NIPPON STEEL

Nippon Steel Corporation, First Quarter FY2020 IR Briefing
(Held on August 4, 2020)
Summary of Q&A

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

Presenters
Katsuhiro Miyamoto, Representative Director and Executive Vice President
Hidetake Ishihara, Managing Executive Officer
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Q Are you expecting to record an operating loss on a non-consolidated basis in the second half of fiscal 2020, while forecasting consolidated business profit of ¥30 billion?

A As you stated, we are currently expecting an operating loss on a non-consolidated basis in the second half. On a consolidated basis, however, our group companies in the steel business and those in the non-steel segment are projected to generate a profit and contribute to the consolidated business profit of ¥30 billion. The main reasons for projecting a continued non-consolidated operating loss in the second half are an insufficient recovery in output volume and a half-way improvement in the product mix.

Q Is there any risk of recording an additional impairment loss or another huge loss? If you are planning additional structural measures, will you tell us when you will make such a decision and announcement?

A As an individual disclosure item, we will post a loss on disposal and demolition associated with the shutdown of upstream facilities in the Kyushu Works Yawata area (Kokura) in the second quarter. As we proceed with the structural measures for production facilities, we will post losses on inactive facilities for other facilities on an individual basis at the time of implementation. Other than such losses on inactive facilities, we are not assuming any major impairment loss.

In the midst of this harsh business environment, we may bring forward some structural measures or add more measures. These will be promptly disclosed when they become concrete plans.

Q Please provide details of the ¥104.0 billion profit deterioration at group companies in FY2020 forecast compared to FY2019.

A In general, profits at domestic and overseas re-rollers greatly deteriorated due to a decline in production output. Operational support companies are also experiencing profit deterioration, caused by a decline in the amount of business. Moreover, mines and EAF operators are also experiencing a profit decline of over a ten billion yen each.

Q You said that electrical steel sheet is in short supply. I thought that your investment plan was decided, based on close dialogue with customers. Will you explain why such a capacity constraint happened? Will you also elaborate on why you think that customers would switch procurement from Chinese products to your products after you build up more capacity?

A We closely consult with our customers but believe that stronger-than-expected needs for a reduction in CO_2 emissions and energy saving have boosted demand for motor vehicles. We are carrying out an investment plan to expand capacity for electrical steel sheet but there will be a certain in-between period when we will not have sufficient supply on time. Taking comprehensive product value, quality, and other factors into consideration, we firmly believe that we are the world's top maker of high-end electrical steel sheet.

Q What are your assumptions for material prices and product prices in the second-half forecasts?

A The market price of iron ore is currently rising and the current level is incorporated in the second-half forecasts. Coking coal prices are expected to slightly increase due to an anticipated recovery in demand in the second half. We have therefore incorporated some increase in major material costs in the second half, compared to the first half.

Concerning product prices, the overseas product market has been recovering from its bottom in April to May. Our shipment-based product prices are rising from the bottom in June and our anticipated prices for the second half are based on our expectation of a flattish market from the current level. In sum, our assumptions are higher raw material costs, flattish product prices, and therefore a decline in spread in the second half.

Q Amid the current COVID-19 situation and weaker demand for automobiles, is it difficult to ask for a correction in long-term contract prices when negotiating with automakers?

A Despite being affected by COVID-19, we will not change our determination at all to ask our customers to reflect our product value and contribution in product prices, and to secure an appropriate margin that enables sustainable investment in facilities and R&D. The situation is tough but we will conduct negotiations in an orderly way.

Q You announced the relining of a blast furnace in Nagoya Works in June. Why have you decided to reline the facility, for which you just recorded an impairment loss in February?

A We announced in June that we would spend a little less than ¥50 billion to reline the No. 3 blast furnace at thein Nagoya Works. When considering structural measures for production facilities, we believe it is extremely important to establish profitable and competitive integrated steelworks. Our Nagoya Works is superior in terms of its organization and capability in integrated manufacturing of high value-added products. When we recorded the impairment loss, we incorporated maintenance and renewal of the current facilities, including the blast furnace relining we announced in June, and still assumed positive future cash flow. The booking of the impairment loss therefore does not necessarily rule out investment going forward. We intend to further improve costs and prices and make other efforts which had not been incorporated in the cash flow assumptions back in February because there was no assurance of implementation back then. By doing so, we are seeking to build up more profit and cash flow and make the Nagoya Works a core steelworks mainly for high-grade steel.

