

Nippon Steel Corporation, Third Quarter FY2022 IR Briefing (February 9, 2023) Summary of Q&A¹

Presented by:

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Business environment

- Q If raw material prices continue to rise, material prices in 1Q FY2023 will be higher than in 2H and 4Q FY2022. In such a case, will you continue to ask customers to bear a fair portion of the cost increase during the price negotiation for direct contract-based sales? At the same time, how are you thinking about the risk that competition with inexpensive imports into Japan and electric arc furnace products would lower your domestic market share for civil engineering & construction materials and other products?
- A Coking coal market prices have remained at a historically high level, although they have declined from the recent high. Their future trend is hard to predict as it depends on economic trends in China and the supply and demand of steel products.

Under such circumstances, our stance will be the same as in the past. We will ask direct contract-based customers to continue the arrangements we have done so far so that the entire supply chain proportionately bears external costs. Please also note that sales prices are not determined solely by raw material prices. How our added value is considered and reflected in prices will also continue to be important.

As for the volume of imported steel products into Japan, we recognize that it has not increased nor decreased significantly.

- Q You explained that there is room to revise the minimum target earnings of ¥600 billion and more. Is it OK to assume earnings by adding the items described in the "Outlook of FY2023" on page 29 of the briefing document on top of the underlying business profit which is comprised of the five elements?
- A President Hashimoto says that we will achieve an underlying business profit of ¥600 billion or more regardless of the environment. I cannot say anything clearly about the next fiscal year, but ¥600 billion will be a base of our policies and action, and we want to try to keep on growing earnings. Our vision of achieving ¥1 trillion in business profit is difficult to be realized only in Japan, and overseas growth strategy is crucially important.

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Based on information as of the date of the briefing.



- Steel spread and sophistication of product mix
- Q You are anticipating the average selling price to decline by about ¥10,000 per ton in 4Q compared to 3Q. This must be largely affected by the impact of exchange rates on export prices. What kind of changes do you think could occur compared to the current assumption?
- A In the pre-fixed direct contract-based sales business, the 4Q prices have already been negotiated and set with customers using half-year contracts. With customers using quarterly contracts, the 4Q prices have also been negotiated already, using the 3Q price levels as reference, and have been almost completely settled by December. Therefore, we are expecting little change from the current assumption.
- Q The spread in direct contract-based sales dipped in 1H due to an increase in external costs after the price was fixed and agreed with customers. The spread since then, in 2H FY2022, is recovering. Is it appropriate to look at the current level of the spread achieved to be at the average level for FY2022? You said that you will maintain the spread in FY2023 and onward. Will it be possible to further improve the spread?
- A As shown on page 17 of the briefing document, when we negotiated the pricing for 2H FY2022, we took into account the temporary spread narrowing that occurred due to high raw material prices in 1H, and we were able to reflect this in the spread for 2H.

Let me now explain how we corrected the depressed prices in FY2021. We held individual discussions with customers in order to restore appropriate prices from a comprehensive perspective, that factors in not only fluctuations in raw material prices, but also the value of our products, our contributions to customers, our added value such as stable supply, and differences between domestic and overseas prices. As our customers have generally accepted our requests, we were able to improve the prices of our steel products, which were said to be the world's cheapest even while having the world's best quality, bringing our prices up to the global standard in 2H FY2021. We are now roughly expecting this pricing level to be maintained for the entire FY2022.

Maintaining and expanding the spread is a constant, ceaseless effort. This is not only a matter of the effort to make the entire supply chain proportionately bear external costs that cannot be controlled by Nippon Steel. Another important aspect is to seek customers' recognition in material terms of the added value of our products and services. To that end, we need to make efforts to improve our quality and proposal capabilities. We will also continue to work to expand the spread by moving toward a more sophisticated order mix and increasing marginal profit.

