

Sanyo Special Steel Co., Ltd.
IR Briefing Regarding the Business Results for the FY2020 2Q
Q&A Summary

Date: Thursday, October 29, 2020

Speaker: Director, Member of the Board and Managing Executive Officer;
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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 please give us a detailed explanation about the recording of inventory valuation gain, and the amount of impact?

A. When inventory unit price exceeds the selling unit price due to sudden decrease in production volume etc., we need to recognize a loss on valuation of inventories based on accounting rules. The recorded loss on valuation of inventories will be reversed when the inventory unit price drops below the selling unit price. When we announced in the previous forecast (7/31), we expected this reversal period to be in the second half of 2020. However, the recovery in production volume was earlier than expected, and therefore inventory valuation gain was recorded in the second quarter of 2020. The inventory valuation amount of loss in the first quarter and gain in the second quarter are same, which is 0.8 billion yen.

Q. Could you please tell us any ideas of non-consolidated business forecast for FY2020?

A. For FY2020, we expect positive factors such as a) increase in sales volume, b) decrease in repair cost, c) decrease in fixed cost, along with cautious factors such as d) lower ratio of highly profitable alloy steel, e) rise in scrap price, f) delayed impact on manufacturing costs due to cost rising in the first half. We believe the sales product mix to deteriorate, due to continuing destocking of stainless steel, which is quite profitable.

Q. How do you view the financial performance for FY2021?

A. Regarding Sanyo, we expect a positive impact from sales volume increase due to the recovery in customer demand, and a negative impact due to the completion of unemployment compensation scheme. Regarding Ovako, we strive to gain operating income that exceeds the amortization of goodwill which is 2.6 billion yen. Although it seems to be somewhat a high target from the current performance, Ovako can have a large positive effect from increasing the quantity due to its high marginal profit unit price. In addition, we expect that fixed cost will further be reduced by means of restructuring. Regarding MSSS, we expect to become profitable next year. To conclude, we aim to achieve positive results on consolidated basis and restart paying dividends.

Q. Could you please tell us about the progress of the synergies among Nippon Steel, Ovako and Sanyo?

A. Regarding the synergies, it takes some time to switch the manufacturing site because of customer approval, but sales related synergies in other areas are increasingly accomplished. We will relentlessly aim to fully realize the synergies by March 2025.

Q. Could you please tell us about domestic demand trends for special steel by each industrial sector?

A. Currently, the demand for automobiles, both for automobile manufacturers and automobile parts manufacturers are strong. But there is a possibility that inventory may be accumulated and we continue to watch the movement of automobile industry closely. Construction machinery has been in a destocking phase for a long time, but it finally has bottomed out and is expected to recover. For industrial machinery, capital investment-related items such as machine tools and robots have not yet recovered. We consider that the reasons are future uncertainty such as the US-China trade dispute and the US presidential election, hence capital investment decisions are postponed. Destocking for stainless steel is continuing due to its long supply chain. Tool steel is mostly for automobiles and the inquiries from customer are increasing.

Q. How do you think the post-corona demand would be?

A. We consider that the demand environment will not completely return to pre-corona level as one of the possible scenarios. Even if the demand does not return to the pre-corona level, we have to become a more profitable company. Therefore, we will continue or endeavor to lower break-even point by reducing fixed costs on consolidated basis.

Q. There are reports that say China plans to phase out conventional gas-burning cars by 2035. Also there are many reports about carbon neutrality. How will these affect your business?

A. Since we manufacture special steel from scrap, we assume that our CO₂ emissions are relatively low. We are working to save energy and reduce CO₂ emissions throughout the supply chain as we showed in our IR material Page 27 to tackle with the challenge zero activity. Ovako, which is located in Europe, is well concerned of environmental issues and is working on steel heating using hydrogen.

Regarding China reports, we do not think that the demand for special steel will be affected both significantly and immediately. We will continue to expand our presence of high-cleanliness steel since we regard the change to EV and HEV as a positive business opportunity.

Q. Could you please tell us about the mechanism how to calculate exchange rate impact in Ovako?

A. Basically, Ovako makes transactions in euros, but some of Ovako's subsidiaries are based on Swedish krona. Hence, foreign exchange effects appear when Ovako makes consolidated statements in euros. Regarding foreign exchange effects, Ovako record the effects resulting from operating transactions as operating income and losses, and record the effects resulting from intra-group loan transactions as non-operating income and losses.

Q. Is there any possibility that the oxygen shortage in India will become a constraint on the production and sales of MSSS while demand is expected to recover?

A. The oxygen shortage affected the production and sales of MSSS in the July-September 2020. The newly infections of coronavirus in the state of Maharashtra, where MSSS is located, is declining, and we think oxygen shortage will be resolved momentarily. The amount of oxygen procured by MSSS has also increased significantly, and we do not think it to be a restraining factor for sales volume in the second half.

Q. Could you please tell us about the cost outlook for electrodes, in 2nd half of FY2020 and FY2021?

A. We think that the price will not increase in the second half of 2020. In case supply and demand of electrodes in 2021 may become tight due to the increase in production volume, it may have an impact on the procurement cost. We would like to continue to increase the usage of inexpensive Chinese products to offset the possible increase of electrode price.

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