

**Nippon Steel Corporation, FY2021 IR Briefing
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Summary of Q&A¹**

Presented by:

Eiji Hashimoto, Representative Director and President

Takahiro Mori, Representative Director and Executive Vice President, CFO

Takahiko Iwai, Managing Executive Officer, Head of Accounting & Finance Div.

◆ **Profit/loss and dividends**

Q Will you provide us with a breakdown of your expected business profit of ¥600 billion or more excluding one-off factors for FY2022.

A We don't have an exact breakdown of the ¥600 billion at this time because the business environment is extremely uncertain. However, there are five pillars in the breakdown of the business profit of ¥600 billion that we have said we will secure excluding one-off factors regardless of the external environment. Rough targets are ¥250 billion for the domestic steel business (non-consolidated operating profit excluding inventory valuations, etc.), ¥100 billion for the overseas steel business, ¥100 billion for raw material interests, ¥100 billion for domestic group companies, and ¥50 billion for the three companies in the non-steel segments. In FY2021, we have achieved all of the above targets except that of the non-consolidated domestic steel business.

Although the domestic steel business is experiencing a very severe environment in FY2022, we don't think it will be impossible for the non-consolidated domestic steel business to secure ¥250 billion for the following reasons among others. First, minimum-cost operations and stable production activities are currently being conducted because measures have been taken to counter the problem of losses incurred due to poor operations in FY2021, especially in the ironmaking process. Second, the seamless pipe business, which was in deficit in FY2021, is expected to become profitable due to a sharp rise in inquiries, prompted by the Ukrainian situation, and the depreciation of the yen. We can also anticipate a profit of more than ¥150 billion in the overseas steel business due to factors such as the completion of the disposal of unprofitable businesses and the start of the consolidation of G Steel Public Company Limited and G J Steel Public Company Limited in Thailand, which we have completed acquisition procedures. Moreover, raw material interests may amount to more than ¥100 billion, as raw material prices are rising, while domestic group companies are also expected to generate more than ¥100 billion, as they have implemented structural measures in the past three years. Finally, the three companies in the non-steel segments are also expected to generate over ¥50 billion in business profit. In sum, we believe that ¥600 billion in business profit

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

excluding one-off factors is not a high target but a minimum target to be achieved.

Q Concerning your future vision of global crude steel capacity of 100 million tons per annum and ¥1 trillion in business profit, will you provide an assessment of the current status and talk about future challenges.

A It will not be possible to achieve capacity of 100 million tons and the future milestone of ¥1 trillion in business profit anytime soon but we firmly believe they are achievable. In order to ensure our presence in the world of 2 billion tons of crude steel production that is approaching, our vision is to have 100 million tons of global crude steel production and to become one of the Big Two alongside ArcelorMittal apart from China's state-owned steel mills, each of which aims to reach 200 to 300 million tons.

We will expand our capacity overseas, not in Japan, but there are two constraints. First, we intend to make brownfield investments because it is difficult to obtain permits for building new capacity based on greenfield investments, which is also highly risky and may end up disrupting the supply-demand balance. Second, even brownfield investments via acquisitions are difficult in China, where foreign capital regulations are imposed. Therefore, one of our means to achieve this is to expand capacity in India. In addition to the expansion of AM/NS India on the west coast of India, we will move forward with a project to construct a second steelworks on the east coast.

The second means is to strengthen the capacity of electrical steel sheets, in which Nippon Steel has overwhelming product competitiveness. While demand for electric vehicles is increasing, the United States and Europe do not have a steelworks to produce high-grade electrical steel sheets. Therefore, we are expecting to be asked to manufacture electrical steel sheets locally and to eventually manufacture them from upstream processes. In particular, there is no production base for EV motor cores in the United States, and the cores have to be imported from countries including Canada, Mexico, and Japan. This is making it difficult to increase EV production there. We are therefore anticipating various opportunities in this area.

As we have been saying, we will thoroughly pursue opportunities in overseas areas where demand is growing and in products where we can leverage our product competitiveness and technological capabilities. Although we have made some progress in adjusting direct contract-based prices for customers in Japan, the price level is still low, and major overseas steelmakers are making much higher profits per ton. If we achieve global crude steel capacity of 100 million tons, we believe that our consolidated business profit will exceed ¥1 trillion.

Q Nippon Steel has committed to maintaining a high level of return to shareholders. Are you thinking of maintaining an annual dividend of ¥160 per share in FY2022, as in FY2021, if you achieve a business profit of ¥600 billion excluding one-off factors in FY2022?