Q Thank you for explaining your efforts to advance the product mix and strengthen profitability without relying on increases in quantity. One of the key efforts must be to improve the production capacity and quality of electrical steel sheets. A part of your

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expanded production capacity is planned to be in full operation in 1H FY2023. Going forward, how will you respond to global demand for electrical steel sheets? Please explain, for example, the target ratio of domestic sales and exports of electrical steel sheets, and whether further capacity expansion will be necessary in the future.

A I cannot comment on specific strategic factors, such as the ratio of domestic sales and exports, destinations, and supply and demand. I can however explain that electrical steel sheets are required in places where electricity is used: non-oriented electrical steel sheets are used in the iron core of drive motors for eco-cars, and grain-oriented electrical steel sheets are used in transformers which transmit electricity to homes and factories. Currently, the supply capacity of electrical steel sheets is tight, and there are very strong requests from customers to increase capacity. I believe that capacity will continue to be expanded by us as well as by other companies. We thus need to consider further measures to expand production capacity.

◆ NSCarbolex[™] Neutral

- Q How do you plan to sell NSCarbolex[™] Neutral so as to contribute to earnings? Please tell us your thinking, such as taking a premium over the cost?
- A In the accelerating trend toward decarbonization, the automobile industry, for example, has been developing electric vehicles, which are clearly different from gasoline vehicles. The product value of electric vehicles is different, which allows their prices to be raised. We believe that green steel gets some of its added value by reducing CO₂ emissions in its steelmaking process, without any change in its function as steel material. We are continuing to discuss how society as a whole understands and accepts such value, and we must make society appreciate the value of green steel.

Will the steel industry not do anything about carbon neutrality until all steel is completely green steel? Of course that is not the case. With the aim of realizing a carbon neutral society, the industry has been making efforts to decarbonize the steelmaking process, including those to develop breakthrough technologies. We, Nippon Steel, will start full operation of the Hirohata Electric Arc Furnace in 1H FY2023 and plan to allocate the CO₂ emission reduction amount to the steel products. We will then sell the resultant NSCarbolexTM Neutral, which has been certified as reducing CO₂ emissions in its steelmaking process, to customers seeking green steel. We are also consulting with the relevant government agencies to establish such social system.

- AM/NS India
- Q I understand that AM/NS India will generate profits from the sale of surplus gas in the next fiscal year. Will you explain how it works and whether similar operation will continue in the future?



A AM/NS India has direct reduction ironmaking facilities (Midrex) using LNG and power generation facilities, and LNG accounts for a significant portion of its cost. AM/NS India has been engaged in long-term hedging operations so as to benefit from stable operation and cost, in distinction from the idea of benefiting from profit. It has done so since long before the Russian invasion of Ukraine. A decline in export volumes due to the imposition of export tariffs in 2022, among other factors forced AM/NS India to reduce production and the company ended up having a surplus of hedged LNG, which the company will sell and generate profit. Please consider the implementation of the hedge and the sale of hedged LNG as the company's action seeking business stability: to stabilize costs through hedging and avoid the disadvantage of production reduction through one-off gains in the event of it.

Dividends

- Q The expected dividend payout ratio of 25% for FY2022 is somewhat low, although it falls within the scope of your dividend policy (target payout ratio of around 30% on a consolidated basis). Does this imply your intention not to reduce dividends for FY2023? Is it fair to assume that the dividend for FY2023 will be ¥180 per share at minimum if the underlying business profit does not fall below ¥600 billion? Please tell us your way of thinking.
- A Net profit for FY2022 is expected to set a record high, but to include inventory valuation gains of over ¥200 billion, which are delayed in timing recognition and are non-cash. So it can be said that profit available for dividends for FY2022 is inflated compared to what it actually should be.

The expected dividend amount will still be a record-high as we are generating a high level of profit in FY2022, and moreover, we want to maintain a high level of dividends in FY2023 and beyond. Because of these reasons, we would like to modestly contain the dividend payout ratio for FY2022. It is difficult to comment now on dividends for FY2023 but we will thoroughly discuss the matter within the company when we make FY2023 forecasts.

End

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