

Sanyo Special Steel Co., Ltd.
IR Briefing Regarding the Business Results for the FY2022 1Q
Q&A Summary

Date : Thursday, July 28, 2022

Speaker : Kozo Takahashi, 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 tell us the breakdown of transient factors in ordinary income of OVAKO in FY22/1Q (2.1 billion yen)?

A . The transient factors consist of (a)Sales margin and product mix(1.5 billion yen) and (b)Fixed cost(0.6 billion yen).

(a)Sales margin and product mix includes the impact of price differences by iron scrap market. While the German market price is primarily reflected in the sales price for central European customers, OVAKO procures iron scrap based on the Swedish market price. The temporary price difference between the two markets affected the scrap margin positively.

The impact of foreign exchange rates is also included in (a), which occurred mainly as the amount of debt of OVAKO's subsidiaries denominated in SEK decreased in EUR due to the depreciation of SEK.

(b)Fixed cost includes refund of surplus from the Swedish Health Insurance Organization.

Q . Could you tell us how you see global demand trends in FY22, while the shipment of special steel products was strong in FY22/1Q?

A .We consider the shipment of special steel products was not that strong in FY22/1Q and continue to view the trend of auto production to be cautious. The level of shipment will not recover for a while due to inventory buildup in the supply chain, though we see some suppliers are preparing for auto production recovery. Some believe the shortage of semiconductors will ease, but we do not share that particular assessment.

Demand in special steel has been robust in segments of construction and industrial machinery, and the underlying demand in construction machinery has been particularly firm.

Q . Could you tell us the background why you have revised ordinary income in FY22 forecast upwards, from 14.0 billion yen to 16.0 billion yen? Is it correct to assume that main reason is decrease in the iron scrap price?

A . On April 28, 2022, we announced the number of ordinary income of 14.0 billion yen just as a target for FY22, without disclosing breakdowns by each group entity. On July 28, 2022, we announced the revised ordinary income of 16.0 billion yen, based on the assumption that the current turbulent business environment will continue, where raw material prices still remain high, reduction of auto production continues mainly due to supply chain disruptions including semiconductor shortage, the Russian invasion will prolong and will trigger economic slowdown due to global inflation, although there are some one off upside factors, such as declining iron scrap prices and the impact of transient factors of OVAKO.

Q . Do you predict that sales volume will increase after the recovery of auto production in Japan from FY22/2Q? Do you see that takes longer time due to inventory adjustment?

A . We do not predict auto production in Japan to recover in FY22/2Q and do not expect inventory adjustments in the supply chain or supply bottleneck issues to be resolved in the short term. We consider some more time to be needed for recovery of sales volume of special steel products.

Q . Do you predict that business confidence is bad, in spite of the recovery of auto production in Europe?

A . We have regarded production of trucks and other special vehicles in Europe to be robust, but consider the overall European auto sales to continue below the previous year's level. Business confidence is difficult to forecast due to the prolonged situation in Russia and Ukraine. We will carefully monitor how the market would develop after summer vacation.

Q . Please tell us about the progress of sales price increase in Japan. Also, what are your thoughts on the introduction of energy surcharges in Japan?

A . We announced sales price increases, most recently in September 2021, March 2022 and May 2022 and believe that these price increases have been well understood and recognized by our customers. With energy prices expected to rise further in the second half of this year, we are discussing with customers about the application of energy surcharges. We believe that we are making progress in gaining the understanding from our customers, including the mechanism of surcharge or quasi surcharge system, determining sales prices based on figures published by electric power companies and other sources.

Q . What do you think about the impact of gas rationing in Europe on OVAKO, which has been reported by some media?

A . We are aware of the news as well. Finland has already stopped receiving natural gas through the pipeline directly connected from Russia but has secured natural gas through another pipeline from the Baltic states. Since the share of natural gas in Finland's total energy use is relatively limited (less than 10%) and there possess some natural gas stocks, we do not expect any major supply concerns in the immediate future. The prices will inevitably fluctuate, but we will mitigate the impact with the introduced surcharge system. We surely will keep a close eye on the impact of natural gas supply restrictions on business confidence especially in Germany and Eastern Europe.

Q . OVAKO has achieved carbon neutral in production (hereinafter referred to as CN) from January 2022. How is the customer's reaction for CN steel?

A . All steel products shipped from OVAKO are CN and are subject to climate surcharge. The application of the climate surcharge is no reason for any customers not to buy OVAKO's steel products. Rather, the top management of each customer understands and accepts this concept. Bearing manufacturers are requested to be CN from automakers, and we believe that there are significant advantages for our customers to use CN steel products. Though it is difficult to indicate how much positive volume effect this will have, we believe that OVAKO's shipment will remain stable compared to competitors especially in the phase of downturn.

Q . Scrap steel prices are plummeting. Will this be an obstacle for future price increases in the domestic business?

A . Price adjustments might be discussed with some small number of customers, such as distributors, to whom steel scrap surcharge is not applied. However, we do not believe the plummeting scrap price is an obstacle for the price increases which we have requested for customers mainly due to rising energy costs and ferroalloy prices.

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