A I cannot say anything specific concerning the dividend for FY2022. However, as we are committed to maintaining a high level of return to shareholders, I don't think that our shareholders would be happy if the annual dividend of ¥10 in FY2020 was followed by ¥160 in FY2021, and say, ¥50 yen in FY2022. We are determined to make profits that will be sufficient as the source of dividends to continually pay a similar level of dividend as in FY2021.

Q You have decided to construct a next-generation hot strip mill in the Nagoya Works. Please explain why you will do this in Nagoya, Japan, and not overseas, as well as its profitability and economic rationality.

A As the shift to EV vehicles is continuing, the need to reduce the weight of materials will increase further because EV batteries are heavy. Among lightweight materials, aluminum has not only the problem of high cost, but also the problem of high CO₂ emissions during its life cycle from manufacturing to recycling. In particular, as a means of enhancing material strength for safety while making thinner materials for weight reduction, the only way to do this is to add an alloy for aluminum. This alloy manufacturing process, however, also emits further rCO₂. In contrast, high-tensile strength steel sheets can be made stronger either by adding alloys or controlling the crystalline structure. High-tensile strength steel sheets also have advantages both in terms of CO₂ emissions over their life cycle and in terms of cost. Therefore, the need for high-tensile strength steel sheets is expected to increase further.

To enhance the economy of producing high-tensile strength steel sheets, the cutting-edge technologies that we have developed and refined over the years, such as powerful roll-separating force and temperature control, are indispensable. We also need to manufacture them in an integrated production system from upstream processes. We have decided to construct the next-generation hot strip mill in the Nagoya Works from the viewpoints of maintaining the confidentiality of technological information and ensuring integrated manufacturing, and based on the fact that Nagoya is a major demand area for automobile steel sheets, and the fact that the current hot strip mill in the Nagoya Works is Nippon Steel's oldest, which has been forcing our other steel mills to make products that should have been manufactured at Nagoya.

◆ Management environment

Q Will you share your views on how the Russia-Ukraine situation and China's lockdown are affecting your steel demand.

A Concerning global steel demand, we recognize three main risks—China's slowdown in economic growth, supply constraints mainly for semiconductors, and a surge in energy and resource prices on the back of "greenflation". The ongoing Russia-Ukraine situation and China's lockdown are actually amplifying the magnitude of these risks and have a significant impact on steel demand.

The Russia-Ukraine situation has slowed down the economy in Europe, which relies heavily on Russia for

energy, but in terms of Nippon Steel's sales, China's lockdown has a greater impact than the Russia-Ukraine situation. This is because China's domestic demand, which accounts for more than 50% of world steel demand, is declining and Japanese customers' production problems have been exacerbated by supply constraints on components. We therefore think that the actual damage is more severe.

Q The yen is sharply depreciating. Please explain the impact of the current weaker yen.

A The advantage of the weaker yen is that when the total cost of products manufactured in Japan is converted to dollars, the yen-denominated cost portion depreciates. This increases the international competitiveness of our steel products and is advantageous for the export of our steel products and relative to imported materials. In addition, our domestic customers in the export industry can enhance the international competitiveness of their products, thereby boosting our domestic demand. However, at present, foreign currency costs, especially those related to energy and resource prices, have skyrocketed, and the percentage of yen-denominated cost to total cost has decreased to around 20%, while the effect of the depreciation of the yen-denominated cost, caused by the weaker yen, has diminished. Moreover, both Nippon Steel and our customers cannot expand exports despite the increased international competitiveness which resulted from the weaker yen, due to the current global economic downturn and increased supply constraints.

If the surge in energy and resource prices stabilizes and/or the overseas economy revives and creates an environment where exports can be increased, the yen's depreciation would be a greater tailwind for Japanese manufacturing industries, but I think it will take some time for that situation to occur.

◆ Measures taken and to be taken by Nippon Steel

Q How do you evaluate the correction of your direct contract prices and what are your future challenges?

A Direct contract prices have been corrected in FY2021 to some extent, but we don't think the correction is sufficient at all. In the uncertain business environment of FY2022, in order for us to prioritize the stable procurement of raw materials and the stable supply of steel products, the external cost push, including the impact of the weaker yen, must be promptly and fairly shared in the supply chain, as a matter of course. On top of that, we need to continue making efforts to reflect the added value of our steel products and the contribution to our customers' business in the sales price, so as to secure appropriate margins.

