wakayama Works, the No. 5 blast furnace had been scheduled to blow out and switch to the new No. 2 new blast furnace in the 4th quarter. The end of its long service life caused instability but production is expected to stabilize after the smooth start-up of the new furnace.

An additional drop in production of around 200,000 tons, beside the blast furnace troubles at Oita and Wakayama, was also caused by the malfunction of other blast furnaces, but on a much smaller scale. This was mainly due to poor control of the impact of a change in raw material conditions.

The minor troubles I explained at the 2nd quarter IR briefing have been reduced with proper measures being taken.

Q Let me ask whether you can increase production volume in FY2019 based on the aspects of both supply and demand. What is your outlook for steel demand, given changes in the economic environment including China? On the supply side, you are determined to increase forward investment in repairs. Will you explain your views on a potential recovery in production volume for FY2019?

A At the moment it is difficult to discuss the demand outlook for steel for FY2019. For example, there are various views on the outlook on China, as automobile sales are declining there while the government is implementing economic stimulus measures. The domestic demand outlook also warrants careful monitoring, as demand is basically likely to be firm but there are more uncertainties in the short term.

On the production side, we have been struggling to exceed the level of 10.5 million tons in quarterly crude steel production on a non-consolidated basis. More recently, the operation of our blast furnaces has been stabilizing and other troubles are on a declining trend. If we can achieve a smooth start-up of the new Wakayama No. 2 blast furnace in mid-February, I believe that our production volume will be higher next fiscal year than this year.

Q Brazil's collapsed dam, associated with Vale S.A., may generate the risk of a rise in iron ore prices. Prices of auxiliary materials, such as scrap and alloys, and other material procurement costs, are also staying at high levels. Against this background, what is your view regarding your margin improvement in FY2019?

A Vale has already announced a peak production cut of 40 million tons of iron ore and there is also unconfirmed information regarding an additional 30 million ton production cut. The total of 70 million tons could represent over 4% of global marine trade volume of iron ore. However, unlike hard coking coal, there is extra production capacity for iron ore. We intend to carefully monitor the supply-demand balance.

From the first half of FY2017 to the second half of FY2018, we are projecting a margin improvement of ¥2,700 per ton, including the impact of a rise in prices of auxiliary materials, such as scrap and alloys, and higher logistics costs. This level of margin improvement, however, is not sufficient to realize appropriate sales prices to maintain continuity in supply, as I mentioned on previous occasions. We will continue our efforts aimed at realizing the appropriate sales prices to maintain continuity in supply. The domestic steel market is currently solid but we will aim for a further improvement in prices while continuing to carefully watch changes in the environment such as an increase in the cost of raw materials as well as the market trend of steel products by electric furnace and imported steel products. Concerning the international market, we believe the steel market prices normally tend to move somewhat in line with changes in the cost of raw materials and other items.

Q Out of the downward revision of ¥20 billion in business profit for FY2018 from the previous forecast as of November 2, you mentioned that ¥5 billion will be caused by group companies. How much of this is attributable to the impact of the change in the business environment of the Chinese market and the impact of downward earnings revisions by OVAKO AB (Sweden)?

A OVAKO has reduced its earnings forecast by €16 million, from €35 million to €19 million, partly due to the one-off impact of the introduction of the Worldwide Harmonized Light Vehicle Test Procedure (WLTP). Their downward revision on a pretax basis is even greater. This is a major reason for the decline in the profit forecasts of group companies. There is little change in forecasts for our group companies in China.

Q The stock price of Vallourec S.A. (France) dropped substantially in the 3rd quarter. Did you post an impairment loss in the 3rd quarter? If not, are you planning to do so in the 4th quarter?

A We did not post an impairment loss on our Vallourec shareholdings in the 3rd quarter. The method used for the valuation of securities is the reversal method at the end of each quarter. However, if valuation losses are considered to be temporarily caused by fluctuation in stock prices, an impairment loss does not need to be reported. We believe that is the case for Vallourec. We would rather avoid the case where the stock price recovers from the decline in the 3rd quarter by the end of the fiscal year and valuation needs to be reversed again. Concerning year-end accounting, we plan to

prepare IFRS-based accounting statements from FY2018. If Vallourec's stock price drops substantially at the year-end, the loss will be recorded in the "Other comprehensive income," without affecting profit attributable to owners of the parents.

Q Vallourec is also in a difficult financial position. How are you planning to deal with Vallourec going forward? Is there any possibility of a change in your relationship in the collaborative business with Vallourec, including operations in Brazil?

A NSSMC and the French public investment institution Bpifrance Participations own a little short of 15% of Vallourec's shares each. Bpi, recognizing the importance of showing their commitment to the market, has dispatched an executive to Vallourec and is involved in restructuring. We understand that Vallourec is working on their main challenge, which is to rationalize their operations in Europe. Our joint venture in Brazil is focusing on cost reduction.

End

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