NIPPON STEEL

Nippon Steel Corporation, IR Briefing Concerning
Acquisition of Shares of G Steel and GJ Steel in Thailand (to Make Them Subsidiaries)
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Summary of Q&A[1]

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◆ Background of the acquisition

Q Please explain how you arrived at the acquisition of G Steel and GJ Steel. I believe the acquisition of integrated steel production mills that produce hot-rolled steel sheets from electric arc furnaces (EAFs) in the growing Thai market is an attractive deal, but will you tell us if there were bidders and how you were able to reach agreement to acquire them.

A We started considering this deal in around May of last year. We were informed that Ares SSG (the Fund), which holds shares of these companies, was looking for a buyer. We were introduced to it and began considering the deal. Regarding the competition, we are not in a position to know about that but we can say that Nippon Steel has been investing in Thailand for many years and is highly trusted by the Thai government and the Thai steel industry. As the background to the acquisition, we believe our long-cultivated credibility, which also reflects our other overseas developments, must have had a great influence.

◆ The value and profitability of G Steel and GJ Steel

Q Compared to constructing a new facility with an annual steel production capacity of 3 million tons in Asia, which will cost more than 100 billion yen nowadays, this acquisition appears to be attractively priced at a maximum of 88 billion yen. Will you share your views on this point.

A This deal or our investment may look moderately priced partly due to being an M&A deal and not greenfield construction, in our view. The Fund must be making a profit, as it has agreed on our acquisition price of 48 billion yen. On our side, we conducted due diligence, estimated the outlook by taking into account the fact that the hot-rolling coil (HRC) international market was pretty good last year, and checked the valuation, which confirmed that we could make reasonable profit even in the conservative scenario. That is why we have decided to acquire these companies. We think the deal was closed at this price because both sides have found merits.

Q Both G Steel and GJ Steel had been in the red before the Fund acquired them. What were the

[1] Based on information as of the date of the briefing.

reasons for their sluggish earnings and how did the Fund turn them profitable?

A Before the acquisition by the Fund, these companies were stuck in a vicious circle: they had low profitability due to a lack of orders, aging facilities and poor quality, and their earnings further deteriorated as they could not even conduct regular maintenance due to a lack of funds. After acquiring the companies, the Fund first purchased nonperforming loans of these companies from banks and then made a debt equity swap to restore their financial soundness. Next, the Fund thoroughly reduced the companies' costs, including the streamlining of personnel. At the same time, it carried out the necessary spending for repairs and returned the facilities to a normal state. Although the improvement in earnings was of course partly due to the strong market, we believe that the quite appropriate measures taken by the Fund had a significant impact on the companies' turnaround.

Q Also, can you make a solid profit even if the HRC price falls in the future?

A With regard to the future HRC market, the surge in international HRC prices is being driven mainly by China's major change in its supply policy and the rise in global demand following the economic recovery from the COVID-19 pandemic. We anticipate that China's supply policy will remain unchanged in the future and that the post-COVID-19 demand recovery will continue.

Q G Steel and GJ Steel currently have a low capacity utilization rate. Will they be able to produce at a full capacity of 3 million tons if you intervene by giving technological support to them?

A After conducting an on-site survey, we concluded that they could improve the capacity utilization rate and therefore made a decision to acquire them. Currently, they operate only at night and on weekends when the electricity rate is low, at about half of their capacity. We think the culprit is the lack of product competitiveness. With the present product quality and delivery capability of these companies, it is difficult to secure more volume. However, if we can improve their cost competitiveness, product quality, and delivery capability by using our technology, we believe that G Steel and GJ Steel can raise their capacity utilization rate, given the fact that the Thai market is as large as 18 million tons and they are receiving order inquiries.

Q What are your thoughts on competition with blast furnace steelmakers and hot strip mills in other ASEAN countries, such as Vietnam and Indonesia?

A They are a major threat, but the market in Thailand has been exposed to such a crisis and so various protective trade policies have been implemented. Nippon Steel has made a substantial investment in downstream processing sites, but if trade policy were to exclude Japan's exports of semi-finished products in the face of such a threat, the business we have already invested in would not meet our objectives. We therefore believe that, by becoming insiders through the acquisition of local companies as in the case of G Steel and GJ Steel, we will be able to conduct business under the protection of local trade policies in the event of such a threat.

Q Will you need to make large-scale capital investments, such as for measures to deal with aging

facilities or to manufacture new products?

A Small investments to raise productivity and quality may be needed to capture the ever-growing commodity market, but large-scale investments will not be needed. However, in the future when we think about potential collaboration with Nippon Steel's downstream processes, another investment, such as in secondary refining, may be required to ensure quality that is consistent with this collaboration. We will decide the timing and the type of investment while managing G Steel and GJ Steel.