Q Do you think it will be possible to raise steel product prices by ¥20,000 - 30,000 on the back of the sharp rise in raw material prices? Will steel demand decrease if the steel product price continues rising?

A The concern that demand will fall due to the rise in steel product prices should be discussed by sector. Japan's steel demand mainly comes from three sectors: (1) construction, (2) final domestic consumption

of the manufacturing industry, and (3) final export of the manufacturing industry. Customers in the export industry (3) will benefit from the weaker yen, so there should be room for them to absorb the price increase, and we should be allowed to raise prices. Construction companies (1), especially private-sector construction companies, are in a difficult situation but our sales volume to this sector is not that large so the impact will be minimal. In either case, we cannot produce or supply steel products unless we raise prices in order to procure raw materials from overseas, so we must thoroughly discuss the price issue with our customers and overcome it. If we can make progress through discussions, the distribution and processing industries for steel products will be streamlined. We believe that this will be one of the factors that will make domestic steel product prices look less inferior internationally. Manufacturers, distributors, and processors have no choice but to break through this problem on their own.

Q It was reported that, given the slowing down of demand for steel products and the high level of inventories of three types of steel sheets, the start-up of the relined No. 3 blast furnace (BF) in Nagoya would slightly be delayed while you were watching the trend in steel demand. Will you explain your approach to raising prices while reducing production.

A In my view, the market price, which is determined by supply and demand conditions, is not relevant to the direct contract prices, which are determined by the value of products and our contribution to the customers. An increase in the market price does not necessarily raise the direct contract prices. Nor would we deliberately reduce production in an attempt to raise the direct contract prices.

In negotiations on the direct contract prices, we will discuss the price head on: we will ask customers to bear a fair share of costs as a matter of course, and then discuss prices thoroughly with customers regarding the value of our product and our contribution, but if we cannot agree on the price with the customer, the premise of a stable supply may not be maintained. Overseas, there is also an open-price system in which manufacturers unilaterally present the price and customers respond with order volume, but this system is unlikely to be appropriate in Japan. In the case of Japan, as steel demand from purely domestic demand-based construction sector and domestic consumption-based manufacturing sector is falling, we need to focus on the export-oriented manufacturing sector, work together with customers to win international competition and adopt the approach of increasing demand for their products, which mean to increase indirect exports for us, by working together with customers to win international competition. Among developed countries, per-capita annual demand for steel is 300 kg in Europe and the United States and it has been maintained at 500 kg in Japan. The surplus of 200 kg in Japan is for indirect exports. Our market strategy based on a broader viewpoint is to maintain the manufacturing industry's demand for indirect exports in Japan, as Japan doesn't have significant natural resources and energy-related domestic demand for steel products cannot be expected. For this reason, we believe thorough discussion with customers is a better method than the open-price system.

Q You have not provided guidance for your non-consolidated crude steel production forecast in FY2022. Please give us a rough idea on how production volume will change compared to FY2021.

A The scale of crude steel production depends on the scale of production capacity and the number of orders that can ensure profitability. Production capacity will be roughly 40 million tons if we can perform stable production, despite the decrease in capacity during the relining period of the No. 3 BF in the Nagoya Works. While it is difficult to foresee the number of orders that will ensure profitability as the overseas hot-rolling coil market has been negatively affected by the Russia-Ukraine situation and China's lockdown, we roughly estimate that crude steel production in FY2022 will be around 37-40 million tons.

◆ **Carbon neutral related**

Q You may need to reline the BFs in Kashima and Oita within the next 10 years. You are unlikely to have much time to decide whether to pursue the hydrogen direct reduction process in a BF or high-grade steel production in a large-size electric arc furnace (EAF).

A As you pointed out, the relining of the BF is one of the appropriate timings to realize the practical implementation of breakthrough technologies aimed at carbon neutrality. We really need to work out specific plans since our steelworks are large but may not have sufficient empty space to build an electric furnace next to the BF.

Q Will you elaborate more on your comment about starting to supply carbon neutral steel over the course of FY2023?

A The construction of an EAF with an annual production capacity of 700,000 tons is underway in the Setouchi Works Hirohata Area, and test operations will begin around next month. If we can externally purchase green power for production by the EAF in Hirohata, we should be able to start the supply of carbon neutral steel over the course of FY2023. The Hirohata Area will then be the first in the world to produce the highest-grade electrical steel sheets by using an integrated EAF process.

End

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