NIPPON STEEL

Nippon Steel Corporation, FY2022 IR Briefing
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Summary of Q&A[1]

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◆ Profit and loss for FY2022 and FY2023

Q Will you give us an overview and describe the strategies of your domestic, overseas, and raw material businesses, which are supporting such strong earnings forecasts despite seemingly very poor market conditions?

A First of all, looking at the global steel industry, we recognize that the situation is the worst since 2000, and we expect that the situation will remain so at least until the end of this year, or may deteriorate further in the future.

In such a situation, only India and some other countries will see an increase in global demand, while China, which accounts for a large share of the steel industry, has not yet seen any economic effect centered on the real estate market, and the U.S. high interest rate policy is expected to have adverse effects going forward.

In these circumstances, iron ore prices are unlikely to keep rising. The price of coking coal in FY2022 was at an abnormally high level, and it would be no surprise to see the price fall. Fortunately, we have so far been able to reflect the surge in raw material prices in our product prices.

Currently, it is rumored that China must have been increasing exports due to its excess capacity and production. We have two strategies to counter that. The first is to place more focus on high-grade steel, which cannot be produced in China, in Japan. The second is to expand our business in India, a market that is growing and is difficult for China to enter.

As a result of these efforts, we believe that we can achieve ¥800 billion in underlying business profit in FY2023 despite the severe situation.

Q You expect steel products shipments to increase by 130,000 tons in FY2023 vs. FY2022. Does this mean that you plan to increase volume in line with your outlook for domestic demand? In FY2022, I think the pricing policy was part of the reason why you cut back

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

volume. Will you explain how you see shipment volume for FY2023?

A First, we will not lower product prices to capture orders with the aim of increasing shipment volume, which will cause earnings to deteriorate. We do not expect domestic demand to recover in FY2023. I would like you to understand that shipment volume of steel products will be roughly flat, excluding the impact of the blast furnace relining in FY2022.

Q Why are you expecting the spread to decline by ¥4,000/ton from 2H FY2022 to 1H FY2023?

A The deterioration in the spread will be caused by adjustments in raw material prices resulting from the pre-fixed pricing system. Since raw material prices are not determined when the product price is fixed, there is always a timing difference, and adjustments are made after the actual shipment. Some comparison period may make the spread look deteriorated, depending on the amount of the adjustment,, however we will never strategically depress the spread. We would recommend that you look at the spread trend annually, such as “FY2022 vs. FY2023,” which reflects the impact of the adjustment less.

Q I think that the spread can improve solely due to a product mix improvement, such as the sophistication of the order mix that you are currently working on. So why are you expecting the spread in FY2023 to be the same as in FY2022?

A We have engaged in various discussions with customers to improve our spread. At this moment, we forecast the spread will remain unchanged, but we will strive to further upgrade our order mix, as you pointed out correctly, and aim to improve the overall margin.

Q Will you provide more details of your overseas business, which is forecast to generate ¥120 billion in underlying business profit in FY2023?

A Our business in India will generate improved profit due partly to the effects of the acquisition of key infrastructure such as ports and power generation facilities. G/GJ Steel in Thailand is currently struggling due to the sluggish Chinese and ASEAN markets, but as Nippon Steel has participated in G/GJ Steel, the company is in the process of improving its production capability and its management, which spans procurement of steel scrap to product sales. We believe that G/GJ Steel will become a stronger company before very long. In addition, as we have withdrawn from businesses that we could not economically rationalize to continue, we no longer have businesses that will impede earnings.

Nippon Steel’s strategy for its overseas business is to invest in markets where demand is definitely growing, or where we can leverage our technological and product strengths. For example, the reason for our large-scale investment in India is that demand is growing in the market, while the difficulty to acquire land in India makes it very hard to newly enter the market on the supply side. India also structurally has very few imports. For Nippon Steel, which has already become an insider, India is a great market and we are confident that our investment in India will definitely be profitable.

◆ **Future strategy**

Q What are your challenges in achieving underlying consolidated business profit of ¥1 trillion?