Q You have decided to invest ¥70 billion in electrical steel sheet. Will you explain how much this investment will contribute, relative to the present output and profit level? Please also talk about further investment plans if there are any.

A I cannot specifically state the amount of increase in volume or profit with regard to capital spending in electrical steel sheet. However, we decide the investment plan based upon discussions with customers and believe it will result in the achievement of a sufficient profit level. We used to generate high profits in electrical steel sheet but prices have come down, as Korean and Chinese steelmakers' began producing it, so it is now becoming difficult to make a profit. We decided on the ¥70 billion investment in order to get out of the current situation as well. Additional investment is under consideration and will be announced once it is fixed. We will strive to achieve top-level profit in electrical steel sheet by building a rock-solid production system, including additional investment.

Q Please describe the consumption trend for steel products in Japan from the first half into the second half and how you are thinking about your own moves in production and shipments.

A Japan's consumption of steel products is projected to increase by 1.6 million tons in the second half relative to the first half, supported by a 1.7 million ton increase in the manufacturing industry. Meanwhile, Nippon Steel's shipments are projected to increase by 1.5 million tons, underpinned by a recovery in domestic demand mainly from the manufacturing industry and a pick-up in export shipments. While customers' inventory adjustments appear to have had a great impact on the shipment decline in the first half, it is hard to predict the extent of the recovery that can be anticipated from the inventory adjustments in the second half.

Q **Please explain why sales of seamless pipes dropped significantly in the first half.**

A The seamless pipe business inherently has a high ratio of long-term contracts. Given current falling oil prices, some orders were canceled. In terms of output, shipment volume in the first half decreased by about 30% year-on-year, but shipment of super high-end products decreased by only about 10%. Therefore, the decline in profit in the first half is actually much less than the decline in overall output.

Q **What are the key points in deciding to resume operation of the blast furnaces in banking in a volume recovery phase in Japan?**

A Our basic strategy is to maximize marginal profit by upgrading our product mix, in addition to realizing appropriate scale of fixed costs by pursuing an optimal production framework. If low-profit orders recover, we will not necessarily lift the banking of blast furnaces simply because marginal profit can be made. Banking is the means with the least cost demerit in the case of production adjustments. Conversely, in a volume recovery phase, we will first restore the productivity of blast furnaces and their blowing-stop time. After taking these steps, we will consider whether to lift the banking, taking into consideration the potential amount of orders for products with high marginal profit.

Q **Your large-scale structural reform at this time entails downsizing the production framework in Japan and expanding business overseas at the same time. I understand that immediate downsizing in Japan is most crucial but will you explain the change in output and measures to improve profit overseas, looking ahead?**

A You correctly described our policy for structural reform. Each of our overseas operating companies is promoting its own business plan. The companies in India, North America, and other places are positioned to generate a certain profit, excluding one-off factors, such as inventory valuation differences. In fact, AM/NS India is planning to boost its crude steel production output from 7 million tons at present to 8.6 million tons in the near future. It is also going ahead to secure mining resources to enable steel production capacity of 12-15 million tons. AM/NS Calvert in North America is suffering from stagnant profit, as it is exposed to the energy sector in addition to the automotive sector but has no operational problems and will seek to upgrade its product mix. We are considering and implementing a growth strategy for each project in such a way. Some operating companies, such as those in Indonesia, are struggling due to currency weakness or difficult economic conditions but we are discussing specific individual measures with JV partners.

Q Will you confirm that in your present plan, you are not incorporating blowing-in of any blast furnace in banking at the stage of restoring production in the second half?

A Yes, that has not been incorporated in our forecast at this time. However, demand trends are changing every day and we intend to flexibly respond to them with an optimal production framework.

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