

Sanyo Special Steel Co., Ltd.
IR Briefing Regarding the Business Results for the FY2021 1Q
Q&A Summary

Date : Friday, July 30, 2021

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** Please be noted that the actual Q&A session was in Japanese and this English translation is prepared for reference purpose only.*

Q . Could you tell us how much profit or loss is expected at actual basis in the FY2021, i.e., excluding transient factors such as the impact of changing fiscal year end of Ovako and the time lag of iron scrap surcharge?

A . The FY2021 ordinary income forecast of 10.5 billion yen includes the effect of changing fiscal year end of Ovako by +1.8 billion yen and the iron scrap surcharge time lag of -4.7 billion yen for Sanyo and +1 billion yen for Ovako respectively. Therefore, the genuine ordinary profit of FY2021 excluding these factors would be about 12.5 billion yen. However, if the iron scrap price becomes higher than the estimated 55 thousand yen per ton, the surcharge time lag impact will be more negative. We consider it necessary to pay close attention to the trend of iron scrap price.

Q . Could you explain why the increase in sales volume has a relatively large impact on profit and loss at Ovako?

A . Since Ovako has in-house secondary processes and trading functions, Ovako has a relatively high marginal profit per ton and therefore is affected more by the fluctuation of sales volume. In addition to the increase of sales volume, measures to control fixed costs, such as basically hiring temporary workers to increase production capacity, have also contributed to the profit recovery of Ovako.

Q . With the support of the Swedish Energy Agency and the collaborations with Volvo Group etc., Ovako has started construction of a fossil-free hydrogen plant. Could you tell us about the effects on steel and costs to heat steel using hydrogen?

A . Ovako has already conducted trials to heat steel prior to rolling using hydrogen instead of the current LPG, and has confirmed that heating with hydrogen does not affect quality of steel. Sweden has abundant carbon free and inexpensive electricity resources; hence, we expect no cost increase, rather, depending on the price of electricity, we even consider the possibility of cost savings.

Q . Although the current market price of scrap iron H2 in Himeji area is about 50 thousand yen per ton, the presuppositions after July 2021 is 55 thousand yen per ton, and that of crude oil price after July 2021 is 80 dollars per barrel. Have you made these presuppositions from conservative views?

A . The current market price of scrap iron H2 in Himeji area is a little over 50 thousand yen per ton. In the business forecast for FY2021, we have made the presuppositions higher than the current prices since raw material and fuel prices are expected to increase.

Q . You changed the fiscal year end of Ovako from 31st December to 31st March from FY2021. From now on, I consider that Ovako's financial performance for the second quarter and the third quarter will deteriorate due to seasonal factors. Could you let us know if my assumption is correct or not?

A . You are exactly right. Ovako has summer holidays for about 1 month in the second quarter (from July to September) and Christmas holidays for about two weeks in the third quarter (from October to December). Therefore, Ovako's sales volume in 2Q and 3Q will decline and its financial performance will deteriorate.

Q . Could you tell us Ovako's operating income for the first quarter of FY2021 (from January to June, 2021), divided into January-March and April-June?

A . 2.7 billion yen for January-March, 2021 and 3.5 billion yen for April-June, 2021.

Q . What is the market price of scrap iron in Himeji area for the first quarter of FY2021?

A . The average of market purchase price from April to June 2021 is about 47 thousand yen per ton.

Q . How will Sanyo, on non-consolidated basis, pass on the increasing costs of materials to the unit price of sales, to which you do not apply the surcharge mechanism?

A . The iron scrap surcharge mechanism is not applied to 20% of our sales volume, and almost all of them are to distributors. In January and June, we already have announced to raise sales price by 10 thousand yen per ton respectively. If the iron scrap price increases more, we surely will raise the sales price again. Furthermore, the price of alloys is also increasing. The applied ratio of alloy surcharge is less than that of iron scrap; hence, we have started discussion about applying alloy surcharge to more customers.

Q . On 14 July, 2021, the European Commission has announced about the Carbon Border Adjustment Mechanism (CBAM), and EU Emissions Trading System (EU ETS). It is said that free allocation of greenhouse gas will be decreased from 2026. I suppose that Ovako, whose CO₂ emission is very low, has advantage in the future. Could you tell us how you consider these measures, and whether Ovako's products will be affected by CBAM?

A . We expect that the some cost increase might happen in the future due to the revision of EU ETS. However, since CO₂ emission of Ovako is very low, we consider that EU ETS will not affect Ovako significantly and would not deteriorate Ovako's relative competitiveness. With regards to CBAM, Ovako's products are subject to this mechanism if introduced, and we consider the introduction of this mechanism be relatively advantageous to Ovako. We will continue to pay close attention to the developments and details of these two mechanisms.

Q . Could you please tell us the reasons why the profit of the second quarter in FY2021 is expected to drastically deteriorate compared to that of the first quarter in FY2021?

A . The reasons are as follows;

- 1) The positive impact of changing fiscal year end of Ovako is included in FY2021/1Q.
- 2) Ovako has summer outage for about 1 month in FY2021/2Q.
- 3) Sanyo has summer regular plant outage for about 1 week in FY2021/2Q.
- 4) The prices of iron scrap and alloys are rising and expected to rise in FY2021/2Q. On the other hand, sales price will not catch up with the rising prices of those materials due to time lag.

The time lag of iron scrap surcharge in FY2021/2Q will be negative by almost 1 billion yen compared to FY2021/1Q.

Q . Please tell us how Ovako has greatly reduced CO₂ emissions since 2018? It is surprising that in 2020 Ovako has reduced the emission in the manufacturing process by 54%, compared to that of 2015.

A . Ovako has drastically reduced CO₂ emissions mainly because of switching to carbon free and cost competitive electricity. In Sweden and Finland, where Ovako's production sites are located, carbon free electricity (hydropower, wind power) resources are overwhelmingly abundant compared to other nations. Ovako has managed to shift to the carbon free electricity without increasing cost.

Q . Has the demand from customers for Ovako's products been increasing in EU because of its low emissions?

A . Regarding the global movement toward carbon neutrality, the interest for Ovako's products, made with far low CO₂ emissions, has been increasing, and we expect it to further amplify in the future. In case we would supply carbon free material, we would like to ask the understanding from our customers to pay some premium to supply carbon free steel.

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