A First, we are now smoothly implementing the structural measures. If we can achieve our current plan in FY2023, we will complete structural reforms in the sense of rebuilding profits. Next, from FY2024, we would like to realize the ¥1 trillion vision by 2030 and formulate specific plans to reduce CO_2 emissions by 30% compared to FY2013 for decarbonization.

So far, we have lowered the break-even point by 40% through structural measures and an improvement in direct contract-based sales pricing. Going forward, a recovery in production volume by one million tons alone can result in an increase in profit of several tens of billions of yen. I think we have reached the point where our domestic business can be resilient on the downside and generate more profit on the upside. Moreover, when the structural reforms are completed by FY2025, in addition to the effects of structural measures related to fixed costs and other items, the effects of the more sophisticated order mix will appear. A fairly strong structure is thus being established for the domestic steelmaking business.

In the overseas steel business, we will expand integrated steel businesses that can secure more added value. In particular, the effects of our current business expansion in India will emerge in the future. I think we can quite possibly reach ¥1 trillion in underlying consolidated business profit, including the raw materials business. However, it is not enough to simply accumulate another ¥200 billion on top of the expected underlying business profit of ¥800 billion for FY2023. In order to structurally achieve ¥1 trillion, we need to take measures to raise profits by about ¥500 billion, taking into account the risk of profit decline caused by competition with other companies.

In that sense, we need to evolve to a further vertically integrated business structure, which includes entry into the upstream raw material business and the downstream trading functions. By doing so, I believe that ¥1 trillion in profit will no longer be a vision but a specific target.

Q What measures are you considering to achieve a more vertically integrated business structure?

A We are considering entering the upstream raw material business, but we cannot mention any specific projects at this moment. Let me however mention two points. First, there have been fewer companies that aggressively invest in iron ore or coking coal, while we need highquality raw materials to achieve carbon neutrality. We thus have to invest on our own. The same can be said for reduced iron. The procurement timing, quantity, specifications, etc. of the reduced iron are determined based on our individual plans, but there is a high risk of not being able to procure the required quantity when needed, if we remain in the position of a mere procurer. That is why we need to do it as a part of our own business.

The second point is that the more vertically integrated business structure will lead to an increase in consolidated earnings. In particular, the steel raw materials business will become a new hot spot triggered by the decarbonization trend. Looking ahead, for example, we may manufacture reduced iron in Australia or make slabs and hot coils there and import them into Japan in the future, since it is easy to procure steel raw materials, green electricity and green hydrogen in Australia. We believe that decarbonization will cause a second major transformation in the steel industry since China began full-scale steel production in 2000. If we intend to respond appropriately and in a timely manner to these changes, we will have to do everything from raw materials to steel products on our own.

Q Today, you announced an additional large-scale investment in electrical steel sheets. This represents a considerable amount of investment on a cumulative basis. I would assume that some of these investments may start contributing to profits from FY2023. Will you tell us about the profit contribution of this electrical steel sheet as much as you can?

A Electrical steel sheets are high-value-added products and will definitely contribute to earnings. Although we cannot tell you the specific amount of profit, we are implementing the investment based on a proper study and checking of the profitability of the investment.

This time, we decided to invest additionally because our already-announced investment will not be sufficient to meet the growing global demand for electrical steel sheets, especially for high-end products. Needless to say, we foresee prospective supply needs and we believe the new investment will also be profitable.

If we do not supply the electrical steel sheets properly, automakers may commonly manufacture electric vehicles using lower-grade electrical steel sheets. In addition, while motor core manufacturers are also actively investing, the manufacturers we are working with will not be able to make investments with confidence unless we increase our supply capacity for electrical steel sheets. From various perspectives, we believe that the risk of not investing is higher than the risk of investing.

◆ Dividends and share prices

Q What are your thoughts behind the dividend of ¥140 or more that you stated?

A We are not saying that we will continue to pay dividends of ¥140 or more forever, but we are quite committed to this dividend statement for FY2023. In other words, the dividend for FY2023 will not be below ¥140.

We aim to achieve the projected underlying business profit of ¥800 billion, and we will make efforts to further increase profit so as to increase dividends.

Q Your capital expenditures, including those related to carbon neutrality, will increase going forward. Will you change the current dividend payout ratio target of around 30%, or specifically 35% in the case of FY2023, in the future? Will it change when looking at 2030, for example?