Q How do you plan to procure steel scrap, which will become raw material for EAF steelmaking, for G Steel and GJ Steel?

A G Steel and GJ Steel use scrap as the main raw material and pig iron for about 10% of the raw materials. Approximately 30% of scrap used is imported. Scrap procurement is their lifeline but may become difficult in the future if the move to achieve carbon neutrality further advances. For this reason, G Steel and GJ Steel will build relationships with overseas suppliers in addition to strengthening relationships with existing suppliers, or Nippon Steel will build a scrap procurement network, which is a challenge.

◆ Relationship with Nippon Steel's global business strategy

Q Can G Steel and GJ Steel quickly collaborate with your local downstream companies?

A G Steel and GJ Steel will need to have the ability to manufacture high-grade steel if they are to collaborate with our downstream processing facilities in Thailand. However, after acquiring G Steel and GJ Steel, we will first focus on increasing their productivity and improving their quality to enable them to achieve stable profits in the commodity product market. Under these circumstances, we will make a comprehensive assessment on the improvement of their product quality responsiveness, and take appropriate measures. We think it will take quite a long time, but in the future G Steel and GJ Steel will naturally have to collaborate with our downstream processes, and we are also bearing in mind their use based on the objective of carbon neutrality.

Q Will this acquisition complete your investment in ASEAN aimed at achieving global crude steel capacity of 100 million tons?

A After incorporating this acquisition and our expansion in India, we will still be short by around 10 million tons to achieve our target of 100 million tons. We are inclined to make brownfield investments such as this acquisition if there is any project that matches our policy. Such a project, which will not be limited to ASEAN or any other particular country or region, will be assessed individually.

Q You have explained that G Steel and GJ Steel could become future potential development bases for promoting your Carbon Neutral Vision. What kind of base do you have in mind?

A At the COP26, Thailand announced that it would be carbon neutral by 2050 and have net zero emissions by 2060. If this progresses, electricity will change to a carbon neutral power. Then, if we purchase carbon neutral power and use EAFs for steelmaking, we can make carbon-neutral steel.

Nippon Steel's three strategies to achieve carbon neutrality are: (1) hydrogen reduction by blast furnace (BF) steelmaking, (2) 100% hydrogen use in direct reduction, and (3) production of high-grade steel in large-size EAFs. It takes time to do all of these perfectly and there are also significant technical challenges. Since it is technically less difficult to produce high-grade steel in the smaller EAFs of G Steel and GJ Steel than in large EAFs, we expect G Steel and GJ Steel will play a role in the transition phase.

Q **I understand that you intend to reduce exports of HRCs as part of the shift to a more sophisticated order mix according to your Medium- to Long-term Management Plan. This must also mean a shift in the business model to replace exports with production by local mills. Will you share your thoughts on whether the acquisition of G Steel and GJ Steel will contribute to this.**

A In the Thai steel market, our exports of high-grade steel are totally separated from sales by G Steel and GJ Steel. We will capture high-grade steel business through direct exports from Japan and indirect production at local downstream sites where semi-finished products exported from Japan are processed, while G Steel and GJ Steel will capture commodity product business. For the time being, G Steel and GJ Steel aim to capture the growth of the commodity market and secure stable profits. They will also improve quality during this process and decide whether to enter into the high-grade steel business or not. The export of HRCs from Japan may potentially be replaced by local production, but for the moment, we expect exports from Japan, especially of high-grade steel that cannot be produced in Thailand, to continue.

Q **This acquisition involves EAFs. Please explain your approach to choose the types of upstream facilities for future overseas development.**

A We do not have a fixed approach for upstream facilities, either BF or EAF. As we have taken a combined approach pursuing (1) hydrogen reduction by BF steelmaking, (2) 100% hydrogen use in direct reduction, and (3) production of high-grade steel in large-size EAFs in our Carbon Neutral Vision, we can no longer exclusively focus on the BF method but this does not mean we will choose either the BF method or the EAF method. We hope you understand that we will have complex upstream facilities going forward.

Q **Unlike AM/NS Calvert, which focuses on high-grade steel, the acquisition on this occasion is a business involving mainly commodity steel in an emerging country, which must require different key points in management. What will the post-acquisition administrative and management structure be like?**

A We will renew the management structure after closing the deal. Currently, G Steel and GJ Steel have four executives including the CEO from the Fund. They will be replaced by Nippon Steel's executives. With regard to the sales structure, we value the current connections of G Steel and GJ Steel with their customers, and plan to send our staff to deal with the businesses where their delivery and quality standards have not satisfied customers' requirements. While respecting their current structure, we will make them stronger by injecting our strengths. Unlike AM/NS Calvert, which has an ArcelorMittal-led sales structure, we will be deeply committed to establishing a proper management structure, as we believe that ASEAN is our home market, we understand the Thai market, and we have established connections and credibility particularly in Thailand.

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