A We have not yet formulated a management plan for 2030, so I cannot say anything about the future policy. Of course, we intend to secure a certain level of cash flow under any circumstances. Our policy of providing a certain level of shareholder returns will remain unchanged.

Q What measures are you considering to ensure that the stock price is appropriately evaluated in the market?

A The Tokyo Stock Exchange (TSE) is requesting companies whose PBR is persistently less than 1 time to disclose their efforts for improvement and their progress. The TSE has pointed out not merely the improvement of PBR, but also the importance of sustainable growth and enhancement of corporate value. In the FY2022 Earnings Summary briefing material, we have described our growth strategy and measures to improve our corporate value, which we believe have been continually executed. Unfortunately, however, our current PBR is less than one. While capital and profits are improving rapidly, the PBR will not approach one unless the stock price goes up. This is expected to take some time, so I think our current task is to help you better understand the strategies and results that we are implementing. In order to increase the trust of investors and analysts, we are determined to clearly explain our thinking and to create more opportunities for dialogue. This is the first time we have announced the dividend forecast for the following fiscal year in the annual results announcement. This is because we wanted to send a message that we are eager to maintain the high-level dividend payout, which is at an unprecedented level for Nippon Steel. Including this message, we aim to help you better predict our earnings and returns.

◆ Carbon neutrality

Q Please tell us about your efforts related to carbon neutral steel in FY2023 and how

they will contribute to earnings.

A R&D investments and other costs will increase first and our efforts related to decarbonization will not contribute to earnings for the time being. In FY2023, we will start supplying green steel under the brand name NSCarbolex™ Neutral. The shift to an electric arc furnace (EAF) in the Setouchi Works Hirohata Area will be completed in 1H FY2023 and this will reduce CO_2 emissions by 600,000 tons in annualized terms. This means that we can ship 300,000 tons in annualized terms of green steel in terms of conversion to steel. As this shipment requires a third-party certification approved by the government, we will obtain the certification and then start supplying green steel products.

Q Could you elaborate on the shift to EAFs in the Kyushu Works Yawata Area?

A Let me first explain why we are focusing on a shift to EAFs. There are high technical hurdles in realizing hydrogen injection into BF and hydrogen direct reduction of iron (shaft furnace etc.), and it is unclear whether Japan's hydrogen supply system will be sufficiently developed by 2030. Therefore, in order to achieve a 30% reduction in CO_2 emissions by 2030 vs. 2013, we cannot place the main focus on hydrogen injection into BF and hydrogen direct reduction of iron (shaft furnace etc.), and so we are focusing on promoting a shift to EAFs, which do not use hydrogen in steelmaking. Yawata and Hirohata have been selected because of their knowledge and experience, as Yawata is a supply base for electrical steel sheets and Hirohata has already been producing electrical steel sheets using an EAF.

Concerning the timing of this announcement, we will not be able to achieve the anticipated results in 2030 unless we start full-scale studies now. This is because we need to ask utility suppliers and many other related parties for their cooperation. We will also have to operate both the blast furnace and the EAF for a certain period of time, and we need to study and plan the operating conditions for that period.

◆ Specific implementation of HR and PR initiatives to recruit and retain diverse human resources (supplementary explanation)

One of Nippon Steel's major management challenges for FY2023 is to recruit and retain diverse human resources. The Japanese steel industry is not highly recognized in the job market, and we are aware of the challenges in recruitment, especially for personnel at manufacturing sites.

With regard to the hiring of non-manufacturing staff, Nippon Steel reduced its hiring for about 10 years starting in 1995, when the steel industry's business performance was severe. The employees hired during this period are about to reach the age of 40-50. One of the problems is that this age bracket is small even though they will become responsible for management in the future.

In addition, Nippon Steel has to overcome various other issues in order to grow and generate profits amid the continued harsh business environment. This requires many excellent human resources to play an increasingly active role. We have been considering this issue for some time and as our profit, employee remuneration, and dividend levels have finally reached certain sufficient levels, we will now start focusing on the HR and PR initiatives stated in the briefing material.

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